THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

JUDGMENT

Reportable

Case No: 923/2017

In the matter between:

SASOL OIL PROPRIETARY LIMITED **APPELLANT**

and

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **RESPONDENT**

Neutral citation: *Sasol Oil v CSARS* (923/2017) [2018] ZASCA 153 (9 November 2018)

Coram: Lewis, Ponnan, Cachalia and Makgoka JJA and Mothle AJA

Heard: 21 August 2018

Delivered: 9 November 2018

Summary: Contracts for the sale of crude oil by one entity within the Sasol Group, to another, and the back to back sale of the same oil to yet another entity in the group, were not simulated in order to avoid a liability to pay tax; nor were they entered into solely for the purpose of avoiding the payment of tax for the purpose of s 103(1) of the Income Tax Act 58 of 1962.

ORDER

On appeal from: Tax Court, Johannesburg (Mali J sitting with two other members):

1 The appeal is upheld with the costs of two counsel.
2 The order of the Tax Court is set aside and is replaced with the following order:
'The appeal against the additional assessments issued to the appellant on 30 April 2010 by the Commissioner for the South African Revenue Service for the 2005, 2006 and 2007 years of assessment is upheld and those assessments are set aside.'

JUDGMENT

Lewis JA (Ponnan and Cachalia JJA concurring)

[1] In this appeal against the decision of the Tax Court sitting in Gauteng (Mali J and two other members), there are two main issues. First, whether two contracts for the sale of crude oil sourced in the Middle East, acquired by a company in the Sasol Group in the Isle of Man, sold to another company in the Sasol Group based in London, and in turn sold and shipped to Sasol Oil (Pty) Ltd (Sasol Oil), the appellant, in Durban, were simulated transactions and should be disregarded by the Commissioner for the South African Revenue Service, the respondent, in the assessment of taxation in 2005, 2006 and 2007. I use the term 'Sasol Group' loosely to include all the holding companies and subsidiaries that are relevant to this appeal.

[2] Second whether, if the transactions were not simulated, they fell within the provisions of s 103(1) of the Income Tax Act 58 of 1962, and were thus to be disregarded for the purpose of assessing liability for income tax in the hands of Sasol Oil. The Commissioner issued additional assessments in the years in question, against

which Sasol Oil appealed. The amounts in dispute are in excess of R68 million, penalties in terms of s 76 of over R68 million and interest in terms of s 89 *quat*.

[3] The two contracts in issue before the Tax Court were entered into between Sasol Oil and Sasol International Services Ltd (SISL), and between SISL and Sasol Oil International Ltd (SOIL). In terms of these, SISL agreed to sell crude oil and deliver it to Sasol Oil on a DES (delivered ex ship) basis, and SOIL agreed to procure crude oil and deliver it to SISL on an FOB (free on board) basis.

[4] The Tax Court found that the impugned transactions were simulated and did not therefore consider the implications of s 103(1). It upheld the Commissioner's assessments and confirmed the imposition of penalties and the obligation to pay interest. This appeal is with the leave of the Tax Court. I shall deal with the relevant provisions of the Act in due course. It is important first to describe the Sasol Group entities and the roles they played at various times.

Sasol Oil

[5] Sasol Oil was at all times a subsidiary of Sasol Ltd. The business of Sasol Oil was the refining of crude oil and the marketing of fuels produced from coal. It did this at a refinery inland. It made its profits by buying crude oil at a lower price than the refined products that it sold and supplied throughout South Africa. Before oil sanctions were lifted in 1991, Sasol Oil purchased its crude oil from the State's Strategic Fuel Fund. When sanctions were lifted, Sasol Oil started sourcing and importing crude oil from a number of suppliers in the Middle East, mostly from Iran, Saudi Arabia and Kuwait. It had in place term contracts for the supply of crude oil, which gave it security of supply and lower prices than were available in the open market, for crude oil bought on the spot.

Other corporate entities in the Sasol Group

[6] From 1991 to 1997 Sasol Oil purchased and shipped crude oil from the suppliers in the Middle East, and spot oil from Western African suppliers. At that time

as well, the Sasol Group started to ‘globalize’. There were companies established in different locations, the relevant ones being Sasol Trading International Ltd (STI), incorporated in November 1997 in the Isle of Man. Sasol Trading Services Limited was incorporated in the United Kingdom, based in London, in December 1997. Its name was changed to Sasol International Services UK (SISL) in February 1998. STI and SISL were wholly owned subsidiaries of Sasol International Holdings (Pty) Ltd (SIH), incorporated in South Africa in September 1997.

The period from December 1997 to July 2001

[7] The Sasol Group undertook a major restructuring of entities within the group. The restructuring resulted in a change of oil procurement functions. From 1997 STI, rather than Sasol Oil, started procuring from Middle Eastern suppliers, and sold the crude oil acquired in terms of term contracts to Sasol Oil. It shipped the oil to the Durban port on a DES basis (delivered ex ship). Sasol Oil paid STI for the oil and its services.

The period from July 2001 to July 2004

[8] STI procured crude oil from the Middle Eastern suppliers in terms of their term contracts and sold it to SISL, delivering on an FOB basis (Free on Board). SISL in turn sold the crude oil to Sasol Oil, delivering it to Sasol Oil at the Durban port on a DES basis. The name of SIH was changed to Sasol Investment Company (SIC) in June 2002. In April 2004, Sasol Oil International (SOIL) was established in the Isle of Man, as a wholly owned subsidiary of Sasol Oil. STI and SISL remained wholly owned subsidiaries of SIC.

The implication of the changes from 2000 to July 2004

[9] The Sasol Group, from 1997, had one office in the Isle of Man, the business establishment of STI, which procured crude oil for on sale to Sasol Oil. And there was an office in London where SISL performed shipping and marketing services, mostly for STI. By the end of 2000, the people running the businesses of STI and SISL were concerned about the duplication of office accommodation and staff required. The

principal players were Mr Desmond Gird, who had joined the Sasol Group in 1981 and Mr Henri Loubser, a chemical engineer, who joined the Group in 1982. Gird was Sasol Oil's trading manager. He moved to SISL in London in February 1998, where he was the head of the company and from 2000 also a director. Loubser oversaw the chemical processes in Secunda, South Africa, and the refinery in Sasolburg – Natref. In May 2001 he was appointed as a director of SISL. I shall discuss their evidence in more detail later.

