



C:SARS v Capitec: A case of VAT equilibrium?



+27 83 417 5904



pieter@pvdz.co.za



www.pvdz.co.za



The Supreme Court of Appeal (SCA) recently upheld SARS' appeal in a case against Capitec Bank Limited. The case involved input tax deductions in respect of loan cover payouts. The SCA ruled that Capitec supplied the loan cover in the course of providing credit, an exempt supply. One of the factors considered by the court was the impact that an input tax deduction would have on the equilibrium of Capitec's VAT position. This article provides an overview of the case and raises a question on the equilibrium equation in the context of a vendor that makes exempt supplies.

In *Commissioner for the South African Revenue Service v Capitec Bank Limited* (94/2021) [2022] ZASCA 97 (21 June 2022) the Supreme Court of Appeal ruled that Capitec Bank Limited ('Capitec') could not deduct input tax in respect of loan cover payouts to borrowers. This article considers the case, in particular the court's views on the VAT equilibrium.

Facts

Capitec conducts a retail banking business, which includes unsecured lending. It provides loan cover to the customer as part of the standard terms of personal loans. Capitec pays premiums to an insurer and becomes entitled to payouts if the loan is not repaid on account of the borrower's death or retrenchment. It applies the insurance proceeds to settle or reduce the customer's outstanding loan. Capitec does not charge the customers a separate consideration for this cover.

Dispute

Capitec deducted input tax on the payouts it applied to settle loans of deceased or retrenched borrowers. This was in terms of section 16(3)(c), which allows a deduction for:

'an amount equal to the tax fraction of any payment made during the tax period by the vendor to indemnify another person in terms of any contract of insurance...'

This deduction is only available where the supply of insurance is a taxable supply.

Capitec contended that the interest and fees from the borrower was consideration for the taxable supply of loan cover or, alternatively, the loan cover was a taxable supply for no consideration (as contemplated in section 10(23)). SARS argued that Capitec did not charge consideration for the loan cover and supplied it to customers in the course of the credit business, which makes exempt supplies rather than taxable supplies.

Judgment

The SCA indicated that Capitec is in the business of providing credit, an exempt supply. The fees charged represent a minor component of that business. In the

absence of specific consideration for the supply of the loan cover, the supply of insurance in terms of the loan cover did not qualify as an enterprise. The insurance contract had one consequence that benefitted both Capitec and the borrower. The purpose and effect of the loan cover was to extinguish Capitec's credit risk. It ruled that Capitec supplied the loan cover in the course of providing credit, an exempt supply. It further considered section 10(23) to be a valuation rule that does not affect a supply's character. As a result, Capitec could not deduct the input tax.

Equilibrium

In paragraphs 31 to 33 of the judgment, the court considered the VAT equilibrium in Capitec's books:

- ▶ The insurer levied output tax on the premiums paid; Capitec deducted this tax as input tax.
- ▶ The insurer claimed deductions for payouts (in terms of section 16(3)(c)); Capitec paid output tax on these payments (in terms of section 8(8)).
- ▶ If Capitec deducted input tax on the payouts, this would skew the equilibrium.

However, a vendor may only deduct input tax on services acquired for purposes of consumption, use or supply in the course of making taxable supplies. In addition, section 8(8) only triggers a deemed supply if a vendor receives an indemnity payment under a contract of insurance to the extent that it relates to a loss incurred in the course of carrying on an enterprise.

A vendor that makes exempt supplies should arguably be consistently treated as the end consumer for all purposes in any VAT equation. If Capitec arranged and supplied the loan cover in the course of making exempt supplies, as the court found, this casts doubt on its ability to deduct input tax on the premiums paid. It is also questionable whether section 8(8) applies to the payments that Capitec received from the insurer.

@PvdZ Consulting. Please note that this newsletter is prepared for awareness purposes. It should not be construed as advice in any matter.



+27 83 417 5904



pieter@pvdz.co.za



www.pvdz.co.za

