

SOUTH AFRICA / JUDGMENT

Benhaus Mining (Proprietary) Limited v Commissioner of the South African Revenue Services (13863) [2017] ZATC 4; 80 SATC 455 (30 November 2017) [2017] ZATC 4

COURT

Tax Court

BEFORE

Weiner, Mathibela, Mashanda

CASE / FILE NUMBER

13863

Source: saflii.org · Research copy typeset by Esheria. Not court-issued or certified.

Source record

REPUBLIC
OF SOUTH AFRICA
IN THE TAX COURT OF SOUTH AFRICA
HELD AT JOHANNESBURG
CASE NO: 13863
REPORTABLE
OF INTEREST TO OTHER JUDGES
REVISED.
30/11/2017
In the matter

between:

BENHAUS
MINING (PROPRIETARY)
LIMITED
Appellant
and
COMMISSIONER OF THE SOUTH AFRICAN
REVENUE
SERVICES
Respondent

JUDGMENT

CORAM WEINER J, WITH MATHIBELA et MASHANDA, Assessors

INTRODUCTION

- [1] The appellant conducts business as a “contract miner”. It concludes contracts with third parties who hold mining rights and it undertakes to render certain services to such parties.
- [2] Prior to 26 September 2013, the appellant reflected the income received from the holders of the mining rights as mining income and was so assessed by the respondent. This entailed, inter alia, that capital allowances on equipment were deducted in full.
- [3] On 26 September 2013, the respondent raised additional income tax assessments in respect of the appellant’s 2005 to 2009 years of assessment.

[4] In terms of such assessments:

4.1 The appellant’s income was assessed as non-mining income (and accordingly capital allowances were added back and wear and tear allowances were granted).

4.2 Other adjustments were made and understatement penalties were levied on the appellant.

4.3 Interest on underpayment of provisional tax was levied pursuant to the adjustments.

[5] The issues to be decided are:

5.1 Whether the appellant conducted mining operations and mining as defined in section 1 of the Income Tax Act during its 2005 to 2009 years of assessment and accordingly whether the appellant derived income from “mining operations as contemplated in section 15 of the Act”. (“the main issue”)

If the appellant is held not to have conducted mining operations and therefore only wear and tear allowances are allowed, as opposed to the full capital allowance, the issue is whether the allowances allowed in terms of section 11(e) of the Act should be R267 528 904,00 as calculated by the respondent or R469 815 843,00 as contended for by the appellant. i.e whether they should be allowed over a period of two or three years.

5.2 Secondly, the issue of recoupments. The issue is whether the proceeds from the disposal of assets in the amounts and in the years of assessment had already been included in the appellant’s mining income or not, and accordingly, whether the respondent correctly included the amount in the appellant’s income as recoupments in terms of paragraph (j) of the definition of gross income in section 1 of the Act. The appellant treated same under mining operations and therefore recoupments were treated as part of the capex. If it is not mining operations, one has to determine whether, when the assets were sold, the depreciation should be part of gross income in terms of section 8(4)(a) of the Act.

5.3 Thirdly, the question of understatement penalties: whether the respondent has discharged the burden of proving the facts on which the respondent based the imposition of the understatement penalties and, if so, whether such penalties should be remitted or reduced.

5.4 Fourthly, section 89quat interest levied by the respondent in terms of section 89quat(2) of the Act should be remitted in whole or in part in terms of section 89quat(3) of the Act.

MAIN ISSUE

[6] The main issue in this appeal is whether the appellant derived income from mining operations which would have entitled it to the mining capital allowances. The decision on this issue will affect the remaining issues referred to above. Miners are subject to the ordinary provisions of the Income Tax Act No 58 of 1962 (“the Act”). There are however certain provisions which grant certain beneficial dispensations. For the purposes of the present appeal the following sections of the Act are relevant:

6.1 Section 15 of the Act provides:

“There shall be allowed to be deducted from the income derived by the taxpayer from mining operations:

(a) an amount to be ascertained under the provisions of section 36 in lieu of the allowances in section 11(e).”

6.2 Section 36(7C) provides that:

“The amounts to be deducted on the section 15(a) from income derived from the working or any producing mine shall be the amount of capital expenditure incurred.”

6.3 The definition of “capital expenditure” in section 36(ii) referred to in 15(a) refers to “expenditure ...on shaft sinking and mine equipment ...”.

6.4 Section 11(e) of the Act allows a “wear and tear deduction” of such sum as the Commissioner may think just and reasonable, which would represent “the amount by which the value of machinery, plant, implements, utensils and articles ... has been diminished by reason of wear and tear or depreciation during the year of assessment”.