[10] In brief, Gird testified about oil trading and the need for crude oil to be procured for Sasol Oil. He and Loubser, who was his immediate manager, had discussed rationalization of the offices in the Isle of Man and London. When the Sasol Group had started the internationalization project, they had envisaged a base in London, which was the leading oil trading and financial centre, and which had excellent shipping infrastructure. But because of UK tax rates they had also needed to set up a business establishment on the Isle of Man which was considered to be a 'tax haven', and the decision had been made to locate the trading function there, hence STI's incorporation in the Isle of Man in 1997.

[11] This evidence is supported by an application made through Investec Bank to the South African Reserve Bank (SARB) in September 1997. It was anticipated that the profits made by STI would serve as capital for foreign expansion and would not be subject to South African exchange control regulation.

[12] In September 1998, STI and Sasol Oil entered into a crude oil supply agreement (the Original Supply Agreement) in terms of which STI would procure crude oil and sell and ship it to Sasol Oil on a DES basis. STI would be near London and would therefore benefit from SISL's expertise in marketing intelligence in tracking crude oil prices and from introductions to other traders operating in London.

[13] In 2000 the Sasol Group made a bid to acquire a German chemicals group, Condea. The board of directors of SIH (the holding company of STI and SISL) requested a review of the SIH structure in anticipation of the acquisition of Condea.

Gird was instructed to review the operations of STI and SISL and to submit a restructuring proposal, after a professional firm's review of it, to the board in February 2001. Pursuant to this, Gird prepared a proposal in early December 2000, suggesting that the crude oil trading function be relocated from STI in the Isle of Man to SISL in London.

[14] Loubser presented the proposal prepared by Gird to the Sasol Oil Board on 8 February 2001. The essence of the presentation was that there was an 'unavoidable duplication of effort by STI, SISL and Sasol Oil'; the costs of maintaining their offices and business contacts was too high in the light of lack of growth of the business; and the costs of commuting between the Isle of Man and London should be avoided. The cost saving of rationalizing the respective functions of STI and SISL was estimated to be R3 million per year. Gird's proposal, presented by Loubser, further suggested that the oil and products trading be relocated to SISL in London. Any South African products trading would be relocated from STI to Sasol Oil.

[15] On 20 February 2001, the board of Sasol Oil resolved that the Gird proposal should be considered by the Group Executive Committee (GEC) of the Sasol Group. Pursuant to this, Loubser who was a member of the Sasol Oil Board and was present at the meeting, requested Gird, who was in London at the time, to obtain a legal opinion on the UK tax implications of the proposed restructuring, which Gird did. He consulted Mr Kevin Ashman of the solicitors' firm Lovells shortly thereafter. Gird and Ashman met on 21 February 2001.

The Lovells advice

[16] On 7 March 2001, Ashman wrote to Gird setting out his advice. He confirmed that the proposed relocation of the crude oil trading function from the Isle of Man to London would not have any adverse UK implications for SISL, save that there would be an increase in SISL's UK tax as a result of the increase in the ambit of the business. The proposal put to him was that while STI would remain in the Isle of Man to continue its other activities there, the crude oil trading function would be moved to London. That had staffing and office implications for SISL and STI. SISL would need additional staff

in London, and Mr Jan Bredenkamp of STI, as the principal oil trader at STI, with considerable experience and many contacts in the crude oil trading market, would have to move to London.

[17] Bredenkamp's move to London, as part of the Gird proposal, was a key component of the proposed new structure. But it transpired, after Gird had taken advice from Lovells, that Bredenkamp was not willing to move away from the Isle of Man, as I shall discuss shortly. It was partly for this reason that the Sasol Group decided not to follow the Lovells advice in its entirety. Equally importantly, Ashman suggested that a clean break be made between the STI contracts for the purchase of crude oil with Middle Eastern suppliers and new contracts to be negotiated by SISL with the suppliers.

[18] Sasol Oil's chief concern expressed to Ashman was that historical profits made by STI in the Isle of Man might be taxed by UK Inland Revenue since there was a possibility that SISL might be regarded as a branch of STI: if this were so, historical profits made by STI could be exposed to UK corporation tax.

[19] The commercial reasons for relocating the STI operation to London – rationalization of staff and proximity to the London trading market – had thus to be weighed against the disadvantages of relocating the crude oil supply there as well. The particular problem that the Sasol Group anticipated was the cancellation of the term contracts – that might give the Middle Eastern suppliers the opportunity not to renegotiate contracts with the Sasol Group and to find other purchasers. Gird testified that the Sasol Group had been fortunate in securing these term contracts as there were many entities waiting in line for the allocation of crude oil on a term contract.

[20] The second problem not anticipated by Loubser and Gird when they made the original proposal to the Sasol Group was that, after receiving the Lovells advice, they ascertained that Bredenkamp was not willing to move to London – thus achieving the clean break that Lovells suggested was necessary. Bredenkamp had established a presence on the Isle of Man and had bought a home there. He wished to remain on

the Isle of Man. His skills and contacts were essential to the acquisition of crude oil. He was also needed on the Isle of Man for other Sasol Group businesses he conducted there, such as a chemical business. Bredenkamp, who died some years before the additional assessments were issued by the Commissioner, wrote a memorandum for the Sasol Group dated 14 June 2001.

[21] Bedenkamp recommended that the crude oil trading function (acquisition from the Middle Eastern suppliers) remain with STI, and all other business, such as shipping, be moved to SISL in London. As Bredenkamp said in his proposal 'This will entail SISL buying the crude oil on a FOB basis, arrange the shipping insurance, inspections etc and assume the risk'. He said also that it would entail cancelling the supply agreement between STI and Sasol Oil.

