The effect of anti-avoidance tax legislation on the protection of a legal interest in wealth creation and preservation

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ABSTRACT

Two interests, regulated by two separate areas of the law: the one, a yet to be recognised legally protectable interest in wealth creation and preservation; and the other, firmly positioned statutory provisions of the General Anti-Avoidance Rules (hererinafter "GAAR"), standing opposite each other. One may only consider these two interests to be in a balancing act, if both were equally recognised, receiving equal protection – both from external influences and from each other.

This research sets out to answer the question, what the effect of anti-avoidance tax legislation is on the protection of a legal interest in wealth creation and preservation. It is a well-known principle in our South African common law that an individual is free to order his or her affairs in whatever manner brings about the most beneficial tax treatment.¹ This research challenges this statement in the sense that the limitations imposed by the GAAR, through its various requirements² may have the effect that an individual’s apparent freedom to structure his affairs as he pleases to enjoy tax benefits, is continuously infringed on. This results in the limitation of an individual’s right to enjoy the legal entitlements³ of his or her interest in his or her wealth creation and preservation.

The first item to determine, in chapter 2, was whether an individual’s interest in the creation and preservation of his or her wealth is an interest possible of enjoying legal recognition and protection. Only once that has been determined, could the criteria and the working of the GAAR be researched in chapter 3, as it pertains to the interests identified in chapter 2. Finally, chapter 4 puts the findings of chapter 2 and 3 to the test in the form of two case studies.

¹ Inland Revenue Commissioners v Duke of Westminster 1936 A.C. 1; CSARS v NWK Ltd 2010 ZASCA para 168; Kilburn v Estate Kilburn 1931 AD; Commissioner for Inland Revenue v Conhage (Pty) Ltd 61 SATC para 391.
² Section 80A – L of the ITA.
³ Para 2.1.4.2 below.
OPSOMMING

Twee balange, wat deur twee verskillende areas van die reg gereguleer en onderskei word staan weerskante van mekaar. Die een, opsoek na erkenning as ‘n beskermbare regsbelang in die skep en beskerming van rykdom; en die ander, standvastig geaposisioneer en statutêr vervat, bekend as die belasting teenvermydingsmaatreëls. Mens kan hierdie twee belange ag as om in ‘n stryd te wees om gelyk te staan, maar slegs indien albei gelyk erken word en gelyke beskerming geniet – beide van eksterne faktore en van mekaar.

Hierdie navorsing stuur oom ‘n antwoord te bekom op die vraag na wat die effek is van belasting teenvermydingsmaatreëls op ‘n individu se beskermbare reg op sy of haar belang in sy of haar rykdom skepping en beskerming. Dit is ‘n algemeen erkende beginsel van die Suid-Afrikaanse gemenereg dat ‘n individu vry is om sy of haar sake so te reël ten einde die mees gunstige belastingbehandeling te geniet. Hierdie navorsing stel hierdie stelling op die toets in die sin dat die beperkings wat belasting teenvermydingsmaatreëls, en die verskeie vereistes daarvan, op die vrye gebruik van ‘n individue se rykdomskeppings- en beskermingsvermoë stel, deurlopend inbreuk maak op die bogenoemde reg. Die resultate is die beperking op ‘n individue se reg om sy of haar eiendomsbevoegdhede, soos wat dit vervat is in sy of haar regsbeskermbare belang, te geniet.

Die eerste aksiepunt was om vas te stel, in hoofstuk 2, of ‘n individu se belang in die skep en beskerming van sy of haar rykdom, wel regsbeskerming kan geniet. Eers sodra dit vasgestel was, kon die kriteria van die belasting teenvermydingsmaatreëls soos wat dit verband hou met hierdie belang wat in hoofstuk 2 geïdentifiseer is, vasgestel word. Uiteindelik het hoofstuk 4 voortgeset om twee feitestelle te gebruik om die teorië van hoofstuk 2 en 3 te toets.

4 Inland Revenue Commissioners v Duke of Westminster 1936 A.C. 1; CSARS v NWK Ltd 2010 ZASCA para 168; Kilburn v Estate Kilburn 1931 AD; Commissioner for Inland Revenue v Conhage (Pty) Ltd 61 SATC para 391.
5 Section 80A – L of the ITA.
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<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tr>
<td>THRHR</td>
<td>Tydskrif vir Hedendaagse Romeins-Hollandse Reg</td>
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<tr>
<td>CILSA</td>
<td>Comparative and International Law Journal of Southern Africa</td>
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<tr>
<td>GAAR</td>
<td>General Anti-avoidance Rules (as it is referred to in the Income Tax Act)</td>
</tr>
<tr>
<td>LAWSA</td>
<td>The Law of South Africa</td>
</tr>
<tr>
<td>ITA</td>
<td>Income Tax Act 58 of 1962</td>
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<td>SA MERC LJ</td>
<td>South African Mercantile Law Journal</td>
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Chapter 1 Introduction and problem statement

1.1 Problem statement

A well-known principle, originally set down in the case of *Inland Revenue Commissioners v Duke of Westminster* 1936 A.C. 1 (hereinafter the Westminster-case), and once again confirmed in *CSARS v NWK Ltd* 2010 ZASCA 168 (hereinafter the NWK-case), is that there is nothing wrong with arranging one’s affairs in a manner to avoid some or other liability or to gain some or other advantage. Tax avoidance, being the legal utilisation of tax systems, is exactly that. However, the legislator addressed this very issue once again, with the introduction of new general anti-avoidance rules (hereinafter GAAR) into the *Income Tax Act* 58 of 1962 (hereafter the ITA) in 2006.6

In terms of section 80A of the ITA a tax avoidance arrangement will be regarded as being impermissible if that arrangement was made with the sole or main purpose of obtaining a tax benefit8 and the nature of the arrangement differs from that of a normal, day-to-day business transaction9 with commercial substance.10 An arrangement would further be impermissible if it creates rights and obligations that would not normally be created, were it not for the tax arrangement.

Therefore, tax avoidance is legal on the one hand, but impermissible on the other hand if it is firstly primarily aimed at reducing a taxpayers’ tax liability;11 and secondly is carried out of the normal course of business.

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6 The first GAAR was in terms of Section 90 of the previous Income Tax Act 31 of 1941. This was replaced in the new ITA with Section 103(1), which was the predecessor to the current GAAR contained in Section 80A-L of the ITA.
7 Revenue Laws Amendment Act 20 of 2006.
8 Section 80A states that “An avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit”.
9 Section 80A(a)(i). “…out by means or in a manner which would not normally be employed for bona fide business purpose...”.
10 Section 80A(a)(ii). “…it lacks commercial substance, in whole or in part...”.
11 *Income Tax Case No 1113 1967* 30 SATC 8(C); *Income Tax Case No 1178 1972* 35 SATC 29(C); *Secretary for Inland Revenue v Gallagher* 1978 3 All SA 1 (A); *Secretary for Inland Revenue v Geustyn, Forsyth & Joubert* 1971 3 SA 540 (a); *Hicklin v Secretary for Inland Revenue* 1980 1 All SA 301 (A).
An argument stands to be made that an arrangement cannot be impermissible on the basis that its primary goal is saving taxes, if the savings created through that arrangement forms part of a comprehensive and holistic financial or estate plan. This is evident in the fact that a primary objective of estate planning – as a key aspect in a holistic financial plan – is to legally minimise a variety of taxes, including capital gains tax, donations tax and estate duty that may arise upon the demise of an estate owner.12

An arrangement that forms part of such an elaborate, legally structured estate plan, with the objective of protecting an individual’s wealth and optimise other business and investment opportunities can then also be classified as being in the normal course of business. Every individual has an interest in creating and preserving his or her wealth, firstly for future generations; and secondly, to facilitate optimal business growth and enjoyment during his or her lifetime.13 The author is of the opinion, and will refer to it in more detail in chapter 2, that careful and legal estate planning, built around full-disclosure and transparent tax planning, should be considered as a legally protectable interest.

If the above submission is acknowledged, any limitation to protect this right by legislation may be regarded as being a direct infringement of a protectable interest in wealth preservation.

In pursuance of this argument, the research will firstly set out to define and consequently classify the characteristics of a legally protectable interest. The principles of how this accepted legal concept applies to other areas of the law – such as the Law of Insurance14 – will then be applied to the interest an individual has in preserving his or her wealth.

A comprehensive literature study of primary sources such as legislation and secondary sources such as case law, will aim to determine whether there are any

13 Chapter 2 will expand on the nature of this inherent interest.
14 Reinecke et al General Principles of Insurance Law 49.
merits to the argument that the interest an individual has in wealth creation and preservation, should be regarded as a legally protectable interest in terms of South African Law.

Secondly, before any conclusions can be drawn with regards to anti-avoidance tax legislation and a possible infringement against a legally protectable interest, this research will undertake to understand what the substance of section 80A-L of the ITA is. In this endeavour, research will be conducted to identify the characteristics of section 80A of the ITA, which replaced section 103(1) of the ITA, which previously regulated the matter.

Finally, as an illustration to what the expected outcome of the research will be, a number of estate planning tools will be set out, clearly indicating how the primary objective is pure tax savings. The effect of the infringement of an individual’s subjective right to the creation and preservation of his or her combined wealth, may be found to result in the misuse and abuse of the ITA in an attempt to forcibly enjoy this subjective right. Where the enjoyment of an individual’s subjective right is in direct contradiction with a statutory provision, such as the GAAR, it is inevitable that one of the interests will bow down to the other. In the case of the subjective right, by means of a limited enjoyment thereof; and in the case of the application of the GAAR, by means of a possible misuse of the ITA. Where the subjective right to the creation and preservation of an individual’s combined wealth is acknowledged, the need to disguise these arrangements in a way as to avoid any contravention of section 80A of the ITA, will be negated.

### 1.2 Research question

The primary research question which lead to the undertaking of this research was: What is the effect of the GAAR in sections 80A-L of the ITA on the protection of a legal interest in wealth creation and preservation?

However, in order to answer the primary research question, a number of secondary questions was formulated:
• What requirements or characteristics must an individual’s interest in the creation and protection of his or her wealth comply with in order to receive recognition as an interest which is worthy of the enjoyment of legal protection?

• Why will an individual seek legal protection for his interest in his wealth, if the components which makes up the collective of his wealth already enjoys legal protection?

• What is the legal basis, structure and qualities of GAAR as it is set out in the ITA?

• Will the object of creation and preservation of an individual’s wealth in a holistic attempt to secure family financial security across generations, suffice as a bona fide (business) purpose as envisioned by Section 80A of the ITA?

• Will an arrangement which has its sole purpose to receive a tax benefit be regarded as a permissible avoidance arrangement, if it can be shown that such tax benefit, itself, forms part of the furtherance of the wealth creator’s object of growing and expanding his family’s wealth and financial security?

1.3 Research methodology

The research method conducted in the fulfilment of this research will be based on a literature study. In classifying the nature of a protectable legal interest, specific attention will be given to common law principles, academic articles, textbooks and case law. Furthermore, principles of other disciplines of the law, where this right is recognised, will be drawn and applied to this research and estate law in the broader sense.

Studying the merits and legal basis of the general anti-avoidance tax provisions will mainly be based on primary legislation, the legislator’s memorandum’s, industry debates and the application thereof by the Commissioner of Revenue in relevant case law.
1.4 Framework of the study

Chapter 2 will research different spheres of the South African law, such as the Law of Insurance and the Matrimonial Property Law in an attempt to position the interest that an individual has in the creation and preservation of his or her wealth. However, particular focus will be placed on the Doctrine of Subjective Rights to find legal protection for the interest identified.

Chapter 3 will attempt to provide insights into the fundamental principles of anti-avoidance tax legislation as it is reflected in the ITA. From a tax and estate planning perspective, this research will highlight the pitfalls of the tainted elements of the current GAAR, in order to allow estate planners to steer clear from impermissible tax avoidance arrangements.

With Chapter 2 and 3 setting the tone for both halves of the research question, the final endeavour will be to determine what the effect of the findings in Chapter 3, concerning the GAAR on Chapter 2’s recognised legally protectable interest is. The best way in which to determine this, will be by means of two case studies. As a result, Chapter 4 will present two case studies, the first where the primary objective of the wealth creator is to transfer wealth across generations; and the second where the primary goal of the arrangement is tax savings, but with the idea to grow the estate owners’ wealth with the funds saved on tax.

Chapter 5 will conclude the findings of the research, presenting an answer to the research questions posed.
Chapter 2 Classification of a legally protectable interest and its application to the concept of wealth preservation

2.1 Classification of a legally protectable interest

2.1.1 Introduction

In order to determine whether there are any merits in an argument which begs the recognition of an individual’s interest in his or her generation and protection of his or her wealth, it is important to first place the possibility of such a right, into the context of our legal system. As with the recognition of any legal interest, the primary aim of such recognition will be to facilitate the grounds for protection against infringement of such an interest.

In setting the tone for his research into the existence of subjective rights, Joubert\textsuperscript{15} words it perfectly:

\begin{quote}
Immers, dat die reg nie slegs uit norme bestaan nie, maar dat die mens, die regsubjek, inderdaad ook regte teenoor ander persone besit, spreek nie net uit die ingeboore regsgevoel nie maar uit die hele geskiedenis van die reg en uit die stryd van die mens om teenoor sy medemens, die staat e.d.m. te handhaaf wat hom volgens Goddellite beskikking regtens toekom.\textsuperscript{16}
\end{quote}

It speaks to the instinctive sense of justice, that is within every legal subject, to enjoy and exercise rights towards other legal subjects to protect those interests that legally vests in him. In the South African legal system these rights and responsibilities are dealt with within the private law branch of the substantive law.\textsuperscript{17}

This chapter sets out to answer the question as to what requirements or characteristics an individual’s interest in the creation and protection of his or her wealth must comply with in order to receive recognition as an interest which is

\textsuperscript{15} Joubert 1958 \textit{THRHR} 100.
\textsuperscript{16} It is indeed so that, the law does not only consist of norms, but that an individuial, the legal subject, also enjoys rights towards other persons, which does not only speak to a person’s inherent sense of justice, but also to the whole history of the law and the battle of people to maintain towards his fellow man what he is legally entitled to according to Devine disposition.
\textsuperscript{17} Horsten \textit{et al} \textit{Inleiding tot die Suid-Afrikaanse Reg en Regsleer} 285.
worthy of the enjoyment of legal protection.

Research into the legal recognition of an interest in an object required an investigation into the most obvious source where such an interest currently enjoys thorough legal protection – the Law of Insurance. However, as will be seen below, the motion of an insurable interest as a basis for the characteristics of any other legally protectable interest, was soon realized to be grossly misplaced. The insurable interest serves as the object of the contract of insurance, as opposed to an interest in another object.

The class of legally protectable interests that this research was tasked to find, looks at the interest that a legal subject has towards an object. This will be done by means of a thorough discussion into the Doctrine of Subjective Rights through its five categories.

Once the characteristics of a legally protectable interest as it is found in real rights, personality rights, personal rights, intellectual property rights and personal immaterial property rights, has been defined, these principles will be applied to an individual’s interest in the creation and preservation of his or her wealth. In order to fully understand what this interest, seeking legal protection, entails, the concept will be defined and positioned in the sphere of a holistic estate planning discipline.

2.1.2 Law of Insurance

The concept of a legally protectable interest is best described through the law of insurance with the object of insurance being that of an insured’s insurable interest. The principle of an insurable interest, as established in English law, was classically defined by Lord Eldon in *Lucena v Craufurd* (1806) 2 Bos & PNR 269 (HL) 302, as:

... a right in the property, or a right derivable out of some contract about the property, which in either case may be lost upon some contingency affecting the possession or enjoyment of the party.

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In essence, the above states that the English law requirements for an insurable interest involves an insured either having a legal right in property, or a liability connected to such property, exposed to loss or liability, at an uncertain event.19

The case of Macaura v Northern Assurance Co Ltd (1925) AC 619, clearly illustrated the abovementioned requirements of an insurable interest in the English law. The insured was the majority shareholder and primary creditor of a private company, trading in timber. As such, he insured the company assets in his own name. When he eventually needed to claim against the insurance, they rejected the claim due to a lack of insurable interest.

