

# Demystifying the Value-Added Tax Act implications of fixed property transactions in South Africa

Muneer E Hassan,\* Marina Bornman\*\* and Adrian Sawyer\*\*\*

## **Abstract**

The South African Value-Added Tax (VAT) Act lacks a logical structure for fixed property transactions, making it difficult to teach, apply and administer. This study examines the organisational structure of the VAT Act as an element of legal complexity. The study establishes guidelines to simplify VAT implications for fixed property transactions. Semi-structured interviews were conducted following a literature review. Research shows that improving statute structure, layout and organisation improves readability. This study confirms that the fixed property provisions of the VAT Act complicate the law, increasing compliance and administrative costs. The literature review and interview findings support the development of the guidelines to simplify complex transactions in the VAT Act. The principles in the guidelines include section grouping, headings and subheadings and clear signposting, and in this article these are applied to practically illustrate the VAT implications for fixed property transactions.

**Keywords:** fixed property, statutory drafting, structure, layout, organisation, design, complexity

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\* Department of Accountancy, College of Business and Economics, University of Johannesburg, Auckland Park, Johannesburg, South Africa. Corresponding author, e-mail: muneerh@uj.ac.za. This article is derived from the doctoral thesis, Muneer E Hassan, *A framework for a simpler South African Value-Added Tax Act*, University of Johannesburg, 2023 (awaiting publication). Gratitude is expressed to the National Treasury, South Africa, for granting permission to interview staff, the South African Revenue Service (SARS) for granting permission to interview staff, the South African Institute of Taxation (SAIT) for granting permission to interview members of the VAT Committee and the South African Institute of Chartered Accountants (SAICA) for granting permission to interview members of the VAT Sub-Committee.

\*\* Professor, Department of Accountancy, College of Business and Economics, University of Johannesburg, Auckland Park, Johannesburg, South Africa.

\*\*\* Professor of Taxation, UC Business School and Faculty of Law, University of Canterbury (NZ), Extraordinary Professor, Department of Taxation, School of Accountancy, University of South Africa, Pretoria (SA).

## 1. INTRODUCTION

*‘Knowledge is a process of piling up facts; wisdom lies in their simplification’.*<sup>1</sup>

The *Value-Added Tax Act 89 of 1991* (VAT Act) was implemented in South Africa on 30 September 1991. The VAT Act incorporates specific rules pertaining to fixed property transactions. In order to address the intricate nature of the subject matter, the South African Revenue Service (SARS) released a comprehensive guide titled ‘VAT 409: Guide for Fixed Property and Construction for Vendors (Issue 7)’ to explain the VAT implications associated with fixed property transactions (SARS, 2023). Since its initial publication in September 1991, coinciding with the implementation of the VAT Act, an additional six updates have been released. The VAT implications associated with fixed property are, however, inherently complex. The presence of scattered sections that must be evaluated for fixed property transactions serves to enhance and complicate the implications associated with such transactions, thereby rendering these implications challenging to instruct, implement and administer.

To illustrate the problem, an analysis pertaining to various transactions involving fixed property are set out in this article. These transactions include purchase or sale of fixed property by a VAT vendor, purchase of fixed property by a connected person and acquisition of second-hand fixed property. The pertinent sections in the VAT Act that necessitate consideration when a VAT registered vendor acquires or disposes of immovable property are as follows: section 1, which defines ‘fixed property’; section 9(3)(d), which outlines the specific timing of supply for fixed property; section 16(3)(a)(iiA), which establishes the special value rule for the buyer, and sections 16(4)(a) and (b), which stipulate the special value rule for the seller.

Section 9(3)(d), which pertains to the specific time of supply rule for fixed property, lacks any explicit references to section 16(3)(a)(iiA) governing the special value rule for the buyer, or sections 16(4)(a) and (b) governing the special value of supply rule for the seller. However, sections 16(3)(a)(iiA) and 16(4)(a) and (b) make a reference to section 9(3)(d). The seller’s special value of supply rule for fixed property transactions, which is distinct from the general and special value of supply rules outlined in section 10 of the VAT Act, is contained in sections 16(4)(a) and (b). This observation suggests that a logical structure of the VAT Act is lacking.

When a connected person buys fixed property, it is important to consider the specific provisions of the VAT Act. These provisions include section 1, which defines ‘fixed property’, section 9(3)(d), which deals with the special time of supply for fixed property, and section 10(4), which addresses the special value of supply for connected persons.

Notwithstanding the special time of supply rule applicable to connected persons, the more precise time of supply pertaining to fixed property, specifically the occurrence of either registration or payment, supersedes the time of supply for connected persons as stipulated in section 9(3)(d) of the VAT Act. It is worth noting that section 9(2), which contains the special time of supply rule for connected persons, does not make any

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<sup>1</sup> Martin H Fischer, quoted in Carl C Gaither and Alma E Cavazos-Gaither (eds), *Gaither’s Dictionary of Scientific Quotations* (Springer, 2008) 719 (citing Howard Fabing and Ray Marr, *Fischerisms* (CC Thomas, 1944) 2); BrainyQuote, [https://www.brainyquote.com/quotes/martin\\_h\\_fischer\\_121669](https://www.brainyquote.com/quotes/martin_h_fischer_121669).

reference to section 10(4) in relation to the special value of supply for connected persons. Furthermore, section 10(4) does not contain any instances of circular referencing, such as making a reference to subsection 9(2) of the VAT Act.

The VAT Act contains important provisions that must be taken into account when a VAT vendor purchases second-hand fixed property. These provisions include section 1, which defines ‘fixed property’ and ‘second-hand goods’, as well as section 16(3)(a)(ii)(bb) which specifies the special time of supply for second-hand fixed property. Additionally, section 16(3)(a)(ii)(aa) in conjunction with paragraph (b) of the definition of ‘input tax’ in section 1 addresses the concept of notional input VAT.