[22] Bredenkamp's proposal was accepted by the STI board of directors on 23 June 2001. Gird's evidence was that the only change to the original proposal that he and Loubser had conceived was that the crude oil procurement would remain with STI on the Isle of Man, which, having bought it, would sell it in turn to SISL, and SISL would sell the oil, and ship it to Sasol Oil. That is the chief element in the structure that the Commissioner complains of. There was no reason, he contended, for STI, having procured the crude oil, to sell it to SISL and for SISL to sell it (back to back) to Sasol Oil in South Africa. The 'interposition' of SISL was an element that could not be explained other than as a stratagem to avoid the payment of tax in South Africa. That is the Commissioner's chief reason for the argument that the sales of crude oil by STI to SISL and then from SISL to Sasol Oil were simulated.

[23] The policy of the Sasol Group was to submit proposals and draft agreements to the tax department in the group for approval. Gird accordingly sent the modified proposal for the relocation of shipping to London by SISL to Mrs Beulah van Wyk, who at the time was the chief financial officer of Sasol Oil. She in turn sent it to Mr Eric Louw who was in the Group Tax department of Sasol Ltd for advice on whether the proposed structure was optimal from a tax point of view. Louw was formerly a tax director at the accounting firm Price Waterhouse Coopers (PWC). He issued an

opinion on 5 July 2001 confirming that the modified proposal was tax compliant and optimal. He asked PWC for a confirmatory opinion, which was provided on 16 July 2001.

[24] Mr Okkie Kellerman (the senior tax manager) and Mr Mark Badenhorst (the tax partner) of PWC repeated the structure of the modified proposal in their written advice. They pointed out that SISL already had access to oil market information which, before the relocation, had been transmitted to STI in the Isle of Man. SISL also had 'experience and expertise in managing volatile shipping rates, oil losses during transportation, insurance, demurrage, deadfreight, loss control and inspection costs and negotiating co-freight arrangements and other oil companies'. STI, they said, 'has experience and expertise in the negotiation of contracts for the supply of crude oil on the open market. It does not have the expertise to arrange shipping of the purchased oil'.

[25] However, PWC cautioned that there had to be 'sufficient commercial justification for SISL to sell the crude oil to Sasol Oil and to undertake the shipping of the crude oil'. If not, the use of SISL could be seen as a scheme to avoid tax in SA and the new structure could be disregarded for SA tax purposes, they said. They also advised that 'sufficient real risks and functions should be transferred into SISL to provide sufficient commercial justification and to limit the UK and SA transfer pricing risks'.

[26] The GEC approved the modified structure presented at a meeting by Loubser on 5 July 2001. The minutes of the meeting record that:

'A presentation by Mr Henri Loubser emphasised the need to review Sasol's structure in light of certain legislative changes.

The proposal was to cease the contract between STI and Sasol Oil and move is to [SISL]. This would optimize the tax regime.'

[27] The Commissioner's contention both in the Tax Court and on appeal is that the scheme was devised by Gird and Loubser in order to avoid the payment of a newly

introduced residence tax in 2001. Gird and Loubser denied that this was so. Loubser denied that the minutes correctly reflected his presentation. He pointed out that he had made the presentation to the GEC but had said nothing about the tax implications of the transactions proposed. He was a chemical engineer and not a tax expert, he said, and would never have presumed to advise on legal or tax matters. I shall return to their evidence and the cross examination of them in due course.

Tax advice in South Africa

[28] The argument by the Commissioner that the back to back sales were simulated transactions, or abnormal in the sense of s 103(1), is based not only on the advice that PWC gave in respect of the structure in response to the Gird and Loubser proposal that was sent to PWC by Van Wyk. He also relied on tax advice given by PWC to the Sasol Group on 14 March 2001 in respect of the change of the income tax regime from being source based to being residence based, which came into effect in June 2001. The advice was recorded in a letter to the directors of Sasol Ltd written on 3 April 2001. This followed a meeting of the GEC (for the whole Sasol Group), the minutes of which recorded that 'Mr Louw of PWC made a presentation on Residence Tax Legislation, which would be introduced for Sasol on 1 June 2001'. Mr Rynhart van Rooyen 'stated that Sasol is currently very weak on tax planning and that urgent actions are required to remedy the situation.'

[29] That was why the Sasol Group, through Van Wyk, approached PWC and consulted them on 14 March 2001. Kellerman and Louw advised on 3 April 2001 that a UK based company should be used for oil trading activities in order to avoid residence based tax. They suggested that STI should sell crude oil that it had sourced to a company in the UK, the UK resident company, and that the UK company should sell that oil to Sasol Oil, which is what Loubser and Gird had proposed earlier in the year. Their evidence was that the proposal evolved because of the Lovells advice, and the realization subsequently that STI needed to keep Bredenkamp on the Isle of Man, and that it would be foolish to terminate the term crude oil contracts with the Middle Eastern suppliers.

The residence based tax introduced in 2001

[30] The Act was amended in 2001 to insert a new s 9D. The purpose of the amendment was explained in an explanatory memorandum issued by the National Treasury in 2002.

'Under the residence (ie worldwide) taxing system [introduced by the amendment], South African residents are subject to tax on their income earned domestically and abroad. One important facet of this system is how to address income earned by South African owned foreign companies and other South African owned foreign entities of a similar nature. If this latter form of income goes untaxed, South African residents can avoid tax simply by shifting their income to foreign entities, and the income earned by foreign entities will be taxed only once repatriated as a dividend. . . This failure to impose immediate tax is of great significance because taxpayers often delay repatriation for years or never repatriate funds at all.

Section 9D is designed to prevent deferral through South African owned foreign entities. However, international law only allows South Africa to tax foreign residents on their South African source income. International law does not allow South Africa to directly tax foreign entities on their foreign source income, even if those foreign entities are completely owned by South African residents.

However, in order to remedy the problem of deferral while complying with international law, section 9D (like other internationally used regimes of this kind) taxes South African owners on the foreign income owned by their foreign entities as if those foreign entities immediately repatriated their foreign income when earned.'

