THE TAX COURT OF SOUTH AFRICA
(JOHANNESBURG)

(1)	REPORTABLE: Yes
(2)	OF INTEREST TO OTHER JUDGES: Yes.
(3)	REVISED.

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DATE	SIGNATURE

Case no: IT14294

In the matter between:

THE COMMISIONER FOR THE
SOUTH AFRICAN REVENUE SERVICE Excipient

and

MASSMART HOLDINGS LIMITED Respondent

Case Summary: **Tax Court – Practice – Exception – Procedure of excepting to a pleading finds application in an appeal to the tax court.**
Exception that statement of grounds of appeal lacks averments sufficient to sustain the appeal, dismissed.

JUDGMENT

MEYER J

[1] The excipient, the Commissioner for the South African Revenue Service (SARS), excepts to the r 32 statement of grounds of appeal of the appellant (the present

respondent), Massmart Holdings Limited (Massmart), on the grounds that it lacks averments sufficient to sustain the appeal.

[2] The first question to be determined is whether the procedure of excepting to a pleading finds application in an appeal to the tax court. SARS' exception is brought in terms of r 23(1) of the Uniform Rules of Court, read with r 42(1) of the Tax Court Rules. Rule 23(1) of the Uniform Rules of Court affords a party the procedural right to deliver an exception where 'any pleading is vague and embarrassing or lacks averments which are necessary to sustain an action or defence'. Rule 42(1) of the Tax Court Rules provides that if 'these rules do not provide for a procedure in the tax court, then the most appropriate rule under the Rules for the High Court made in accordance with the Rules Board for Courts of Law Act and to the extent consistent with the Act and these rules, may be utilised by a party or the tax court'.

[3] Rule 18(4) of the Uniform Rules of Court provides that '[e]very pleading shall contain a clear and concise statement of the material facts upon which the pleader relies for his claim, defence or answer to any pleading, as the case may be, with sufficient particularity to enable the opposite party to reply thereto'. Rule 22(2) provides that a 'defendant shall in his plea either admit or deny or confess and avoid all the material facts alleged in the combined summons or declaration or state which of the said facts are not admitted and to what extent, and shall clearly and concisely state all material facts upon which he relies'.

[4] A taxpayer, in terms of s 107 of the Tax Administration Act, 28 of 2011 (the TAA), has the right to 'appeal against the assessment . . . to the tax board or tax court in the manner, under the terms and within the period prescribed in [the TAA] and the [Tax Court Rules]'. An appeal to the tax court – called an appeal because the taxpayer appeals against SARS' assessment or decision – is in fact a trial. Evidence may be lead, and the taxpayer bears the burden of proof. SARS and the appellant in the tax court must also exchange 'pleadings'. SARS, in terms of r 31(1) of the Tax Court Rules, 'must deliver to the appellant a statement of the grounds of assessment and opposing the appeal'. An appellant, in terms of r 32(1), 'must deliver to SARS a statement of grounds of appeal'. SARS' statement of the grounds of assessment and opposing the

appeal must, inter alia, set out a clear and concise statement of 'the material facts and legal grounds upon which SARS relies in opposing the appeal' (r 31(2)(c)) and an appellant's statement of grounds of appeal must similarly set out 'the material facts and the legal grounds upon which the appellant relies for the appeal and opposing the facts or legal grounds in the statement under rule 31' (r 32(2)(c)).

[5] The statement of grounds of assessment and opposing the appeal and the statement of grounds of appeal provided for in rules 31 and 32 of the Tax Court Rules have the same object as pleadings in the Superior Court Practice; to define the issues so as to enable the other party to know which case it has to meet. (See *Robinson v Randfontein Estates GM Co Ltd* 1925 AD 173 at 198; *Presidency Investments (Pty) Ltd v Patel* 2011 (5) SA 432 (SCA) at 440 A-B.) The parties may, in terms of r 35 of the Tax Court Rules, agree that a statement of grounds of assessment and opposing an appeal or a statement of grounds of appeal or a reply to a statement of grounds of appeal, be amended, and, if the other party does not agree to the amendment, the party who requires the amendment may apply to the tax court for such relief. It is trite that 'the modern tendency of the Courts lies in favour of an amendment whenever such an amendment *facilitates the proper ventilation of the disputes between the parties*'. (See *Rosenberg v Bitcom* 1935 WLD 115 at 117; *Magnum Simplex v The MEC Provincial Treasury* (556/17) [2018] ZASCA 78 (31 May 2018), para 9.)