[7] The benefit of a section 15(a) and section 36 deduction, as opposed to a section 11(e) allowance, is that the former sections allow the expenditure on a capital asset to be deducted in full during the first year of the acquisition, whereas a section 11(e) allowance is generally determined by referring to the expected life of the particular asset and the deduction takes place over that period of time.

[8] In regard to the main issue as to whether or not the appellant was engaged in mining operations and was deriving income therefrom, the following facts are common cause:

8.1 The appellant carries on business by contracting with clients to provide mining-related services to its clients in the mining sector.

8.2 The appellant does not hold any mining rights itself.

8.3 The mining-related services in question are in respect of open cast mining and include the following activities:

8.3.1 Site establishment including the fencing of the lay down and the workshop.

8.3.2 Construction and maintenance of access roads.

8.3.3 Construction and maintenance of primary and secondary haul roads.

8.3.4 Removal of topsoil and stock piling it all at designated areas.

8.3.5 Excavation and stock piling of the overburdened material at the designated areas.

8.3.6 Removal of waste.

8.3.7 Construction of storm water culvert sections.

8.3.8 Dwelling and blasting of overburdened and mineral-bearing ore.

8.3.9 Delivering the mineral-bearing ore to the client's designated premises for processing; rehabilitation of the mining area upon completion including concurrent rehabilitation in the form of backfilling, dewatering of open pits.

8.3.10 Rehabilitation of the mining area.

("the services").

[9] The essence of the contracts is that the appellant extracts mineral-bearing ore from the ground, on behalf of a client, in return

for a fee calculated at a rate per ton of mineral-bearing ore which is delivered to the client's processing plant. The ore extracted by Appellant was run-of-mine ("ROM") chromite ore or chrome-bearing ore

[10] During the relevant tax years most of the appellant's clients conducted chrome mining businesses and the ore extracted by the appellant was /chrome-bearing ore.

[11] The clients derived their income from the sale of the minerals extracted from the ore delivered by the appellant. The appellant in most instances derived a fee income from rendering the services in question.

[12] The appellant based its income tax returns on the fact that it was carrying on mining operations. Accordingly, its fee income constituted "income derived from mining" and it claimed the capital allowances in respect of the cost of equipment. In terms of the additional assessments,

the respondent disallowed the capital allowances claimed and added it back to taxable income for the relevant tax years and instead allowed wear and tear allowances.

- [13] The appellant either in its current name, or as it was previously known that is Benhaus Northwest (Proprietary) Limited, alternatively through its BEE subsidiary Benhaus Marketing (Proprietary) Limited entered into contracts with several companies to perform contract mining.

WHAT IS CONTRACT MINING

- [14] Van Blerk Mining Tax in South Africa[1] stated as follows:

“It sometimes occurs especially in the case of open cast mining that the mine owner subcontracts all or a portion of the mining operations to a third party. For example a contracting arrangement could require a third party to use earthmoving equipment to win ore by open cast methods and transport this ore to a processing plant. In these circumstances can it be said that the subcontractor is conducting mining operations.”

Van Blerk answers as follows:

“Since the right to mine precious stones and precious metals vests in the State and since all those who wished to undertake these activities must obtain a lease from the State it can be said that the major portion of mining conducted in South Africa is on a ‘contract’ basis. Quite obviously lessees mining in these circumstances are conducting mining operations.”

In dealing with a situation such as the present Van Blerk states:

“Can it be said that the same principles apply when the contract operates on the basis of a charge which relates to his inputs and efforts rather than receiving a share of the profits. ... If the contractor undertaking mining operations where he effectively conducts such operations for the benefit of another and receives no share in the results and profits other than a negotiated fee related to his efforts and costs. ... This must be so as the contractor is conducting a process by which a is one from the earth; as a consequence the income which he derives will be taxed in accordance with mining tax rates and the expenditures will be deductible in accordance with the special mining tax positions.”

- [15] The appellant relies upon Gloucester Manganese Mines Postmasburg Limited v CIR[2], where the taxpayer granted to a third party the sole right to mine manganese on certain property in return for a lease charge of 25% of the net profits. In regard to the lessee’s position, the court stated:

“If the present case concerning the liability to tax of the lessee company under the mineral lease in question it would I think be clear that the monies accruing to it from the exploitation under the mineral lease of the manganese found on the farm would be income derived by it from mining operations.”[3]

- [16] Section 15 of the Act provides that the taxpayer must derive income from mining operations for the provisions to apply. “Mining operations” and “mining” are defined in section 1 of the Act to include “every method or process by which any mineral is won from the soil or from any substance or constituent thereof”.