[31] The Commissioner's additional assessments attributed the income of SOIL (which had stepped into STI's shoes in the Isle of Man) to Sasol Oil in 2005, 2006 and 2007, invoking s 9D in order to do so, on the basis that the sales from SOIL to SISL and then on to Sasol Oil were simulated transactions, in fraudem legis. The Commissioner's contention is that the structure conceived by Gird and Loubser in 2001, which changed after the Lovells advice, was designed to avoid the implications of the new residence based tax, and was not as a result of the factors that Gird and Loubser adverted to (the importance of maintaining term contracts for the supply of crude oil, and the fact that Bredenkamp was determined to remain on the Isle of Man).

[32] Before dealing with the PWC presentations and the advice that it had given to the Sasol Group, it is convenient to set out the relevant provisions of s 9D as they were in the tax years under consideration.

'Net income of controlled foreign companies

(1) For the purposes of this section—

'business establishment' in relation to a controlled foreign company, means-

(a) a place of business with an office, shop, factory, warehouse or other structure which is used or will continue to be used by the controlled foreign company for a period of not less than one year . . . .

'controlled foreign company, means any foreign company where more than 50 per cent of the total participation rights in that foreign company are held, or more than 50 per cent of the voting rights in that foreign company are directly or indirectly exercisable, by one of more residents' ….

(2A) For the purposes of this section the 'net income' of a controlled foreign company is respect of a foreign tax year is an amount equal to the taxable income of that company determined in accordance with the provisions of this Act as if that controlled foreign company had been a taxpayer, and as if that company had been a resident for purposes of the definition of 'gross income'. . . .

(9) In determining the net income of the controlled foreign company in terms of subsection (2A) there must not be taken into account any amount which –

…

(b) is attributable to any business establishment . . . of that controlled foreign company in any country other than the Republic: Provided that the provisions of this paragraph shall not apply to any net income that is attributable to –

…

(ii) any amounts derived from –

(aa) any sale of goods by that controlled foreign company to any connected person (in relation to that controlled foreign company) who is a resident, unless—

(A) that controlled foreign company purchased those goods within the country of residence of that controlled foreign company from any person who is not a connected person in relation to that controlled foreign company;' (My emphasis.)

Section 1 of the Act defines a 'connected person', in relation to a company as its holding company, or its subsidiary or any other company where both such companies are subsidiaries of the same holding company.

[33] It is common cause that in the years of assessment (2005 to 2007) SOIL was a controlled foreign company of Sasol Oil. SOIL was resident in the Isle of Man and had a foreign business establishment there. SOIL (as STI had done prior to SOIL's incorporation in 2004), received amounts of money (or the rights to it accrued) from the sale of crude oil; these amounts would have fallen within the taxable income of SOIL if it had been a resident and these amounts were attributable to the foreign business establishment. Accordingly, unless such amounts were derived from sales of crude oil to a person connected to SOIL, the connected person being a resident of South Africa, those amounts were not to be taken into account in determining the net income of SOIL for the purposes of s 9D.

[34] SISL too was not resident in South Africa, but in the UK. Thus if the crude oil was sold by SOIL to SISL, the foreign business exclusion would apply and these amounts would not be taken into account in determining the net income of SOIL for the purpose of s 9D. On the other hand, if SOIL had sold the crude oil directly to Sasol Oil, which was both a connected person and a South African resident, the foreign business exclusion did not apply (in terms of the proviso in (ii)(*aa*) of 9D(9)(*b*)). If SOIL had purchased crude oil within its country of residence from any entity that was not a connected person, the subparagraph (A) exclusion would apply.

[35] The back to back sale of crude oil by SOIL, which procured it from the Middle Eastern suppliers, to SISL, and the sale and the supply then by SISL to Sasol Oil in South Africa were attacked by the Commissioner as being simulated, designed only to achieve the avoidance of residence based tax in the hands of Sasol Oil. He considered that he was entitled to disregard the sales from SOIL to SISL and to regard the sales as having been directly to Sasol Oil.

[36] There were essentially two grounds for this assessment. The first was that the real substance of the supply agreements was a sale of oil directly to Sasol Oil, and that SISL's role was a sham – the substance over form principle. The alternative ground was that s 103(1) applied as the transactions were abnormal and had the effect only of avoiding a tax liability. Mali J in the Tax Court found that the transactions were

indeed simulated and that SISL's role in the scheme was a sham such that the Commissioner was entitled to disregard it in his assessments for the 2005 to 2007 tax years. Mali J also found that the exclusion in 9D(9)(b)(ii)(*aa*)(A) did not apply. And having found that the sale to SISL and the sale to Sasol Oil were sham transactions, she did not consider it necessary to consider the application of s 103(1). The Tax Court held that Sasol Oil was liable for s 76 penalties and s 89*quat* interest. These are the issues that require consideration by this court in the appeal.

Substance over form and the evidence led for Sasol Oil

[37] The appeal by Sasol Oil to the Tax Court was based on the contention that the transactions in question were genuine. Five witnesses testified about the reasons for the sale of crude oil to SISL, and the implementation of the transactions, and Sasol Oil led the evidence of an expert in procuring and shipping crude oil, Mr Harvey Forster. No evidence was led for the Commissioner, but that is hardly surprising as it would not have had access to the internal workings of the Sasol Group. All the witnesses were rigorously cross examined and the Commissioner was very critical of the evidence, labeling it inconsistent and unreliable. Mali J found that the testimony for Sasol Oil was not credible, a serious finding with which I shall deal in due course. But first I shall set out the essence of the testimony for Sasol Oil.

[38] Gird testified that the new supply agreements – between STI and SISL and between SISL and Sasol Oil – were implemented once the GEC had approved them, in July 2001. The agreements were signed only in December of that year, but the effective date of each was agreed to be 1 July 2001. There was no agreement of sale between STI and Sasol Oil. The Sasol entities had intended that once STI had procured crude oil, it would sell it to SISL, which acquired ownership of the oil while it was shipped to Sasol Oil. In turn SISL transferred ownership pursuant to its supply agreement to Sasol Oil in South Africa. Gird relied on invoices between the respective parties to show the sales figures and prices at which STI sold to SISL and SISL sold to Sasol Oil. SISL issued quarterly credit notes to Sasol Oil to account for losses borne by it – differences in actual volumes delivered and demurrage.