[6] The exception procedure is a useful procedure 'to weed out cases without legal merit'. (See *Telematrix (Pty) Ltd v Advertising Standards Authority* SA 2006 (1) SA 461 (SCA), para 3.) It follows, therefore, as a matter of logic, that if either the r 31 statement or the r 32 statement does not contain averments which sustain the relevant party's case or is without legal merit, then the exception procedure provided for in the Uniform Rules of Court is equally an appropriate mechanism to deal with the question in the tax court. The exception procedure is consistent with the TAA and the Tax Court Rules. That the application of the exception procedure to 'pleadings' in the tax court is not contentious, is clear from *ITC* 1899 79 SATC 315. There, SARS filed a notice of exception to the appellant's amendment of its grounds of objection. Eksteen J upheld the exception on the basis that the proposed amendment was not legally sustainable.

[7] The high-water mark of Massmart's objection to the application of the exception procedure to the tax court practice appears to be that there may be circumstances that would render it undesirable to allow an exception before the tax court has heard all the evidence. The argument places the cart before the horse. The test on exception is whether, on all possible readings of the facts, no cause of action or defence is made out. It is for the excipient to satisfy the court that the conclusion of law for which the other party contends cannot be supported on any interpretation that can be put forward by the facts (See *Children's Resources Center Trust v Pioneer Food (Pty) Ltd and Others* 2013 (2) 213 (SCA), para 36.) In other words, as was held in *Eastern Produce Cape (Pty) Ltd t/a Linton Park Wines v Glen Fourie International Consultancy* [2011] ZAWCHC 229 (17 May 2010) para 15, '[a] pleading is only excipiable if no possible evidence lead on the pleadings can disclose a cause of action or defence'. (See also *Theunissen v Transvaalse Lewende Hawe Koöp Bpk* 1988 (2) SA 493 (A) at 500; *Amalgamated Footwear and Leather Industries v Jordan and Co Ltd* 1948 (2) SA 891 (C) at 893.) Furthermore, in appropriate cases a court will decline to grant an exception and require that the decision whether or not the pleading discloses a cause of action or defence be decided after the hearing of evidence at the trial. (See *Children's Resource Center Trust* para 37.) I conclude, therefore, that the procedure of excepting to a pleading finds application in an appeal to the tax court.

[8] The context within which SARS brought the exception is uncontroversial. In its 2007 to 2012 income tax returns, Massmart claimed capital losses in relation to an employee share trust scheme. On 26 June 2013, SARS issued tax assessments to Massmart in respect of the 2007 to 2009 years of assessment and, on 28 August 2014, in respect of the 2010 to 2012 years of assessment. SARS disallowed the capital losses claimed in respect of the employee share trust scheme and imposed understatement penalties. Massmart lodged objections to those assessments, which objections SARS disallowed. Massmart then lodged a notice of appeal against the disallowance of its objections. SARS delivered its statement of grounds of assessment opposing the appeal in terms of r 31 of the Tax Court Rules, and Massmart delivered its statement of grounds of appeal in terms of r 32. The appeal will be heard by the full tax court later this year (the first appeal).

[9] SARS brought an interlocutory application in the first appeal before the tax court. Therein it objected to Massmart's statement of grounds of appeal on the basis that it includes grounds of appeal that constitute new grounds of objection that were not included in Massmart's notice of objection in terms of r 7 of the Tax Court Rules when it objected to SARS' assessments in respect of the 2007 to 2012 years of assessment. SARS' interlocutory application was heard by Keightley J on 7 August 2017 in the tax court. Judgment was handed down on 2 September 2017. The application was dismissed with costs, including those of senior counsel.

[10] In her judgment, Keightley J summarised the material facts pertaining to the alleged new grounds of appeal as set out in Massmart's statement of grounds of appeal, thus:

'[10.1] The Trust Deed (governing the Trust) required the Trust, on the instruction of Massmart, to grant call options to certain employees to acquire shares at a strike price at a later date.

[10.2] When an employee exercised an option, the Trust had to acquire the shares and sell them to the employee at the stated strike price. The shares were acquired at the expense of Massmart.

[10.3] The Deed further required Massmart to bear the losses made by the Trust as a result of granting the options, in circumstances where the price obtained from employees based on the strike price was less than the cost of acquiring the shares.