Lord Buckmaster,20 presiding over this case, held that as shareholder and creditor, the insured was merely entitled to the profits of the company and the surplus assets on distribution in the event of the winding up of the company.21 He continued, that as a shareholder, the insured had no right to any definable asset of the company and that any equation to determine the effect of any loss of a specific asset to the value of this shareholding, will be impractical. Lord Sumner reiterated22 these statements and summarized by saying that neither the debt, nor the shares was exposed to the fire and based on the requirements of an insurable interest, he had no right or equitable interest in the timber itself. It was held that a shareholder of a company does not have any insurable interest in the assets held by a company.23

Adapted from the above, the South African law did not follow the above two requirements and instead defined the concept of an insurable interest for the first time in Littlejohn v Norwich Union Fire Insurance Society (1905) TH 374 (hereinafter the Littlejohn-case). In the Littlejohn-case, Mr Littlejohn had taken out insurance over property, which was in fact owned by his wife, Mrs Littlejohn, to whom he was married out of community of property. After a fire destroyed the property, which the couple used in the operation of their business, the insurance company rejected

19 Reinecke et al General Principles of Insurance Law 37.
20 Macaura v Northern Assurance Co Ltd (1925) AC 619.
22 Reinecke et al General Principles of Insurance Law 37.
the claim for the replacement of the property insured, on the basis of (amongst other issues) a lack of insurable interest by Mr Littlejohn as he was not the owner of the property insured.\textsuperscript{24}

Although the assets held by the business was owned by Mrs Littlejohn, in her separate out of community of property estate, the reality was that she was not actively involved in the operations of the business. Mr Littlejohn was the general manager and was fully responsible for the operation and success of the business. The profits earned from the business was put towards the living costs of the communal household.\textsuperscript{25}

After referring to a number of cases, both locally and abroad, Judge Wessels stated\textsuperscript{26} that in answering the question of insurable interest, he had to ask himself the question as to whether Mr Littlejohn was in a worse position after his wife’s insured property was lost in the fire and whether that had caused him to suffer a loss. Furthermore, the fact that the profits of the business operations was used towards Mr and Mrs Littlejohn’s joint household, confirmed that it was in Mr Littlejohn’s interest that the property insured be replaced exactly as it was before the fire. In summary, Mr Littlejohn had an interest in the preservation of the property because he had the benefit of its existence and was prejudiced by its destruction.\textsuperscript{27}

It stands that an insurable interest – as a legally protectable interest – will exist where an individual has an interest in property, which will cause him economic loss in the event of the destruction of such property. In Judge Wessel’s words:\textsuperscript{28}

\begin{quote}
If an insurer can show that he stands to lose something of an appreciable commercial value by the destruction of the thing insured, then even though he has neither a jus in re nor a jus ad rem to the thing insured his interest will be an insurable one.
\end{quote}

\textsuperscript{24} Littlejohn v Norwich Union Fire Insurance Society (1905) TH para 375.
\textsuperscript{25} Littlejohn v Norwich Union Fire Insurance Society (1905) TH para 378.
\textsuperscript{26} Littlejohn v Norwich Union Fire Insurance Society (1905) TH para 381.
\textsuperscript{27} Littlejohn v Norwich Union Fire Insurance Society (1905) TH para 381.
\textsuperscript{28} Littlejohn v Norwich Union Fire Insurance Society (1905) TH para 380.
However, in terms of the Law of Insurance, the concept of a legally protectable interest is the object of the contract of insurance,29 as opposed to the object itself, being the legally protectable interest. The interest that an insured hold in the property insured, does not – for purposes of the Law of Insurance and as such the recognition of an insurable interest – exist automatically, as with subjective rights. It is simply the basis of a contract of insurance.30

Whether the interest the individual has towards the protection and preservation of property can also fall within one of the categories of a subjective rights,31 as will be seen below, is a question on its own. An insurable interest is not defined as a legally protectable interest which exists apart from the contract of insurance.

In searching for legal requirements that may define an interest that an individual has in the protection and creation of his or her wealth, it has become apparent that the qualities of an insurable interest, as the object of the contract of insurance is unique to the Law of Insurance and cannot easily be applied in vacuum to the question at hand. However, the fundamental concept confirmed in the Littlejohn-case32, that an individual has an interest in the preservation of the property when he benefits from its existence and can be prejudiced by its destruction, confirms that our law recognizes the protectability of interests in property when it holds economic value to the holder of the interest.

Taking this basic understanding forward, in an attempt to find principles in the South African law which may accommodate the idea of a legally protectable interest in the creation and preservation of wealth, further research into the nature of subjective rights is warranted.

2.1.3 The nature of subjective rights

Subjective rights come into existence when the law acknowledges individual

30 Castellain v Preston (1883) 11 QBD 380 (CA) 397; Reinecke, Van Niekerk, Nienaber LAWSA 28.
32 Littlejohn v Norwich Union Fire Insurance Society (1905) TH 374 para 381.
interests, worthy of legal protection, which already factually exists before such legal recognition occurs.³³ As a result, a subjective right only comes into existence once the law recognises an interest worthy of protection.³⁴ Joubert³⁵ defines a subjective right as the recognition of a fundamental occurrence in the reality of the law.

As times change, so does socio economic circumstances and the needs of individuals to enjoy legal protection in relation to different legal objects come to life. A common example used by scholars³⁶ is the recognition of a right to privacy which was identified as a result of the increasing technological developments. Knobel³⁷ explains it perfectly when he states that new threats to old interests proved to be a catalyst for the recognition and protection of interests in the form of subjective rights.

However, as these needs for legal recognition of an already existing interest arise, the interest in question should be put to the test before it can be defined as a legal object in relation to the doctrine of subjective rights. The interest at hand must exhibit two qualities: Firstly, the object must be of value or use to the holder of the right in the sense that it fulfils a need of the legal subject.³⁸ In this instance Neethling differed from Joubert who was of the opinion that the object had to be of economic value.³⁹ This position⁴⁰ against the latter scholar’s statement is supported, since not all subjective rights in existence, such as personality rights, will have an economic value.

The second quality that an object must display in order to qualify as a legal object to which a subjective right can be acknowledged, is that it must be sufficiently independent in the sense that it should be capable of use, enjoyment and disposal⁴¹ in an existence separate from the legal subject seeking protection. Once an

³³ Neethling and Potgieter Neethling-Potgieter-Visser Deliktereg 55.
³⁴ Knobel 2001 THRHR 575.
³⁵ Joubert 1958 THRHR 98.
³⁶ Neethling and Potgieter Neethling-Potgieter-Visser Deliktereg 55; Knobel 2001 THRHR 575.
³⁷ Knobel 2001 THRHR 575.
³⁸ Neethling and Potgieter Neethling-Potgieter-Visser Deliktereg 56.
³⁹ Joubert 1958 THRHR 112.
⁴¹ Knobel 2001 THRHR 576.
individual’s interest in an object has been qualified as a subjective right by means of the abovementioned qualities being present, a mere individual interest has been recognised as a legally protectable object. As a result, the Doctrine of Subjective Rights can be applied.

2.1.4 The Doctrine of Subjective Rights

2.1.4.1 Introduction into the Doctrine of Subjective Rights

The Doctrine of Subjective Rights suggests that legal subjects are holders of subjective rights to something – being the legal object – which right is enforceable against other legal subjects.

Knobel further explains the doctrine as one which encompasses two interdependent relationships. The first being the relationship between the legal subject (the holder of the right) and the legal object. This relationship defines the contents of the legal subject’s right towards the legal object – being the right of disposal, use and enjoyment.

The second relationship which the doctrine is based on, is the relationship between the legal subject (the holder of the right) and other people (other legal subjects). This relationship infers the right that the holder of the right must enforce his or her powers over other legal subjects. The infringement of a subjective right constitutes delictual wrongfulness, protectable by the remedies of the Law of Delict.

Subjective rights are classically divided into five categories, based on the legal object in question, being (a) real rights; (b) personality rights; (c) personal rights;

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42 Neethling and Potgieter Neethling-Potgieter-Visser Deliktereg 56.
43 Knobel 2001 THRHR 574.
44 Knobel 2001 THRHR 574.
45 Joubert 1958 THRHR 111.
46 Knobel 2001 THRHR 574.
(d) intellectual property rights and finally (e) personal immaterial property rights.\textsuperscript{49}

In the interest of identifying either the existence of an existing subjective right, seeking recognition, or to propose a new subjective right, and furthermore in order to fully understand the characteristics of those subjective rights that already enjoy legal protection, the abovementioned categories of subjective rights demand further examination.\textsuperscript{50}

2.1.4.2 Real rights

The writer is of the opinion that WA Joubert can be seen as the forefather of the Doctrine of Subjective Rights in South Africa as his research into the classification of subjective rights formed the basis for every scholar thereafter and still forms part of our courts’ reference material to this day. In his own words,\textsuperscript{51} real rights as a category of subjective rights is as old as the Roman Dutch Law itself and very little needs to be said to prove same.

Pienaar defines a real right as a claim that a legal subject has to a thing as enforced against other persons.\textsuperscript{52} This definition illustrates the dual relationship that has been shown above to be present in a subjective right. The Doctrine of Subjective Rights dictates that there will always be a subject-object relationship and a subject-subject relationship.\textsuperscript{53}

As far as it pertains to real rights as a category of subjective rights, the subject-object relationship can be found in the entitlements of ownership, which – while impossible to compile an exhaustive list – confers the powers that the owner of property has in relation to that object.\textsuperscript{54} These entitlements include the entitlement to use the thing (\textit{ius utendi}); the entitlement to dispose of a thing (\textit{ius disponendi});

\textsuperscript{49} Neethling 1987 \textit{THRHR} 316.
\textsuperscript{50} Joubert 1958 \textit{THRHR} 113.
\textsuperscript{51} Joubert 1958 \textit{THRHR} 113.
\textsuperscript{52} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} 47.
\textsuperscript{53} Joubert 1958 \textit{THRHR} 110.
\textsuperscript{54} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} 92.
and the entitlement to claim a thing back from an unlawful possessor (\textit{ius vindicandi}),\textsuperscript{55} to name a few.

With regards to the subject-subject relationship, a real right receives its protection with regards to other legal subjects, in the case of movable property, by means of delivery,\textsuperscript{56} or by means of registration in the Deeds Office, in the case of immovable property.\textsuperscript{57} Registration of a real right at the Deeds Office, provides a public record of real rights and as stated \textit{in Cape Explosive Works Ltd v Denel (Pty) Ltd} 1999 (2) SA 419 (T), once a real right has been created (registered) it is maintainable against the whole world.\textsuperscript{58}

For purposes of subtracting qualifying requirements for the application to other areas of law, it is notable that a real right as a category of subjective rights, requires registration of the right to immovable property at the Deeds Office; and one of the recognised forms of delivery in the case of movable property.

2.1.4.3 Personality rights

Personality rights as a category of subjective rights, differ from the other, recognised categories such as real rights, personal rights and immaterial property rights, in that it is non-patrimonial in nature.\textsuperscript{59} In his comparative overview of personality rights, Neethling\textsuperscript{60} notes that there is general consensus that personality rights are by nature non-patrimonial and cannot exist independently of a person since they are inseparable from an individual’s personality. As a result, an individual is said to hold personality interests at birth and that they are consequently terminated at death.\textsuperscript{61}

South African Common Law recognises three personality interests, namely bodily integrity (\textit{corpus}), dignity (\textit{dignitas}) and a person’s good name (\textit{fama}).\textsuperscript{62} It is

\begin{itemize}
\item \textsuperscript{55} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} para 93.
\item \textsuperscript{56} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} para 73.
\item \textsuperscript{57} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} para 65.
\item \textsuperscript{58} \textit{Cape Explosive Works Ltd v Denel (Pty) Ltd} 1999 (2) SA 419 (T).
\item \textsuperscript{59} Neethling \textit{et al} Neethling’s \textit{Law of Personality} 13.
\item \textsuperscript{60} Neethling 2005 \textit{CILSA} 223.
\item \textsuperscript{61} Neethling \textit{et al} Neethling’s \textit{Law of Personality} 15.
\item \textsuperscript{62} Loubser \textit{et al} Deliktereg \textit{in Suid-Afrika} 54.
\end{itemize}
submitted that these legal interests serve as the object of an individual’s subjective right in terms of the Doctrine of Subjective Rights, thereby creating the subject-object relationship. The subject-subject relationship is enforced on the basis that any infringement on an individual’s legally protectable personality interests constitutes an *injuria* which is actionable in the Law of Delict.\(^63\)

2.1.4.4 Personal rights

Personal rights refer to the performance by another on the strength of a legal obligation *ex contractu*, *ex delicto*, or from other sources.\(^64\) Research in an attempt to understand the characteristics and the legal nature of a personal right proved clearly that, jurists cannot help themselves but to refer to the differentiation between real rights and personal rights, in order to understand personal rights as such.\(^65\) It is submitted that a comparative study on the difference between real rights and personal rights (both categories of subjective rights), does perhaps prove to provide the best understanding of the nature of personal rights.

In his critical comments on the topic, Sonnekus\(^66\) gave an accurate summary, stating that the difference between a real right and a personal right lies in the different nature of the objects of the rights. This is in line with an earlier submission that subjective rights are classically divided into five categories, based on the legal object in question.\(^67\)

A real right is a right to tangible property, while a personal right is a right to performance from a specific person.\(^68\) Sonnekus uses the example of a right that a legal subject has towards another person to perform to a certain extent, for instance to deliver a horse (*ex contractu*). This constitutes a personal right to performance,

\(^{63}\) Loubser *et al* Deliktereg in Suid-Afrika 54.
\(^{64}\) Knobel 2001 *THRHR* 575.
\(^{67}\) Universiteit van Pretoria v Tommie Meyer Films (Edms) Bpk 1997 4 SA 376 (T) para 387.
irrespective of the fact that the performance comes in the form of tangible property (the horse).\textsuperscript{69}

As a second element to the differentiation, Sonnekus refers to the origin of the right to the object seeking legal protection.\textsuperscript{70} Real rights are acquired either by means of an original acquisition of the real right, or by means of a derivative acquisition of the real right.\textsuperscript{71} Personal rights find their objects to originate \textit{ex contractu, ex delicto} or from other sources.\textsuperscript{72}

At this point the distinction between real rights and personal rights – however valuable – is no longer necessary. However, the application of these principles to the Law of Matrimonial property may prove valuable, in an attempt to move closer to the type of personal rights that applies to the question this dissertation will answer.

An exhaustive discussion on the Law of Matrimonial property and its patrimonial consequences will be of little value for the purposes of this research. However, as a practical example of an interest an individual may have in his or her wealth, or that of their spouse, a brief note will be made on the patrimonial consequences of a marriage out of community of property, with the application of the accrual system.

It is accepted that spouses who wish to be married out of community of property, will enter into a valid antenuptial contract in terms of which they specify the matrimonial property system, i.e. with or without the application of the accrual system.\textsuperscript{73}

During the marriage, the marriage is out of community of property and out of community of profit and loss, whereby each spouse retains full ownership and

\textsuperscript{69} Sonnekus 1991 \textit{The Journal of South African Law} 179.
\textsuperscript{71} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} 72.
\textsuperscript{73} Heaton \textit{The Law of Divorce and Dissolution of Life Partnerships in South Africa} 60.
control of his or her own estate, but on divorce or death the spouses share in the growth that their respective estates has shown.\textsuperscript{74}

The accrual of a spouse’s estate is the amount by which the net value of his or her estate at the dissolution of the marriage, exceeds the value of his or her estate at the commencement of the marriage.\textsuperscript{75} Each spouse’s accrual value then gets adjusted by the Consumer Price Index.\textsuperscript{76}

The spouse with the smaller accrual, then holds a personal right to 50\% (or whatever percentage agreed to in the antenuptial contract) of the value of the difference between the larger and smaller accruals, against the spouse with the larger accrual.\textsuperscript{77}

The personal right in this context is accepted on the premise that a legal subject (spouse A) holds a right to the accrual of the estate (legal object) of another legal subject (spouse B), the object which finds its origin in the form of the legally registered antenuptial contract \textit{(ex contractu)}.

However, it is crucial to note that this personal right only comes into existence on death or divorce, as the spouses retain their full, separate estates up until dissolution of the marriage. It is submitted that, where an individual holds an interest in a future right – being the possible accrual of another’s estate at the dissolution of a legally recognised relationship (marriage), that such a right cannot be considered a subjective right in the form of a personal right as one of the qualities of a subjective right is that the right must already be in existence,\textsuperscript{78} as opposed to an expectation to a right.

However, it begs the question whether the expectation of a future legally protectable interest in a personal right, does not create an interest in the status quo, its risks and opportunities? In other words, if an individual’s expectation to a

\begin{itemize}
\item\textsuperscript{74} Heaton \textit{The Law of Divorce and Dissolution of Life Partnerships in South Africa} 64.
\item\textsuperscript{75} Section 4(1)(a) of the \textit{Matrimonial Property Act} 88 of 1984.
\item\textsuperscript{76} Section 4(1)(b)(iii) of the \textit{Matrimonial Property Act} 88 of 1984.
\item\textsuperscript{77} Vorster Koers \textit{Bulletin vir Christelike Wetenskap} 360.
\item\textsuperscript{78} Neethling and Potgieter \textit{Neethling-Potgieter-Visser Deliktereg} 55.
\end{itemize}
personal right, the value of which can be influenced (grown or depleted) by external events (risks), such an individual may have an interest of another nature, in the sustainability of the estate of his or her spouse in the above example, during the subsistence of their marriage.

2.1.4.5 Intellectual property rights

Intellectual property rights as a category of subjective rights refers to the legal subject, who holds a right to the objects of his mind, which rights is enforceable towards other legal subjects. The best way in which to further elaborate on this category of subjective rights is to focus this discussion on one type of intellectual property, a trade secret.

A trade secret as a protectable interest is a distinct type of intellectual property right. As part of the Law of Competition, it enjoys common law protection instead of the statutory protection afforded to its counterparts, which are protected under Copyright law, Trademarks and the Law of Patents.

In the case of Motion Transfer and Precision Roll Grinding CC v Carsten and Another 1998 4 All SA 168 (N) 9 the requirements that qualify a piece of information as a trade secret, were confirmed, as originally set out by Van Heerden and Neethling. Firstly, the information must be capable of application in trade or industry. Secondly, the information must be secret and confidential. And finally, the information at hand must be of economic value to its owner.