- [17] This definition was discussed by the Supreme Court of Appeal in *Western Platinum Limited v Commissioner of the South African Revenue Services*[4], where the following was stated:

“Mining operations by themselves cannot produce income. However the definitions of mining and mining operations being context-dependent is capable of accommodating commercial transactions. Since there can be no derivation of income without commercial activity, we are entitled to read that into the definition. In the case of minerals or metals from a mine such as an income-producing transaction would commonly be a sale. One would therefore at least have to interpose a sale (and the associated delivery and payment) between the extraction of the minerals and the income thus postulating a business ...”

I am nevertheless unable to accept the argument for the appellant that the Act contemplates as the source of the income the mining trade carried on by the appellant. In order to derive income a taxpayer must generally carry on a trade. That is not to say that the trade although it is a *sine qua non* of the trading income, is its source. Section 36(7C) of the Act speaks not of mining or mining operations but of “income derived from the working of any producing mine”. This expression (arguably more focussed than the expression mining and mining operations) leaves no doubt that to be mining income its source must be minerals taken from the earth. “the income had to be directly connected to the mining source”[5]

- [18] In the *Western Platinum* judgment the court held as follows:

“[9] The appellant’s counsel suggested that any income flowing from the trade of mining would be sufficiently closely connected to the mining operations to qualify as mining income. Counsel for the respondent on the other hand contended that only the proceeds of the sale of minerals would be sufficiently closely connected to the mining operations (the extraction and refinement of the minerals) to be properly characterized as mining income.

- [10] The appellant’s approach is too generous. The respondent’s, on the other hand, is too narrow. Direct connection is a flexible concept. Its application does not inexorably lead to categorisation of any income item other than the price itself as only indirectly or remotely connected with the mining source.”
- [19] The appellant contends that the term “business” has been defined in various judgments to include every profitable activity and is therefore a wider concept than trading. See *Valkin v Daggafontein Mines Limited*[6]; *Burgess v CIR*[7].
- [20] Appellant also relies upon the definition of “trade” in section 1 of the Act which includes “every ... business, occupation or venture”. It contends that the correct position, is as stated in *CIR v BP Southern Africa (Pty) Ltd*[8] and quoted with approval in *Western Platinum Limited v CIR*[9] that is that the phrase “income derived from mining operations” means “income derived from the business of extracting minerals from the soil”.

[21] The respondent, on the other hand, submits that the concept of a 'venture' must include an element of risk as was stated in *Burgess v CIR*. Appellant, however, refers to *Burgess* where Grosskopf JA held:[10]

"In conclusion on this point I must make it clear that, although an element of risk is included in the concept of a 'venture'

in its ordinary meaning, I must not be taken to suggest that a scheme like the present would only constitute a 'trade' if it is risky. Whether it would or not would depend on its own facts. If there is no risk involved, it might still be covered by given an extended meaning to 'venture' or by applying the rest of the definition, which is in any event not necessarily exhaustive."

[22] Appellant further contends that neither in the *Western Platinum* judgment nor in the *BP Southern Africa* judgment is there mention of the fact that some kind of commercial risk is a requirement for the business to fall within the definition. They further refer to the fact that neither *Van Blerck* nor any other authority mentions the so-called risk test.

[23] Appellant accordingly submits that the term "income derived from the business of extracting minerals from the soil" is wide enough to cover its business. According to the appellant's submission, what one needs to look at is the work the taxpayer does and not how he has been compensated, that is by a third party purchaser or by the holder of the mineral rights. It contends that income derived from the business of extracting minerals from the soil is income derived from mining operations irrespective of whether the taxpayer sells the minerals in the open market or not.

[24] It is common cause that Benhaus extracts the mineral-bearing ore not for its own account but on behalf of and for the benefit of the client in whom the ownership of the mineral-bearing ore vests. Appellant contends that the clients derive their income from the sale of the minerals extracted from the ore delivered by Appellant and it derives a fee from rendering the services. Respondent, on the other hand, submits that income derived from this service is not income derived from mining operations.

EVIDENCE

[25] Having dealt with the legal position in regard to the definitions applicable, the evidence of the parties needs to be analysed. The Appellant called Mr Botha, the founding shareholder and director of the appellant. Appellant consisted of a group of companies which was unbundled in 1994. Botha acquired the entire shareholding in Appellant and pursued the business of providing the services to companies holding mining rights. In 1998, on the advice of his accountant and auditor, Mr Woest, the appellant began rendering tax returns of Appellant on the basis that it derives its income from mining operations.

[26] In 2004, Appellant incorporated a subsidiary Benhaus Marketing (Proprietary) Limited ("Marketing") in which minority shares were held by previously disadvantaged persons. It was used to tender for work and conclude contracts with clients who required BEE compliant service providers. Several contracts were concluded, some between Marketing

and the clients; others directly between Appellant and the clients. Marketing subcontracted its obligations, under the agreements it concluded with its clients, to Appellant, as Marketing did not have equipment or employees to perform its obligations, whereas Appellant did. Appellant performed the services for its clients, as well as for Marketing's clients, for a fee. Marketing was paid directly by clients for the services. Marketing paid such amount over to Appellant after deducting a 1% commission. Appellant was paid directly for serviced rendered to its clients.