[10.4] Massmart bore a *de facto* commercial loss arising from these acquisitions and disposals of shares. Consequently, Massmart incurred expenditure equal to the share sale losses incurred by the Trust resulting from Massmart's instructions to the Trust to issue share options to the employees.'

[11] Keightley J concluded (para 31)-

'. . . that on a proper interpretation of TCR 32(3), as a matter of law, Massmart was not precluded from raising a new ground of objection in its statement'

and that the new grounds of objection set out in Massmart's statement of appeal were in any event in substance the same as those stated in terms of its initial objection under r 7(1) (para 33). She held that the objection (para 35)–

'. . . still involves what Massmart says were capital losses it suffered as a result of the employee share option scheme. It no longer relies on the earlier contention that this was ascribable, from

a legal perspective, to Massmart being the sole beneficiary of the Trust, with vested rights, and hence vested losses. It now intends to contend in the appeal that its capital losses arose out of the fact that in terms of the Trust Deed, Massmart funded the acquisition of the shares, and bore the losses, both from a legal and *de facto* perspective.'

And that (para 36)-

'. . . [t]he original objection was based on Massmart being the sole beneficiary of the Trust, while the new grounds place reliance on Massmart funding the purchase of the shares and bearing, both legally and *de facto*, the losses suffered in the process. In substance, it is the same issue that is before the court on appeal: whether the capital losses arising from the employee share option scheme are capital losses which are deductible by Massmart for capital gains tax purposes.'

[12] In its 2013 income tax return, Massmart claimed a capital loss of R122 008 055 in respect of shares in the name of the Massmart Holdings Limited Employee Share Trust (the trust) in the capital of Massmart (the shares), disposed of by the trust to employees of Massmart and/or its subsidiaries at a sum less than the base cost of the shares. The shares were owned by the trust. Massmart avers that the trust deed required the trust, on the instruction of Massmart, to grant call options (the options) to certain employees (the offerees) to acquire shares at the strike price as at a later date. When the offerees exercise the options, the trust sold the shares to the offerees at the strike price. In order to be able to deliver the shares thus sold to the offerees, the trust generally had to buy shares in the market. The acquisition and disposal of the shares typically resulted in a loss, which loss was factually borne by Massmart. In the result, so Massmart avers, it actually incurred expenditure equal to such losses incurred by the trust as a result of it directing the trust to issue the options to the offerees. The *raison d'être* of the share incentive scheme is to facilitate the acquisition of shares in Massmart by its own and other group employees, which scheme is considered to be in the interests of Massmart, i.e. the employees will work hard to achieve an increasing share price, and this will benefit both Massmart and the employees who are shareholders *via* the trust structure.

[13] On 14 March 2016, SARS issued an assessment to Massmart in respect of its 2013 year of assessment. Again, the assessment disallowed the claimed capital losses

in respect of the same employee share option scheme. Massmart lodged an objection against the assessment, which SARS again disallowed. Thereafter, Massmart lodged a notice of appeal against the disallowance of the objection. SARS delivered its r 31 statement and Massmart responded by delivering its r 32 statement (the second appeal). The present exception is directed at Massmart's statement of grounds of appeal, SARS contending that it does not contain sufficient allegations to sustain a claim to a capital loss as contemplated by para 4 of the Eighth Schedule to the Income Tax Act, 58 of 1962 (the ITA), read with the definition of 'asset' in para 1 and the definition of 'base cost of an asset' in para 20(1)(a).

[14] Part 2 of the Eighth Schedule deals with taxable gains and assessed capital losses. At the relevant time, s 26A of the ITA provided that '[t]here shall be included in the taxable income of a person for a year of assessment the taxable capital gain of that person for that year of assessment, as determined in terms of the Eighth Schedule'. Paragraph 2 of the Eighth Schedule applied to assets owned and disposed by the relevant taxpayer. Paragraph 1 defined 'asset' as including '(a) property of whatever nature, whether movable or immovable, corporeal or incorporeal, excluding any currency, but including any coin made mainly from gold or platinum; and (b) a right or interest of whatever nature to or in such property'. Paragraph 11(1) provided that '[s]ubject to subparagraph (2), a disposal is any event, act, forbearance or operation of law which results in the creation, variation, transfer or extinction of an asset, and includes- . . . (b) the forfeiture, termination, redemption, cancellation, surrender, discharge, relinquishment, release, waiver, renunciation, expiry or abandonment of an asset'. Paragraph 4 provided that '[a] person's capital loss for a year of assessment in respect of the disposal of an asset – (a) during that year, is equal to the amount by which the base cost of that asset exceeds the proceeds received or accrued in respect of that disposal'. And paragraph 20 (1)(a) provided that '[d]espite section 23(b) and (f), but subject to paragraphs 24, 25 and 32 and subparagraphs (2) and (3), the base cost of an asset acquired by a person is the sum of – (a) the expenditure actually incurred in respect of the cost of acquisition or creation of that asset'.