Testing information against the requirements of a trade secret is crucial in order to differentiate between a legally protectable interest, confined within the sphere of intellectual property rights on the one hand and general information in public domain on the other hand. As a result, a better understanding of the difference

79 Knobel 2001 THRHR 575.
81 Copyright Act 98 of 1978.
82 Trademarks Act 194 of 1993.
83 Patents Act 57 of 1978.
84 Van Heerden and Neethling Unlawful Competition 225.
between the elements of the nature of rights that are capable of legal protection and those that are not, are called for.

In his definition compiled in his comparative research through sources in the American law, German law and the South African law, Knobel\textsuperscript{86} defined a legally protectable trade secret as information, which the owner has the will to keep secret, which has commercial or industrial application, has an economic value and is concrete enough to enjoy an existence separate from its owner.

The requirement that, for information to be considered a legally protectable trade secret, it should be concrete enough to enjoy an existence separate from its owner, is perhaps inclusive of the requirement of commercial application. It is submitted that in order for information to find application in commercial or industrial uses, it should be capable of a physical existence separate from its owner, be it in writing, a plan, a program, etc.\textsuperscript{87}

For the purposes of this research, the basis of the requirements of the test for legal protection of a trade secret will be examined in order to draw possible similarities, or a lack thereof, to an individual's wealth to determine whether an interest in wealth preservation should enjoy legal protection.

Having secrecy or confidentiality of information as a first requirement\textsuperscript{88} for the classification of a protectable trade secret is easily the most obvious of tests to be applied. Van der Merwe\textsuperscript{89} defines the secrecy requirement as meaning that the information in question falls under the control of its owner and is only known to the owner or a limited number of other persons (such as employees) with the owner's knowledge and consent.\textsuperscript{90}

\textsuperscript{86} Knobel \textit{The Right to the Trade Secret} 288.
\textsuperscript{87} Knobel \textit{The Right to the Trade Secret} 186.
\textsuperscript{88} Van Heerden and Neethling \textit{Unlawful Competition} 225.
\textsuperscript{89} Van der Merwe \textit{et al Law of Intellectual Property in South Africa} 62.
\textsuperscript{90} \textit{Atlas Organic Fertilizers v Pikkewyn Ghwano & Others} 1981 (2) SA 173 (SC) para 139; Van Heerden and Neethling \textit{Unlawful Competition} 225.
Furthermore, it is submitted that simply because the owner of the information, seeking legal protection of a trade secret, invested time and effort in the development and considers the information at hand to be a secret, it does not mean that information which already forms part of public knowledge can also enjoy legal protection as a trade secret.\textsuperscript{91} In the \textit{Atlas Organic Fertilizers} (2) SA 173 (SC) (hereinafter the \textit{Atlas Organic Fertilizer}-case), the court confirmed that information which seeks protection should differ from what was previously, generally known.

However, for purposes of this research and in an attempt to apply the requirement of secrecy to other applications in the law, further focus will be placed on the owner of the information’s actions towards protecting his subjective right to his trade secret. In the \textit{Atlas Organic Fertilizer}-case when faced with the question regarding the secrecy requirement of the trade secret, the learned Judge Van Dijkhorst referred\textsuperscript{92} to the absence of proof that the production sequence (information seeking protection as a trade secret) was kept secret or limited to certain employees only.

This speaks to the active measures that had to be taken by the owner of the information, to protect it on the grounds of a recognisable trade secret. Knobel\textsuperscript{93} is of the opinion that the lengths that the owner of valuable information will go to, to protect the method in the applicable trade, gives an idea of the perceived value of trade secrets in the commercial world. Knobel\textsuperscript{94} deems the owner’s will to protect the secret at hand crucial to the extent that where the owner does not display a will to keep information a secret, it is not worthy of legal protection.

South African case law on the fulfilment of the second requirement that information seeking legal protection as a trade secret should have a commercial or industrial application – which may include an existence separate from its owner – is scarce.

 Plenty of case law, such as the \textit{Motion Transfer}-case and \textit{Townsend Productions (Pty) Ltd v Leech and others} 2001 2 All SA 255 (C) refer to the definition of a trade

\begin{flushleft}
\textsuperscript{91} Atlas Organic Fertilizers v Pikkewyn Ggwano & Others 1981 (2) SA 173 (SC).
\textsuperscript{92} Atlas Organic Fertilizers-case para 139.
\textsuperscript{93} Knobel \textit{The Right to the Trade Secret} 1.
\textsuperscript{94} Knobel \textit{The Right to the Trade Secret} 185.
\end{flushleft}
secret, as formulated by Van Heerden\textsuperscript{95} to confirm that the requirement of commercial or industrial use of information, is not in dispute and as a result the court didn’t need to comment on same.

Panellists of the World Trade Organisation observed in a public forum held on 1 October 2013\textsuperscript{96} that trade secrets exist in the absence of law; and that trade secret protection is often used because patent protection is unavailable due to the unpatentable nature of the information in question.

If the requirement of the application of information, seeking legal protection as a trade secret, in trade and industry is accepted to be similar, if not the same, as the requirement specified in Section 25(1) of the Patents Act\textsuperscript{97} for an invention to qualify as a registerable patent, the rationale behind the requirement of the latter can also be applied to the requirement of a trade secret.

In relation to a patentable invention, Gerntholtz\textsuperscript{98} observed that an invention must have the ability to be put into practice or operation in a field where commodities of any kind are exchanged for money or other goods. Therefore, it is submitted that this requirement is closely related to the requirement of economic value as it pertains to a trade secret, which may loosely explain the courts’ reluctance to draw a distinct differentiation.

Knobel\textsuperscript{99} emphasises that the requirement that secret information should find application in trade and industry, should be formulated in terms of a potential to be applied, rather than an actual application. This then closely relates to the potential of information to be concrete enough to enjoy an existence separate from its owner. In other words, the information, which is to be protected, should have the potential to be presented in a concrete manner, be it in writing, a plan, a model etc., as it

\textsuperscript{95} Van Heerden \textit{Unlawful Competition} 225.
\textsuperscript{97} Patents Act 57 of 1978.
\textsuperscript{98} Gerntholtz \textit{Principles of South African Patent Law and a Comparative Reference to German Patent Law} 53.
\textsuperscript{99} Knobel \textit{The Right to the Trade Secret} 182.
should have a potential use in trade and industry. An undeveloped, vague concept in the mind of the maker, cannot enjoy protection if it cannot be reduced to physical form.\textsuperscript{100}

In answering the question whether a specific piece of information has a specific economic value to its owner, in order to determine as a third requirement, whether it can qualify as a trade secret, Van Heerden and Neethling\textsuperscript{101} indicated two factors to consider.

Firstly, the information must have the potential to be, or actually be, of use to a rival.\textsuperscript{102} In the case of \textit{Coolair Ventilator Co (SA) (Pty) Ltd v Liebenberg and Another} 1967 2 All SA 125 (W) (hereinafter the \textit{Coolair Ventilator}-case) the information was considered confidential information as the substance of the act which lead to the potential damages to the owner of the information was two-fold. Firstly, the employee who leaked the information to the rival, realised how valuable the information will be for the rival, and secondly shared that information with the express intention to harm the owner of the confidential information.\textsuperscript{103} This speaks to a patrimonial loss to the owner of the information, and as a result qualifies as information with an economic value.

Neethling’s second factor to consider for information to qualify as a trade secret, is the work, skill and time that were needed to produce the trade secret in question.\textsuperscript{104} If the economic value of the information that needs protection is substantiated in the time and cost that has been spent in developing information that is worthy of legal protection. In the case of \textit{Northern Office Micro Computers (Pty) Ltd and Others v Rosenstein} 1981 4 All SA 509 (C) 524., the court found that if a person (the Respondent in this case) was permitted to simply copy information that took the owner thereof time, work and skill to develop, it will unfairly nullify the advantage that the owner had over its competitors. The court furthermore referred

\textsuperscript{100} Knobel \textit{The Right to the Trade Secret} 186

\textsuperscript{101} Neethling \textit{et al Unlawful Competition} para 266.

\textsuperscript{102} \textit{Coolair Ventilator Co (SA) (Pty) Ltd v Liebenberg and Another} 1967 2 All SA 125 (W).

\textsuperscript{103} \textit{Coolair Ventilator}-case 31.

\textsuperscript{104} \textit{Northern Office Micro Computers (Pty) Ltd and Others v Rosenstein} 1981 4 All SA 509 (C) 524.
to case law which confirmed that the maker of a document used his or her brain power to produce a wanted result which can only be produced by another who is willing to go through the same process and effort.\textsuperscript{105} It can therefore be submitted that information is considered eligible for legal protection on the basis of economic value, if that information is of equal value or use to another and if obtaining such value or use would have had a monetary cost – either in the form of funds, time or knowledge – associated to it.

2.1.4.6 Personal immaterial property rights

Personal immaterial property rights pertain to those intangible products of the human mind, which is closely linked to the personality traits of the owner of the right.\textsuperscript{106} Neethling\textsuperscript{107} proposed a further category of subjective rights on the basis that the Doctrine of Subjective rights is generally accepted and that there exist no limitations to the further development of the doctrine.\textsuperscript{108} In this instance, Potgieter\textsuperscript{109} notes that there is no reason why a new protection worthy legal object, or even a category, cannot be recognised within the scope of the Doctrine of Subjective rights.

It is on this basis that Neethling\textsuperscript{110} then continues to search for a category within the Doctrine that supports the subjective right to earning capacity and the right to creditworthiness. However, the limitation between the existing four categories were highlighted by Neethling, stating that the right to earning capacity and the right to creditworthiness, has qualities of more than one existing category.\textsuperscript{111}

An individual’s earning capacity is directly reliant on his or her personality traits, such as intelligence, expertise, health, personality, etc., while his creditworthiness shares a close relationship with his good name. However, an earning capacity also

\textsuperscript{105} Saltman Engineering Co Ltd v Campbell Engineering Co Ltd 1948 65 RPC 203 (CA).
\textsuperscript{106} Knobel 2001 \textit{THRHR} 575.
\textsuperscript{107} Neethling 1987 \textit{THRHR} 316.
\textsuperscript{108} Potgieter 1978 \textit{THRHR} 328.
\textsuperscript{109} Potgieter 1978 \textit{THRHR} 328.
\textsuperscript{110} Neethling 1987 \textit{THRHR} 317.
\textsuperscript{111} Neethling 1987 \textit{THRHR} 317.
encompasses qualities that are directly linked to tangible objects, such as tools, books, etc., while a person’s creditworthiness looks at an individual’s patrimonial assets. The result is the recognition of a category of legally protectable legal interest which consist of immaterial, intangible property, as the product of the human spirit and effort, with economical value.

2.1.5 Conclusion on subjective rights and the use thereof

The research into the qualities of subjective rights, the Doctrine of Subjective Rights and the categories of subjective rights has delivered satisfactory findings. It has been confirmed that a legal subject, seeking legal protection regarding an interest towards a legal object can be put to the test, as set out above, in order to determine if a subjective right exists.

Once it has been established that a subjective right exists, the task at hand is to place that right into the correct category of subjective rights in order to enjoy legal protection from that sphere of subjective rights. If no such suitable category exists, as was the case with Neethling’s right to earning capacity, further measures should be taken to determine if a new, further category can be defined.

2.2 Application of the characteristics of a legally protectable interest on an individual’s right to preserve his or her wealth

2.2.1 Positioning of the interest seeking legal recognition

The research conducted above confirmed the merits of the legal question at hand to the extent that further application of the legal principles of the private law to the problem statement, as set out in Chapter 1, is called for.

The first point of departure is to define the right seeking legal protection, being the right to the creation and preservation of one’s wealth. Once the nature of the interest seeking legal protection is fully understood, it will have to be put to the test

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112 Neethling 1987 THRHR 318.
113 Neethling 1987 THRHR 319.
of subjective rights. The outcome will determine whether the right in question can further be studied and categorized, or whether the interest seeking legal recognition requires further development before an application can be made.

What follows is an attempt to position the interest in the creation and preservation of an individual’s wealth within the context of the research at hand.

2.2.2 Positioning of an interest in wealth generation and protection

The Webster’s New Encyclopaedic Dictionary\textsuperscript{114} defines the word "wealth" as all property that has a money value or an exchangeable value. All property can be loosely defined as patrimonial rights and patrimonial objects.\textsuperscript{115} Patrimonial rights can then furthermore be distinguished as real rights, personal rights and immaterial property rights.\textsuperscript{116} It should be clear at this point that these patrimonial rights also constitute the categories of subjective rights.

It can therefore be drawn to understand that the concept of wealth serves as a collective noun which refers to a group or selection of all the categories of subjective rights. It is submitted that each of the assets which may form part of an individual’s wealth, be it immovable property, intellectual property, cash, shares and contractual rights to performance, already enjoys plenty recognition and protection in the South African law through the Doctrine of Subjective rights.

However, the concept of the collective of an individual’s patrimonial wealth is the object at hand when estate planning, including tax planning, is undertaken. The separate elements, or subjective rights, to an individual’s wealth cannot be seen in a vacuum as they are so closely interdependent as well as interconnected to the wealth creator’s non-patrimonial rights in the form of personality rights.

This leads to the question as to why an individual will seek legal protection for his interest in his wealth, if the components which makes up the collective of his wealth

\textsuperscript{114} Webster’s New Encyclopaedic Dictionary 1995.
\textsuperscript{115} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} 22.
\textsuperscript{116} Pienaar \textit{et al} Silberberg and Schoeman’s \textit{The Law of Property} 23.
already enjoys legal protection. The simple answer to this is that the risks and possible infringement that the wealth creator seeks to protect is not against the separate components of his wealth, such as his real rights, personal rights, etc., but rather against the creation and preservation of his collective wealth as one, inseparable object. The effect of wealth taxes, which is directly aimed at the recognised collective object, will be dealt with in more detail in chapter 3 of this dissertation.

As to why an individual has a natural, perhaps even primal, instinct to want to protect and expand his or her wealth, is perhaps a subject for another discipline of research. However, this inherent interest can possibly be traced in the psychology of investment sentiment in the form of greed and fear, the principles of capitalism and the natural instinct of the hunter-gatherer.

2.2.3 Implementation and purpose of a holistic approach to estate planning

From the above understanding of the concept of wealth, it can now be said that a key part of a wealth creator’s enjoyment and use of his wealth, in the broad sense, is to plan towards the optimisation and growth thereof, while catering to the protection thereof from an array of direct and indirect risks. This is done through estate planning.

Estate planning is a science in own right and entails far more movable elements than simply the writing of a will and the registration of a trust. In the words of William C Clay: "There is more to it than that".117

Meyerowitz118 defined estate planning as follows:

The arrangement, management and securement and disposition of a person’s estate so that he, his family and other beneficiaries may enjoy and continue to enjoy the maximum from his estate and his assets during his lifetime and after his death, no matter when death may occur.

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117 Davis et al Estate Planning 1-4.
From this definition several valuable points can be deducted. As a point of departure, it is worth noting the use of the word "arrangement" which will become crucial in chapter 3 of this dissertation when focus is placed on anti-avoidance tax legislation and its emphasis on the concept of an arrangement.

Furthermore, the above definition leaves no confusion as to the fact that estate planning is an active and precise activity and is not an accidental result of several different transactions or decisions. In their commentary on this subject, Judge Davis and his colleagues\textsuperscript{119} highlight that it is implicit within the definition that the planning occurs timeously and in an orderly fashion.

Finally, the maximum enjoyment of assets held by an individual, the wealth creator, for him and his descendants form the centre point in the concept of estate planning.

The objectives of a truly holistic estate plan will include the following:\textsuperscript{120}

(a) Commercial soundness in the sense that a wealth creator’s interests should be structured in a manner which allows the maximum growth of the assets, while adequately providing optimum protection against risks, which are unique to the client.

(b) The provision for adequate liquidity to the extent that the assets are not held in structures or vehicles which are extremely illiquid where the wealth creator (legal subject) cannot obtain access to cash on hand to cater to his, his family’s or his business’ income needs, both during his life and thereafter. Appropriate liquidity will include liquidity to pay taxes and see to the administration of the individual’s deceased estate as and when it becomes necessary.

(c) The estate plan should incorporate the principles of good governance to the extent that all of the compliance and paperwork are in order at any given moment. Transfer documentation, share certificates, last will and testaments,

\textsuperscript{119} Davis \textit{et al} Estate Planning 1-3.
\textsuperscript{120} Rabenowitz \textit{et al} The South African Financial Planning Handbook 2017 868; Davis \textit{et al} Estate Planning 1-5.
trust deeds, etc. should be easily obtainable to ease the transfer of wealth from one generation to another or from one vehicle to another.

(d) Flexibility to any structure or vehicle is crucial to ensure that a holistic estate plan remains dynamic in changing circumstances and thereby continue to provide the wealth creator and his successors with optimum use and enjoyment of their wealth.

(e) Minimising costs, which includes taxation, only constitutes one of the key objectives of a holistic estate plan. Minimising costs means more capital remains to grow an individual’s wealth and therefore is crucial to consider in any transaction or arrangement. However, without a comprehensive knowledge of the different wealth taxes, pure tax planning may end up costing the wealth creator more damage in the long run. Estate planning that is focussed on the minimisation of tax, will more often than not, fail in the broader sense of the objectives of estate planning.

