

Transfer Duty

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New Transfer Duty Amendments

For some time now the practice of registering properties in the names of close corporations, companies and trusts with a view to avoiding transfer duty on the resale, has been growing. This avoidance is achieved by selling the member's interest / shares or beneficial interest in the entity to the purchaser. To stop this practice and to enable the South African Revenue Services (SARS) to collect the lost transfer duty again, the Transfer Duty Act has been amended with effect from 13th December 2002.

Basically, certain definitions in the Transfer Duty Act have been amended to the affect that sales of residential property-owning entities will now be subject to the same rate of transfer duty as if the property was sold by the entity to the purchaser. For example, the following definitions have been added:

- **Residential property** means "any dwelling house, holiday home, apartment or similar abode, improved or unimproved land zoned for residential use [including any real rights therein]"
> [There are some exclusions which are dealt with below](#)
- **Residential property company** means "any company that holds property that constitutes residential property or a contingent right in property." ("Company" means a company or close corporation or a trust).
> [More about trusts](#)

Read together with the rest of the Transfer Duty Act, transfer duty is therefore now payable on these transactions. But on what amount is the duty calculated? Transfer duty has always been calculated on fair market value, which is in most cases the actual selling price of the property. The definition of fair value has also been amended to disregard the liabilities on the balance sheet of the company, for example the loan accounts and shares leaving only the market value of the asset to be taken into account. Effectively this means that the same rate of transfer duty is applicable to the transaction as would have been paid with a normal sale.

Who is responsible for the transfer duty? In terms of the Transfer Duty Act, the duty has always been payable within six months of the date of the transaction by the person who acquired the property, i.e. the purchaser. Section 3 of the Transfer Duty Act has now been amended to read that where the purchaser fails to pay the duty within the period, the public officer of the company and the seller are jointly and severally liable for such duty. Please note that this places an onerous burden on the seller to ensure that the duty is paid or secured before finalisation of the transaction. The reasoning behind this amendment can be understood against the backdrop of normal transactions. The Deeds Office acts as policeman and will not register a transfer without the transfer duty receipt. Of course a sale of shares / sale of member's interest agreement are not registered in the Deeds Office [the change of ownership of shares / member's interest is registered with the Registrar of Companies in Pretoria] and this amendment can be seen as an extra policing mechanism for the efficient collection of transfer duty.

It is clear that with the above amendments, SARS has succeeded in targeting the avoidance of transfer duty on residential property and has probably succeeded in stopping the sales of property-owning companies. A potential purchaser no longer will enjoy the savings in transfer duty, to set off against the danger of hidden creditors, as well as having a more onerous Capital Gains Tax on the net profit upon resale and it is likely that this practice will be mostly discontinued.

It was also clearly the intention of the amendments to exclude commercial businesses involving residential property. Companies who have registered for value added tax [VAT] carrying out an enterprise, as defined, are excluded from the definition of "residential property company", as is "an apartment complex, hotel, guest house or similar structure consisting of five or more units used for renting to five or more unrelated persons." This exclusion relating to five or more units may not have been thought through very well. Firstly, the exclusion seems to refer to a single structure. Why would a landlord of such a structure be treated differently to a landlord who perhaps owns five or more separate residential properties scattered through the town? Secondly, what is a unit? Is it a unit as defined in the Sectional Titles Act, i.e. a flat or sectional title unit or perhaps a room or suite of rooms? Thirdly, it appears that the sale of shares in a shareblock building also falls under the definition of a residential property. Was it the intention of the legislature also to attack this transaction, which has never been viewed by SARS as transfer duty avoidance? [admittedly, these transactions have become less popular after the introduction of the Sectional Titles Act].

More about trusts

The issues around "sale of trusts" has always been much more complex than the sale of shares / member's interest in a corporation. In fact, some attorneys are very reluctant to admit that a trust can be "sold" at all. To date, SARS has held the opinion that transfer duty is payable on these transactions. The amendments to the Transfer Duty Act also include "a contingent right to any residential property held by a discretionary trust" accompanied by certain changes to the structure of the trust including new trustees etc. Without becoming too technical however, the words 'contingent right' have a specific meaning in the law of trusts and some discretionary trusts are set up in such a way that the beneficiaries have no contingent right at all. We are not sure if SARS has overcome this problem with the above amendments and many purchasers of trusts, concluded before 13th December 2002, may believe that the Receiver has conceded defeat on the position of transfer duty on those transactions.