In order to gain a comprehensive understanding of the VAT obligations associated with the acquisition of second-hand fixed property, it is imperative to consult external documents such as SARS Interpretation Note 92, which sets out the documentary proof prescribed by the Commissioner, including the taxable supply of fixed property and second-hand fixed property acquired under a non-taxable supply (SARS, 2016). These examples highlight the dispersion of provisions in the VAT Act as well as other documents issued by SARS, which must be considered when assessing a specific transaction or event in the VAT Act, in this instance fixed property transactions. SARS states as follows on its website: ‘Interpretation notes are intended to provide guidelines to stakeholders (both internal and external) on the interpretation and application of the provisions of the legislation administered by the Commissioner’.<sup>2</sup> In terms of section 1 of the *Tax Administration Act No 28 of 2011* (SA) (TAA) as read with section 5(1) of the TAA, a ‘practice generally prevailing’ is ‘a practice set out in an official publication regarding the application or interpretation of a tax Act’. An ‘official publication’ is defined in section 1 of the TAA to specifically include an interpretation note. Put differently, interpretation notes are not law and are, as a result, not binding in determining the meaning of a provision. This assertion reinforces the contention that there is a pressing necessity for a resolution to the research problem, namely the complexity of the VAT Act; specifically, the legislation should be unambiguous, thereby reducing the reliance on SARS’ guides and interpretation notes. The efficacy of SARS’ guides and interpretation notes in resolving disputes and withstanding legal challenges is called into question, as demonstrated in the case of *Marshall NO v Commissioner for the South African Revenue Service* (CCT 208/17) [2018] ZACC 11 (Constitutional Court of South Africa). Taxpayers are advised to exercise caution when relying on interpretation notes and guidance provided by SARS. The confirmation of the taxpayer’s or SARS’ interpretation of the relevant tax legislation may be achieved by referencing the corresponding interpretation note or guide, provided that such an interpretation aligns with an objective and independent understanding of the legislation and is mutually accepted by both SARS and the taxpayer.

The examples serve to demonstrate the quantity of sections that necessitate evaluation in the context of fixed property transactions. The absence of a clear manifestation of the concept of grouping sections together becomes apparent when examining the VAT implications associated with fixed property transactions.

The objective of this study is to provide assistance in the organisation of the fixed property transactions of the VAT Act in South Africa, utilising guidance derived from

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<sup>2</sup> See SARS, ‘Interpretation Notes’ (last updated 8 August 2023), <https://www.sars.gov.za/legal-counsel/interpretation-rulings/interpretation-notes/> (accessed 18 May 2024).

existing literature and semi-structured interviews. The primary objective is to show how these guidelines can be implemented in order to effectively demonstrate how the layout, design and structure of the VAT Act can be enhanced with regard to fixed property transactions, thereby facilitating simplification.

Section 2 of the article presents a concise overview of the literature review pertaining to tax complexity. In addition, it discusses empirical studies that provide evidence of the correlation between an incoherent tax structure and the presence of tax complexity. Furthermore, this section offers guidelines for simplifying the tax structure. Section 3 provides a description of the research methodology utilised in this study, which is followed by section 4, which outlines the key findings derived from the interviews and analysis. The conclusion is presented in section 5.

## **2. LITERATURE REVIEW**

This study aims to elucidate the theoretical underpinnings of tax complexity. In this context, the literature review commences with a discussion of existing literature pertaining to enhancements in legal complexity, with particular emphasis on logical structure. The review then delves into specific literature findings regarding the presence of incoherent structure in VAT legislation, both on an international scale and in relation to the South African VAT Act. Lastly, the review encompasses a comprehensive analysis of general literature concerning guidelines for logical structure in the realm of legal drafting.

### **2.1 Tax complexity**

The concept of tax simplification pertains to the endeavour of enhancing the comprehensibility of the tax system (Tran-Nam, Oguttu & Mandy, 2019). Consequently, the determination of the concept of tax simplification is contingent upon the constituents of tax simplicity, or conversely, tax complexity. The concept of tax complexity, despite its extensive utilisation, lacks a universally agreed-upon definition, measurement or consensus. Tax complexity arises as tax legislation becomes increasingly intricate (Richardson & Sawyer, 2001). There are, however, different approaches to characterising tax complexity. Some authors describe tax complexity based on fundamental attributes (Slemrod, 1989), while others describe it using the process approach (Tran-Nam & Evans, 2014; Ulph, 2015).

Tran-Nam (1999) proposes a methodology that differentiates between tax complexity that adheres to legal frameworks (formal) and tax complexity that has economic implications (effective). Legal complexity refers to the level of difficulty associated with reading, comprehending, interpreting and applying a specific tax statute in various practical situations. Hence, the definition provided establishes that legal simplicity holds significant importance for academics, professional tax lawyers, tax advisors and judges.

Tran-Nam (1999) posits that the level of intricacy inherent in tax legislation is contingent upon two key factors: the linguistic elements employed to articulate the law, such as the use of plain language, grammatical accuracy, sentence length, active voice and logical structure; and the substantive aspects of the law, including ambiguity, exemptions, rebates, concessions and annual modifications. The present study primarily concentrates on the examination of logical structure, a constituent of legal complexity, as articulated in this description.

## 2.2 General literature: legal complexity and logical structure

The 1994 Organisational Review of the Inland Revenue Department (Sir Ivor Richardson, chair) and the Consultative Committee on the Taxation of Income from Capital (Arthur Valabh, chair) (also known as the Valabh Committee) were the primary drivers of the rewrite project in New Zealand (Sawyer, 2016). One of the recommended key features in the Valabh Committee's 1991 report (Consultative Committee on the Taxation of Income from Capital, 1991) was the reorganisation of the legislation (namely the *Income Tax Act 1976* (NZ) and the *Inland Revenue Department Act 1974* (NZ)) into a more logical and coherent scheme in the New Zealand rewrite project. The Valabh report dealt with key reforms to the scheme of tax legislation (Smaill, 2021, p. 2). Richardson and Sawyer (1998) examined the New Zealand government's commitment to reorganising and eventually updating income tax legislation in 1992. Their study examined how the reorganisation affected the length of average sentences. Despite the fact that the rewrite was only partially complete, the results of this study were encouraging for the New Zealand government's sentence length goals. Before the completion of the rewrite project, Pau, Sawyer and Maples (2007) conducted a further empirical analysis using readability measures to examine New Zealand's rewritten sections in the *Income Tax Act 2004* and other tax materials, such as Tax Information Bulletins and binding rulings. Even though the rewrite project was not complete at the time, the readability indexes demonstrated that the *Income Tax Act 2004* was much easier to read than the *Income Tax Act 1994* (and the *Income Tax Act 1976*). Saw and Sawyer (2010) conducted an evaluation of the effectiveness of the New Zealand rewrite project by analysing the readability levels of the New Zealand Income Tax Act and other related documents. The findings of a study conducted by Tan and Tower (1992) were compared to those of Saw and Sawyer (2010), revealing that New Zealand's efforts to revise tax regulations were effective in terms of enhancing readability (Sawyer, 2013). The New Zealand Income Tax Act underwent a series of revisions, beginning with the restructuring of the *Income Tax Act 1976* and the *Inland Revenue Department Act 1974*. These changes ultimately resulted in the enactment of the *Income Tax Act 1994*, along with the *Tax Administration Act 1994* and the *Taxation Review Authorities Act 1994*. Therefore, the reorganisation of the statutes improved their readability.