- [27] Botha testified that Appellant does not sell the mine chromite ore to its clients but gets paid for providing the services in terms of the contracts. The fees earned consisted of once-off fixed fees for once-off services, such as the site establishment and site de-establishment. Topsoil and overburden removal as well as rehabilitation was charged at a rate per cubic metre. The extraction and delivery of the ROM ore was calculated at a rate per ton. Botha testified that there are three stages involved in chrome mining using the open cast method. Firstly, the removal of topsoil and overburden, blasting the rocks to expose the reef, extracting the ore, crushing and screening the ore and delivering and stockpiling it at the washing plant. The screening process is not a process of separation of the metal from the waste, but just to reduce the size of the bulky material.
- [28] The second stage involves the milling of ROM chromite ore and subjecting it to the washing process. This is performed by Appellant's clients, the mining houses who own and operate the washing plants.
- [29] The third stage entails melting the lumpy higher concentrate ore in the furnace to separate waste from metal to produce ferrochrome. The smelters are owned and operated by the clients and mining houses. Appellant does not perform this operation. Ferrochrome is sold by the clients on the open market.
- [30] The respondent relies on the fact that Appellant is not exposed to any commercial risk associated with mining and selling ferrochrome. Thus, it contends that the activities are non-mining operations. There are no lengthy time lags between capital outlay and generating of income. Appellant's fees are not affected by the quality of the ore. That risk is borne by the clients. In addition its fee is not affected by the volatility of metal prices in the global markets. Its fee income is not affected by the exchange rate of the Dollar /Rand.
- [31] In regard to the write off period, Botha's reasoning was that he did not want to risk breakdowns so he decided to trade the equipment in earlier than the useful life. He admitted that these machines could still be used well beyond two years.
- [32] In regard to recoupments, Mr Malan the auditor and accountant of the appellant testified that the proceeds from disposal of equipment has been allowed in full and included in the unredeemed capital expenditure schedule, as he had treated the appellant as conducting the business of mining operations. Obviously, if it was not a non-mining company the proceeds from the sale would be added back to gross income.

- [33] The respondent contends that from its letter of audit findings and until the pleadings, SARS has stated that Appellant did not provide the details required in regard to disposed assets. Accordingly SARS assumed that the assets were acquired and deducted in full before 2005, and therefore, Appellant must have recouped the full amount of the proceeds. Respondent further contends that Appellant has consistently neglected to provide information to gainsay SARS's assumption and has never challenged the calculation of the amounts.

SPECIAL CONCESSIONS

- [34] Section 15(a) provides for special capital expenditure deductions and special concessions in favour of certain industries. Mining is one such industry.
- [35] Prior to claiming these concessions, it must be determined whether the capital expenditure qualifies for a special concession.
- [36] The respondent contends that Appellant firstly doesn't earn income derived from mining operations as set out above. Secondly, and in any event, does not meet the requirements set out in Section 36 of the Act.
- [37] Respondent submits that in order to qualify for the benefits under the section, income earned from each contract and/or each separate mine and the expenditure incurred in respect of each contract and/or each separate mine was not separately disclosed in the tax returns. Thus the income paid to Marketing and thereafter to Appellant was co-mingled with income received directly from the mining houses and not separately disclosed in the relevant tax returns. In addition, a small proportion of the income was derived from the hiring of equipment. This too was not separately disclosed as income not derived from performing the services.
- [38] Respondent contends that Section 36(7C) must be read with subsection (7E) and (7F). It is imperative to comply with section 36(7E) and (7F) to derive the benefit of the special capital expenditure deduction.
- [39] Section 37(7C) reads as follows:
- "Subject to the provisions of subsection (7E) and (7F) and (7G) the amounts to be deducted under section 15(a) from the income derived from the working of any producing mine shall be the amount of capital expenditure incurred."*
- [40] Section 15(a) of the Act read, at the time, that deductions from the income derived by the taxpayer from mining operations would be allowed – for an amount to be ascertained under the provisions of section 36 - in lieu of the allowances in section 11(e).
- [41] Respondent contends that, without ring fencing the precise income derived from the working of any producing mine, it is not possible to claim the capital expenditure as the mining and non-mining operations are not distinguished nor was the income and expenditure of each particular mine and contract dealt with separately. Subsection 36(7E) provides that when a taxpayer carries on a mining trade and a non-mining trade, capital

expenditure can only be deducted against taxable income derived from the mining trade. Subsection (7F) provides that where a taxpayer carries on mining operations to more than one mine, the deduction of capital expenditure incurred in respect of any one mine must be limited to taxable income derived from that mine. Respondent contends that this is an essential prerequisite to claiming the concessions and that Appellant failed to comply therewith.