Conclusion

The above amendments will have two main results, no doubt clearly intended by SARS. The

sale of residential property companies/CCs will probably dry up and more and more developers who previously sold residential property companies/CCs to purchasers without transfer duty, will be forced into VAT registration.

Prepared by Andrew Murray (April 2003)

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Change to Transfer Duty Policy - Nominations

As you know it has for some time been acceptable to the Receiver of Revenue that a Purchaser may reserve the right to nominate an alternative party as purchaser in his stead without the transaction attracting additional transfer duty.

If the sale agreement was silent as to the time period for nomination, the nomination had to be effected within 24 hours. If a time period was stipulated for in the contract [as long as the time period was not too long] then the nomination was permitted to be effected within the time period stipulated.

The situation has now changed. As regards all contracts concluded on or after **1st September 2003** nominations will only be accepted by the Receiver of Revenue if the nomination occurs **on the same day on which the contract is signed**. If done later, then transfer duty will be assessed on the nomination as if it was a second sale.

Please urgently amend your standard documentation relating to nominations and/or advise any Purchasers who might be relying on the nomination option. If the change has caused significant difficulties already, then the matter can [with the assistance of the Seller] be solved by canceling the existing agreement with the first Purchaser and doing a new one with the nominee. This is perfectly legitimate and will not attract any transfer duty.

You must also not forget that an alternative purchaser can only be nominated if that intended nominee already exists. It is therefore not permitted to nominate a trust unless the trust is already registered.

Prepared by Milton Koumbatis

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Change To Transfer Duty Policy – Nominations (Revised)

We have already informed our clients that due to a recent ruling on the part of the Receiver of Revenue the right of a purchaser to nominate an alternative purchaser without additional transfer duty obligations has been significantly curtailed. In this regard we repeat that such nomination must occur on the same day as the agreement of sale is concluded.

Although the ruling was intended to stop abuse of the nomination procedure [buyers were using the nomination clause as a method of "on-selling" without incurring additional transfer duty] the reality is that the ruling is affecting purchasers who have no such intention in mind and who genuinely wished to have a relatively short period of time to decide on the identity of the party who would be taking transfer of the property.

For the benefit of our clients we wish to set out / remind you of the following mechanisms which are still legitimately available for purposes of assisting such "legitimate" clients:

1. The client who wishes the property to be registered in the name of a close corporation or company which the client still wishes to create

Under normal circumstances it is impossible in law to enter into an agreement with a party who does not exist. In terms of the Company/Close Corporation Laws of the Republic of South Africa, it is however possible to enter into a contract with a Company / Close Corporation in the process of formation. In such circumstances you would describe the purchaser in the sale agreement as "Mr Joe Soap in his capacity as trustee for a Company / Close Corporation in the process of formation". You must however furthermore stipulate in the body of the agreement [or on an addendum] that "Mr Joe Soap warrants that the Company / Close Corporation will be registered within a period of ____ days from date of signature hereof and will, within such period, be bound in law to the terms of this agreement. Should the Company / Close Corporation not be timeously registered and/or bound, then Mr Joe Soap in his personal capacity will be deemed to be the purchaser. Should the Company / Close Corporation be timeously registered and bound then Mr Joe Soap by virtue of his signature hereto, binds himself as surety for the Company / Close Corporation, waiving the benefit of excussion."

2. A client wishes to cause the property to be registered in the name of a Trust and wishes still to register the trust

It is impossible in law to enter into an agreement with a trust which does not yet exist and there are no exceptions to this rule. An agreement therefore describing the purchaser as "Mr Joe Soap in his capacity as trustee for a Trust to be formed" is completely invalid. The only way to get around this particular challenge is to incorporate into your sale agreement with Mr Joe Soap a clause reading as follows – "It is recorded that the purchaser herein wishes to have the property registered in the name of a Trust which the purchaser intends to establish. The parties accordingly agree that in the event of the purchaser causing the Trust to be properly registered within a period of ____ days from date hereof, this agreement will be cancelled and a new agreement entered into between the seller and the trust on terms identical hereto. The purchaser shall however in such new agreement bind himself as surety to and in favour of the seller for due performance of all the obligations of the Trust, waiving the benefit of excussion".

Prepared by Milton Koumbatis

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Tripartite Agreements and Transfer Duty

The Receiver of Revenue is now planning yet another step to close loopholes in the transfer duty legislation and in this regard plans an amendment which will effectively eliminate the use of "Tripartite Agreements".