[39] Acting as both owner and shipper of the crude oil, SISL issued instructions to STI regarding the detail for the bills of lading and STI issued instructions to the crude oil suppliers. Bills of lading were issued to STI and then endorsed by STI to SISL. SISL thus had the right to claim delivery of the crude oil. The Middle Eastern suppliers had different requirements as to credit arrangements between them and STI. One, the Saudi Arabian Oil Company, referred to as Aramco, required a standby letter of credit for every purchase of crude oil. It would issue bills of lading at load port directly to STI, which would endorse them in favour of SISL.

[40] Mr Philip du Toit of STI, later a director of SISL, and when SOIL was incorporated, of SOIL, testified that he personally endorsed the bills of lading on behalf of STI to SISL. Du Toit had taken over the procurement function of the Sasol Group from Bredenkamp. At the time of giving evidence, Du Toit was employed by SISL in London and had assumed responsibility for the procurement of crude oil for the refinery.

[41] Another supplier, Naftiran Intertrade Company Limited, required documentary letters of credit for every purchase of crude oil. The issuing bank required from the seller the bills of lading, invoices, certificates of quantities and of quality before it issued the letter of credit. After reviewing the documents and confirming compliance the bank would endorse the bills of lading to STI. Du Toit then endorsed them to SISL.

[42] Gird testified that the SISL annual financial statements accorded with the supply agreements and reflected their implementation. The 2002 statement described SISL's principal activities in the year as 'the provision of market information to the Sasol Group' and added that 'from July 2001 the company participated in inter-group oil trading and shipping of crude oil'. The same statement reflected SISL's ownership of the crude oil while being shipped and reflected the oil in its balance sheet as trading stock in transit.

[43] Gird's view was that as owner of the crude oil in transit, SISL bore the risk and losses in respect of the oil. (The supply agreement to Sasol Oil in any event provided

that this was the case.) his evidence accorded with the description of SISL's business by Ernst and Young in a study on Sasol Limited's transfer pricing. The study stated that while SISL took ownership of the oil and sold it on to Sasol Oil, SISL was 'essentially a distributor of oil and [it] has no sophisticated procurement function'. Its primary function was the arrangement of shipping to Sasol Oil.

[44] Gird was asked to deal with the term of the supply agreement that SISL bore the risks in respect of the crude oil being shipped. He explained that the risks were real: SISL did not necessarily deliver the same quantity of crude oil to Sasol Oil that it had bought from STI. In the majority of cases the quantity that was loaded was less when it reached South Africa and was pumped off the vessel onto which it had been loaded. This was because of evaporation, clingage of oil to walls, and the vessel needing to depart before all the oil had been pumped out. Secondly, loss could be incurred with demurrage charges – exceeding the number of hours allocated, in which case the vessel owner would charge for 'standing time'. It was standard, he said, when offloading at Durban, that there would be standing time. Another loss factor was what Gird termed 'dead freight' – using less capacity than a vessel could hold, but for which SISL would be charged. The changing price of crude oil, in a notoriously volatile market, was another factor that can affect the risk. Yet Sasol Oil was not obliged to pay for the lesser quantity of oil than that reflected on the bill of lading. Gird outlined further risk factors but there is no need to deal with them all.

[45] Mr Harvey Foster testified as an expert in crude oil trading and shipping. It was his view that it was commercially advantageous for the shipper of oil to South Africa – SISL – to be based in London. At the time, London was the hub of the shipping world. The people with the skills in crude oil trading and with the expertise in shipping were based in London. Personal interaction between traders was essential. London was the choice location for oil trading houses.

[46] Foster also testified about the risks involved in shipping. These included finding a suitable vessel for both the load port and the discharge port; availability within the loading window; the quality and quantity loaded; piracy along the West and East

coasts of Africa; and arrival and discharge times, and the types of losses that Gird had described. While conceding that most of these risks were insured against, he considered that there was nonetheless risk where the insurer repudiated the policy on the basis that the shipper had not acted reasonably in guarding against the risk foreseen.

[47] When cross-examined on the risk it was put to him that in the transfer pricing study undertaken by KPMG for the Sasol Group, it was stated that the risk of losses during transit were minimal because SISL was fully insured. The shipping fees earned by SISL were therefore justifiably low. The study indicated that the losses incurred by SISL were less than 0.5% of the volume of oil shipped. Foster maintained, however, that there was nonetheless risk of loss that was not insurable and that if the shipper used people who were not experts in the field the risks were very high. Although the fees charged per barrel by SISL were low, the total sums earned when millions of barrels of crude oil were shipped were not to be underestimated.

[48] The other point of contention related to whether the shipper necessarily needed to acquire ownership of the crude oil while it was in transit. This is important to the Commissioner's argument that the right that SISL acquired in respect of the crude oil was a hollow one, since it could do nothing with the oil but ship it to Sasol Oil. It did not have the normal entitlements of ownership. I shall thus return to the issue when applying the general principles of the law to the facts. Suffice it to say for the moment that Foster testified that it was more efficient for the shipper to acquire ownership of the crude oil while it was in transit since it was then able to manage its own risks. This practice, which was common according to Foster, also ensured that the shipper had an insurable interest and that the insurer would indemnify it against the losses incurred.

[49] Foster also testified that crude oil procurement and crude oil shipping required different skills, and were performed by some traders using different teams of people. It was common to have one procuring entity (in this case STI and later SOIL) and one

shipping entity (SISL). SISL's lack of a sophisticated procurement function, and STI's continued procurement role, was consistent with general practice in the industry.

Incorporation of SOIL

[50] It will be recalled that SOIL took over the functions of STI when it was incorporated in 2004. The Sasol Group had undergone considerable restructuring as a result of the introduction, in November 2000, by the Minister of Minerals and Energy of a Liquid Fuels Charter which required all South African companies dealing with petroleum and liquid fuels to enable the empowerment of historically disadvantaged people in the country. The Sasol Group, in implementing its obligations under the charter, sought to enter into mergers with non-South African entities. In the rearrangement, SIH's interest in STI was transferred to Sasol Oil.