- [42] In dealing with the interpretation of the legislation and applicable legal principles the respondent refers to the judgment of Wallis JA in *National Joint Municipal Pension Fund v Endumeni Municipality*[11].

“[18] Over the last century there have been significant developments in the law relating to the interpretation of documents, both in this country and in others that follow similar rules to our own.¹³ It is unnecessary to add unduly to the burden of annotations by trawling through the case law on the construction of documents in order to trace those developments. The relevant authorities are collected and summarised in Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School.¹⁴ The present state of the law can be expressed as follows. Interpretation is the process of attributing meaning to the words used in a document, be it legislation, some other statutory instrument, or contract, having regard to the context provided by reading the particular provision or provisions in the light of the document as a whole and the circumstances attendant upon its coming into existence. Whatever the nature of the document, consideration must be given to the language used in the light of the ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose to which it is directed and the material known to those responsible for its production. Where more than one meaning is possible each possibility must be weighed in the light of all these factors.¹⁵ The process is objective not subjective. A sensible meaning is to be preferred to one that leads to insensible or unbusinesslike results or undermines the apparent purpose of the document. Judges must be alert to, and guard against, the temptation to substitute what they regard as reasonable, sensible or businesslike for the words actually used. To do so in regard to a statute or statutory instrument is to cross the divide between interpretation and legislation. In a contractual context it is to make a contract for the parties other than the one they in fact made. The ‘inevitable point of departure is the language of the provision itself’,¹⁶ read in context and having regard to the purpose of the provision and the background to the preparation and production of the document”.

See also *City of Tshwane v Marius Blom and Another*[12]:

- [43] In dealing with the interpretation, Respondent also refers to the strict construction of the empowering legislation which was referred to in the *Western Platinum Limited* case. Reference was also made to the *Margo Commission*[13] where the rationale for the deduction of capital expenditure granted by the Act to taxpayers, carrying on mining operations, was

summarised as follows:

“14.17 The mining industry is granted a special allowance, known as the redemption allowance, for the redemption of capital expenditure. It is not granted the wear-and-tears, crapping or obsolescence allowances on plant and machinery granted to traders, manufacturers and others. It is in this respect that the tax assessment of a mining concern differs radically from that of any other industry or trade, although it is similar in certain respects to farming...”

14.26 The justification for allowing the immediate write-off of capital expenditure in mining is grounded on one point of principle and two practical considerations. The point of principle is that, mining being an exceptionally risky venture, no lease consideration or tax should be payable until capital expenditure has been recouped in full. It is argued that, were any other policy to be followed, there would soon be fewer mines and a smaller tax base. The practical considerations are that immediate write-off is simpler, especially in a mining environment; and that the alternative would be to write assets off over their useful lives, which in many cases would entail highly contentious estimates of the life of the mine.”

[44] Further the respondent submits that the Davis Tax Commission[14] provides the rationale behind the special concessions given to the mining industry:

“2.1. Life cycle of mines

The nature of mining is such that mining operators are exposed to protracted lead times before the generation of revenue. This problem is exacerbated due to the high upfront capital infrastructure costs associated with establishing a mine. Therefore, in the early period of operations, risks and expenditures are very high, while revenue inflows are delayed for a considerable time (this issue is discussed in greater detail as a prelude to the discussion on tax incentives proffered to mining taxpayers).

2.1. Evolution of special mining tax incentives

The life cycle of a mine is shaped by various factors which differentiate it from manufacturing concerns. These factors need to be understood in order to have some appreciation for those drivers giving rise to the provision of special tax incentives to the mining industry.

Mining is a cyclical industry and investments in the different stages of the mining industry lifecycle (exploration, development, production and mine closure) tend to follow these cycles. In general, as already noted, mining is a long-term activity requiring significant upfront capital investment and expertise to develop large ore-deposits to the mining production stage. The steps of moving from greenfields exploration⁹⁵ through to the development of operating mines (when income is finally generated) may involve multiple decades and many billion rands to bring a project to fruition. Over this period the project will be exposed to fluctuating commodity cycles, changing technology and risks on the geology and technical side of a project, as well as other extraneous potential risks. Mining is also a geographically situated activity which is subject to significant risk from sudden changes described earlier. Other industries are far more mobile and will relocate to different jurisdictions should the political or legislative environment change significantly.”