Setting out the need for and scope of an holistic estate planning endeavour is particularly important for this research, especially as we move into chapter 3, to show firstly how estate planning is merely one of the competencies of the right to the creation and preservation of an individual’s wealth – if such right is proved to exist. Secondly, it is important to understand how estate planning, with a truly holistic goal in mind, which properly includes all the above objectives, is much more than simply tax planning.

2.2.4 Classification of an interest in wealth generation and protection as a subjective right

Before an interest that a legal subject already has in a legal object, but which is yet to be recognised as a legally protectable right can enjoy such recognition, the interest in question should qualify as a subjective right in terms of the Doctrine of Subjective rights.\textsuperscript{121}

\textsuperscript{121} Neethling and Potgieter *Neethling-Potgieter-Visser Deliktereg* 56.
The first quality that the object, being an individual’s interest in the creation and preservation of his collective wealth, must possess, is that it must hold value or use in the sense that it fulfils a need of the legal subject (the wealth creator).\textsuperscript{122} The disciplined use and growth of an individual’s wealth is primarily aimed at addressing and catering to every conceivable financial need of the wealth creator and his family. Elements that form part of this plan is taking personal factors, such as the individual’s age, health, available funds; lifestyle factor’s and lifestyle goals; financial objectives, such as being out of debt or retiring early; timeframes; and the decision-making framework into consideration.\textsuperscript{123}

With reference to the Law of Insurance, as thoroughly discussed above, and confirmed in the \textit{Littlejohn}-case,\textsuperscript{124} an individual has an interest in the preservation of property when he benefits from its existence and can be prejudiced by its destruction.

Furthermore, with regards to the earlier discussion on Matrimonial property law in the category of personal rights, it has been submitted that an individual’s personal right to the accrual of his or her spouse, shows a monetary interest. This interest, which a person may have in his or her own estate, or that of his or her spouse, may already exist long before the termination of the marriage and the creation of the personal right.

The qualities discussed with regards to intellectual property rights, with a specific focus on a trade secret alluded purposefully to the will an owner of information must have to keep his trade secret, a secret. This point is of great importance is it speaks to the wilful action of a legal subject to want to protect his or her legal interests. Estate planning with its main objective of planning towards expansion and protection of an individual’s wealth, has been said to be a timeous effort in an orderly fashion\textsuperscript{125} to achieve the objectives at hand. It does not simply happen and

\textsuperscript{122} Neethling and Potgieter \textit{Neethling-Potgieter-Visser Deliktereg} 56.
\textsuperscript{123} Rabenowitz \textit{et al} \textit{The South African Financial Planning Handbook} 2017 5.
\textsuperscript{124} \textit{Littlejohn}-case para 381.
\textsuperscript{125} Davis \textit{et al} \textit{Estate Planning} 1-3.
requires the wealth creator’s explicit direction and will to protect his interest in his wealth.

It is submitted that the interest an individual has in the growth and preservation of his wealth certainly includes the quality that it is of tremendous value and use to the wealth creator.

The second quality under scrutiny is whether the right at hand, seeking legal protection, can be sufficiently independent in the sense that it is capable of use, enjoyment and disposal.\textsuperscript{126} The very essence of estate planning as it pertains to the protection and preservation of an individual’s wealth is the transferability of the wealth to future generations. Van der Westhuizen\textsuperscript{127} defines estate planning as follows:

\[
\begin{align*}
\ldots \text{the decision in advance by an estate owner of what to do with his assets and liabilities during his lifetime and upon his death, how to do it, when to do it and who to do it.}
\end{align*}
\]

The use of trusts and companies and the registration of limited real rights, to name a few, constitute some of the methods used in a holistic estate plan which aims at the transfer of wealth both during the life of the wealth creator and thereafter.\textsuperscript{128} It can therefore be said that an individual’s interest in the creation and preservation of his or her wealth enjoys an existence separate from the holder of the right and can be enjoyed, used and disposed of independent of the wealth creator.

Now that it has been confirmed that an individual’s interest in the creation and preservation of his wealth constitutes a legally protectable interest in the form of a subjective right, the next step will be to place this subjective right within a category, alternatively propose a new category of subjective rights.

It has been confirmed that the concept of an individual’s wealth is a collective noun which refers to his interest in property, both corporal and incorporeal. This means that the creation and preservation of an individual’s collective wealth, being the

\begin{footnotes}
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\item \textsuperscript{126} Knobel 2001 \textit{THRHR} 576.
\item \textsuperscript{127} Davis \textit{et al} \textit{Estate Planning} 1-4.
\item \textsuperscript{128} Rabenowitz \textit{et al} \textit{The South African Financial Planning Handbook} 2017 873-880.
\end{itemize}
\end{footnotes}
legal object of this subjective right, is not tangible and cannot be registered in the Deeds Office or physically delivered in the case of movable property, as is the requirement for the existence of a real right.\textsuperscript{129} As a result, this newly defined subjective right cannot fall in the category of real rights.

As far as the category of personality rights pertains, an argument is set to be made regarding the close link that the generation of an individual’s wealth is to his personality, similar to Neethling’s\textsuperscript{130} argument regarding an individual’s earning capacity. However, personality rights are not separable from the legal subject who holds the right\textsuperscript{131} and are furthermore not be transferable as it comes to life at the birth of an individual and terminates at his or her death.\textsuperscript{132}

It has been established that an interest in the creation and preservation of wealth is in fact transferable over generations and legal entities and has a legal personality completely separable from that of the wealth creator. It is conceded that, similar to an individual’s earning capacity, his or her interest in the creation and protection of their wealth has qualities which are closely linked to personality traits, but that this subjective right cannot be placed in the category of personality rights.

Referring to wealth as the collective noun of all rights in property, the creation and preservation of wealth as a legal object, cannot be placed in the category of personal rights, as personal rights is merely one component of the object of wealth. It can also not be said that a wealth creator has any form of an expectation of performance from another legal subject.

Using a trade secret as a study into the nature of intellectual property rights as a category of subjective rights, it was confirmed that a trade secret had to firstly have an element of secrecy, secondly have an application in trade and industry in its concrete form and finally have a specific value.

\textsuperscript{129} Pienaar et al Silberberg and Schoeman’s \textit{The Law of Property} 65.
\textsuperscript{130} Neethling 1987 \textit{THRHR} 318.
\textsuperscript{131} Neethling 2005 \textit{CILSA} 223.
\textsuperscript{132} Neethling \textit{et al Neethling’s Law of Personality} 15.
If the creation and preservation of wealth as a legal object for the purposes of a subjective right is to be put to the test in the category of intellectual property, it will be shown to not necessarily have a secrecy quality (although often highly confidential). It is concrete enough to enjoy an existence separate from its owner but will not find an application in trade and industry and will definitely not show economic value in the sense that it is worth anything to a competitor or rival. While it is not a trade secret, it will also not qualify as any other form of intellectual property currently receiving statutory legal protection.

The final category where the newly defined subjective right in a person’s wealth can find application, is that of personal immaterial property rights. Based on Neethling’s research into the placement and recognition of an individual’s earning capacity, it is submitted that the interest in the creation and preservation of an individual’s wealth is a subjective right, eligible of legal recognition and protection in the category of personal immaterial property rights. An individual’s interest in the creation and preservation of his or her wealth is closely linked to his personality rights such as his intelligence, expertise, personality, etc. It holds separate components of real rights and personal rights, while remaining fully intangible and contains substantial economic value and use to its owner.

On the acceptance of the above and the recognition of an individual’s right to the protection of his wealth, chapter 3 will set out to answer the question of what the effect of anti-avoidance tax legislation is on the enjoyment and protection of this legally protectable subjective right.

### 2.3 Conclusion

With the research question in mind, the purpose of this chapter was to determine, as a point of departure, whether an individual’s interest in the creation and preservation of his or her wealth constitutes a legally protectable interest.

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133 Neethling 1987 *THRHR* 318.
134 Neethling 1987 *THRHR* 318.
Through the application of the Doctrine of Subjective rights and the ability to define what this interest seeking legal protection will look like, it has been confirmed that an individual’s interest in the creation and preservation of his or her wealth is in fact a subjective right, in the category of personal immaterial property rights. With its legal recognition and protectability in place, the next part of this research will ascertain the effect of anti-avoidance tax legislation, which to a great extent limits the enjoyment of this, now recognisable right.

Chapter 3 is set to research the origin of anti-avoidance tax legislation as well as its application to case law in order to determine whether the legislation at hand unduly limits the enjoyment of a subjective right in wealth creation and preservation.
Chapter 3 The basis of anti-avoidance tax legislation

3.1 Introduction

In an attempt to finally determine the effect of anti-avoidance tax legislation on the legal interest that an individual may have in the creation and preservation of his or her wealth, the first point of departure was to determine whether such an interest is in fact protectable by our law. Chapter 2 set out to answer this question and research was able to confirm that the interest that one has in the protection and creation of his or her wealth may constitute a subjective right, protectable as a personal immaterial property right.

Chapter 3 seeks to further pursue the research question, by critically evaluating the legal basis, structure and qualities of the GAAR as it is set out in the ITA. The GAAR refers to a provision in the ITA which controls avoidance arrangements, by defining transactions which are impermissible. However, before that can be done, the relevance of this secondary question needs to be positioned as it pertains to the difference between tax avoidance and tax evasion. It is important to note that the purpose of this research is situated on the side of legal tax avoidance and will in no way attempt to legitimize tax evasion as a criminal act.

3.2 Tax avoidance versus tax evasion

3.2.1 Legal basis for differentiation

One of the most famous and valuable legal resources to any tax practitioner, wealth creator and attorney is the principle of legal tax avoidance as confirmed in the landmark English court case, the Westminster-case:136

Every man is entitled if he can to order his affairs so as that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, however unappreciative the
Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay increased tax.

Put into layman’s terms with a hint of humour, a Morgan Stanley advertisement\textsuperscript{137} once confirmed the same sentiment:

You must pay taxes. But there's no law that says you gotta leave a tip.

More recently, the NWK-case\textsuperscript{138} carried this principle forward and continues to differentiate between tax avoidance and tax evasion and the grounds thereof. It also introduces the concept of simulated transactions:

Tax effective arrangements are not unlawful, and a taxpayer may organise his financial affairs in such a way as to pay the least tax permissible. However, the same cannot be said for disguising a transaction to make it appear to be something that it is not, especially if that has the purpose of tax evasion, or the avoidance of a peremptory rule of law.

Tax avoidance constitutes legal tax planning which refers to the taking of steps aimed at achieving a more favourable tax outcome, than would have otherwise been the case, within the ambit of the ITA.\textsuperscript{139} Kajinga\textsuperscript{140} states that tax avoidance is the avoidance of tax in a way that is consistent with the limitations imposed by the GAAR as well as the statutory law. Tax evasion is a criminal act, which involves false statements and omission of information to reduce or avoid the creation of a tax obligation.\textsuperscript{141} Legality is, according to Kajinga, the most basic distinction between tax evasion and tax avoidance.\textsuperscript{142} In contrast to tax evasion, tax avoidance involves full disclosure of all information and does not involve elements of dishonesty.\textsuperscript{143}

At this point it is imperative to point out that this research is focussed on the effect of anti-avoidance tax legislation on the creation and protection of wealth, as it pertains to legal tax planning or tax avoidance. Full disclosure and honesty with

\textsuperscript{137} Johnson M et al 2009 Federal Tax Course 107.
\textsuperscript{138} Para 347.
\textsuperscript{139} Cilliers Anti-Avoidance para 46.2.
\textsuperscript{140} Kujinga 2014 CILSA 430.
\textsuperscript{141} Stewart 1970 CILSA 169.
\textsuperscript{142} Kajinga A Comparative Analysis of the Efficacy of the General Anti-Avoidance Rule as a measure against Impermissible Income Tax Avoidance in South Africa 15.
\textsuperscript{143} Cilliers Anti-Avoidance para 46.2.
regards to true and accurate facts is key to a successful wealth plan and strategy – utilised (in the words of the Westminster-case) with ingenuity in order to create a more favourable outcome for the collective family wealth.

In order for a creative, but legal, tax avoidance arrangement to remain permissible, it needs to avoid the grasp of the GAAR. The requirements of what makes an estate planning tool or structure an impermissible tax avoidance arrangement is crucial in order for bona fide tax and estate planning to provide the wealth creator with the solution he requires to achieve his family wealth goal.

3.3 **General Anti-Avoidance Rules: The fall of section 103(1) of the Income Tax Act and the rise of sections 80A – 80L**

3.3.1 **The weaknesses of section 103**

The previous regime, being Section 103 of the ITA, was replaced in 2006 with the current GAAR as it is set out in section 80A – 80L of the ITA. Treasury provided the industry with its reasons as to why the ‘old’ GAAR is to be replaced by means of an Explanatory Memorandum.

The reasons cited echoed those frustrations aired by academics and practitioners, stating that the old GAAR proved to be inconsistent, and at times ineffective in its task to combat the ever-evolving avoidance arrangements that the industry designs in an attempt to legally reduce tax. Kujinga offers a tone of sympathy when he refers to a GAAR, in general and around the world, as serving a complex function, to "target one form of tax avoidance (impermissible tax avoidance) while simultaneously honouring another form (permissible tax avoidance)".

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144 Revenue Laws Amendment Act 20 of 2006.
146 Kujinga 2014 CILSA 435 uses the words "failure, limited success or controversy", citing that SARS was unsuccessful to invoke the Section 103(1) in major cases such as CIR v Geustyn, Forsyth and Joubert 1971 3 SA 537 (A); Hickling v SIR 1980 1 SA 481 (SA) and CIR v Conhage (Formerly Tycon) (Pty) Ltd 1999 4 SA 1149 (SCA).
147 Kujinga 2014 CILSA 430.
3.3.2 The structure and application of the new GAAR

Section 80A – 80L of the ITA, which replaced the previous regime of GAAR on 2 November 2006 was introduced to combat the weaknesses of Section 103(1) of the ITA. However, it is important to note that the new legislation does not apply retrospectively and that any arrangements entered into before this date, may be subject to the provisions of Section 103(1) of the ITA.

Section 80A of the ITA sets out the criteria of an impermissible tax avoidance arrangement. The wording of Section 80A(1) of the ITA shows that, in order for the GAAR to become applicable, there needs to be an avoidance arrangement where the primary purpose of the avoidance arrangement was to obtain a tax benefit. An arrangement which qualifies in terms of Section 80A(1) of the ITA, will only become an impermissible avoidance arrangement once any one of the tainted elements, as set out in Section 80A(1)(a)-(c) of the ITA, is present. These tainted elements, which will be discussed in detail below, are in essence the pitfalls to steer clear from when undertaking tax planning as part of estate planning. The remainder of the structure of the GAAR, as it pertains to the Commissioner's remedies, powers and the general definitions is not of particular value to the research question at hand as it does not show the limitations that the GAAR impose on bona fide tax and estate planning, but rather refers to the result of such arrangement when found to be impermissible.

3.4 What is an impermissible tax avoidance transaction?

3.4.1 Defining an arrangement

As briefly referred to in chapter 2 of this research, an arrangement, as it applies to different applications of the law, is a crucial term to define. In terms of Section 80L of the ITA, an "arrangement" means:

Any transaction, operation, scheme, agreement or understanding (whether enforceable or not), including all steps therein or parts thereof, and includes any...

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148 Section 80A of the ITA.
of the foregoing involving the alienation of property.

This definition is by far more extensive than the definition offered by Section 103(1) of the old GAAR, which defined an arrangement as a "transaction, operation, or scheme".\(^{149}\) From this new definition, particular consideration is to be given to the wording "agreement or understanding" as it implies the requirement of two or more involved parties, who have an understanding as to mutual performance.\(^{150}\)

Furthermore, the wording "including all steps therein or parts thereof" should be seen in the context of Section 80H of the ITA, which gives the Commissioner the authority to apply the GAAR to steps or parts of an arrangement. While the terms "all steps" and "parts thereof" have not been defined in the ITA, Clegg and Stretch\(^ {151}\) states that it suggests that each "step" or "part" relates to a distinct transactional element of the whole. Broomberg criticises the draftsman of the GAAR, when referring to the definition of an arrangement, including "in steps or in parts", asking:\(^ {152}\)

> Can he [the Commissioner] do so when the step or part so elected loses its commercial substance when considered in isolation?

In agreement with Broomberg’s concern it is submitted that this may eliminate an argument that a specific agreement or transaction falls within the scope of an otherwise valid arrangement and should therefore be protected against the GAAR.

Before any arrangement can be seen as an avoidance arrangement, open to the scrutiny of the GAAR, it needs to qualify in terms of Section 80A of the ITA.

In order for estate planning to reach its true objective, being the allowance of an estate owner to create and preserve his wealth across generations, arrangements, which forms part of the definition of estate planning,\(^ {153}\) needs to remain clear from the pitfalls as identified and combatted in the GAAR.

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\(^ {149}\) Section 103(1) of the *ITA*, now amended.

\(^ {150}\) *Newton v FCT* 1958 2 All ER 759 (PC).

\(^ {151}\) Clegg and Stretch *Income Tax in South Africa* para 26.3.2.