Tripartite Agreements have been relied upon as a mechanism of turning what are effectively two transactions into one for purposes of transfer duty. In this regard and by way of example to illustrate the workings of the agreement, we shall assume that Mr Seller has entered into an agreement of sale with Mr First Purchaser relating to immovable property owned by Mr Seller. Before the transfer is registered Mr First Purchaser receives an offer on the property from Mr Second Purchaser and wishes to sell the property to Mr Second Purchaser.

Under normal circumstances two transfers would occur [i.e. from Mr Seller to Mr First Purchaser and then from Mr First Purchaser to Mr Second Purchaser] and transfer duty would be paid on both. This consequence was however avoided by way of an agreement concluded between all three parties [hence the term tripartite] providing as follows:

1. Mr Seller and Mr First Purchaser agreed to the cancellation of the sale agreement concluded between them.
2. Mr Seller agrees to sell to Mr Second Purchaser the property.
3. Mr Seller agrees to pay to Mr First Purchaser an agreed amount [normally all or some of the difference between the first purchase price and the second] as consideration for having agreed to the cancellation of the sale agreement which previously existed between them.

As a result of such tripartite agreement only one property transfer would occur [from Mr Seller to Mr Second Purchaser] and only one lot of transfer duty would be paid.

As and when the Receiver of Revenue's intended amendment to the legislation becomes law, the position will change and transfer duty will be levied on both transactions regardless of the contents of the "tripartite agreement".

It is therefore important before allowing clients to enter into a tripartite agreement to determine from the Receiver of Revenue whether the proposed amendment has yet been promulgated.

Prepared by Milton Koumbatis

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Proposed changes to Transfer Duty Legislation

The Government has published a second Revenue's Laws Amendment Bill which contains proposed changes to the transfer duty legislation. The particulars of the changes are as follows:

1. Signature of declarations by estate agents

Both buyers and sellers have always been required simultaneously with payment of transfer duty to provide the Receiver of Revenue with a declaration regarding the transaction. The declaration currently utilized causes both buyer and seller to confirm to the Receiver of Revenue that the price which the Receiver of Revenue is being shown in the deed of sale and on which transfer duty is being offered, is an honest and market related price, determined at arm's length. The Receiver of Revenue is in other words fishing for private arrangements between the parties whereby the price has been artificially reduced to avoid transfer duty and private arrangements made for additional payments. These declarations are equivalent to sworn affidavits and a false declaration is accordingly equivalent to the common law crime of perjury. The proposed amendment now entitles the Receiver of Revenue to insist that the estate agent who brokered the sale also sign a similar declaration if the Receiver so wishes. Whether the Receiver of Revenue will insist upon this in every transaction remains to be seen.

2. Reporting of sales

As we all know, it is already our law that transfer duty on any sale must be paid no later than 6 months from the date of conclusion of the deed of sale. Under normal circumstances this stipulation is of no great importance as most sales contemplate transfer taking place well within a period of 6 months and transfer duty is accordingly paid much earlier. In the circumstances however of a postponed transfer date, the law becomes relevant and the parties to the transaction will have to ensure that the transfer duty is paid within the 6 month period, failing which interest and penalties are raised. The proposed amendment requires estate agents to report in prescribed form to the Receiver of Revenue within a period of 6 months from date of sale all sales which the agent brokers. This amendment is presumably intended to enable the Receiver of Revenue to determine whether transfer duty has been paid on such sales and if not, to take action against the parties who have failed to pay.

3. Reporting of unprofessional conduct

The amendment also entitles the Receiver of Revenue in the event of any professional [including estate agent] having been found to have been involved in a scheme designed to unlawfully avoid transfer duty, to be reported to his governing body for further sanction.

4. Criminal sanction

The amendment also provides that any person who assists another person to unlawfully evade the payment of transfer duty will be committing an offence and if convicted be liable to a fine or to imprisonment for a period not exceeding 60 months.

The message that is being conveyed by these amendments to the estate agent community is clear. Do not allow yourselves to be drawn into any scheme or arrangement suggested by either buyer and seller which is designed to unlawfully avoid payment of transfer duty. Hidden addenda providing for additional payments not shown in the sale agreement and/or separate agreements providing for the purchase and sale of the movable content of a house at grossly inflated prices should obviously be avoided.

Prepared by Milton Koumbatis

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