- [45] The respondent contends that none of these reasons for the special concessions to mining companies apply in the case of contract mining performed by Appellant, which is not exposed to the kind of risks facing mining companies proper and that the legislature intended to give the benefits to the latter and not to the former.
- [46] The respondent's submission is that there are huge start-up costs and no immediate or short term income for mining companies proper. It is contended that when the mine reaches production stage it is considered reasonable that they must recoup their capital expenditure before starting to pay tax. This the respondent contends, is not a problem that arises in contract mining cases as there is almost immediate income and no real mining risk as envisaged by the Margo Report and the Davis Tax Commission.

THE SUTHERLAND JUDGMENT

- [47] In the matter of Classic Challenge Trading (P/L) V C Sars[15], Sutherland J had to deal with the question whether contract mining constitutes mining operations as defined in the Act. Sutherland J held as follows:

"Mere extraction is not enough to render a contract and earns a fee for extraction as a person eligible to fall into the class of persons who are engaged in mining operations as defined. The contract is not in the 'trade of mining' rather the contract is in the trade of servicing a mine's requirements by the extraction of material."

- [48] Sutherland J went on as follows:

"The introduction of the concept of a 'producing mine' is plainly a serious constriction of the scope of the deduction benefit; i.e. not every mine can qualify. What needs to be produced is minerals. A worked out mine cannot be 'producing'."

Axiomatically, a mine that produces minerals shall also produce revenue, whether or not a profit is achieved. But a mine that fails

to 'win' any minerals cannot be a 'producing mine'. From this provision it must be inferred that the benefit is aimed at a limited class of miners."

"The upshot of these provisions, in my view, is that the section 15 deduction entitlement can be available only to taxpayers whose

'mining operations' involve capital expenditure of the nature described which is capable of computation by these formulae. Taxpayers whose 'mining operations' involve 'capital expenditure' that cannot fit into this straitjacket are not taxpayers who fall into the class intended to be beneficiaries of the special up-front capital deduction benefit."

"The perception that investors in mining who invest huge sums and wait long periods for a return need relief through special tax benefits is at the heart of the special capital deduction provisions. The Davis Committee (Supra) observed in 2014:

In addition to the general tax provisions, the mining sector is also eligible for various deductions, capital and other tax incentives as described below.

2.1 Evolution of special mining tax incentives

The life cycle of a mine is shaped by various factors which differentiate it from manufacturing concerns. These factors need to be understood in order to have some appreciation for those drivers giving rise to the provision of special tax incentives to the mining industry.

Mining is a cyclical industry and investments in the different stages of the mining industry lifecycle (exploration, development, production and mine closure) tend to follow these cycles. In general, as already noted, mining is a long-term activity requiring significant upfront capital investment and expertise to develop large ore-deposits to the mining production stage. The steps of moving from greenfields exploration through to the development of operating mines (when income is finally generated) may involve multiple decades and many billion rands to bring a project to fruition. Over this period the project will be exposed to fluctuating commodity cycles, changing technology and risks on the geology and technical side of a project, as well as other extraneous potential risks. Mining is also a geographically situated activity which is subject to significant risk from sudden changes describes earlier. Other industries are far more mobile and will relocate to different jurisdictions should the political or legislative environment change significantly.

In an effort to ameliorate the risk posed to mines during their production life cycle, special tax allowances have been provided over the years (discussed more fully below). These incentives provide for the following allowances:

- a) To cater for the large upfront investments made by mines
- b) The costs of decommissioning mines (mostly environmental rehabilitation costs)
- c) In the case of gold mines (for many years gold was the mainstay of South African mining), providing certain additional allowances (mainly intended as a proxy for the cost of money involved in financing the capital outlays involved in commissioning a mine)
- d) Also, specifically in the case of gold mining, tax relief for those taxpayers mining marginal ore bodies.

2.3. Deductions

2.3.1.....

2.3.2 Depreciation

Normally taxpayers are allowed to write off assets acquired and used for purposes of trade over the useful life of such assets. Special write-off allowances are granted for manufacturing operations, owners of commercial property, owners of hotels, pipelines, and so forth, but for purposes of this report this is not elaborate on. To the extent that part of a mining taxpayer's operations do not constitute mining operations as defined, it therefore has to avail itself of these general write-off allowances.

The abovementioned is of importance in that these general provisions are only overridden as far as they pertain to a mining taxpayer carrying on mining operations. Furthermore, mining taxpayers carrying on mining operations. Furthermore, mining taxpayers are entitled to a 100% capital redemption allowance (discussed below) in lieu of the allowances that would otherwise be granted (not in addition) to non-mining taxpayers.