[51] STI continued with its other businesses on the Isle of Man, and the procurement of crude oil was moved to SOIL, when it was incorporated, also in the Isle of Man. SOIL was a wholly owned subsidiary of Sasol Oil. When the Reserve Bank approved the new structures, STI assigned to SOIL the supply agreements with the crude oil suppliers. Invoices issued by SOIL to SISL showed that SOIL started on-selling crude oil to SISL in 2004. The bills of lading issued by the Middle Eastern suppliers were endorsed by Du Toit on behalf of SOIL in favour of SISL. The annual financial statement of STI in 2004 reflected that the functions of the procurement of crude oil and its sale to SISL were transferred to SOIL.

The substance over form argument

[52] The assessments in question and the arguments of the Commissioner before the Tax Court and on appeal are that the impugned transactions were devised by Gird and Loubser, and approved by the GEC, in order to tailor the Sasol Group's liability for tax when s 9D was introduced. The apparent transfer of the shipping function to SISL by STI and the sale to SISL and the onward sale to Sasol Oil were transactions that were simulated in order to avoid Sasol Oil paying tax on income earned by an entity that was resident in South Africa. A key component in the argument is that in the

advice given by PWC to the Sasol Group in April 2001, before the transactions were concluded in July 2001, Louw and Kellerman stated:

'The following ultimate modus operandi is recommended to minimize Sasol's tax liability on its oil trading activities:

- A company is incorporated in the UK ("SUK") with 100% of its shares being held by SIH.
- STI continues to purchase oil on the open market at market-related prices but sells the oil to SUK at a market-related margin that will reflect the risks assumed and the functions performed by STI.
- SUK owns the oil but it only bears the shipment risk, which it is insured against. The product and all other risks involved in oil trading remain with STI, which earns a market-related margin for the acceptance of such risks. *The existence and use of SUK must have commercial justification.* (My emphasis.)
- SUK then on-sells the oil to Sasol Oil, adding a small margin for bearing only the shipment risk.
- SUK buys oil, drilling fluids, solvents and other chemicals from Sasol Oil and other SA group companies and on-sells them to STI. Again, SUK only bears the shipment risk for the product delivered to STI while the product and all other risks involved in selling the product are accepted by STI. A small profit margin for bearing only the shipment risk is realized by SUK in the UK.
- STI on-sells the products in the open market at a market related price to earn a market-related margin for the acceptance of all the other risks and functions.'

The advice continued:

'To ensure that the use of SUK is not seen as a scheme to avoid tax in SA it is important to ensure that commercial justification exists for the use of SUK. The transferring of real risks and functions into SUK could provide sufficient commercial justification.'

[53] The opinion, the Commissioner argues, is what informed the entire stratagem. There was no real reason for the sale of the oil by STI, and then SOIL, to SISL and no intention to transfer ownership of the oil while it was in transit to SISL. The substance of the transactions was in reality a sale by SOIL to Sasol Oil. SISL's real role was as a shipper. While conceding that the passing of ownership is not an essential element of a contract of sale, the Commissioner contends that Sasol Oil's entire case is based on the contention that the crude oil was transferred to SISL, and that it did not

discharge the onus of proving that it was STI's, and later, SOIL's intention to pass ownership to SISL rather than to Sasol Oil, and that the supply contracts were simulated dishonestly. It must be recalled, however, that when the back to back supply agreements were first concluded, in 2001, neither STI nor SISL were subsidiaries (foreign controlled companies) of Sasol Oil: Sasol Oil would not have been liable, at that stage, and until 2004, for residence based tax on STI's income. The transactions thus did not have the effect of avoiding liability for tax. And so the Sasol Group could not have anticipated, in 2001, that subsequently a subsidiary of Sasol Oil itself would have earned income for which it would become liable for tax.

The test for simulation

[54] This court has held on several occasions that the mere production of agreements does not prove that the parties genuinely intended them to have the effect they appear to have. In *Erf 3183/1 Ladysmith (Pty) Ltd v CIR* 1996 (3) SA 942 (SCA), Hefer JA, dealing with a contention that agreements should be given effect in accordance with their tenor (form), said (at 953B-D):

'This is plainly not so. That the parties did indeed deliberately cast their arrangement in the form mentioned, must of course be accepted; that, after all, is what they had been advised to do. The real question is, however, whether they actually intended that each agreement would *inter partes* have effect according to its tenor. If not, effect must be given to what the transaction really is.'

And similarly in *CIR v Conhage (Pty) Ltd* 1999 (4) SA 1149 (SCA) Hefer JA confirmed that a taxpayer must show on a balance of probabilities that the agreements reflect the actual intention of the parties. (See also *CSARS v NWK Ltd* [2010] ZASCA 168; 2011 (2) SA 67 (SCA) para 40.

[55] The principle urged upon us by Sasol Oil, on the other hand, is that stated more than a century ago in *Zandberg v Van Zyl* 1910 AD 302 at 309.

In *Zandberg* Innes JA said:

'Now, as a general rule, the parties to a contract express themselves in language calculated without subterfuge or concealment to embody the agreement at which they have arrived. They intend the contract to be exactly what it purports; and the shape which it assumes is what they

meant it should have. Not infrequently, however (either to secure some advantage which otherwise the law would not give, or to escape some disability which otherwise the law would impose), the parties to a transaction endeavour to conceal its real character. They call it by a name, or give it a shape, intended not to express but to disguise its true nature. And when a Court is asked to decide any rights under such an agreement, it can only do so by giving effect to what the transaction really is: not what in form it purports to be. The maxim then applies *plus valet quod agitur quam quod simulate concipitur.* But the words of the rule indicate its limitations. The Court must be satisfied that there is a real intention, definitely ascertainable, which differs from the simulated intention. *For if the parties in fact mean that a contract shall have effect in accordance with its tenor, the circumstances that the same object might have been attained in another way will not necessarily make the arrangement other than it purports to be.* The enquiry, therefore, is in each case one of fact, for the right solution of which no general rule can be laid down.' (My emphasis.)

