OF INTEREST

IN THE HIGH COURT OF SOUTH AFRICA

(EASTERN CAPE LOCAL DIVISION, PORT ELIZABETH)

Case No:1213/2020

In the matter between:

ICR UTILITY MANAGEMENT PROPRIETARY LIMITED	First Applicant
KOENA ESTATES PROPRIETARY LIMITED	Second Applicant
and	
MATULE PATIENCE HEADBUSH	First Respondent
THOMAS FRANK LAWRENCE N.O.	Second Respondent
ALEXANDER SELLO HEADBUSH N.O.	Third Respondent
MATULE PATIENCE HEADBUSH N.O.	Fourth Respondent
JOHN ROSS THANDO KEENA HEADBUSH N.O.	Fifth Respondent
LAWRENCE MASIZA VOSTER INC.	Sixth Respondent
SOUTH AFRICAN REVENUE SERVICES	Seventh Respondent

JUDGMENT

Govindjee AJ:

Background

[1] This is an application for declaratory and interdictory relief, compelling the payment of tax to the South African Revenue Service ('SARS').[1]

[2] The applicants' practice note frames the dispute as follows:

> '…the matter is not a tax dispute, but it is a dispute between the Applicants who had a duty to withhold the (dividend) tax, and the First Respondent and the trust (represented by the Second to Fifth Respondents) who are liable for the tax, as to what methodology is to be followed in order for the taxes to be paid to SARS.'

According to the applicants' founding affidavit, 'The foundation of this application, and the right which the Applicants have in order to request this relief…flow from the provisions of the tax legislation, more in particular the liability which the income tax legislation imposes upon the First Respondent and the trust to pay the taxes herein mentioned.'[2]

This affidavit goes on to add:

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[1] SARS is the Seventh Respondent and apparently abides the outcome of the application, having failed to file any papers in the matter.

[2] Para 8.

> 'In this instance, the tax obligation was not as evidently clear as that of employees' tax which is a very well known feature in ordinary day business dealings, but the point remains that the parties ultimately liable in law for the taxes are the First Respondent and the trust.'

[3] There is agreement that the matter concerns dividends tax.[3] On the first to sixth respondents' version (referred to, for convenience, as 'the respondents'), the application does not concern the question of the liability of dividends tax but rather the question of who, in terms of the Sale of Shares agreement ('the agreement') is liable to pay that tax. From that perspective, the issue is whether the agreement amended, *inter partes*, the liability for the actual payment of the dividends tax to SARS. The respondents frame the question as one directly related to the interpretation of the terms of the agreement, and thus requiring arbitration in terms of the provisions of that agreement.

[4] The agreement was entered into during November 2018. The applicants purchased back some of their own shares from the first respondent and the Sello Headbush Vula Trust ('the Trust'), represented by the second to fifth respondents, in their capacity as trustees). The purchase price of R7,2 million was paid into the trust account of the sixth respondent during December 2018.

[5] Clause 4.4.3 of the agreement reads as follows:

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[3] Section 1 of the **Income Tax Act, 1962** (Act 58 of 1962) defines 'dividend' to mean any amount distributed by a company to its shareholders, and the expression 'amount distributed' *inter alia* includes any reduction of the profits of a company as a result of the acquisition, cancellation or redemption of shares issued by that company.

> 'All payments to be made to the Sellers in terms of this Agreement shall be made in cash or electronic bank transfer, without any deduction and free of any deductions, bank exchange or set off and into the bank account nominated by the Sellers in clause 4.4.2 above.'

[6] In terms of clause 4.5:

> '**Tax:**
>
> 4.5.1 Each of the Parties shall be liable for and make payment of all taxes levied on each of them respectively, in respect of this Agreement and the contemplated transactions, as and when same falls due, subject to the provisions of clause 4.5.2 below.

[7] The closing of the transactions was regulated by Clause 5, read in conjunction with annexure 'B' to the agreement, providing for signature, retention of documentation and exchange of the documents of title provided the purchase price was paid.