It is important to bear in mind that the 100% capital redemption allowance is not elective; once a taxpayer satisfies the requirements of the definition of mining operations and mining, such a taxpayer is compelled to claim 100% capital redemption allowance as envisaged in section 15 read with 36 of the Income Tax Act.”[18]

(Underlining supplied)

- [49] Respondent accordingly contends that Appellant's activities do not constitute mining operations and its fees do not qualify as income derived from working of any mine. It accordingly does not qualify for deduction of capital expenditure in terms of section 15(a) read with section 36 of the Act.
- [50] Sutherland J also referred to the 'risk element' being a prerequisite. The appellant however contends that the notion that risk as a requirement of a trade was not supported either in the Burgess judgment or in the Gloucester Manganese Mines judgment which Sutherland J relied upon. The appellant however contends that, in any event, it did take risks in that owned equipment and it incurred expenditure for the working equipment. Further risks related to insufficient contracts being obtained, strikes, possible breach of contract and breakages of machinery and equipment. Botha also testified that in the event of the rock and overburden removed by the appellant not containing chrome, appellant does not earn anything. Further if the material delivered over the weighbridge is not of a certain grade the appellant would not be paid.
- [51] Sutherland J also found[19] that the phrase “won from the soil or any substance or constituent thereof” contained in the definition of mining operation and mining in section 1 of the Act, “suggest the inclusion of processes that might be quite distinctive or physical separate from the actual digging of the stuff out of the ground but nevertheless remain a mining operation”.
- [52] Sutherland J came to the conclusion that:

“In the train of activity which constitutes mining operations it seems plain that the mere activity extraction is a necessary but not sufficient attribute for the taxpayer to fall into the class of persons involved in mining operations.”[20]

[53] Appellant contends that if the Classic Challenge judgment was correct, it would mean that no mining capital allowances at all would be available to any of the parties. Firstly, the owner of the mineral rights and the party selling the minerals does not incur any expenditure in respect of the mining equipment and secondly, the contract mining would be denied the mining capital allowances and could only claim the usual wear and tear allowances. I agree that the statement that the tax payer must be involved in every step of the operations cannot be correct. However, in view of the decision at which I have arrived, it is not necessary for the purposes of this judgment to debate this issue further.

[54] Respondent accordingly contends that, as Appellant does not qualify for deduction of capital expenditure in terms of section 15(a) read with section 36, it will however qualify for deduction of depreciation allowance in terms of section 11(e), which reads as follows:

“11. For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived—

(e) save as provided in paragraph 12 (2) of the First Schedule, such sum as the Commissioner may think just and reasonable as representing the amount by which the value of any machinery, plant, implements, utensils and articles (other than machinery,

plant, implements, utensils and articles in respect of which a deduction may be granted under section 12B, 12C or 12E) owned by the taxpayer or acquired by the taxpayer as purchaser in terms of an agreement contemplated in paragraph (a) of the definition of “instalment credit agreement” in section 1 of the Value-Added Tax Act, 1991 (Act No. 89 of 1991), and used by the

taxpayer for the purpose of his or her trade has been diminished by reason of wear and tear or depreciation during the year of

assessment.”

[55] The rate of depreciation allowance is determined by the Commissioner in his discretion based on the economic useful life of the equipment. Certain practice notes have been issued to prescribe write off periods for different assets.

[56] The respondent has granted Appellant depreciation allowances in respect of the same assets which claims were disallowed under section 15(a) read with section 36. The question is whether or not the period should be two years from the date of acquisition or three years from the date of acquisition. According to the evidence of Botha and Malan it was conceded that the equipment was still fit for the purpose for which it was used after the two year period. Respondent submits that Appellant’s own policy based on its subjective considerations cannot override objective considerations that inform the write off periods of general application..

RECOUPMENTS.

[57] The parties are in agreement that, if Appellant does not carry on mining operations, the recoupment from the sale of depreciable assets falls to be included in gross income. In terms of the definition of the phrase “capital expenditure incurred” in section 36(11), proceeds from the disposal of assets included in capital expenditure must be applied to reduce the amount of unredeemed capital expenditure. The question is whether the amounts were so included. Appellant alleges that they

were included. SARS disagrees. The quantum of the amounts of recoupment is not in dispute. Once it is held that the taxpayer does not qualify for capital expenditure deduction the recoupment amount remains untaxed and must be included in gross income.

[58] Malan conceded that SARS was not provided with the details of the disposed assets to enable SARS to verify the acquisition dates. As a result, SARS made an assumption that all the disposed assets were acquired before the 2005 tax year and therefore their cost had been deducted by Appellant in full during the years up to 2004 in terms of section 15(a) read with section 36 of the Act.

[59] Based on this assumption that the disposed assets were acquired prior to 2005 and therefore deducted in full for tax purposes, the whole amount of proceeds realised from their disposal had to be included in Appellant’s gross income.

[60] Respondent submits that the proceeds from the disposal of the assets had not been previously included in appellant’s gross income. Although these proceeds were netted off against the balance of unredeemed capital expenditure in the capital expenditure schedule, these amounts remained untaxed as the schedule was disregarded when appellant was taxed as a non-mining company.