The Office of Tax Simplification (OTS) was originally established in the United Kingdom in 2010 for a duration of five years. Its primary objective was to conduct an in-depth examination of different facets of the tax system and provide comprehensive recommendations for both immediate and long-term improvements. It was explicitly instructed to refrain from engaging in policy matters and to formulate suggestions that would not have an impact on the overall revenue generated by the tax system. The OTS was officially established as a permanent fixture within the tax framework of the United Kingdom in 2015, obtaining comprehensive legal authorisation (Dodwell, 2021). The OTS has been dissolved subsequently (OTS, 2022). Sawyer (2023, pp. 1-2) argues that the decision to disband the OTS is based on misinformation and is likely to be regressive, potentially undermining the significant progress achieved by the OTS.

The OTS devised a complexity index with the aim of facilitating the examination of various dimensions of the tax code. The OTS then concentrated its endeavours on areas that yielded the highest level of benefit. The development of the index occurred gradually and underwent multiple iterations before ultimately being refined to encompass 10 distinct factors (OTS, 2017). One inquiry raised regarding the readability of a provision pertained to its standalone comprehensibility as opposed to its potential

reliance on extensive cross-referencing and validation of definitions found in other sections of the code. There is a contention that if the gathering of pertinent information necessitates substantial exertion, the rating should be subjected to a supplement. Therefore, the OTS considered the distribution of sections and cross-referencing to definitions when determining the complexity index. The United Kingdom implemented a reform initiative aimed at restructuring legislation through the use of contemporary language and concise sentences. In addition, this initiative provided coherent definitions and explicit cross-references to enhance clarity and comprehension (Budak & James, 2018).

### 2.3 Specific literature findings: incoherent structure of the VAT Act

The Tax Review Committee (Judge D Davis, chair) (Davis Tax Committee) (2018, p. 91, emphasis added) discusses the simplification of the corporate tax system in South Africa:

One radical suggestion has been that the Act should be *re-written and re-structured* in its entirety. *Such a rewrite would undoubtedly result in a rearrangement of the provisions of the Act into a more coherent logical sequence.* This may enhance the efficiency of the compliance environment of taxpayers.

No published study has indicated that the legal complexity found in South Africa's Income Tax Act is also found in the VAT Act, except for Young (2021) who discussed the logical structure of the VAT Act in her study. The purpose of her study was to explore methods to streamline the South African tax system.

Young (2021, p. 8) provides an analysis of the logical structure inherent in the South African VAT Act:

Cross-references between sections also abound, making the interpretation of the sections extremely complex. Section 16(3) of the VAT Act includes fourteen subsections, some with numerous sub-subsections and provisos, each of which is cross-referenced to a different section in the Act.

### 2.4 General literature: guidelines on logical structure

The logical arrangement of a statute contributes to its comprehensibility (Thuronyi, 1996). A well-structured statute facilitates the identification of relevant information and the exclusion of irrelevant sections for a particular taxpayer, thereby aiding in the process of locating answers to specific inquiries. To ensure organisational coherence, it is imperative to group provisions pertaining to the same topic together. Moreover, it is imperative that every subdivision of the statute, including individual sections, be organised in a coherent and systematic manner (Dale, 1977; Thuronyi, 1996). The legislative scheme impacts the quality of legal drafting by reflecting an ideal representation of how well an Act of parliament should be structured and written in terms of substance and form (Crabbe, 1993). The legislative scheme focuses on the logical progression of different topics and the organised symmetrical layout of sections. In academic discourse, it is customary to commence by presenting the overarching principle, subsequently delving into any deviations or particular regulations that pertain to distinct instances. In a literature study conducted by Kimble (1996-1997), an examination of the use of plain English in legal writing was undertaken. As a result of this investigation, a series of recommended guidelines was proposed, encompassing the

organisation of related concepts and the arrangement of components in a coherent and rational manner.

One instance of inadequate organisation can be observed when a substantial statute lacks proper division into sections, thereby compelling the reader to conduct a comprehensive search throughout the entire statute in order to locate the pertinent provisions (Thuronyi, 1996). According to Thuronyi (1996), a tax statute that is well written often contains various cross-references, both explicit and implicit. Explicit cross-references refer to specific sections or provisions in the statute, while implicit cross-references involve the use of terms that are defined elsewhere in the statute.

Modifying legislation structurally can make it more visually appealing and easier for readers to understand (Hunt, 2002). Recommendations in this regard involve organising provisions in a sequential order and grouping together provisions with the same subject (Hunt, 2002, p. 25).

According to Petelin (2010, pp. 212-213), a recommended approach to enhancing clarity in writing involves initially constructing a profile of the target audience and prospective readers. Petelin (2010) provides a comprehensive set of guidelines categorised under the headings of 'substance and structure' and 'style (verbal and visual)'. According to Petelin (2010), substance and structure encompass a coherent and logical arrangement of information, with a suitable sequence that follows the order of presenting general information before specific details and exceptions. This should be accompanied by the use of appropriate transitional words and phrases (Petelin, 2010, p. 213). In order to attain coherent and well-organised content, it is imperative to structure the text based on the reader's perspective rather than that of the author. According to Cutts (2013), it is essential for readers to have the ability to effectively navigate the text, locate the specific information they are seeking and comprehend it.

The implementation of simple tax legislation is necessary to ensure that taxpayers are able to understand and adhere to the regulations accurately and in a manner that is economically efficient (American Institute of Certified Public Accountants (AICPA), 2017). In summary, the recommendations for enhancing the logical structure in legal drafting encompass the following aspects: grouping, use of headings, explicit cross-referencing and tailoring the writing to suit the intended audience.

### **3. RESEARCH METHODOLOGY**

This study consisted of two distinct phases, namely a comprehensive review of existing literature and semi-structured interviews. The research design followed a sequential approach, wherein Phase 1 involved a literature review that partially influenced the formulation of the interview questions used in Phase 2. The literature review examined empirical studies that have been conducted on the topic of incoherent legislative structure and guidelines for tax simplification to a logical structure. The interviews sought perspectives from individuals who were affected by the research issue regarding their suggestions for improvements to the logical structure as a component of legal complexity in the VAT Act. The existing literature was compared to the findings derived from the interviews conducted.