[15] Massmart avers that it acquired a right against the trust to require the trust to issue options to the offerees and, on the exercise of such options, to acquire shares to the extent necessary, at Massmart's expense, and to deliver them to the offerees at the strike price specified in the option contracts. Massmart contends that, pursuant to the arrangement between it and the trust, its right (to require the trust to issue options to the offerees and to satisfy them when exercised by the offerees) was extinguished upon the trust performing its obligations by delivering the shares to the offerees on exercise of the options. In that manner, so Massmart contends, it incurred a capital loss of R122 008 055 during the 2013 year of assessment. It contends that the expenditure was directly related to Massmart's action in directing the trust to issue the options to the offerees and to satisfy those options on the exercise thereof by the offerees.

[16] SARS' exception is brought on two main grounds: First, that what has been claimed as an 'asset' is not an asset as defined in para 1 of the Eighth Schedule. SARS argues that the source of Massmart's alleged 'right' is not clear from its statement of grounds of appeal nor does it indicate the nature of the right or alleged 'asset'. An 'asset', SARS argues, on a proper contextual interpretation, must have commercial and economic value and the proceeds in respect of the disposal of the asset should bear some relationship to the value or commercial value of the asset. The reason why no proceeds were received by Massmart for the disposal of the right or asset, so argues SARS, was because the asset had no commercial or economic value. Second, that what has been claimed as expenditure actually incurred in determining the base cost of the asset is not expenditure actually incurred, as contemplated in para 20(1)(a) of the Eighth Schedule. SARS argues that no expenditure was actually incurred by Massmart in acquiring the right or asset. The contention that expenditure actually incurred by Massmart equals the loss suffered by the trust, according to SARS, is strained and non-sensical. No expenditure is alleged to be incurred when Massmart states it acquired the right (the asset) – every time it directed the trust to issue options and deliver shares to the offerees pursuant to the exercise of the options. Instead, expenditure is only alleged to be incurred when the alleged rights were extinguished.

[17] Massmart, on the other hand, argues that for capital gains tax purposes, when it directed the trust to issue the options and to deliver the shares to the offerees pursuant to the exercise of the options by the offerees, it acquired the right to require the trust to perform the obligations arising from the direction issued by it and accepted by the trust. The right thus acquired by it, so Massmart argues, constituted an 'asset' as defined in para 1 of the Eighth Schedule. The right, according to Massmart, is a personal right within the rubric of the words 'incorporeal' and 'property of whatever nature' in the definition of 'asset'. The phrase 'property of whatever nature', it argues, is of a 'wide and unqualified nature' and *'prima facie* unlimited'. (Compare *Commissioner for Inland Revenue v Ocean Manufacturing Ltd* 1990 (3) SA 610 (A) at 618.) There is no reason, so Massmart argues, why a right, to qualify as an 'asset' within the meaning of para 1, must come into existence as a result of an 'agreement' or that it must be acquired rather than be created. In any event, Massmart further argues, the trust deed was an agreement to which Massmart was a party and there was obviously a further agreement when the trust agreed to comply with Massmart's request to offer certain share options to certain employees and, thereafter, to give effect thereto by acquiring shares – at Massmart's expense – and selling them to the employees. The *raison d'être* of the share incentive scheme, according to Massmart, demonstrates that the right to require the trust to sell shares to employees was a right with value to Massmart.

[18] Massmart further argues that the asset (its right) was extinguished as a result of the performance of its obligations by the trust, which constituted a 'disposal' within the meaning of para 11(1) of the Eighth Schedule, the 'extinction of an asset'. A disposal, in terms of para 11, includes 'any event' or 'extinction of an asset' by way of forfeiture, termination, redemption, cancellation, surrender, discharge, relinquishment, release, waiver, renunciation, expiry or abandonment'. There were, according to Massmart, no 'proceeds received or accrued' from the disposal of the asset, as defined in para 1, as nothing was received by or accrued to Massmart 'in respect of that disposal'. It argues that the receipt or accrual of proceeds in respect of a disposal is not required. It remains a disposal of an asset for capital gains tax purposes if, for example, it was abandoned or scrapped because it has no value, in which event the proceeds of such disposal are likely to be zero.