PENALTIES

[61] In terms of section 222(1) of the TAA in the event of an understatement by a taxpayer, the taxpayer must pay the understatement penalty unless the understatement results from a bona fide inadvertent error. The total amount of the understatement is R124 269 913,00 which exceeds the R1 million threshold for substantial understatement. Section 223(3) of the TAA empowers SARS to remit understatement penalties if SARS is satisfied that the taxpayer either made full disclosure or was in possession of an opinion by an independent registered tax practitioner that confirmed the taxpayer’s position.

[62] The respondent contends that full disclosure was not made and the opinion of the tax practitioner was only obtained after the returns were submitted. Factually therefore, there was no reliance on an expert.

SECTION 89quat INTEREST

- [63] Section 89quat was repealed by the TAA, but continues to apply as the effective date of its repeal is yet to be proclaimed.
- [64] In terms of the section, interest subject to the provisions of subsection (3), was payable by the taxpayer at the prescribed rate on the amount by which the normal tax exceeds the credit amount. In terms of subsection (3), where the Commissioner, having regard to the circumstances of the case, is satisfied that any deduction claimed by the taxpayer has not been allowed and the taxpayer has on reasonable grounds contended that such deduction should have been allowed, the Commissioner may direct that interest shall not be paid by the taxpayer. The test therefore is whether the submissions that Appellant was carrying on mining

operations for the purposes of section 15(a) and section 36 were based upon reasonable grounds. Respondent contends that having regard to the Western Platinum decision, it was not reasonable for Appellant to persist with treating itself as deriving income from mining operations. Again, the appellant did not have an expert opinion at the time, on which it based this decision.

CONCLUSION

- [65] The appellant has not succeeded in demonstrating that it derived its income from mining operations. This question is somewhat vexed having regard to the definition, which seems to include the appellant's business, and the comments made in the Margo Report and the Davis Tax Commission, which demonstrate why the appellant's business is excluded from the definition and the permissible deduction. If one takes a purposive view of the Legislation, the latter comments must come to the fore in dealing with the interpretation to be placed on such legislation.
- [66] However, the question then arises whether, if the appellant had demonstrated that the income was derived from mining operations, has there been compliance with the relevant subsections of Section 37 of the Act. There clearly has not and in the circumstances, the deductions claimed could not be allowed.
- [67] For the reasons stated above, the assessments in respect of recoupments, penalties and interest cannot be challenged.

- [68] Accordingly, the following order is made:

68.1 The appeal is dismissed with costs.

S.E. WEINER

JUDGE OF THE HIGH COURT

GAUTENG LOCAL DIVISION, JOHANNESBURG

Attorney for appellant:

Lacante Henn Inc

Counsel for appellant:

Advocate P.J.J. Marais SC

Advocate J. Truter

Attorney for respondent:

Ms A. Mohammed

Counsel for respondent:

Advocate A.R. Bhana SC

Advocate N.K. Khumalo

Date matter heard:

28 November 2016 to 30 November

2016 & 8 June 2017

Judgment date:

[1] Pages 7 to 21 paragraph M First Edition.

[2] 12 SATC 229.

[3] At 232

[4] 2004

(4) All SA 611 (SCA) 67 SATC 1.

[5] At paragraph [7].

[6] 1960

(2) SA WLD at 511F.

[7]

[1993] ZASCA 88; 1993 (4) SA 161 (A) at 181I-J.

[8] 1997

(1) SA 375 (CPD) at 379 C - D

[9] [2004] 4 All SA 611

[10] At 182G - E

[11] 2012

(4) SA 593 (SCA) at 18.

[12] 2013

(3) All SA 481 (SCA).

[13] (Report of the Commission of Inquiring into the Tax Structure of the Republic of South Africa RP 34/1987 (ISBN 0621106887))

[14] interim Report on Mining for Finance Minister (December 2014, pages 24 and 41)

[15] Unreported judgment of Sutherland J, Case Number 13686 (30 March 2017)

[16] At paragraph [36]

[17] At paragraph [42]

[18] At paragraph [48]

[19] At paragraph [12]

[20] At paragraph [23]

Source & reproduction note

Judgment wording, source notices and original paragraph numbers are retained. Esheria supplies the layout and this PDF's page numbers; these are not the source pagination. This is a research copy, not an official or certified court document. Check quotations, citations and publication restrictions against the original source before relying on it.

ORIGINAL SOURCE <https://www.saflii.org/za/cases/ZATC/2017/4.html>

CASE PAGE <https://chat.esheria.ai/case-law/south-africa/benhaus-mining-proprietary-limited-v-commissioner-unknown-topic-atc-2017--6a3ea5203b1caa91298163b3>

Prepared on 10 October 2026 · Esheria