The retrieval of information and documents was achieved by conducting online searches using search engines such as Google Scholar and the University of Johannesburg's databases, specifically UJoogle, Jutastat Online and Lexis Library. In addition to

conducting online searches, the authors also explored the websites of reputable accountancy firms and governmental entities such as SARS and the National Treasury, as well as international organisations such as the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF). The search incorporated various keywords, such as Value-Added Tax Act, unstructured, complexity, difficulty, simplicity, scattered, dispersed, uncertainty and ambiguity.

Primary data were collected through semi-structured interviews from participants who had direct experience working with the VAT Act. Due to the intricate nature of the research problem and the limited representation of experts in the stakeholder cohorts, interviews were deemed more advantageous compared to surveys. The research inquiry encompassed legal complexity, thereby necessitating the use of interviews as a suitable method for data collection, as suggested by Babbie and Mouton (2001).

The study employed expert sampling as a purposive sampling technique, which involves gathering data from individuals possessing specialised knowledge (Rai & Thapa, [2015]). The selection of the sample consisted of VAT specialists from both academia and industry who had direct experience of and engagement with the VAT Act. The authors employed their expertise and experience to exercise judgment in this process.

The sample of interviewees consisted of four stakeholder groups, each selected for specific reasons: (i) tax academics specialising in VAT instruction at a postgraduate level in the context of a South African university, where the focus was on the academic perspective, exploring the difficulties encountered in the process of teaching VAT; (ii) advisors who serve on the VAT Sub-committee of the South African Institute of Chartered Accountants (SAICA) and/or the VAT Committee of the South African Institute of Taxation (SAIT), with the consent of these professional bodies, the advisors being selected due to their expertise and practical experience, which allowed them to provide valuable perspectives on the subject matter; (iii) SARS personnel employed in the VAT department working with administration and interpretation of the Act, the individuals being chosen with the approval of the SARS Commissioner, and (iv) with permission from the Head, Tax and Financial Sector Policy at the National Treasury, individuals who were involved in the development of the VAT Act, to offer their perspectives on the underlying reasoning behind the present design, arrangement and structure of the VAT Act, as well as to propose potential areas for enhancement.

The inclusion of these four stakeholder groups was based on the presence of VAT experts in each group who engaged in regular work and interactions pertaining to the VAT Act. The individuals involved in this study demonstrated a comprehensive grasp of the research problem; specifically, the interviewees possessed a close proximity to the matter under investigation, namely the logical structure of the VAT Act. The judiciary was regarded as a stakeholder but was ultimately excluded due to their limited daily engagement with the VAT Act, which hinders their comprehensive understanding of its overall structural concerns. Instead, judges primarily focus on the interpretation of the VAT Act.

SAICA states that it is ‘the leading accountancy body in South Africa’.<sup>3</sup> SAIT ‘is the largest of the professional tax bodies in South Africa’, and endeavours ‘to enhance the tax profession by developing standards in education, compliance, monitoring and

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<sup>3</sup> SAICA, ‘About us’, <https://www.saica.org.za/about> (accessed 25 May 2024).



performance'. According to SAIT,<sup>4</sup> the institution 'contributes to the development of world class professional practises and people'.

Table 1 presents a summary of the number of interviews conducted with each of the four stakeholder groups.

**Table 1: Summary of Interviews with Each Stakeholder Group**

Stakeholder group	Number of interviews
Academics	7
Advisors	5
SARS	2
National Treasury	1
<b>Total</b>	<b>15</b>

The collection of detailed demographic information from the participants was deemed unnecessary for the purposes of this study. A duration of one hour was allocated for each interview. The shortest interview lasted 45 minutes, while the longest lasted one hour. The compilation of essential inquiries comprised a total of 10 questions. A subset of primary inquiries encompassed a series of additional questions. The primary focal points of the inquiries encompassed issues related to the lack of coherence in structure, use of plain language, sentence length, employment of active or passive voice, presence of ambiguity, exemptions such as rebates and concessions, amendments, economic policy, best practices and potential solutions. The primary objective of this research, which was a component of a broader study, was to examine the issue of the incoherent structure in the context of fixed property transactions, with a specific emphasis on identifying best practices and proposing potential solutions. The predominant language spoken by the individuals participating in the interviews was either English or Afrikaans. Special attention was given to formulating questions that were unambiguous and easily comprehensible. The preservation of confidentiality was ensured. Despite the authors' adherence to a chronological order in posing questions, the interviewees' responses exhibited a tendency to deviate from the immediate query, as the discussions occasionally underwent shifts in focus. The authors granted permission for this action, as it facilitated the acquisition of comprehensive qualitative data.

The interviews were transcribed by two professional transcribers. In order to uphold the confidentiality of the individuals being interviewed and the content of the interviews,

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<sup>4</sup> SAIT, 'About us', [https://www.thesait.org.za/page/About\\_SAIT](https://www.thesait.org.za/page/About_SAIT) (accessed 25 May 2024).

both transcribers entered into confidentiality agreements. The accuracy of all transcriptions was verified by the authors through a comparison with the interview recordings. The initial recordings and corresponding transcriptions will be securely stored for a duration of five years, after which they will be destroyed.