[8] During February 2019, the auditors of the applicant, subsequent to the implementation of the agreement, made enquiries regarding the payment of dividends tax to SARS as a result of the implementation of the transaction. The applicants' understanding of the dividends tax position is as follows:[4]

[4] Paragraph 7.2. of the founding affidavit.

- The agreement provides that each party is liable for all taxes levied on each of them;
- As the transaction was a share buyback from retained income, payment by the two companies of the purchase prices to the first respondent and the Trust are regarded as dividend payments, so that dividends tax was applicable to the transaction;
- In terms of the **Tax Administration Act, 2011,**[5] the applicants were to withhold the dividends tax, but did not do so because they were contractually obliged to make payment of the full purchase price into the trust account of the sixth respondent, which they did.
- This portion of the money paid to the sixth respondent remained the property of the applicants and the sixth respondent had no authority to release the funds of the applicants, without the applicants' prior instructions and permissions.

[9] The application appears to be motivated by the concern that SARS '…may accuse the Applicants, and may even endeavour to hold the Applicants liable, on the basis that the Applicants did not subtract from the amounts paid to the First Respondent and the trust, the tax component.' The applicants contend that it is the first respondent and the Trust that is ultimately liable in law for the dividends tax.[6] They seek to be placed in the position they would have been in had they subtracted the dividends tax prior to the closing of the transaction.

The legal position

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[5] Act 28 of 2011.

[6] Par 16 of the applicants' heads of argument.

[10] A survey of the applicable statutes suggests that both the applicants and respondents could be responsible for the payment of the dividends tax. Section 64EA*(a)* of the **Income Tax Act, 1962**[7] clearly places the liability for dividends tax in the hands of a 'beneficial owner' of a dividend. It provides that 'Any beneficial owner of a dividends tax, to the extent that the dividend does not consist of a distribution of an asset *in specie*, is liable for the dividends tax in respect of that dividend.' 'Beneficial owner' is defined as 'the person entitled to the benefit of the dividend attaching to a share',[8] suggesting that the first respondent and the Trust are liable for payment of the dividend taxes to SARS. Section 64K goes on to add that if, in terms of section 64EA*(a)*, a beneficial owner is liable for any amount of dividends tax in respect of a dividend, that beneficial owner must pay that amount to the Commissioner by the last day of the month during which that dividend is paid by the company that declared the dividend, *unless the tax has been paid by any other person.*

[11] Section 64G(1) provides, however, that a company that declares and pays a dividend must withhold an amount of dividends tax from that payment calculated as contemplated in section 64E (except to the extent that the dividend consists of a distribution of an asset *in specie*). In terms of section 157(1)*(b)* of the **Tax Administration Act, 2011**, a 'withholding agent' is personally liable for an amount of tax which should have been withheld under a tax Act but was not so withheld. That Act goes on to state that 'an amount paid or recovered from a withholding agent in terms of subsection (1) is an amount of tax which is paid on behalf of the relevant

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[7] Act 58 of 1962.
[8] Section 64D of the Income Tax Act, 1962.

taxpayer in respect of his or her liability under the relevant tax Act'.[9] A 'withholding agent' is defined to mean a person who must withhold an amount of tax and pay it to SARS under a tax Act.[10]

[12] The agreement aside, the position, in sum, appears to be that the applicants are considered to be withholding agents, having declared and paid a dividend as part of the buyback.[11] They should have ordinarily withheld dividends tax from the payment made to the first respondent and the Trust.[12] By failing to do so, they became personally liable for an amount of tax which should have been withheld but was not so withheld. This opens the door to SARS recovering that amount of tax from the applicants, which is ultimately the motivation for this application. Importantly, any amount paid by the applicants to SARS, or that SARS recovers from the applicants, should it choose to do so, would seemingly be paid 'on behalf of the relevant taxpayer in respect of his or her liability under the relevant tax Act'.[13] As beneficial owner of a dividend, it is the first respondent and Trust that is responsible for dividends tax.[14] Recovery from the applicants, or payment made voluntarily by the applicants to SARS, would be recovery or payment on behalf of the first respondent and the Trust.