[56] This very famous statement was repeated in *Commissioner of Customs and Excise v Randles, Brothers and Hudson Ltd* 1941 AD 369 at 395 by Watermeyer JA where, referring to the passage cited, he said:

'I wish to draw particular attention to the words "a real intention, definitely ascertainable, which differs from the simulated intention", because they indicate clearly what the learned Judge meant by a "disguised" transaction. A transaction is not necessarily a disguised one because it is devised for the purpose of evading the prohibition in the Act or avoiding liability for the tax imposed by it. *A transaction devised for that purpose, if the parties honestly intend it to have effect according to its tenor, is interpreted by the Courts according to its tenor, and then the only question is whether, so interpreted, it falls within or without the prohibition or tax.*' (My emphasis.)

[57] In *NWK* I pointed out the difficulties inherent in applying this test. The test itself is uncontroversial. We must ascertain the intention of the parties having regard not only to the terms of the impugned transactions but also to other factors, including the improbability of the parties intending to give them effect. Applying the same test, the judges in that case were divided in their approach to the application of the principle to the facts.

[58] I suggested in *NWK* that

'[T]he test to determine simulation cannot simply be whether there is an intention to give effect to a contract in accordance with its terms. Invariably where parties structure a transaction to achieve an objective other than the one ostensibly achieved they will intend to give effect to the transaction on the terms agreed. The test should thus go further, and require an examination of the commercial sense of the transaction: of its real substance and purpose. If the purpose of the transaction is only to achieve an object that allows the evasion of tax, or of a peremptory law, then it will be regarded as simulated. And the mere fact that parties do perform in terms of the contract does not show that it is not simulated: the charade of performance is meant to give credence to their simulation.'

[59] The judgment in that matter was apparently thought to have changed the law. It did not. It pointed out merely that in order to establish simulation one could not look only at the terms of the disputed transaction. And it suggested that simulation was to be established not only by considering the terms of the transactions but also the probabilities and the context in which they were concluded.

[60] Wallis JA has twice explained the passages that have apparently given rise to confusion. He explained in *Roshcon (Pty) Ltd v Anchor Auto Bodybuilders CC* 2014 (4) SA 319 (SCA) paras 35 to 37 what the misconceptions had been and said:

'The notion that *NWK* transforms our law in relation to simulated transactions, or requires more of a court faced with a contention that a transaction is simulated than a careful analysis of all matters surrounding the transaction, including its commercial purpose, if any, is incorrect. The position remains that the court examines the transaction as a whole, including all surrounding circumstances, any unusual features of the transaction and the manner in which the parties intend to implement it, before determining in any particular case whether a transaction is simulated.'

[61] And in *CSARS v Bosch* [2014] ZASCZ 171; 2015 (2) SA 174 (SCA) Wallis JA said, referring (in para 40) to *Roshcon*:

'There I stressed that simulation is a question of the genuineness of the transaction under consideration. If it is genuine then it is not simulated and if it is simulated then it is a dishonest transaction, whatever the motives of those who concluded the transaction. . . . .Tax evasion

is of course impermissible and therefore if a transaction is simulated, it may amount to tax evasion. But there is nothing impermissible about arranging one's affairs so as to minimize one's tax liability, in other words in tax avoidance.'

The pillars of the Commissioner's argument as to simulation

The PWC advice

[62] One of the pillars of the Commissioner's argument in respect of simulation is that the Sasol Group followed PWC's advice on the 'ultimate modus operandi'. The purpose of that advice was to minimize the Group's tax liability, and in particular the newly introduced residence based tax in effect from June 2001. There is nothing sinister in that.

[63] As I said in *NWK* (para 42)

'It is trite that a taxpayer may organize his financial affairs in such a way as to pay the least tax permissible. There is, in principle, nothing wrong with arrangements that are tax effective. But there is something wrong with dressing up or disguising a transaction to make it appear to be something that it is not, especially if that has the purpose of tax evasion, or the avoidance of a peremptory rule of law.'

And see the statement of Wallis JA in *Bosch* above.

[64] Much was made by the Commissioner of the fact that Sasol Oil had not alluded to the PWC letter of 3 April 2001. And Gird and Loubser were cross-examined as to whether they had been aware of this advice when proposing the back to back sales in 2001. They denied knowledge of PWC's April 2001 opinion at the time of concluding the STI, SISL and Sasol Oil transactions. They were not legal or accounting professionals, and did not sit on the boards of the companies that eventually concluded the transactions. Loubser, as I have already said, denied having referred to tax legislation when he made his presentation to the GEC on 5 July 2001. The minutes had mistakenly attributed this to him, but he had not seen the minutes before the additional assessments were issued.

[65] Loubser was firm in testifying about his role at the GEC meeting. He said that it was not the practice in the Sasol Group for the management, as business people, to make recommendations as to tax. That was the function of the members of the GEC, following advice taken by them. The Commissioner put to him that he was not being truthful, which he denied. The Commissioner continues to argue that Loubser must have known of the PWC advice and structure. In my view, it is perfectly plausible that Loubser knew only of the advice that Van Wyk and Louw obtained from PWC in July 2001, after his presentation to the GEC. And the fact that he was aware that there would be tax implications in respect of the placing of SISL in the supply chain is neither here nor there. He knew the structure had to be approved from a tax compliance point of view, and that was why he had asked Van Wyk to get approval from PWC.

[66] In any event, the mere fact that parties have followed professional advice (in this case from PWC) in order to minimize the tax payable by them is not wrong nor does it point to deceit. The real question is whether they actually intended a sale by STI (then later SOIL) to SISL and whether SISL intended to acquire ownership of the crude oil from STI (SOIL). Or did they dishonestly purport to do so *solely* for the purpose of avoiding the tax that would be payable by Sasol Oil?