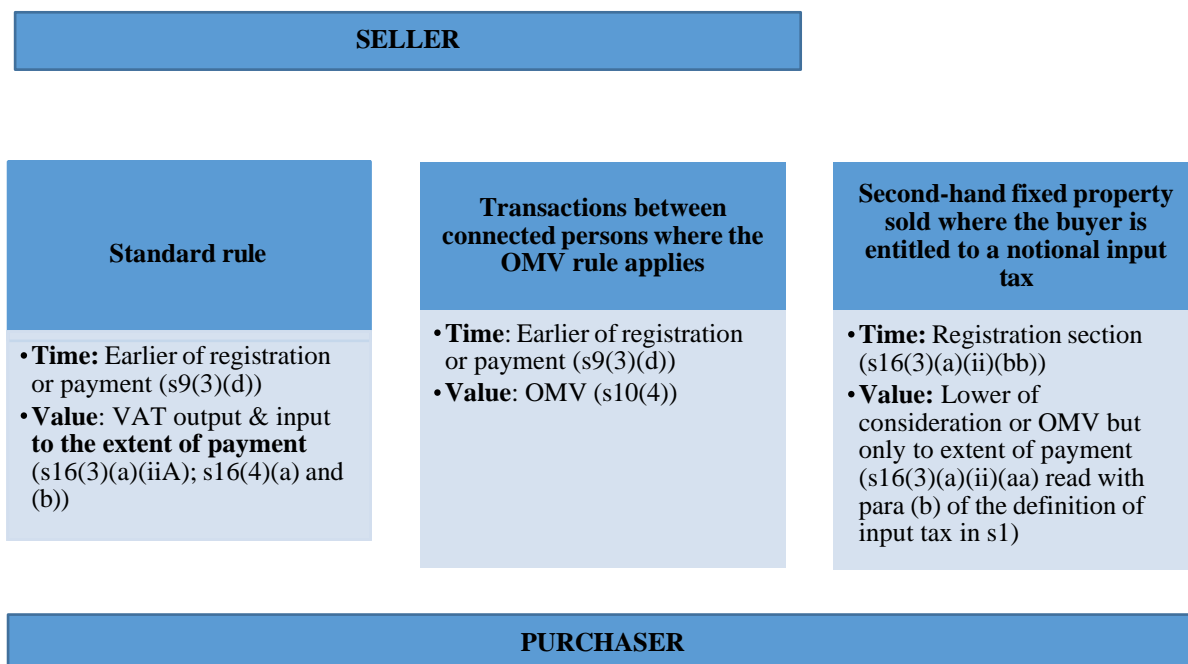
The data were analysed in the following manner: transcriptions were subjected to coding, where codes were subsequently organised into categories, and these categories were further consolidated into overarching themes, as recommended by Bryman and Bell (2014). The data management tool employed by the authors was ATLAS.ti Windows (Version 22.2.5.0). Prior to the commencement of data collection and interview procedures, ethical clearance and approval were obtained from the respective institutions of the participants. In addition, the participants were required to provide their informed consent in order to participate in the research study.

## **4. FINDINGS**

The interviewees presented examples to substantiate the claim that the VAT Act has an incoherent structure. The analysis in this section of the article is presented in the following manner: because fixed property was mentioned by most of the interviewees as an example to illustrate the scattered incidence of sections in the VAT Act, and these transactions are a common daily occurrence, the section starts with the results of a further analysis of fixed property in the VAT Act informed by the literature. This section then examines the viewpoints expressed by the interviewees regarding the lack of logical structure of the VAT Act. This is followed by examples to demonstrate the consensus among the interviewees that the VAT Act exhibits an incoherent structure and the scattered nature of the relevant sections. The section ends with suggestions by the interviewees that can serve as guidelines to simplify the VAT Act.

### **4.1 Fixed property: analysis**

There are three specific scenarios that fell under the scope of this analysis. First, the standard rule was considered. Secondly, transactions between connected persons were examined, with a focus on cases where the open market value rule is applicable. Lastly, the analysis included second-hand fixed property, specifically addressing the claiming of notional input tax. The VAT implications and relevant sections of the legislation pertaining to fixed property transactions are depicted in Figure 1.

**Fig. 1: VAT Implications in Relation to Fixed Property**

OMV = open market value as defined in section 1 of the VAT Act, read with section 3

According to section 1 of the VAT Act, the term ‘goods’ encompasses fixed property. Therefore, fixed property as defined includes land and real rights in such land, unit, share or time-sharing interest.

#### 4.1.1 Standard rule

##### *Summary of the VAT implications*

Irrespective of the accounting method they have chosen, vendors who engage in taxable supplies of fixed property are required to report output tax based on the amount of consideration received for the supply (SARS, 2022). In a similar vein, the recipient is eligible to claim a deduction for input tax, but only to the extent that payment of the consideration has been made. This means that these supplies are treated as if they were on a payment basis, as long as the time of supply has been initiated.

##### *The law*

The relevant sections in the VAT Act that pertain to the sale and acquisition of fixed property by a VAT vendor are section 1, which defines ‘fixed property’, section 9(3)(d) which deals with the special time of supply for fixed property, section 16(3)(a)(iiA) which outlines the special value rule for the buyer, and section 16(4)(a) and (b) which specify the special value rule for the seller.

*Interpretation of the standard rule*

At the outset, it must be mentioned that the transfer of immovable property is either subject to VAT or transfer duty (Franzsen & Van de Merwe, 1996). The transaction is subject to VAT in the case where the seller is a registered VAT vendor who transfers immovable property in the course and furtherance of its enterprise activities. The term 'fixed property' as defined in section 1 of the VAT Act refers to any property or real right associated with it. This definition applies when the property is transferred. The transfer of ownership of immovable property (or any right in immovable property) is done by way of registration in a deeds registry. The transfer of immovable property is regulated by the *Alienation of Land Act, 1981*. As mentioned, such alienation is either subject to transfer duty in terms of the Transfer Duty Act, or VAT. The parties cannot choose which Act applies. The VAT Act applies only where the requirements in the VAT Act are met. The time of supply for fixed property transactions is the earlier of registration or on the date when any payment related to the consideration is made. This is outlined in sections 9(3)(d), 16(4)(a) and 16(4)(b). Case ITC 1623, 59 SATC 342 confirmed that a right to the deduction of input tax arises at the time of 'supply'. For fixed property, section 9(3)(d) specifies that the 'supply' occurs on the date of registration of transfer. In Case ITC 1622, 52 SATC 334, it was necessary for the Court to establish the timing of the disposal (not the time of supply) of fixed property to determine if it constituted the disposal of a business as a going concern. In 1992, the vendor obtained the right to buy specific fixed property. The option was executed, and the property was transferred in 1994. The vendor argued that the disposal of the fixed property took place in 1992 when the option was initially obtained. However, the Court disagreed, stating that 'the grant of an option does not dispose of anything at all. An option is no more than an offer' (52 SATC 334, p. 337).

The aforementioned condition does not encompass a 'deposit', as it is not considered a form of 'any payment' until the seller can utilise it as a means of payment for the provision of goods or services. In a similar vein, it should be noted that a payment held in trust by an estate agent or attorney does not qualify as a payment made, as the seller is unable to utilise the funds to fulfil their existing obligation at that particular moment (SARS, 2022). This is because the seller becomes entitled to the money upon registration of the property in the purchaser's name at the deed office. At this stage, the parties have reciprocal personal rights. That is, the seller may demand payment after registration in the purchaser's name, and the purchaser may demand delivery by way of registration of the property in its name.

