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The South African Revenue Service  
Lehae La SARS, 299 Bronkhorst Street  
PRETORIA  
0181

BY EMAIL: [policycomments@sars.gov.za](mailto:policycomments@sars.gov.za)

**RE: Draft Interpretation Note: Remuneration exemption for officers or crew members of a SA ship**

We write to comment on the draft interpretation note on the section 10(1)(o)(iA) exemption from income tax of remuneration derived by a person as an officer or crew member of a South African ship.

A. Interpretation of the definition of "Republic" in the context of the exemption

In terms of section 1(1) of the Income Tax Act:

'Republic' means the Republic of South Africa and, when used in a geographical sense, includes the territorial sea thereof as well as any area outside the territorial sea which has been or may be designated, under international law and the laws of South Africa, as areas within which South Africa may exercise sovereign rights or jurisdiction with regard to the exploration or exploitation of natural resources; (our underlining)

In terms of the exemption contained in section 10(1)(o)(iA) item (bb):

there shall be exempt from normal tax any form of remuneration as defined in paragraph 1 of the Fourth Schedule, derived by any person as an officer or crew member of a South African ship as defined in section 12Q(1) mainly engaged in fishing outside the Republic; (our underlining)

In this exemption, 'Republic' is used in the geographical sense because the test is whether or not the ship is mainly engaged in fishing outside the Republic, compared to inside the Republic. In other words, the test is where the fishing is taking place in a geographical sense. Therefore, the applicable definition of the 'Republic' is not restricted to 'the Republic of South Africa' in the juridical sense, but is the extended definition in the geographical sense.

On the other hand, in the draft interpretation note, the extended definition is applied differently in different circumstances. For example, it is stated under point 4.4 that:

For purposes of item (bb) resident officers or crew members aboard a South African ship mainly engaged in fishing are regarded as being outside the Republic when the ship is either beyond the EEZ or beyond the edge of the continental shelf of South Africa depending on the type of fishing that is done.

For fishing of "living organisms belonging to sedentary species" the Republic will extend **up to the edge of the continental shelf of South Africa**. For all other types of fishing, the Republic does not extend **beyond the EEZ**.

We are of the view that where the extended definition applies (i.e. where the 'Republic' is used in a geographical sense) that the full definition should be applied regardless of the circumstances and that the Republic would then include all areas referred to in the definition. In other words, the 'Republic' (in the geographical sense) is defined on a "one size fits all" rather than a "fit for purpose" basis. Hence, the "type of fishing" is completely irrelevant. There is nothing in the definition of 'Republic' or the wording of section 10(1)(o) to suggest otherwise.

Our view is supported by Divaris<sup>1</sup> as follows:

Taken at face value, the definition of 'Republic' refers, locationally, to a place

- within its landmass,
- within its territorial waters (the twelve-mile zone), or
- within its exclusive economic zone (the 200-mile zone).

There can be no warrant whatsoever for claiming that it applies only to the landmass and the twelve-mile zone, since to do so is to ignore the full text of the definition of 'Republic' in s 1(1).

...

Nor, to repeat the point more generally, may location within or without the Republic depend upon the precise laws, as established by the Maritime Zones Act, applying to various subdivisions of the sea, since the freedoms and limitations imposed by that act constitute powers claimed by and granted to the state under international law and not directions whether an event or a person is within or without the Republic.

If SARS, looking no further than the Income Tax Act, wanted to locate an event or a person within the Republic, it would have to search for a presence either on the landmass or within a border drawn 200 nautical miles from the baselines of that landmass. Under that act, it enjoys, in my view, no other choice, despite the specific reference in the definition of 'Republic' to the territorial sea, that is, presumably, the twelve-mile zone. That reference does not extend to it the choice of selecting the part while ignoring the whole subsuming that part. (our underlining)

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<sup>1</sup> C. Divaris, Tax Shock Horror Newsletter, Issue 155, February 2016 at page 11

Following this “one size fits all” interpretation of the ‘Republic’ would also address the practical difficulties of applying a “fit for purpose” interpretation. Employers cannot be expected to apply different tests for different crew members and separately isolate different activities. Annexure B of the draft interpretation note contains a comparison between section 10(1)(o)(i), (iA) and (ii) where the “fit for purpose” interpretation is followed in relation to the “outside the Republic” requirements contained in these subsections. It demonstrates that some officers or crew members employed on a ship may be regarded as being in the Republic (e.g. those navigating a mining vessel) while other officers or crew members employed on the same ship may be regarded as being outside the Republic at the same time (e.g. the chef on the mining vessel) if the vessel is beyond the territorial waters but not beyond say the continental shelf.

Should SARS agree with our interpretation of the definition of ‘Republic’ in a geographical sense, we would recommend that the draft interpretation note (including point 4.4 and Annexure B) be revised accordingly. The same principles would also apply for section 10(1)(o)(i) and (ii) and their interpretation notes.

**B. Officer or crew member outside the Republic – not a requirement for section 10(1)(o)(iA) item (aa)**

Reference is made under point 4.4 to the requirement that the officer or crew member must be outside the Republic, also for those aboard a South African ship mainly engaged in international shipping. Under item (aa), the only test is whether the ship is mainly engaged in international shipping. There is no requirement to determine whether such employee was outside the Republic. Therefore, officers and crew members of a South African ship engaged in international shipping enjoy the exemption even in respect of their coastal activities occurring inside the Republic. Stated differently, these officers and crew members do not have to bifurcate their international shipping activities into South African versus external components in terms of the exemption (i.e. the whole international shipping activities is exempt).

C. Application of the exemption to non-residents

It is stated under point 4.2 that:

The exemption under section 10(1)(o)(iA) applies to “any person” but practically can only mean an individual who is South African resident. Remuneration received by or accruing to a person other than a resident (non-resident) for services rendered outside the Republic is not from a South African source and therefore not subject to normal tax in South Africa.

We question whether SARS’s practical understanding is correct in this regard. South African ships can have foreign crew members and officers. Flags and crew members / officers often do not correspond in national terms. Because the South African flagged ships will come into port in South Africa from time to time, some of the services rendered by the crew will likely be rendered in the Republic and from a South African source. Therefore, non-residents could also potentially benefit from the exemption (before any DTA).

D. International traffic

Reference should also be made to the OECD Model DTA Commentary on Article 3 for support for the definition. Refer point 5 of paragraph 1 to the commentary on Article 3.

E. Mainly engaged in fishing

It is stated under point 4.3.2 that:

...the ship must be engaged in fishing outside the Republic for more than 50% of its time.

We think that this should be when compared to the time fishing inside the Republic, similar to the test applied under point 4.3.1 for ships engaged in international traffic when compared to domestic conveyance. Times when a ship is sitting in port for repair, maintenance, etc should be wholly disregarded. The comparison should simply be between local fishing periods versus foreign shipping periods.

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We welcome the opportunity to comment on the draft interpretation note and look forward to future engagements.

Yours sincerely

**Erika de Villiers**  
**Head of Tax Policy**