3.4.2 Section 80A of the Income Tax Act

Section 80A of the ITA provides that an impermissible tax avoidance arrangement will be identified by the presence of two key qualities. Firstly, the sole or main purpose of the arrangement is to obtain a tax benefit; and secondly, there has to be what is referred to as a "tainted element" present.\textsuperscript{154} Kajinga states that the word "and" of the ITA is crucial because a sole or main purpose to avoid tax is insufficient if not accompanied by an indicator of an impermissible avoidance arrangement.\textsuperscript{155} In his LLD-thesis, Kajinga\textsuperscript{156} continues that the sole or main purpose will still need to satisfy the basic elements of the GAAR, in that the arrangement should have at least one tainted element present.

For purposes of the ITA, the first quality, that the sole or main purpose of the arrangement is to obtain a tax benefit,\textsuperscript{157} is a mandatory requirement for the existence of an avoidance arrangement – both permissible and impermissible.\textsuperscript{158} If an arrangement cannot be shown to have tax avoidance as its main purpose, there is no need or use to further look into the presence of a tainted element. The GAAR is furthermore only triggered once one of the other elements are present.\textsuperscript{159}

The tainted elements, as set out in sub-sections (a) – (c), can be summarised as follows:\textsuperscript{160}

a) The element of abnormality, both in the context of business\textsuperscript{161} and in the context other than business,\textsuperscript{162} as well as where rights and obligations are created which differs from what can be expected in an arm’s length transaction.\textsuperscript{163}

\textsuperscript{154} Explanatory Memorandum on the Revenue Laws Amendment Bill 2006 62 and 63.
\textsuperscript{155} Kajinga 2015 \textit{SA MERC LJ} 222.
\textsuperscript{156} Kajinga \textit{A Comparative Analysis of the Efficacy of the General Anti-Avoidance Rule as a measure against Impermissible Income Tax Avoidance in South Africa} 107.
\textsuperscript{157} Section 80A of the \textit{ITA}.
\textsuperscript{158} Section 80L of the \textit{ITA}.
\textsuperscript{159} De Koker and Williams \textit{Silke on South African Income Tax} para 19.39.
\textsuperscript{160} Explanatory Memorandum on the Revenue Laws Amendment Bill 2006 63.
\textsuperscript{161} Section 80A (a)(i) of the \textit{ITA}.
\textsuperscript{162} Section 80A (b) of the \textit{ITA}.
\textsuperscript{163} Section 80A (c)(i) of the \textit{ITA}.
b) Where the arrangement lacks commercial substance, in whole or in part.\textsuperscript{164}

c) Where the arrangement would result directly or indirectly in the misuse or abuse of the provisions of the ITA.\textsuperscript{165}

3.4.2.1 Main purpose to avoid tax

If the main purpose of an arrangement is anything other than the avoidance of tax, the GAAR will not find application as it is the key requirement to turn an arrangement (as defined) into an avoidance arrangement. Furthermore, only when one of the tainted elements exist, will the avoidance arrangement turn into an impermissible avoidance arrangement.

However, Section 80G (1) of the ITA firmly places the onus of proof on the taxpayer to show that an avoidance arrangement had its sole or main purpose as something other than the obtaining of a tax benefit. Broomberg considers the shifting of the onus of proof as a profound change from the old regime (Section 103(1) of the ITA) to the current Section 80G (1) of the ITA.\textsuperscript{166} The ITA makes it clear that it is a general presumption that an avoidance arrangement has its sole purpose to be that of tax savings or reduction, unless the contrary can be showed in the light of the relevant facts and circumstances.\textsuperscript{167} This means that the only thing that is left for the taxpayer to do, is to show that none of the other requirements for the application of the GAAR is present.\textsuperscript{168}

The case of \textit{Commissioner for Inland Revenue v Conhage (Pty) Ltd} 61 SATC 391 (hereinafter the Conhage-case), showed that the taxpayer may to a certain extent enjoy the benefit of the doubt. However, it must be noted that this case was decided under the previous regime of Section 103(1). Broomberg states in

\textsuperscript{164} Section 80A (a) (ii) of the ITA.
\textsuperscript{165} Section 80A (c)(ii) of the ITA.
\textsuperscript{166} Broomberg 2007 \textit{Tax Planning Corporate and Personal Vol} 21.
\textsuperscript{167} Section 80G(1) of the ITA.
\textsuperscript{168} Broomberg 2007 \textit{Tax Planning Corporate and Personal Vol} 21.
disappointment that the draftsman of the new GAAR was out to destroy the principle set down in South African courts, specifically referring to the *Conhage*-case.\(^{169}\)

*In casu*, the taxpayer (“Tycon”) required capital to expand its business and Firstcorp Merchant Bank Ltd. (“Firstcorp”) was happy to make the funds available. Both parties were aware of the tax benefits of a sale and leaseback agreement in terms of which Tycon would sell certain of its manufacturing plant and equipment to Firstcorp and in return lease it back. As a result, the parties agreed to follow this route as a manner in which to solve Tycon’s capital need.\(^{170}\)

The Commissioner invoked Section 103 of the ITA as soon as it became aware of the arrangement, when Tycon tried to deduct the lease expense from its taxable income in the particular year of assessment. The Commissioner was of the opinion that the transaction was a simulated transaction in that the true nature and the substance of the agreements differ.\(^{171}\) The Commissioner believed that Tycon in actual fact borrowed the capital from Firstcorp and disguised the transaction as a sale and lease agreement with the sole purpose of obtaining a tax benefit.\(^{172}\)

On this issue Tycon contended that the only reason why the sale and leaseback agreements were the preferred instrument to a straightforward loan, was in fact the tax benefit which it held.\(^{173}\) That said, it did not mean that the purpose for entering into the transaction was solely for tax purposes. The primary objective of the arrangement between Tycon and Firstcorp was to obtain capital – not to reduce tax.\(^{174}\) The reduction of tax was an added benefit when the method was selected for the implementation of the primary objective of the transaction.

The Supreme Court of Appeal sided with Tycon in this regard and stated that a taxpayer is free to minimise his tax by arranging his affairs in a suitable manner and if the same commercial outcome can be achieved in various different ways, the


\(^{170}\) *Conhage*-case para 392.

\(^{171}\) *Conhage*-case para 392.

\(^{172}\) *Conhage*-case para 392.

\(^{173}\) *Conhage*-case para 392.

\(^{174}\) *Conhage*-case para 398.
taxpayer may enter into the type of transaction which attracts no tax or the least amount of tax possible.\textsuperscript{175}

The use of the sale and lease agreement as a tool to obtain the finance that Tycon required, made "perfectly good business sense".\textsuperscript{176} The parties did not fraudulently disguise the nature of their agreement,\textsuperscript{177} nor did they intend not to honour the agreement in its true form. Tycon knew very well that the sale and lease agreement will entail them handing over the ownership of their plant and equipment.\textsuperscript{178} They weighed up the loss of assets in ownership against the benefit of obtaining capital without going into a loan agreement. They did in fact hand over the ownership to Firstcorp and thereby executed the agreements in true sense. It was not a simulated transaction.\textsuperscript{179}

When it came to the test of the validity of Tycon’s intention as to why they chose the most favourable tax method to reach their primary objective, the court considered the facts surrounding how Tycon came to the decision. The court commented on how Tycon did thorough research into different options available to obtain the capital it required; how it entertained offers from other financial institutions to enter into the sale and lease agreements; how its financial directors and advisors specifically considered the disadvantage of the sale and lease agreement (being loss of ownership) and the disadvantages of loan agreements; and how extensive arm’s length negotiations were conducted with Firstcorp.\textsuperscript{180} This goes to show that the groundwork and opinions gathered before entering into an arrangement which may co-incidentally entail a tax benefit, will go far in making the case of a \textit{bona fide} business purpose, as required by Section 80A(a)(i) of the ITA.

It is important to note that this case was decided based on the old GAAR’s Section 103(1) of the ITA. As mentioned above, some of the criticism of the new Section

\begin{footnotesize}
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\item Conhage-case para 392.
\item Conhage-case para 396.
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\item Conhage-case para 396.
\end{enumerate}
\end{footnotesize}
80A of the ITA, was that it removed the subjective element in determining what the intention of the taxpayer was. The new GAAR requires an objective review of the arrangement, which will not take the taxpayers intention into consideration.\textsuperscript{181} In explaining the difference between an objective and subjective test to determine what the main purpose of an arrangement is, Judge Corbett held the following in \textit{Secretary for Inland Revenue v Gallager} 1978 (2) SA 463 (A) 471B (hereinafter the \textit{Gallager-case}) (which was determined by the previous GAAR):

By an objective test in this context it evidently meant a test which has regard rather to the effect of the scheme, objectively viewed, as opposed to a "subjective" test which takes as its criterion the purpose which those carrying out the scheme intend to achieve by means of the scheme.

A further statement from the \textit{Conhage-case} that speaks to the relationship between a \textit{bona fide} purpose and the methods undertaken to facilitate the arrangement, is highlighted in the following:\textsuperscript{182}

But, even if the particular type of transaction was chosen solely for the tax benefits, it would be wrong to ignore the fact that, had Tycon not needed capital, there would not have been any transaction at all.

De Koker and Williams come to the conclusion that in determining the purpose of an avoidance arrangement, regard must be given to the arrangement, objectively, namely whether there was a tax benefit – and where the only effect of the arrangement was a tax benefit, then it can be said that the sole or main purpose of the arrangement was the said tax benefit.\textsuperscript{183}

This clearly shows the order of the taxpayer’s dealings. The purpose needs to exist first, before the appropriate – most tax efficient – solution can be found. If there was no purpose, there would not be an arrangement. This interpretation implies that where the arrangement is selected, for a tax purpose, and the parties then only begin to seek a legitimate purpose argument, that the arrangement may fall foul of the first requirement of the GAAR. De Waal asks whether the arrangement have

\textsuperscript{181} De Koker and Williams \textit{Silke on South African Income Tax} para 19.38.
\textsuperscript{182} \textit{Conhage-case} para 398.
\textsuperscript{183} De Koker and Williams \textit{Silke on South African Income Tax} para 19.38.
any other purpose or commercial sense, other than creating a tax benefit.\textsuperscript{184} It is submitted that the answer to his question may lead the planner to know if the first requirement of Section 80A of the ITA is adhered to.

Broomberg notes that the only way to determine whether a taxpayer has entered into a transaction with the main purpose to avoid tax, it will be necessary to make some or other comparison regarding the taxpayer’s position before and after the implementation of the transaction.\textsuperscript{185} This refers to the so-called "but-for"-test as set down in the case of \textit{Commissioner for Inland Revenue v Louw} 1983 2 All SA 291 (A) (hereinafter the \textit{Louw-case}) in the words of Judge Corbett: \textsuperscript{186}

In order to determine whether the advancing of the loans enabled respondent to get out of the way of, escape or prevent an anticipated liability for tax one must, I think, ask oneself the question whether, but for the loans, equivalent or even lesser amounts would probably have been received by respondent in a taxable form, i.e. as salary or dividend.

In the case of \textit{Smith v Commissioner for Inland Revenue} 1964 2 All SA 83 (A)\textsuperscript{187} the "but-for"-test was used by asking whether "Had it not been for the transactions ..."

The "but-for"-test is closely associated with the requirement that the arrangement must result in a tax benefit, in other words, an impermissible avoidance arrangement as envisioned by Section 80A of the ITA. Therefore, for purposes of this research, the question begs whether a tax benefit would have been created if the taxpayer had not entered into arrangements to exercise his subjective right to create and preserve his wealth? In other words, had it not been for the wealth creator’s subjective right to his legally protectable interest in the creation and preservation of his wealth, would the arrangement, which results in a tax benefit, have ever come to light?

Chapter 4 of this research will seek to answer this question, by differentiating between two further possible scenarios. In the first instance, entering a tax-efficient

\textsuperscript{184} De Waal 2012 \textit{The Rabel Journal} 1082.
\textsuperscript{185} Broomberg 2007 \textit{Tax Planning Corporate and Personal} Vol 21.
\textsuperscript{186} \textit{Louw-case} para 307.
\textsuperscript{187} \textit{Smith v Commissioner for Inland Revenue} 1964 2 All SA 83 (A) para 91.
transaction in terms of which assets are transferred to a family trust, primarily for
the purpose of securing family wealth in the broad sense will be examined. In the
second instance, the creation of the family wealth by means of the benefit obtained
when a transaction is entered into for its tax advantages is scrutinised. An example
of the latter will be where a particular transaction is entered into for the sole purpose
of receiving a tax benefit, where the result of such a tax benefit will mean the
expansion of the family’s wealth through, for example, the increase of investment
returns and the minimisation of the tax liability.

The tax planner or attorney, who advises a wealth creator on methods to enlarge
and preserve his or her wealth by means of legal avoidance arrangements, needs
to be particularly concerned with the following tainted elements, as the key to turn
a permissible avoidance arrangement into an impermissible avoidance arrangement.

3.4.2.2 Tainted elements

Impermissible tax avoidance arrangements are those transactions characterised by
tainted elements which include abnormality,\(^{188}\) the absence of commercial
substance\(^{189}\) and misuse and abuse.\(^{190}\)\(^{191}\)

3.4.2.2.1 Abnormality

The abnormality element is largely based on the previous GAAR’s Section 103(1),\(^{192}\)
and seeks to identify arrangements which have been entered by means other than
what would have normally been used for \textit{bona fide} business or other purposes,
other than obtaining a tax benefit.\(^{193}\)

\(^{188}\) Section 80A (a)(i) and (b) of the \textit{ITA}.
\(^{189}\) Section 80A (a)(ii) of the \textit{ITA}.
\(^{190}\) Section 80A (c)(ii) of the \textit{ITA}.
\(^{191}\) Kujinga 2014 \textit{CILSA} 435.
\(^{192}\) \textit{Explanatory Memorandum on the Revenue Laws Amendment Bill, 2006} 63.
\(^{193}\) Section 80A (a)(i) and (b) of the \textit{ITA}. 
In terms of Section 80A(c)(i) of the ITA, the abnormality requirement as a tainted element in the GAAR, is defined in a context other than business to create rights or obligations not normally created between persons dealing at arm’s length.\textsuperscript{194}

The previous GAAR’s Section 103(1) of the ITA, was amended in 1996\textsuperscript{195} to include the abnormality requirement. According to Kujinga, these amendments was "inadequate and problematic", as it was too dependent on the circumstances of the transactions and was therefore open to a counter argument that the transaction was common, in the sense that it was so widely used - and therefore normal.\textsuperscript{196}

The key words in the Section 80A of the ITA as it refers to the normality requirement are "means" and "manners".\textsuperscript{197} The manner in which an avoidance arrangement is conducted, is of special concern as it is the "how" that will determine if the transaction was abnormal. In this instance, \textit{Hicklin v SIR} 1980 1 SA 481 (A) 495A-D (hereinafter the \textit{Hicklin}-case), reminds us that a normal, arm’s length transaction is one where the parties are independent from one another, each seeking to obtain the best outcome from the transaction for themselves. This test is fair in a situation where the parties are independent from each other, but where the parties are related, or have an existing relationship, one should look at the entire relationship and not analyse one transaction in isolation.\textsuperscript{198}

It is submitted that what will be regarded as being normal practice in a particular situation, will differ from case to case. Interactions between family members where the purpose of the transaction is to protect a family interest, will differ from what is normal or natural in a commercial contract involving third parties. The requirement of abnormality as a tainted element, should be separated from the concept of what the main purpose (saving tax) of the transaction is. In other words, where rights and obligations where created which differs from a normal, arm’s length dealing, the purpose of that transaction should not be confused with the main purpose of

\textsuperscript{194} Explanatory Memorandum on the Revenue Laws Amendment Bill 2006 63.
\textsuperscript{195} Revenue Laws Amendment Act 46 of 1996.
\textsuperscript{196} Kujinga 2014 CILSA 442; De Koker and Williams \textit{Silke on South African Income Tax} para 19.39.
\textsuperscript{197} De Koker and Williams \textit{Silke on South African Income Tax} para 19.39.
\textsuperscript{198} Kujinga 2014 CILSA 443.
the arrangement, being that of tax savings. Only once the main purpose has been established as being to save on tax, can one determine whether the methods used to get there can be regarded as normal, *bona fide* actions.

In seeking to answer the practical questions that will be posed in chapter 4, the test of abnormality will form the golden thread against which each arrangement should be tested. However, in the scope of wealth creation and preservation, the focus of the test may shift from one where the question asks if an arrangement is one that would normally be considered in the day-to-day business world, to a question where normality may depend on the extent to which a family wealth creator may deem it normal to apply methods to safeguard and grow the family’s wealth.

3.4.2.2.2 Lack of commercial substance

The second tainted element as set out in terms of Section 80A(a)(ii) of the ITA, that an arrangement is seen as an impermissible tax avoidance arrangement if, along with taxation being the primary purpose of the transaction, it lacks commercial substance in the business context, refers to Section 80C of the Act.

The general rule set down in Section 80C of the ITA, is that an arrangement lacks commercial substance if it would result in a significant tax benefit for a party, but does not hold an evenly significant effect upon either the business of the taxpayer, or the net cash flow of that party – apart from the effect attributable to the tax benefit itself.\(^{199}\) Put differently, an avoidance arrangement lacks commercial substance if the tax benefits presented to the taxpayer significantly overshadows the taxpayers interest in the transaction.\(^{200}\)

The latter part will be of particular interest in chapter 4, where the argument stands to be made that the net cash flow attributable to the beneficial tax arrangement will

\[^{199}\text{Section 80C (1) of the ITA; Explanatory Memorandum on the Revenue Laws Amendment Bill 2006 63.}\]

\[^{200}\text{Kujinga 2015 *SA MERC LJ* 243.}\]
be regarded as having commercial substance in the scope of an individual’s wealth preservation across generations.