[19] Massmart avers that the cost of the shares acquired by the trust less the proceeds thereof when they were sold to the employees were paid for in cash by Massmart. The expenditure incurred by Massmart when it incurred expenditure in respect of the right acquired by it to require the trust to acquire and sell shares to the employees, so Massmart argues, falls squarely within the meaning of paragraph 20(1)(a) of the Eighth Schedule, namely 'the expenditure actually incurred in respect of the cost of acquisition or creation of that asset'. The 'base cost' of the right (the asset), as contemplated in para 20(1)(a), Massmart argues, was the expenditure actually incurred by Massmart, which expenditure was equal to the loss made by the trust on the delivery of the relevant shares. Paragraph 20(3)(b) provides that '[t]he expenditure contemplated in subparagraph (1)(a) to (g), incurred by a person in respect of an asset must be reduced by any amount which … has for any reason been… recovered …'. Thus, Massmart argues, the expenditure incurred by it in acquiring the right must be reduced by the amounts received from employees, which results in a reduction of the base cost. The 'capital loss' it suffered for capital gains tax purposes, it argues, is 'the amount by which the base cost of that asset exceeds the proceeds received or accrued in respect of that disposal', as contemplated in para 4(a). This, Massmart argues, is borne out by the commercial reality that it factually incurred expenditure equal to the losses incurred by the trust, resulting in *de facto* commercial losses to it. I accept, for present purposes, that a possible interpretation that can be put forward by the facts is that Massmart funded the purchase of the shares and bearing the losses suffered in the process.

[20] I am of the view that Massmart's appeal raises triable issues and must be determined at the end of the trial in the tax court. Whether the capital losses claimed by it in respect of its 2007 to 2013 years of assessment were properly disallowed by SARS requires the application of legal principles to the particular factual matrix of this case. I am unable to hold that on all possible readings of the facts Massmart's appeal is legally unsustainable. (See: *Children's Resource Center Trust and Others v Pioneer Food (Pty) Ltd* 2013 (2) SA 213 (SCA), paras 34-37.) Moreover, there is also a compelling policy consideration why Massmart's appeal against the disallowance of its objection to SARS' disallowance of its claimed capital losses in respect of its 2013 year of

assessment should be determined by the tax court when the identical appeal against the disallowance of Massmart's objections in respect of the disallowances by SARS of its claimed capital losses in respect of the 2007 to 2012 years of assessment will be heard. The issues in respect of the disallowances of Massmart's objections appear to be identical: whether the capital losses arising from the employee share option scheme are capital losses which are deductible by Massmart for capital gains tax purposes. It would thus be desirable for the dispute in relation to the 2013 year of assessment to be adjudicated together with the identical dispute in relation to the 2007 to 2012 years of assessment. This will avoid separate, and perhaps conflicting, jurisprudence on matters with identical legal and factual issues.

[21] Finally the matter of costs. The tax court may, in terms of s130(3)(b) of the TAA, make an order as to costs provided for in the Tax Court Rules in an interlocutory application or an application in a procedural matter referred to in s 117(3). Rogers J, in *ITC* 1876 77 SATC 175 para 46, said the following:

'In regard to costs, rule 50(5)(a) of the new Tax Court rules, which govern these interlocutory proceedings, states that the Tax Court hearing an application on the Part F of the rules may make an order as referred to in that part, together with any other order it deems fit, including an order as to costs. Although, when it comes to the substance of the tax dispute, costs are generally not awarded unless there has been a frivolous use of power or an unreasonable basis of opposition, in interlocutory matters it is my experience that costs have generally followed the result, unless it would appear unjust to order costs on that basis.'

[22] I am of the view that it would be unjust to apply the ordinary rule that the successful party is rewarded costs, at this stage. The tax court, once it has applied legal principle to the factual matrix of the appeal, will be better suited to determine the question of the costs of this interlocutory application.

[23] In the result the following order is made:

1. The exception is dismissed.
2. The costs of this interlocutory application are reserved for determination on conclusion of the appeal to the tax court.

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P.A. MEYER
JUDGE OF THE HIGH COURT
SITTING AS THE TAX COURT, JOHANNESBURG

Date of hearing:	9 February 2018
Date of judgment:	11 July 2018
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