[13] Is this position altered by the agreement? The applicants were obliged, in terms of clause 4.4.3, to make all payments without any deduction and free of any deductions. As far as tax was concerned, to repeat, clause 4.5.1 provides that 'each

[9] Section 157(2) of the Tax Administration Act, 2011.
[10] Section 156 of the Tax Administration Act, 2011.
[11] Section 156 of the Tax Administration Act, 2011.
[12] Section 64G(1) of the Income Tax Act, 1962.
[13] Section 157(2) of the Tax Administration Act, 2011.
[14] Section 64EA*(a)* of the Income Tax Act, 1962.

of the Parties shall be liable for and make payment of all taxes levied on each of them respectively, in respect of this Agreement and the contemplated transactions, as and when same falls due…'

[14] Read together with the applicable legislative provisions, the intention appears to have been for the first respondent and the Trust to make payment of the dividends tax (because the applicants were contractually obliged to make payment *sans* any deduction). That liability and payment would, in terms of the agreement, arise once the tax had been levied. In all probability, this must relate to the imposition of an amount of tax on the part of SARS, which has not occurred to date.

[15] But this *prima facie* reading of the applicable legislation and the agreement is not the end of the matter. The parties specifically agreed to private arbitration 'should a dispute occur…in regard to any matter arising out of this Agreement or its interpretation or their respective rights and obligations under this Agreement…'

[16] As tempting as it may be to express a firm view on the matters raised, and to seek to clarify the legal position to bring the matter to finality, the question is whether a dispute has now occurred between the parties in regard to a matter(s) arising out of the agreement or its interpretation. That appears to me to be the case. At the very least, there is a live dispute between the parties pertaining to their respective rights and obligations: the applicants should have withheld the dividends tax but failed to do so, making them personally liable to pay the tax on behalf of the first respondent and the Trust, who should themselves have paid the tax to the Commissioner by the last day of the month during which that dividend was paid. Notwithstanding this, the

agreement seeks to postpone liability and payment until taxes are levied or imposed. Should the applicants simply pay the dividends tax that should have been withheld on behalf of the first respondent and the Trust, in terms of section 157(2) of the **Tax Administration Act, 2011**, and then institute an action for the recovery of that amount? Should the first respondent and the trust immediately pay the dividends tax to SARS, despite the applicants' breach of their obligation to have withheld the dividends tax, because they are the beneficial owners of the dividend? Is there any merit in waiting for SARS to actually levy the tax on either of the parties given the circumstances? These are unquestionably disputes that emanate from the way in which the agreement was constructed, and its apparent failure to deal with the issue of dividends tax in accordance with legislative prescripts. I am satisfied that the disputes ventilated are fully covered by the arbitration clause, and that there is no real risk of an arbitrator ruling otherwise. The parties are, in terms of clause 10 of the agreement, obliged to refer such issues to arbitration.[15]

[17] The applicants have failed to make out a case for the relief claimed. Their application is dismissed with costs.

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A. GOVINDJEE

ACTING JUDGE OF THE HIGH COURT

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[15] It might be added that clause 2.9 of the agreement confirms that 'the expiration or termination of the Agreement shall not affect such of the provisions of this Agreement as expressly provided that they will operate after any such expiration or termination or which of necessity must continue to have effect after such expiration or termination, notwithstanding that the clauses themselves do not expressly provide for this'.

Appearances:

Obo the Applicants:	*Adv M.P van der Merwe SC*
Instructed by:	*Jarvis Jacobs Raubenheimer Inc c/o Van Heerden Attorneys, 7 Bird Street, Central, Port Elizabeth*
Obo the 1st to 6th Respondents:	*Adv B.C Dyke SC*
Instructed by:	*Lawrence Masiza Voster Inc., 214 Cape Road, Mill Park, Port Elizabeth*
Heard:	*20 May 2021*
Delivered:	*25 May 2021*