Subsection 2 continues to identify key indicators or characteristics of an avoidance arrangement which is indicative of a lack of commercial substance. This is, however, not a closed list of characteristics.\(^{201}\)

These characteristics, being substance over form,\(^{202}\) round-trip financing,\(^{203}\) the use of tax indifferent parties,\(^{204}\) or elements with the effect of offsetting or cancelling each other,\(^{205}\) will be discussed briefly.

The indicator of substance over form, will enjoy more attention as it finds more relevance as to the nature of the arrangements which may be entered into at the behest of this argument, being the creation and preservation of family wealth.

3.4.2.2.2.1 Substance over form

It is submitted from the above that a taxpayer can structure his or her affairs in such a fashion and enter into \textit{bona fide} transactions which has the effect of avoiding or reducing tax. However, his actions cannot be exercised in a manner which offends the provisions of the law.\(^{206}\) As a result, the courts do not give effect to simulated transactions.

Although Lady Justice is usually depicted with a blindfold to portray her impartiality, this visual metaphor should not be interpreted as a wilful closing of her eyes to the true state of affairs or, in a commercial context, to the true nature of a given transaction.\(^{207}\)

Simulated transactions, also called shams,\(^{208}\) have been defined as acts done and documents executed by which the parties intend to have third parties or the courts

\(^{201}\) Section 80C (2) of the ITA.
\(^{202}\) Section 80C (2)(a) of the ITA.
\(^{203}\) Section 80C (2)(b)(i) of the ITA.
\(^{204}\) Section 80C (2)(b)(ii) of the ITA.
\(^{205}\) Section 80C (2)(b)(iii) of the ITA.
\(^{206}\) SARS v Knuth and Industrial Mouldings (Pty) Ltd 1999 62 SATC paras 65-74.
\(^{207}\) Hutchinson and Hutchinson 2014 \textit{The South African Law Journal} 69.
\(^{208}\) Hutchinson and Hutchinson 2014 \textit{The South African Law Journal} 69; De Waal 2012 \textit{The Rabel Journal} 1078-1100.
believe that there have been legal rights and obligations created between parties, which differ from those rights and obligations (if any) that have in actual fact been created.\textsuperscript{209} The concept of simulation is of particular interest in the Law of Trust where one of the essentialia of a valid trust is whether the founder had the intention to create a trust.\textsuperscript{210} The moment that the word intention is referred to, the natural element which follows is the determination of what the "real intention" was.\textsuperscript{211} This leads to the question whether the real intention of the founder (in the Trust law) or the taxpayer (as it applies to the GAAR) is established in the shape which it assumes? De Waal refers to \textit{Zandberg v Van Zyl} 1910 AD 302 (hereinafter the Zandberg-case),\textsuperscript{212} when he asks the question if the founder (or taxpayer) has given his arrangement the name and shape of a trust, not with the intention to express its true nature, but to disguise it.\textsuperscript{213} De Waal continues in this tone, referring to the Zandberg-case,\textsuperscript{214} and asks whether the being which truly came into existence was not perhaps a fideicommissum, and agency or a partnership, disguised as a trust to gain some or other advantage.

The effect of finding that a founder did not have the intention to create a trust, but instead simulated his arrangement to assume the form of a trust, was highlighted in the landmark case of \textit{Badenhorst v Badenhorst} 2006 (2) SA 255 (SCA) (hereinafter the \textit{Badenhorst}-case). In the Badenhorst-case, Mrs Badenhorst asked the court to deem the property held in trust by her husband, be brought into consideration for purposes of accrual calculations.\textsuperscript{215} According to Mrs Badenhorst, Mr Badenhorst dealt with the trust property as if it was his own, an extension of his personality, his \textit{alter ego} – and as a result the trust is a sham.\textsuperscript{216} However, De Waal comments that in order for a trust to be regarded as a sham or where the court can "pierce the corporate veil" to "go behind the trust form" or "disregard the veneer",\textsuperscript{217}

\begin{thebibliography}{99}
\bibitem{209} Snook v London and West Riding Investments Ltd 1967 1 All ER.
\bibitem{210} De Waal 2012 \textit{The Rabel Journal} 1084.
\bibitem{211} De Waal 2012 \textit{The Rabel Journal} 1082.
\bibitem{212} Zandberg v Van Zyl 1910 AD 302.
\bibitem{213} De Waal 2012 \textit{The Rabel Journal} 1085.
\bibitem{214} Zandberg v Van Zyl 1910 AD 302.
\bibitem{215} \textit{Badenhorst}-case para 1.
\bibitem{216} \textit{Badenhorst}-case para 28.
\bibitem{217} De Waal 2012 \textit{The Rabel Journal} 1079.
\end{thebibliography}
that the trust in question should in actual fact be a trust. Where there was no intention by the founder to actually set up a trust, as the arrangement was a simulation or sham of something different, there is no trust to ignore, and the actions of Mr Badenhorst is best seen as the misuse of a valid trust. With the principles of simulated transactions, as it presents in other areas of the law, the doctrine of substance over form, as an indicator of a lack of commercial substance, requires further evaluation.

The doctrine of substance over form is a South African common law principle which is best captured in the maxim *plus valeat quod agitur quam quod simulate concipitur* – which literally means that the real intention or what was actually done, carries more weight than what seems to have been done. It should be emphasised that the common law principle of substance over from, differs from the requirement set out as a tainted element in the GAAR, in that the court’s approach in the common law sense will differ as opposed to scenario’s where the GAAR can be implemented.

This principle is used by the courts to determine whether a transaction in question is in fact what it purports to be, or whether it is a simulation of something to disguise the true intention of an arrangement. In essence, the court will strip away the disguise and have regard to the true substance of the transaction rather than its appearance. Where the common law approached is followed, the courts will disregard the transaction as a whole and determine the outcome on what the transaction really is. This is in contrast to the statutory, GAAR, approach in terms of which the courts impose a consequence, different from what the parties intended.

One of the best examples where this principle was used to identify an arrangement as a simulated transaction, is found in *Kilburn v Estate Kilburn* 1931 AD (hereinafter

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221 Ger *Rebus* 62; *Kilburn v Estate Kilburn* 1931 AD 504.
222 NWK-case; *Kilburn v Estate Kilburn* 1931 AD.
224 De Koker and Williams *Silke on South African Income Tax* para 19.3.
the Kilburn-case). In essence the facts pertained to a husband who registered a notarial bond for £500 over all his property in favour of his soon-to-be wife on the basis that he had promised her the consideration before the solemnization of the marriage, but was unable to pay such sum prior to the marriage. He therefore acknowledged his indebtedness to her by means of the notarial bond. There was no fixed date linked to the payment and the parties continued to enter into an antenuptial contract in terms of which they got married out of community of property.225

Upon his sequestration, his wife instituted a claim against his insolvent estate for – amongst other assets – her preferential claim as held in terms of the bond so registered.226 The court held that the parties never seriously regarded the debt as due or owing, but merely designed the agreement as a mere device to secure a sum of £500 in favour of the wife and in competition to other creditors, if the husband should become insolvent or pass away.227

It was concluded that there was no real obligation between the parties to pay the sum promised, and since the obligation to which the notarial bond was secured did not really exist in true form, the court held that the spouse could not claim from such a bond, which in reality was meaningless.228

Based on the maxim of plus valeat quod agitur quam quod simulate concipitur the court famously said:229

... Courts of law will not be deceived by the form of a transaction: it will rend aside the veil in which the transaction is wrapped and examine its true nature and substance.

While this common law principle creates the starting point and perhaps rule of thumb in determining whether a transaction is what it purports to be, or whether it is a disguise for some other intention, the enquiry in each case will be one of fact

225 Kilburn-case para 504.
226 Kilburn-case para 503.
227 Kilburn-case para 505.
228 Kilburn-case para 506.
229 Kilburn-case para 507.
of which no general rule can be laid down.\textsuperscript{230}

It is, however, notable that where the common law principle of a sham transaction is applied to nullify some forms of tax evasion, such as in the NWK-case, that the courts will disregard the transaction and give effect to the real transaction, without evoking the statutory GAAR.\textsuperscript{231} While the application of the principles of a common law sham transaction is indicative of the test of substance over form, the mere fact that a transaction is a simulated one, is in principle no impediment to the application of the statutory GAAR.\textsuperscript{232} The principle of substance over form, as it pertains to the GAAR, is a tainted element, which indicates that a transaction firstly have to fall within the ambit of the GAAR by virtue of the sole or main purpose of an arrangement being to save tax, before the substance of the transaction can be tested – whether it is a sham or not.\textsuperscript{233}

3.4.2.2.2.2 Round trip financing

Round trip financing includes an arrangement where funds are transferred between parties, resulting in a direct or indirect tax benefit, all the while significantly reducing, offsetting or eliminating any business risk incurred by the taxpayer.\textsuperscript{234}

The name of the arrangement says it all. In simple terms, the funds are to appear to pass between the parties by way of a commercial consideration, but simply travel in a circle, with the result that everyone is financially in the same position as they were in the beginning, save for the creation of a tax benefit for the "Houdini taxpayer" and the payment of the services of the "hired actors".\textsuperscript{235}

3.4.2.2.2.3 A tax indifferent party

A tax indifferent party is a party to an avoidance arrangement who is either not subject to normal tax, or a party who can significantly offset any amount by

\begin{footnotes}
\item[230] Zandberg v Van Zyl 1910 AD 302.
\item[231] De Koker and Williams Silke on South African Income Tax para 19.3.
\item[232] De Koker and Williams Silke on South African Income Tax para 19.3.
\item[234] Section 80D (1) of the ITA.
\end{footnotes}
expenditure or loss. An arrangement which involves such a tax indifferent party will have the result – either directly or indirectly – that an amount that would have formed part of the gross income or accruals of a capital nature by another party, will now form part of the gross income of the tax indifferent party to the effect that less or no tax is payable on the funds in question.

3.4.2.2.2.4 Offsetting elements

The last indicator as it pertains to whether an avoidance arrangement lacks commercial substance refers to arrangements which has the effect of offsetting rights or obligations that result in a situation where they cancel each other out.

NWK-case, while ultimately decided on under the common law principle of a simulated transaction, is often quoted as authority on the topic of substance over form, as the parties disguised various transactions in an extravagant manner with the ultimate purpose to enjoy more favourable tax treatment.

However, the facts in this case proves to be the perfect example of an offsetting arrangement, which is in fact one of the key indicators which showed that the arrangement in question lacked commercial substance.

Without going into the detail of the facts of the case, it is important to briefly refer to the set of agreements that the parties entered into in an attempt to legitimize an overly complicated arrangement.

NWK, a trader in maize, was offered a structured loan facility by a subsidiary of FNB Bank, to the amount of R96 415 776. The Commissioner held that the loan agreement was a simulated transaction on the basis that an amount of only R50 million was required by NWK, and that the loan agreement of the much larger

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236 Section 80E (1)(a) of the ITA.
237 Section 80E (1)(b) of the ITA.
239 NWK-case para 1.
amount was structured as such as to allow NWK to deduct larger amounts of interest from its taxable income.\textsuperscript{240}

The transactions envisaged by the parties to set up this particular arrangement, with the main purpose of obtaining tax benefits, included the following:\textsuperscript{241}

\begin{itemize}
  \item[a)] "Slab", a subsidiary of FNB, will lend the sum of R96 415 776 to NWK, repaid over 5 years;\textsuperscript{242}
  \item[b)] NWK will repay the capital, at the end of 5 years, by the delivery of 109 315 tons of maize;\textsuperscript{243}
  \item[c)] Interest on the capital sum will be payable every six months, with the requirement that NWK will issue promissory notes with the total value of R74 686 861;\textsuperscript{244}
  \item[d)] "Slab" will sell the promissory notes at well below face value, to FNB, in order to fund the loan to NWK;\textsuperscript{245}
  \item[e)] "Slab" would then sell its rights to take delivery of the maize, after 5 years, to "First Derivatives", a division of FNB;\textsuperscript{246}
  \item[f)] "First Derivatives" would sell its right to delivery of the same maize, to FNB for a sum of R46 415 776 – payable immediately on conclusion of the agreement, despite the delivery of the maize only taking place 5 years later.\textsuperscript{247}
\end{itemize}

The court correctly exclaimed "What a charade!".\textsuperscript{248} While there are various errors in the different contracts, spanning from detail such as not describing the maize

\begin{flushright}
\textsuperscript{240} NWK-case para 2.  
\textsuperscript{241} NWK-case paras 350 - 351.  
\textsuperscript{242} NWK-case para 350 para (a).  
\textsuperscript{243} NWK-case para 351 para (b).  
\textsuperscript{244} NWK-case para 351 para (c).  
\textsuperscript{245} NWK-case para 351 para (d).  
\textsuperscript{246} NWK-case para 351 para (e).  
\textsuperscript{247} NWK-case para 351 para (f).  
\textsuperscript{248} NWK-case para 353 para 21.
\end{flushright}
with enough certainty as to secure accurate delivery; misplacing the transaction as a loan, when it was in actual fact a sale; and the forward purchase agreement in terms of which "First Derivatives" sold its rights to the maize for immediate payment, only to be delivered 5 years later, with no regard to the change in value of maize at that time - what is actually of interest here is the offsetting elements. 249

To fully understand that, while the NWK-case has its fame linked to the application of the common law element of substance over form, 250 this case is a classic example of offsetting elements. The words of De Koker and Williams sets the scene: 251

The self-neutralising criterion attempts to flush out intentionally misleading elements inserted into complex schemes, often involving complicated financial derivatives, in which rights or obligations created in one part of the scheme are seen to be extinguished in another.

The court held that NWK had no intention of repaying the loan through the delivery of maize; Slab had no intention of selling it to FNB; and the cessions from Slab to FNB and of NWK to FNB cancelled each other out. 252 All of this effort (and confusion!) simply to "flush out intentionally misleading elements" 253 in a scheme to allow NWK to deduct larger amounts of interest on the loan from its taxable income. It should be no surprise that the court was able to clearly see behind the form of the arrangement to the substance.

3.4.2.2.3 Misuse or abuse of the provisions of the Act

South African case law has not attended to the clarification of what the scope, test or criteria is for this last, tainted element 254 sets out to be. Stating that an avoidance arrangement will be regarded as an impermissible avoidance arrangement if such arrangement has a primary purpose to avoid tax and has the effect that the ITA has been misused or abused, is extremely wide and vague. For purposes of this

249 NWK-case para 29.
250 Lötz and Nagel 2012 THRHR 688.
252 NWK-case para 30.
254 Section 80A (c)(ii) of the ITA.
research, further investigation into this element proves of little value in an attempt to answer the research question.

### 3.5 Conclusion

In order to answer the research question as to the effect of anti-avoidance tax legislation on the, now arguably recognised, interest that an individual has in the creation and preservation of his wealth, it was important to understand the workings of the GAAR. The above discussion of the GAAR and the statutory requirements, as well as the common law position as it pertains to impermissible tax avoidance arrangements accurately set the stage for the environment in which tax planning arrangements must survive.

Any tax planner, wealth creator or fiduciary advisory should remain wary of overly creative structures, schemes and arrangements, by weighing it up against the criteria of the GAAR. It is now fully understood what is allowed and what is impermissible. The argument now stands to be made, whether the protection of one’s wealth with the long-term view of generational estate planning in mind, will pass the test of a valid purpose for the implementation of permissible avoidance arrangements. Furthermore, the question is raised whether an arrangement which has its sole purpose to receive a tax benefit can be regarded as a valid avoidance arrangement, if it can be shown that such tax benefit, itself, forms part of the furtherance of the wealth creator’s object of growing and expanding his family’s wealth and financial security.

Chapter 4 is tasked at addressing these questions and will attempt to do so, by considering practical scenario’s in a legitimate estate planning conversation.
Chapter 4  The application of the GAAR to arrangements with the main object to protect the subjective right to create and preserve wealth

4.1  Introduction

This research undertook to answer the research question set as to understand the effect of anti-avoidance tax legislation on the protection of a legal interest in wealth creation and preservation.

In order to answer this question, it was necessary to break the problem statement into further, sub-questions. Firstly, before it can be said that anti-avoidance tax legislation may have an effect on the protection of a legal interest, it had to be determined whether such a protectable legal interest existed, or not. In other words - should the interest an individual has in the creation and preservation of his or her wealth enjoy legal protection? If so, in what form and to what extent?

Secondly, once it had been discovered that the legal interest at hand deserved legal protection, it was necessary to position the Law of Taxation – particularly the GAAR – as it pertains to estate planning. It has been held that estate planning is the sum of arrangements which has the ultimate goal of creating and preserving an individual’s wealth, over generations. Chapter 3 sets out to research the structure of the GAAR, as well as the common law principles which supports it. The research identified a number of grey areas as it pertains to the interpretation of arrangements in the estate planning science. These grey areas will call on the court to interpret same over time in order to create clarity where it is direly needed.

That said – and in an attempt to answer the research question posed in this research – two case studies will now be conducted to practically determine the effect of the interpretation of the GAAR on an individual’s subjective right to protect his or her wealth.