Irrespective of the accounting basis under which VAT vendors are registered, vendors who engage in the sale of fixed property and provide taxable supplies are obligated to declare output tax only to the extent that they have received consideration for the supply (SARS, 2022). In a similar vein, when the time of supply has been initiated, the recipient is only permitted to claim input tax deductions up to the amount of consideration that has been paid. This means that these supplies are treated as if they were on a payments basis, as stated in section 16(3)(a)(iiA). It is important to highlight that section 9(3)(d), pertaining to the special time of supply for fixed property, does not include any explicit references to section 16(3)(a)(iiA), which governs the special value rule for the buyer, or section 16(4)(a) and (b), which govern the special value of supply rule for the seller. Nevertheless, sections 16(3)(a)(iiA) and 16(4)(a) and (b) incorporate a cross-reference to section 9(3)(d). It is important to highlight that while the general and special value of supply rules are located in section 10 of the VAT Act, the seller's special value of supply

rule for fixed property transactions can be found in sections 16(4)(a) and (b). This observation serves to emphasise the lack of logical coherence in the design of the VAT Act.

It should be noted that in cases where the special value of supply rule is applicable to connected persons, the standard rule for fixed property transactions is not applicable. In this particular scenario, the specific value supply rule pertaining to connected persons will be given priority over the general rule governing fixed property transactions.

#### 4.1.2 *Transactions between connected persons*

The VAT Act encompasses overarching rules pertaining to the timing and valuation of supplies. Connected persons are subject to specific rules regarding the timing and valuation of supply. The application of a unique provision in the supply rule is primarily activated in situations where connected persons engage in transactions that do not adhere to the principle of arm's length dealing.

##### *Summary of the VAT implications*

In cases where there is a sale of fixed property to a connected person, the aforementioned standard rule for transactions involving fixed property does not apply. In this particular scenario, the specific value of supply rule pertaining to connected persons will be given priority over the general rule governing fixed property transactions.

##### *The law*

The relevant sections of the VAT Act that pertain to the sale of fixed property to a connected person are section 1, which defines 'fixed property', section 9(3)(d), which specifies the special time of supply for fixed property, and section 10(4), which outlines the special value of supply for connected persons.

##### *Interpretation of transactions between connected persons*

A 'connected person' is defined in section 1 of the VAT Act and includes, but is not limited to, natural persons and their relatives; a company and any other company that has control or the shareholders that are substantially the same (therefore a company that has control over its subsidiary companies); a company and any of its branches or divisions that are separately registered for VAT; a company and any natural person where that natural person owns more than 10% of the shares or voting rights in the company; a close corporation and any of its members; a partnership and any of its members, or a trust and any beneficiary.

The general time of supply rule, as described in section 9(1) of the VAT Act, is replaced by a more specific time of supply rule for connected persons, as outlined in section 9(2) of the VAT Act. Under this rule, if goods are to be removed, the date of removal is considered the time of supply. For other goods, the time of supply is when the goods are made available to the buyer. For services, the time of supply is when the services are performed.

The special time of supply rule for connected persons does not apply (section 9(2)(a), first and second provisos) where the time of supply is triggered by the general time of supply rules on or before the date that a return was submitted, or where the whole or

part of consideration cannot be determined at the time of supply to be made to a connected person who is entitled to a full input tax deduction.

It is noteworthy that, notwithstanding the aforementioned special time of supply rule applicable to connected persons, the more precise time of supply pertaining to fixed property, namely the earlier of registration or payment, supersedes the time of supply for connected persons (as stipulated in section 9(3)(d) of the VAT Act). The general value of supply rule extends to connected persons. However, a more precise and specialised rule regarding the value of supply is applicable to connected persons, where no payment is received, or the payment is lower than the market value, or the payment cannot be determined at the time of the supply. In such cases, if the purchaser is not entitled to a complete input tax deduction on the goods or services acquired, this rule is outlined in section 10(4) of the VAT Act. If the scope of the section is fulfilled, it can be inferred that the value of supply corresponds to the prevailing open market value. The special value supply rule between connected persons does not extend to cases where the supply in question constitutes a fringe benefit granted to an employee.

It is noteworthy that section 9(2), which pertains to the specific timing of supply for connected persons, does not explicitly reference section 10(4), which governs the specific value of supply for connected persons. Furthermore, it is important to note that there is an absence of circular reference in the given context. For instance, there is no reference made back to section 9(2) of the VAT Act in section 10(4).

In summary, when there is a sale of fixed property between connected persons, and the special value of supply rule is applicable as outlined in section 10(4) of the VAT Act, the value of the transaction is determined based on the open market value. The special time of supply rule for fixed property will continue to be in effect, specifically the earlier of registration or payment as stated in section 9(3)(d) of the VAT Act.

Irrespective of whether the transfer is between connected or unconnected persons, the purchaser can claim input VAT only to the extent that the purchase price was paid. Thus, the amount on the invoice (the deed of alienation) is the base line amount. However, input VAT is limited to the extent that this amount has been paid/extinguished. Where the parties are connected, and the amount in the deed of alienation is not at arm's length, the market value is used. Again, in this case, input VAT can be claimed to the extent that this amount has been extinguished (see sections 16(4)(a)(ii) and 16(4)(b)(i); De Koker & Badenhorst, 2024; ITC 1622, 52 SATC 334).

Immovable property (i.e., land) is due its nature considered second-hand as it has been previously owned. In the case of the sale of a second-hand fixed property, including land, where the buyer has the right to claim a notional input tax, it is necessary to adhere to the notional input tax rules, which are subject to the same requirements as in the case of all fixed property transactions, so that the input tax can only be claimed once the property has been registered.

Next, the acquisition of second-hand fixed property, in which a notional, i.e., hypothetical, input tax credit can be claimed, is discussed.

### 4.1.3 *Second-hand fixed property: notional input tax*

#### *Summary of the VAT implications*

On the acquisition of second-hand fixed property from a non-VAT vendor, i.e., where transfer duty is applicable, the purchaser is entitled to a notional input tax.

#### *The law*

The relevant sections of the VAT Act that require consideration are section 1, which provides the definition of ‘fixed property’ and ‘second-hand goods’; section 16(3)(a)(ii)(bb), which outlines the special time of supply for second-hand fixed property; and section 16(3)(a)(ii)(aa) in conjunction with paragraph (b) of the definition of ‘input tax’ in section 1, which pertains to notional input VAT.

In addition to the sections in the VAT Act that must be evaluated, SARS Interpretation Note 92 must also be consulted, which sets out the documentary proof prescribed by the Commissioner, including the taxable supply of fixed property and second-hand fixed property acquired under a non-taxable supply (SARS, 2016).

#### *Interpretation of second-hand fixed property*

The definition of ‘goods’ in section 1 of the VAT Act includes second-hand goods. Second-hand goods (including real property) are previously owned and used items (section 1 of the definition in the VAT Act of ‘second-hand goods’). Certain items, such as animals, gold, gold coins, gold-containing goods and ‘old order’ mining rights, are excluded from the definition.

For the acquisition of second-hand goods pursuant to a non-taxable supply, vendors may only deduct the notional input tax to the extent that they have paid the consideration for the supply, irrespective of whether they are registered on the invoice basis or the payments basis (SARS, 2022). The notional input tax is claimed in accordance with section 16(3)(a)(ii)(aa), when read in conjunction with subsection (b) of the definition of ‘input tax’ in section 1 of the VAT Act, i.e., on the lower of the consideration or the open market value, both of which are defined in the VAT Act. Before 10 January 2012, the notional input tax deduction for fixed property purchased from a non-vendor was restricted to the amount of transfer duty that was paid. Vendors can now claim a notional input tax deduction under the VAT Act, calculated based on the tax fraction of the consideration paid or the property’s open market value (National Treasury, 2012, citing the Taxation Laws Amendment Act No. 22 of 2012).

If the second-hand goods are fixed property, the vendor cannot claim the input tax until the transfer of the fixed property has been recorded in a deeds office (section 16(3)(a)(ii)(bb) of the VAT Act). Consultation must also be made with SARS Interpretation Note 92, which outlines the documentary evidence prescribed by the Commissioner, such as the taxable supply of fixed property and second-hand fixed property acquired under a non-taxable supply (SARS, 2016).

In summary, it is necessary to assess various sections scattered throughout the VAT Act when examining the consequences of fixed property transactions, contingent upon the particular circumstances. Moreover, it is apparent that the fixed property transactions lack adherence to the principle of grouping, as well as explicit cross-referencing and the inclusion of headings.

## 4.2 Incoherent structure: VAT Act

The individuals who were interviewed but did not have regular involvement with the VAT Act unanimously expressed their opinion that the VAT Act exhibits a lack of coherence in its structure, resulting in complexity. The following was stated by an academic in relation to the incoherent structure:

You almost don't start with the Act when you start preparing for VAT. You start with other documents. You go to textbooks. You go to the SARS guide ... to get the information that you need. Then you might go to the Act and even then, you don't have the comprehensive picture. You have to look at other sources as well and the risk is always there that you are not aware that it's there and this is for us that are people that deal with taxes and Acts every single day. So, if it's difficult for us to do it, I can't imagine for a person who is just a businessperson, and their specialty is not in law. So, it's definitely a big problem.

Conversely, the interviewees who possessed expertise in VAT did not perceive the incoherent structure as a significant factor contributing to complexity. The lack of concern regarding the dispersed sections can be attributed to their significant years of professional experience with the VAT Act, which has allowed them to develop a natural familiarity with the various sections. An interviewee from the advisors group made the following comment in relation to the incoherent structure:

I've never thought of the VAT Act as complex or disorganised, to be honest, to put it out there, because the VAT Act as you know has been around since '91 ... based on New Zealand ... what I do think is that ... there is definitely scope to do some adjustments to the structure ...

Given their expertise in the VAT Act and their inherent involvement in the VAT Act, it was expected from the outset that participants from the advisors group might hold varying viewpoints regarding the scattered sections, thereby recognising the potential bias in their opinions (see Erard, 1993; Mills, Erickson & Maydew, 1998; Newberry, Reckers & Wyndelts, 1993). It was also expected from the outset that interviewees belonging to the developers group might express unfavourable views regarding the incoherent structure of the VAT Act, perceiving it as a form of criticism. An interviewee from the developers group expressed the following sentiment in relation to the incoherent structure:

I haven't found it to be that difficult to understand being an attorney ... because I've been in VAT for so many years that I sort of know where to find things ... I do see [...] a point that certain cross-references are not there ...

According to Cutts (2013), it is essential for text to be structured in a manner that is logically organised from the reader's perspective. It is imperative that readers possess the ability to effectively navigate through the text, locate desired information and comprehend its content. It is imperative for specialists, drafters and taxpayers alike to be able to read and understand the law.

The interviewees identified three specific examples, namely VAT adjustments, imported services and fixed property transactions, to effectively demonstrate the dispersed incidence of the sections in the VAT Act in relation to a singular transaction



or event. The primary emphasis of this article is on fixed property transactions, thereby excluding an evaluation of VAT adjustments and imported services.

### 4.3 Guidelines for an improved logical structure in the VAT Act

The authors questioned the interviewees about the design considerations that must be taken into account when designing a solution for the incoherent structure. The concept of grouping with headings was mentioned by interviewees for highly complex transactions such as fixed property.

Regarding grouping, an interviewee from the academics group made the following comment:

[W]e have a general rule and then a grouping per concept and like fixed property ... you can also group vouchers and coupons and the fringe benefits you can group, and I made a comment here, it's like the Seventh Schedule. We have the Seventh Schedule now where we group these different sort of fringe benefits and in that the value of supply and things are talked about under the one heading. So, the grouping per concept or theme, I think that was my first thought on how to simplify it.

An interviewee from the academics group further made the following statement during the interview:

[W]hen I teach fixed property I tend to have to structure my notes in a way where I tie together the various sections and put them in one slide or one diagram so that the students can see how it all fits in together consolidated, because I think if I don't do that exercise of putting [it] together for them in terms of what is the type, time and value for each one of those different fixed property scenarios, I think that they would struggle trying to do that on their own by just working through the legislation.

An interviewee from the advisors group further commented as follows:

I mean even the properties [of] which part of it sits in [section] 16 then you first get the time of supply and then you go to [section] 16, so it is a bit laborious almost because you [have] got to read all the sections, it's almost like you [have] got to do a search for fixed property and say oh where does it get in the law as opposed to in one place but then you deal with the time and the value separately ...

Regarding headings, one interviewee from the advisors group provided the following insight:

[Y]ou can even have headings that say you know, registrations, accounting for VAT ... because that's actually how the textbooks set out the various sections of the law, so I think it's a brilliant idea to do that ... you would find the section in a certain place almost because you would know where to go and find it ... and then you can deal with special cases ... [for example] you can even after each section have like a special ... section that deals with special cases.