The first case study will speak to the most obvious, day-to-day dilemma in estate planning: the transfer of wealth across generations in the most tax efficient
manner.

The second case study will push the envelope in that the main purpose of the avoidance arrangement will be to save tax as the cash saved (or even earned) from the tax saving will be used to further generate wealth.

4.2 Avoidance arrangement 1: Main purpose of arrangement is to preserve wealth across generations

4.2.1 Case study

The most common scenario when it comes to a wealth creator’s objectives as part of his or her estate planning, is the transfer of wealth from one generation to another. This is a continuous process, the death of the wealth creator simply being the last opportunity to facilitate the transfer for that generation.

Mr X is such a wealth creator. During a lifetime of hard work and diligent planning, he finds himself nearing retirement, longing for nothing – save for his built-in need, as the *paterfamilias*, to assist with the financial stability and creation of opportunity for his only son, Junior. With this dilemma at heart, Mr X decides that he would like to give Junior a property, owned by the family for three generations, situated in Irene, Pretoria. The sentimental value of this historic residence aside, Mr X fully understands the impact that the provision of residence can have on Junior and his young family. Junior will have the opportunity to utilize his own wealth creation fruits to exponentially build further wealth, without having to service a bank loan for 20 years. Furthermore, the provision of this primary residence will create security and stability to Junior’s life as he and his family will not face the threat of losing their harbour, should Junior’s business dealings ever turn unfavourable.

On Mr X’s visit to his local attorney to request the transfer of the home in Irene to Junior, the attorney, Mr Planmaker, advised Mr X that his generosity towards his son, will cost him R600 000 in donations tax. The property, situated in the upmarket neighbourhood of Irene, is valued at R3 million. As the donor, Mr X will be liable to pay 20% donations tax for the gratuitous disposal of an asset held in his estate.
Mr Planmaker, however, assures Mr X that this is the better road to take, as the estate duty on an estate of Mr X’s size will, after his passing, attract estate duty of 20% for the first R30 million worth of assets and 25% on everything above R30 million. Not to mention the executor’s fees on the total value of the assets, as well as capital gains tax. Mr X soon realizes that, if he were to wait until his passing to give the Irene property to Junior, that the total value of his distributable estate will be much less than the cost of donating the property to him now. This will mean that a large portion of his hard-earned wealth will go towards taxes, with less ending up in the hands of his loved ones. This notion seemed ridiculous to Mr X.

Mr Planmaker, in agreement with Mr X’s frustration, proposes an alternative way to avoid paying the donations tax upon the transfer of the property to Junior. The proposed structure stood as follows:

a) Mr X is to sell the property to an inter vivos family trust, of which Junior and his descendants are the beneficiaries. The value of the property on transfer, will stand at R3 000 000. It should be noted that R3 million is the market value of the property and as a result this sale will not fall within the ambit of Section 58 of the ITA based on an inadequate consideration being received for the disposal at hand. An Offer to Purchase Agreement will be drafted and signed by the parties.

b) The terms of the sales agreement will entail the repayment of the capital amount by means of the creation of a credit loan account in favour of Mr X, in the books of Junior’s family trust. As with the trust’s other financial obligations, Mr X is to understand that the trust will repay the loan account, as and when the trust is able to do so.

c) In line with the provisions of Section 7C of the ITA, the loan account will attract interest at the prevailing repurchase interest rate, plus 1% per

255 Section 1(a) of the First Schedule of the Estate Duty Act 45 of 1955.
annum. This is an important factor as the negative effects of Section 7C will automatically be deemed to exist if the loan is not interest earning.\textsuperscript{256}

d) Mr Planmaker further advises Mr X that, if Mr X is to simply not demand payment of loan account from the trust, for three years, that the claim will prescribe and in effect cancel the debt due.

e) The only risk to this arrangement, would, according to Mr Planmaker, be if Mr X passes away within the period of 3 years and the executor of his estate claims fulfilment of the obligation to pay. To counter this risk, Mr Planmaker advises Mr X to award any outstanding loan account held by the trust, to the trust in terms of his Last Will and Testament. It is conceded that this will have the effect that the full value of the loan account (R3 million, plus the interest thereon) will be an asset in Mr X’s estate, on which he will pay estate duty and executor’s fees. Therefore, if Mr X is to pass away before the loan account could have prescribed, Mr X’s estate will not be in a better or worse situation than it would have been, was it not for the arrangement. The only benefit in this scenario, if Mr X is to pass away before the loan account prescribed, will be that neither Junior, nor the trust that benefits him, will have to actually produce the money of the loan at the time of the estate falling open.

4.2.2 Application of GAAR to the case study

4.2.2.1 Section 80A: Main purpose to avoid tax

From the above case study, it is clear that the main purpose of the arrangement from Mr X’s perspective is the transfer of wealth to his son with the use of an \textit{inter vivos} trust. This main purpose – in line with the findings in chapter 2 – forms part

\textsuperscript{256} Section 7C of the \textit{ITA} determines that where a natural person (such as Mr X) advances a loan to a trust, either directly or indirectly, and such a loan does not bear interest, or bears interest at an amount less than the prevailing official rate of interest, the difference between the actual interest charged on the loan, and what should be charged in compliance with this section, will be deemed to be a donation, on which donations tax is levied. In other words, the loan will either grow in interest, on an annual basis; or where interest is not being charged or charged below the official interest rate, it will be regarded as a donation of income.
of his subjective right to create and preserve wealth as part of his personal estate planning exercise.

However, the question must be asked whether the tax consequences associated with Mr X’s purpose – to give the property to the Trust – is the true reason and purpose of the avoidance arrangement as it has been designed by Mr Planmaker? If this is in fact the case, a further question to ask would be whether the limitations created by the GAAR, as it possibly infringes on Mr X’s subjective, legally protectable right, is the very reason why this arrangement was sought as a last resort?

In order to answer these questions, one will have to first look at Mr X’s intention at the very beginning when he approached Mr Planmaker. Mr X’s primary objective with the transfer of the property was to transfer family wealth over to the trust in which Junior benefits, in fulfilment of his subjective right to enjoy the full rights and ownership of his wealth as it pertains to his inherent right to further create and preserve it. Kindly take note that the primary purpose test under the new GAAR is an objective test. Looking at Mr X’s intention prior to the arrangement is not an attempt at a subjective test as per the previous GAAR, but simply an attempt to understand the reasoning for entering into the arrangement.

At this point it is fair to submit that this arrangement will not fall within the scope of the GAAR as the first requirement for the GAAR to apply is that the arrangement has the main purpose to avoid tax and, objectively speaking, before applying the tainted elements of the GAAR, the primary purpose of this arrangement, was not to avoid tax, but to transfer wealth across generations as part of his holistic estate plan.

However, in the second instance, one needs to look at the avoidance arrangement, structured by Mr Planmaker in favour of Mr X. This being the sale of property agreement, as well as the underlying understanding that the loan will be allowed to prescribe while Mr X will actively fail to collect same from the trust of which Junior

257 De Koker and Williams Silke on South African Income Tax para 19.38; para 3.4.2.1 above.
258 Section 80A of the ITA.
is a beneficiary. Reference needs to be made to the wording of Section 80H of the ITA, which allows the Commissioner to look into parts of an avoidance arrangement in order to determine whether it is an impermissible avoidance arrangement.

It is submitted that, just because the initial object of an avoidance arrangement steers clear from the scope of the GAAR, as it is an object other than mainly that of a tax saving, it does not automatically provides a blanket protection for the entire avoidance arrangement as the GAAR looks at steps and parts of the arrangement.259

In the case of Mr X, it is held that Mr X had the purpose in mind of transferring wealth to his son by utilizing a trust, as he exercises his subjective right recognised for purposes of this case study. However, once faced with possible methods to reach this purpose, Mr X was legally free to choose the arrangement that hosts the most beneficial tax treatment.260

In order to determine whether the arrangement at hand still had its purpose to transfer the wealth to Junior by means of the trust, one needs to objectively ask whether the effect of the grand sequence of events was to have the property transferred, or to create a situation where the transaction avoids the levy of donations tax.261 It is submitted that the Commissioner may objectively interpret the main purpose of the arrangement as it has been structured, not to transfer family wealth, but to transfer assets with the intention to knowingly avoid donations tax.262 It is common cause that the transaction at hand had the effect of avoiding donations tax which would have been levied, but for this arrangement.263 On this basis, the avoidance arrangement will fall within the interpretation of Section 80A of the ITA as a possible impermissible avoidance arrangement.

259 Section 80H of the ITA; Clegg and Stretch Income Tax in South Africa para 26.3.2; para 3.4.1 above.
260 Westminster-case and NWK-case.
263 Louw-case para 307.
4.2.2.2 Tainted Elements

The next test to apply is to determine whether there are any tainted elements in this avoidance arrangement in the form of abnormality, lack of commercial substance, and the misuse or abuse of the provisions of the Act.

4.2.2.2.1 Abnormality

The wording of the Act, as it pertains to the requirement of normality, asks whether the avoidance arrangement was entered into or carried out by means other than would normally be used for a bona fide purpose, or in whether rights and obligations was created that would otherwise have not been created in an arm’s length transaction.

It has been stated that this test is an objective one, in that the facts of the matter at hand needs to be determined on its own merits. What is normal for a businessman in a commercial transaction, will greatly differ from what is normal and natural for a paterfamilias in a family situation – hence the differentiation in the GAAR between Section 80A(a) of the ITA and Section 80A(b) and (c) of the ITA.

In the Louw-case special attention is paid to the requirement of abnormality – as it stood in terms of section 103 of the ITA at the time. In casu a party of engineers incorporated their practice in terms of which they sold their partnership to the incorporated company, for the issue of shares as consideration. The particular detail around the arrangement is what caught the Commissioner’s eye, including, for example, the fact that the agreement was not subject to the payment of interest; the payment of the purchase price was to be made only as and when the company was in a financial position to do so; and the previous partners

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264 Section 80A (a)(i) and (b) of the ITA.
265 Section 80A (a)(ii) of the ITA.
266 Section 80A (c)(ii) of the ITA.
267 Section 80A (b) of the ITA.
268 Section 80A (c)(i) of the ITA.
269 De Koker and Williams Silke on South African Income Tax para 19.38.
270 Louw-case para 292.
271 Louw-case para 292.
272 Louw-case para 292.
determined their salaries from the company without stipulation and considered same on the facts of each respective financial year.\textsuperscript{273}

The court referred to section 103(1)(ii) of the ITA and put extra emphasise on the wording "the nature of the transaction ...".\textsuperscript{274} The court held that one cannot ignore the special relationship of the partners of the business when applying the GAAR, as the Act specifically directs the Commissioner to look into the ‘nature’ of the arrangement\textsuperscript{275}. This principle was carried over to the new GAAR through the use of the words "means and manner" in Section 80A of the ITA and in terms of Section 80A(c)(i) of the ITA, where rights and obligations are created that would not have normally been created between persons dealing at arm’s length. In the Louw-case it was stated that the "normality yardstick cannot be applied as though the company were strangers".\textsuperscript{276} Judge Corbett held that the reality of the situation was that the practice was sold by the partners, who then became its shareholders and directors which means that the company will ultimately be controlled by the same individuals.\textsuperscript{277}

On this basis, Judge Corbett held that in his mind, the ‘abnormalities’ constituted by the Commissioner does not create abnormal rights and obligations, as per Section 80A(c)(i) of the ITA, if seen in the context of the nature of the relationship.\textsuperscript{278} For example, the fact that the repayment of the capital was said to be "as and when the company was in a financial position to do so", is a normal consideration given the fact that the company had very little capital initially and that the partners agreed that the repayment of the purchase price will come from the profits of the company.\textsuperscript{279} The same applies for the interest-free arrangement. By not paying interest, the company’s profitability increases, which will allow the capital to be settled sooner, while directly benefitting the partners – who remained in control of

\textsuperscript{273} Louw-case para 294.  
\textsuperscript{274} Louw-case para 302.  
\textsuperscript{275} Louw-case para 302.  
\textsuperscript{276} Louw-case para 302.  
\textsuperscript{277} Louw-case para 302.  
\textsuperscript{278} Louw-case para 302.  
\textsuperscript{279} Louw-case para 302.
the business through their professional services. Judge Corbett meant that this was sound business, even though it was not an arrangement that would be conducted by parties dealing at arm’s length. De Koker and Williams noted that the Louw-case established that where parties to an arrangement are not strangers but are in a special relationship, the criteria of normality should be considered in the light of the nature of that special relationship.

It was the nature of the agreement; the parties’ special relationship as business partners; the fact that they remained in control of the company and remained the source of profitability through their professional fee writing and the fact that they continued to hold the interest of the company through its shareholding that contributed to the fact that the Louw-case transaction – not at arm’s length – cannot be seen as abnormal if considered on its merits.

In the current exemplary case study, the argument will follow the logic of the Louw-case. Is it abnormal for a father to want to give property to his son, via a trust, in an attempt to secure his financial stability? It cannot be said that it is. In the Pretoria Special Tax Court matter of XYZ Bank Ltd v The Commissioner for SARS 10808 (2001), the appellant relied on Australian authority to illustrate that family dealings serves as an acceptable purpose as it pertains to the normality of a transaction. In the case in reference, Newton v FCT (1958) 1998 CLR 1, Lord Denning stated the following:

In order to bring the arrangement within the section you must be able to predicate – by looking at the overt acts by which it was implemented – that it was implemented in that particular way so as to avoid tax. If you cannot so predicate but have to acknowledge that the transactions are capable of explanation by reference to ordinary business or family dealings, without necessarily being labelled as a means to avoid tax, then the arrangement does not come within the section.

Is it abnormal for a father to sell to his son, by means of a family trust, a property, the repayment of which will occur, at a later stage? Perhaps not. It can be

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280 Louw-case para 302.
281 Louw-case para 302.
283 Newton v FCT (1958) 1998 CLR 1 at 8.
understood that a father will not want to apply pressure on his son and thereby give him the flexibility to repay the capital amount as and when the cashflow of the *inter vivos* trust, allows for it.

Keep in mind that the requirement for abnormality will be applied on the facts of the matter as it stood before the court. In other words, the arrangement as it was entered into.

4.2.2.2.2 Lack of commercial substance

Discussion of the tainted element, being lack of commercial substance, is not applicable in this scenario. It has been held above that the normality requirement has been applied where an arm’s length transaction, as envisioned by Section 80A(c)(i), is lacking, due to the special relationship between the parties. The application of a commercial substance test, as applicable to a *bona fide* business purpose, is therefore not relevant in this non-business scenario.

4.2.2.2.3 Misuse or abuse of the Act

The basis on which a sale was chosen by Mr Planmaker to facilitate the transfer of the property, as opposed to a pure donation, was because the sale does not constitute a disposal without the expectation of consideration. In other words, the estate planner, choosing a sale, confirms that his estate will not be reduced by the arrangement, as one asset will be replaced with another. As a result, no negative tax consequences are connected to the sale, as opposed to a donation which requires the payment of 20% donations tax. By Mr X stating outright (in confidence) that he will not be collecting the payment consideration and instead allowing it to prescribe, he is abusing the Act to the extent that he wants to be taxed on a set of facts, but plan to change the facts at a later stage to fit his agenda. This deliberate plan falls within the definition of an arrangement,²⁸⁴ in terms of the GAAR, as it is a clearly stated understanding with the aim to avoid tax.

²⁸⁴ Para 4.3.1, above.
4.2.2.3 Outcome

It has been shown that the avoidance arrangement contemplated by Mr Planmaker in favour of Mr X falls firmly within the scope of the GAAR in that it results directly or indirectly in the misuse of the provisions of the Act.\textsuperscript{285}

4.2.3 Effect of GAAR on subjective right

With reference to the research question at hand, it can perhaps be said that if it was not for the limitation created by the ITA that the simulated transaction entered into, would not have been arranged. In other words, if it was not for the object that Mr X had in mind to transfer wealth to his son’s family trust, in an attempt to secure and further grow the family wealth across generations, there would not have been a transaction at all.\textsuperscript{286} This argument does not look to legitimize the simulation of the arrangement but instead wishes to ask the question as to the balance of interest from treasury’s goal of the collection of tax on the one hand, and the protection of an individual’s subjective rights on the other hand. Are the provisions of the ITA, specifically the requirements of the GAAR, in effect infringing upon an individual’s legally protectable right to create and preserve his or her wealth? Perhaps.

4.3 Avoidance arrangement 2: Main purpose is to create wealth with funds saved from the tax benefit itself

4.3.1 Case study

Going into the makings of an avoidance arrangement that truly pushes the letter of the law to such an extent that an overly creative solution may fall foul to the scope of the GAAR is one end of the coin. Another possibility where an individual’s subjective right to his or her interest in his or her wealth creation and preservation

\textsuperscript{285} Section 80A(c)(ii) of the ITA.
\textsuperscript{286} Conhage-case 391.
is in direct contradiction with the purpose of the GAAR will be explored in this case study.

At this point in this research, repeating the mantra that every taxpayer is legally allowed to choose the most tax beneficial solution to his purpose, seems like overkill. However, it doesn't make it less applicable when a business owner, Mr Moneybags faces two possible means in which to receive a repayment of a loan made by himself to a private company of which he holds 100% shareholding in.