An interviewee from the developers group made the following comment in relation to missing cross-references: '[s]ometimes they write the time and value of supply in that section ... and sometimes they don't'. There are numerous cross-references between

sections of the VAT Act, making interpretation of the sections exceedingly complex (Young, 2021). The UK Tax Law Rewrite initiative, undertaken at the same time as the NZ Rewrite project, aimed to reorganise UK tax legislation by using clear signposting (Budak & James, 2018). When calculating the complexity index, the OTS considered the distribution of sections, i.e., cross-referencing to definitions (OTS, 2017). A well-written tax statute contains explicit and implicit cross-references (i.e., the use of a term whose meaning is defined elsewhere in the statute) (Thuronyi, 1996).

The interviewees, therefore, expressed their agreement with the concept of grouping and use of headings, which is also substantiated by existing literature (see Kimble, 1996-1997; Petelin, 2010; Thuronyi, 1996). The authors submit that these guidelines, which consist of grouping with headings and cross-referencing, are appropriate for fixed property transactions due to the legal team's consideration of the VAT implications when drafting legal contracts for such transactions.

One of the present authors sent the interviewees the guidelines in order to collect additional qualitative data, i.e., the interviewees' opinions and any suggested improvements (see Bryman & Bell, 2014). Even though the interviewees were only asked to respond to the author's email if they had additional comments or suggestions, nine out of 15 interviewees responded to the request for suggestions and/or improvements. Five of the nine participants were academics, three were consulting professionals (from the advisors group) and one was from the National Treasury. The interviewees made no additional modifications to the guidelines.

#### **4.4 Application of the guidelines**

The authors applied the guidelines for grouping and introducing headings with cross-referencing to fixed property transactions as an example of how to improve the layout, design and structure of the sections (see Figure 2). Even though SARS issued the VAT 409 guide, the focus of this guide is primarily on vendors who are involved in transactions concerning the development, construction and selling of fixed property (SARS, 2022). As such, the guide does not display the grouping of sections that must be evaluated in relation to the three distinct scenarios when considering the VAT implications in relation to fixed property transactions.

**Fig. 2: Improving the Logical Structure of the VAT Act in Relation to Fixed Property**

<p><b>[VAT 409]</b></p> <p><b>1. Fixed property: Standard rule</b>          Definition: Section 1, definition of “fixed property”  <b>Seller</b>          Time of supply: s9(3)(d)          Value of supply: s16(4)(a) and (b))  <b>Purchaser</b>          Value of supply: s16(3)(a)(iiA)</p> <p><b>2. Fixed property: Connected persons</b>          Definitions: Section 1, definition of “fixed property” and “connected persons”  <b>Seller</b>          Time of supply: s9(3)(d)          Value of supply: s10(4)  <b>Buyer</b>          Value of supply: s16(2) read with s20 and (3)(a)</p> <p><b>3. Fixed property: Second-hand</b>  <b>Definitions:</b> Section 1, definition of “fixed property” and “input tax”  <b>Buyer</b>          Time of supply: s16(3)(a)(ii)(bb)          Value of supply: s16(3)(a)(ii)(aa) read with para (b) of the definition of input tax in s1</p>
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This approach aims to streamline the complexity associated with fixed property transactions by directing the reader’s focus towards the three potential scenarios for such transactions (i.e., employing the concept of grouping). In addition, it offers the reader a coherent structure for assessing these scenarios by using headings and sub-headings. It is recommended that the proposed enhancement depicted in Figure 2 be integrated into the introduction of the SARS VAT 404 guide.

## 5. CONCLUSION

The present study examined the lack of coherence in the structure of the VAT Act with a focus on fixed property transactions. This lack of coherence adds to the overall complexity of the Act, thereby posing challenges in terms of teaching, practical application and administration. The study consisted of two distinct phases, specifically a comprehensive review of existing literature and semi-structured interviews.

This study represents a new examination of the incoherent structure of the South African VAT Act as it pertains to fixed property transactions, making a significant contribution to the existing body of literature. The results, which are substantiated by existing

scholarly sources, validate that the lack of a cohesive structure in the VAT Act contributes to its intricate nature. This study presents a primary contribution in the form of proposed guidelines for the restructuring of the VAT Act pertaining to fixed property transactions. The guidelines delineate the fundamental principles that must be integrated when improving the logical structure of the VAT Act in relation to fixed property. The universal guidelines encompass the use of headings and subheadings, the consolidation of intricate sections and explicit cross-referencing. Specifically, it is recommended that sections be consistently placed under their appropriate headings and exhibit clear signposting. The empirical findings of this study serve to enhance the current body of literature, in addition to contributing new insights, namely a practical illustration of the VAT implications for fixed property.

Generally, in interpretation of statutes, headings are not considered in the interpretation of a particular section. However, headings cannot be ignored completely. This is because in some cases they give meaning to the provisions. For example, the interpretation of subclauses may be impacted by headings, or subclauses may be drafted incorrectly, in which case headings may provide clarification. Thus, where headings are used for the simple purpose of grouping sections, the legislation must contain a provision to this effect. The structure of the TAA is divided into chapters which are further divided into parts. The table of provisions also makes it helpful to search for relevant sections. In addition, sections that are grouped together under such a heading must be grouped coherently. For example, under a heading 'fixed property' the provisions under the heading must refer to fixed property transactions only and cross-reference other sections that the provisions in question have an impact on, or to which these provisions are subject.

The primary objective of this study was to enhance the logical framework pertaining to fixed property transactions, considering their frequent occurrence in daily business operations. Consequently, the study did not consider the examination of other transactions that are similarly intricate under the VAT Act.

It is recommended that the proposed enhancement pertaining to the logical framework of the VAT Act with regard to fixed property transactions be included in the SARS VAT 404 guide. It is further recommended as an area for future research that the application of the guidelines used as a practical demonstration for fixed property transactions be extended to other instances of complexity cited in the VAT Act, such as VAT adjustments and imported services. If these practical illustrations were to be incorporated into SARS guides and interpretation notes, it is anticipated that they would enhance the teaching of VAT for students, facilitate the interpretation and implementation of VAT by tax practitioners and streamline the administration of the VAT Act by officials at SARS, particularly in the context of intricate transactions. Amongst other things, well-drafted easy-to-understand tax legislation enhances tax compliance and reduces tax compliance administration costs. This represents the initial phase in the process of simplifying VAT legislation.

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