Mr Moneybags lend an amount – the value of which is of no concern – to a company in which he owns the entire shareholding. He has one of two options in which to structure this arrangement in order to receive the best return on his investment (being the loan in question). The first, and perhaps the more traditional option, will be to set up a loan, which is interest bearing, which the company can pay back in fixed instalments. This option will henceforth be referred to as the ‘loan-arrangement’. Alternatively, he can set up the loan agreement, following which he can take up redeemable preference shares in the company to the same value of the loan at hand. In this fashion, the company will repay the previously said loan, through dividends on the preferent shares held by Mr Moneybags. Preference shares, while considered to be equity, are structured as debt instruments. Holders of preference shares exchanged the debt that they advanced to a company for the issue of preference shares. The interest on their loan is repaid in the form of preferent share dividends, which is linked to a pre-agreed interest rate. Preference shareholders have preferent claims against the company, should it be liquidated, and will receive their payment from the company capital, ahead of ordinary shareholders. This option will be referred to as the ‘dividend-arrangement’.

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The loan-arrangement will mean that Mr Moneybags will pay normal income tax of 45% on the interest earned on the investment. For purposes of this arrangement, it is assumed that he already utilised his normal tax exemption on interest earned.

The dividend-arrangement will see Mr Moneybags earn his returns in the form of a dividend declared on his preferent shares. The company will pay dividend withholding tax to the amount of 20% and Mr Moneybags will not pay income tax based on section 10(1)(k)(i) of the ITA. This arrangement has the result that Mr Moneybags will have a return on investment of 25% more than he would have had with the loan-arrangement. The increase in the return on investment will be in the form of the tax saved (45% - 20% = 25%).

4.3.2 Application of GAAR to the case study

4.3.2.1 Section 80A: Main purpose to avoid tax

From the outset, it can be acknowledged that Mr Moneybags was looking for a solution to maximise the return on his investment. However, he soon found that the only way to do this is by the tax saving itself. The increased return on investment of 25%, which is nothing other than the tax saving itself, is the result of Mr Moneybags paying that amount of tax less and not the company increasing the repayment in some way.

Does this then mean that the primary purpose of the arrangement was to avoid tax? Or can it be said that the primary reason for the arrangement was the enjoyment of his subjective right, as defined in chapter 2, with means to achieve such purpose being by way of a legally allowable tax saving?

In line with Mr Moneybags’ subjective right to the interest he has in the creation of his wealth, it is a fair statement that the need to want to receive the maximum return on investment is part of the enjoyment of his subjective right.

Reference is made to the NWK-case, where the court showed how weighing up the benefits and pitfalls of two different arrangements, speaks to the intention of the taxpayer, as he considered the facts at hand.
In this case study, the effect of the dividend-arrangement, while beneficial for Mr Moneybags’ personal income tax position, is not as beneficial for the company from a tax perspective. In the loan-arrangement, the company would have been allowed to legally deduct the amounts charged in interest, from its taxable income which in turn would have added to the company’s after-tax profitability. With the dividend-arrangement on the other hand, the company does not enjoy this benefit as dividends are declared from the after-tax profit. Keep in mind that these considerations greatly affect Mr Moneybags, as he is the sole shareholder of the company. In other words, what he saves as a tax benefit in his personal name, he losses as a tax benefit in the books of his company.

Taking this fact into consideration, it is submitted that the primary objective in the mind of Mr Moneybags when choosing the dividend-arrangement, was purely to receive the best return on his investment, with the added benefit of a tax saving of 25% in his income tax return.

While the determination of the application of the GAAR stops the moment it has been found that tax was not the primary purpose, in the light of full disclosure, clarity can be obtained when further attention is paid to the tainted elements of the GAAR.

4.3.2.2 Tainted Elements

4.3.2.2.1 Abnormality

It is normal practice, between parties dealing at arm’s length to issue redeemable preference shares to a lender, to finance the company. By utilising this method to reach the same objective, no abnormal rights or obligations have been created. It can therefore not be said that this avoidance arrangement has elements which is abnormal in the course of business.

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290 Section 11 of the ITA.
291 SARS Binding Private Rulings “Refinancing of debt through preference share funding” 191 – 26 March 2015.
4.3.2.2.2 Lack of commercial substance

The arrangement does not lack commercial substance in that it is not a simulated transaction, seeking to hide the true intention of the taxpayer. It does not result in round-trip financing as the rights and obligations created remain in force and effect both in the estate of Mr Moneybags and in the books of the company who will honour the terms of the agreement. Finally, there are no offsetting elements as the tax benefit obtained is not achieved by offsetting funds or tax against each other, it instead makes use of different types of tax.

4.3.2.2.3 Misuse or abuse of the Act

The Act is not misused or abused in any manner. The saving of normal tax through the avoidance of the payment of income tax on interest earned by substituting it with dividend withholding tax is allowable use and interpretation of the ITA in the spirit of the Act.

4.3.2.3 Outcome

On the basis that the arrangement that Mr Moneybags structured is not considered as having a main purpose to avoid tax, but rather to increase a return on investment by means of a tax benefit, the GAAR will not find application and this will be seen as a permissible avoidance arrangement.

However, the true facts behind a similar situation may have the Commissioner disagreeing with this opinion, which will call for case law development where the primary purpose is not tax avoidance, but a financial benefit where the tax saved represents the benefit planned for.

4.3.3 Effect of GAAR on subjective right

It is submitted that if the above case study of Mr Moneybags was to be interpreted as having tax as its primary purpose, thereby making it an impermissible tax avoidance arrangement, that it will answer the research question in that the GAAR is in fact infringing upon an individual's subjective right of wealth creation and
preservation. Further research into the balance of these rights and objectives will need to be conducted.

It has been said that Mr Moneybags is free to take the most tax favourable route to reach his object. If this right is exercised by means of legal tax planning, as part of his holistic estate plan, it cannot be said that the primary objective of an arrangement is tax savings, just because the savings incurred by the arrangement is presented in the form of tax.

An attack by the Commissioner on this arrangement will result in the GAAR depriving Mr Moneybags from the free enjoyment of his legally protectable right to create and preserve his right.

4.4 Conclusion

The above case studies illustrated the application of the GAAR in two sets of facts, as it pertains to a holistic estate plan. In the first, the primary object of the wealth creator was to transfer wealth across generations, in the most tax efficient manner. In the second, the primary object was the increase on return of an investment, through the saving of tax.

In the first instance it was showed that in order for Mr X to achieve his object, that he misplaced his focus and entered into an impermissible avoidance arrangement – as tested against the GAAR. The effect of the infringement of Mr X’s subjective right to create and protect his collective wealth by the implementation of the GAAR, is that it forces tax payers to use creative structuring in a failed attempt to reach their object of catering to their family’s long term needs, without attracting unfavourable tax consequences.

The second case study showed the characteristics of legal tax planning, with no simulations, fraudulent disclosures or abnormal features. However, the object at hand was the creation of wealth, as part of the enjoyment of Mr Moneybags’ right to an interest in the creation of his wealth, obtained by means of a tax saving itself. Mr Moneybags’ purpose should pass the test of the GAAR.
Chapter 5 Conclusion

5.1 The research question

Two interests, regulated by two separate areas of the law: the one, a yet to be recognised legally protectable interest in wealth creation and preservation; and the other, firmly positioned statutory provisions of the GAAR, standing opposite each other. One may only consider these two interests to be in a balancing act, if both were equally recognised, receiving equal protection – both from external influences and from each other.

This research set out to answer the question, what the effect of anti-avoidance tax legislation is on the protection of a legal interest in wealth creation and preservation. In order to do so, various secondary questions were posed, with the aim in mind to break the key issues behind the research question into smaller, more easily digestible portions.

It is a well-known principle in our South African common law that an individual is free to order his or her affairs in whatever manner brings about the most beneficial tax treatment.\(^{292}\) This research challenged this statement in the sense that the limitations imposed by the GAAR, through its various requirements\(^ {293}\) may have the effect that an individual’s apparent freedom to structure his affairs as he pleases to enjoy tax benefits, is continuously infringed on. This results in the limitation of an individual’s right to enjoy the legal entitlements\(^ {294}\) of his or her interest in his or her wealth creation and preservation.

Before any further questions could have been asked, the first item on the agenda was to determine, in chapter 2, whether an individual’s interest in the creation and preservation of his or her wealth is an interest possible of enjoying legal recognition and protection. Only once that has been determined, could the criteria and the working of the GAAR be researched in chapter 3, as it pertains to the interests

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\(^{292}\) Westminster-case; NWK-case; Kilburn-case; Conhage-case.

\(^{293}\) Section 80A – L of the ITA.

\(^{294}\) Para 2.1.4.2 above.
identified in chapter 2. Finally, chapter 4 put the findings of chapter 2 and 3 to the test in the form of two case studies. The first case study intentionally played right into the ambit of the GAAR, while the second case study held up against the application of the GAAR, based on the findings of chapter 2.

5.2 The requirements for the recognition of a legally protectable interest

Chapter 2 briefly researched the nature of the legal protection afforded to interests which an individual may have, in other areas of the law, such as the Law of Insurance and the Law of Matrimonial Property. In the first instance the basis of the concept of an insurable interest was considered, only to determine that the legal protection afforded does not truly pertain to the interest as such, as an insurable interest was merely the object of the contract of insurance. In the latter instance, the principles of the application of the accrual system were considered in order to draw a similarity between the interest a spouse has in the wealth of his or her spouse at divorce or death, and the interest an individual has in his or her own wealth. This proved to be of little value as the interest created in the Matrimonial Property Law as it pertains to the accrual system, only comes into existence at death or divorce. The author is of the opinion that the legally protectable interest in the creation and preservation of one’s wealth is a continuous, lifelong interest.

Finally, after a comprehensive study into the Doctrine of Subjective rights, it was determined that the interest seeking protection, firmly fits within the criteria set to qualify as a subjective right. The doctrine encompasses two interdependent relationships: The first, is the relationship between a legal subject (the wealth creator) and the legal object (the wealth); and the second is the manner in which

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295 Para 2.1.2 above.
296 Para 2.1.4.4 above.
297 *Castellain v Preston* (1883) 11 QBD 380 (CA) 397; Reinecke, Van Niekerk, Nienaber *LAWSA* 28.
298 Para 2.1.4.4 above.
299 Neethling and Potgieter *Neethling-Potgieter-Visser Deliktereg* 55.
300 Para 2.1.4 above.
301 Knobel 2001 *THRHR* 574.
302 Joubert 1958 *THRHR* 111.
this relationship is enforced between the legal subject (the wealth creator) and other legal subjects.

There are currently five categories of subjective rights, being (a) real rights; (b) personal rights; (c) personality rights; (d) intellectual property rights; and (e) personal immaterial property rights. This study put the interest that an individual has in the creation and preservation of his or her wealth to the test in each instance in the above-mentioned categories. After critical evaluation and consideration of the interest seeking legal protection, it was finally concluded that the interest will safely fall within the ambit of a personal immaterial property right – eligible for enjoying legal protection as a subjective right. An individual’s interest in the creation and preservation of his or her wealth is closely linked to his personality rights; holds separate components of real rights and personal rights, while remaining fully intangible and contains substantial economic value and use to its owner.

### 5.3 The criteria for the application of the GAAR on an avoidance arrangement

In order to answer the research question at hand and determine what the effect of the GAAR is on an individual’s subjective right to the creation and preservation of his or her wealth, it was crucial to critically evaluate the true substance of the GAAR as it is contained in Section 80A-L of the ITA.

Section 80A of the ITA sets out to combat impermissible avoidance arrangements, as defined in Section 80L of the act. Chapter 3 critically positioned the concept of an avoidance arrangement, within the scope of holistic estate planning as a

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303 Knobel 2001 *THRHR* 574.
304 Neethling 1987 *THRHR* 316.
305 Para 2.1.4.2-2.1.4.6 above.
306 Para 2.2.2 above.
307 Para 2.2.4 above.
308 Para 2.2.4 above.
309 Section 80A of the *ITA*; Kujinga 2014 *CILSA* 429.
science,\textsuperscript{310} as well as emphasising the crucial difference between tax avoidance and tax evasion.\textsuperscript{311}

In summary, chapter 3 concluded that in order for an avoidance arrangement to fall within the ambit of the GAAR, the transaction in question had to have its main or sole purpose to avoid tax,\textsuperscript{312} plus have any one of the so-called tainted elements,\textsuperscript{313} as set out in Section 80A, present. These tainted elements are the factor that turns a permissible avoidance arrangement into an impermissible avoidance arrangement.\textsuperscript{314} These tainted elements, being abnormality,\textsuperscript{315} a lack of commercial substance\textsuperscript{316} and the misuse or abuse of the ITA,\textsuperscript{317} were researched to fully understand the pitfalls and grey areas of which holistic estate planning arrangements should steer clear of.\textsuperscript{318}

\textbf{5.4 The legally protectable interest in wealth creation and preservation as an acceptable bona fide purpose for tax avoidance}

With the interest that an individual has in the protection of his or her wealth, as a legally protectable subjective right, as determined in chapter 2, it is submitted that avoidance arrangements designed with the primary goal to advance and enjoy this right, should be considered a \textit{bona fide} purpose for legal tax avoidance. As a fully transparent, comprehensive estate plan has one of its main objectives to save tax both during the life of the wealth planner, and thereafter,\textsuperscript{319} a tax avoidance arrangement as part of such an elaborate estate plan, should not be interpreted as to fall within the ambit of Section 80A (1) of the ITA, as having the primary purpose of the arrangement to avoid tax.

\textsuperscript{310} Para 3.4.1 above.
\textsuperscript{311} Para 3.2 above.
\textsuperscript{312} Section 80A (1) of the \textit{ITA}.
\textsuperscript{313} Explanatory Memorandum on the Revenue Laws Amendment Bill 2006 62 and 63.
\textsuperscript{314} Section 80A (1)(a)-(c) of the \textit{ITA}.
\textsuperscript{315} Section 80A (a)(i) and (b) of the \textit{ITA}.
\textsuperscript{316} Section 80A (a)(ii) of the \textit{ITA}.
\textsuperscript{317} Section 80A (c)(ii) of the \textit{ITA}.
\textsuperscript{318} Para 3.4.2.2.1 above.
However, should this interpretation of Section 80A(1) of the ITA fail, as a result of an objective review\textsuperscript{320} of steps or parts of the arrangement,\textsuperscript{321} as opposed to a subjective review of the wealth creator’s true intention in the bigger scheme of his wealth plan, at least one of the tainted elements of the GAAR should be present before the consequences of the GAAR applies.\textsuperscript{322}

Chapter 4 posed two different case studies to test this statement. In the first case study, the primary purpose of the avoidance arrangement was to transfer wealth from one generation to another through the use of a trust as an estate planning instrument. However, in a deliberate attempt to outsmart the ITA, the arrangement attempted to create rights and obligations, that would not have otherwise been created, thereby indirectly misusing the provisions of the ITA, with the primary goal to save tax. Ironically, with the application of the tainted elements of the GAAR, the case study resulted in the arrangement being an impermissible avoidance arrangement.

The effect of the infringement of the wealth creator’s right to legally create and protect his combined wealth, by the GAAR, resulted in tax evasion – however morally inexcusable – as a failed attempt at the enjoyment of his subjective rights.

The second case study did not beat around the bush and instead had the wealth creator utilise, as a primary purpose, the more favourable provisions of the ITA to grow his wealth with the tax saved. The application of the GAAR immediately found that the primary purpose of the arrangement was to save tax, which called for the investigation into the presence of tainted elements.

On the findings of chapter 2, which acknowledges the subjective right that an individual has in the creation and protection of his or her wealth, the case study’s arrangement could not be found to be abnormal, simulated or an abuse of the ITA. It is submitted that the scenario posed in the second case study has not been challenged in a South African court, and that the planning tools utilised may in itself

\textsuperscript{320} De Koker and Williams \textit{Silke on South African Income Tax} para 19.38.
\textsuperscript{321} Section 80H of the \textit{ITA}.
\textsuperscript{322} Section 80A (1)(a)-(c) of the \textit{ITA}.
be questionable strategies. However, it does not take away from the fact that, where the subjective right, as defined, is acknowledged, the application of the GAAR can be done in a more holistic, open-minded fashion.

The effect of the anti-avoidance tax legislation on the protection of a legal interest in wealth creation and preservation comes down to a possible infringement of this subjective right, but only for as far as the interpretation of the ITA is limited to not take the science of full disclosure, estate planning exercise into consideration.

This may call for a subjective approach to the GAAR, as per the previous regime,\textsuperscript{323} as opposed to the objective approach introduced in the current GAAR.\textsuperscript{324} Furthermore, the consideration of steps or parts of an arrangement as per Section 80H of the ITA, should further be investigated as the evaluation of parts of an arrangement in isolation, cannot be said to be a fair assessment of an arrangement that has been designed as part of a holistic estate plan. Finally, if a subjective approach is once again adopted, the surrounding circumstances and supporting documents of the enjoyment of an individual’s subjective right to wealth creation and preservation will form a crucial part of the Commissioner’s exercise of its discretionary powers and should also encourage practitioners to adopt good practice principles and compliance procedures.

\textsuperscript{323} Section 103(1) of the \textit{ITA}.
\textsuperscript{324} Section 80A-L of the \textit{ITA}. 
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