Ownership of the crude oil by SISL

[67] Apart from attacking the credibility of Gird and Loubser in particular, the Commissioner argues that the right SISL purported to acquire in the crude oil while shipping it to Durban was a hollow one. It was not ownership in the true sense. SISL could not freely dispose of the crude oil: it had to deliver it to Sasol Oil in Durban. That was in terms of the supply agreements between the Middle Eastern suppliers and STI (SOIL). The port of destination had to be known to the suppliers. So SISL could not change the destination of the oil once it was on board. Moreover SISL did not need or use the oil – it was but a shipper. And SISL's requirements met those of Sasol Oil exactly. SISL did not determine either the quantity or quality of the crude oil that would be sourced by STI (SOIL). In addition, the price that would be paid by Sasol Oil to SISL was agreed in advance by a guaranteed price formula.

[68] And although SISL bore the risk in the crude oil while it was in transit, this was provided for in the supply agreement between SISL and Sasol Oil. The Commissioner argues that this provision in the contract would not have been necessary if in fact ownership was transferred to SISL. As owner, SISL would have borne the risk. As pointed out by Sasol Oil, however, the fact that the normal consequences of a transfer of ownership are spelled out in a contract is a result of the caution exercised by the drafters of the contract, rather than being necessary to give effect to the contract.

[69] Sasol Oil points out that this is very little different from the issue in *Randles*. I discussed the facts in that matter in *NWK*, as did Wallis JA in *Bosch*, and there is no reason to repeat the detail. In summary, the parties to a number of contracts had agreed that ownership of material would be passed by the importer of the material to manufacturers of garments. But the terms of their contracts took all the entitlements of ownership, including to use and dispose of the material, away from the manufacturer. The contract was agreed so that the importer could obtain a customs rebate. Watermeyer JA said, however, in *Randles*, that there was no requirement that the parties intended to transfer an untrammeled right. He found that the parties had intended ownership to be transferred, and thus it had been.

[70] Was SISL's right to the crude oil comparable to that of the manufacturer's rights of ownership in the material? It is true that SISL's right in the crude oil was fettered. It could not do with it what it chose. In *Randles* the majority was clear that the parties had so much wanted ownership to pass that they must have intended that as a consequence of their contract. Sasol Oil, on the other hand, is in a stronger position than was the importer in *Randles*. Indeed, Sasol Oil is able to show commercial justification for the sale of the oil to SISL in London, which the importer in *Randles* could not do. And there were reasons for SISL controlling and managing the risk as owner while the oil was in transit, as described by Gird and Foster.

Delivery to SISL

[71] The Commissioner contends that the Sasol Oil witnesses were not clear on how the oil was delivered to SISL. Loubser testified that actual delivery took place at the

load point both to STI and then to SISL where the connecting hose from the Middle Eastern supplier was linked to the vessel that SISL had chartered. Loubser considered that delivery to STI and SISL took place simultaneously, which the Commissioner argues is a false construction. Du Toit, on the other hand, considered that delivery had taken place when the bill of lading was endorsed first to STI and then to SISL. If that were the case, since the vessel would already have sailed when the bill of lading was sent to the vessel, SISL would only have acquired ownership when the oil was already in transit.

[72] The supply agreement between STI (and later SOIL) and SISL did not expressly cater for the manner of delivery. The Commissioner argues that it is inconceivable, if the parties had genuinely intended that ownership would pass to SISL, that their contract made no provision for the mode of delivery. Sasol Oil argues, however, that there was constructive delivery to STI and then to SISL in both the Isle of Man and London, and actual delivery to Sasol Oil in Durban. Whether there is actual or constructive delivery is a matter of law. There was no need to provide for the mode of delivery in the contracts of sale.

The complexity of the structures proposed by PWC

[73] The Commissioner argues that the introduction of SISL into the supply chain resulted in a more complicated structure than was originally envisaged by Gird and Loubser. After reviewing the work of STI and SISL in late 2000, it will be recalled, their proposal was to simplify the structures within the Sasol Group and to save costs. They had anticipated that one entity would procure crude oil and ship it to Sasol Oil. That proposal did not work, because they needed the services of Bredenkamp, and needed to keep the term supply agreements in place, so that STI's functions could not be transferred to SISL in London. After obtaining the Lovells advice, they proposed bringing SISL into the supply chain as well as STI. That complicated the structures rather than simplifying them, as they had intended to do.

[74] This argument does not take into account the evidence of Gird and Loubser as to the reasons for not following the Lovells advice. It is true that the proposal they had

made initially was different from that ultimately adopted. But they both explained the changes in a perfectly plausible fashion, and no evidence was led to controvert the reasons for STI remaining in the supply chain. There was a good commercial reason for SISL, in London, taking over the supply of crude oil to Sasol Oil, and the fact that the estimated savings in costs anticipated by the rationalization of the Isle of Man and the London offices were lost, was probably justified by the profits that Sasol Oil would make and the fees that SISL would earn in terms of the supply agreements.

Inconsistencies in documents

[75] The Commissioner contends that in a number of documents extraneous to the supply agreements, such as filings with the United States Security and Exchange Commission, Sasol Ltd described SISL as a 'services company' and STI as a 'trading company'. So too in the KPMG transfer pricing study of 2002 and 2003, it was stated that SISL's primary function was 'to provide shipping services' and that it took on a 'small level of risk in connection with the provision of these services'. This shows, he argues, that SISL was in fact nothing more than a shipper of crude oil to Sasol Oil, and that the purchase by SISL of crude oil was nothing more than a charade – a shipping contract dressed up to look like a sale. These documents show, he argues, that Sasol Oil could not keep up the pretence of buying oil directly from STI and later SOIL, and in general regarded SISL simply as a shipping company. He also relies on a report to the UK Revenue Authority, in 2004, in which SISL indicated that although SISL took ownership of the crude oil that it shipped, it bore minimal risk. The revenue authority queried this, asking why it took ownership of the oil that it was shipping and why it bore minimal risk. SISL's response was that there were three risks that it bore, two of which were unlikely to occur and the third, discharging less oil than it had taken on board in the first place, was insured against. I have already dealt with the loss of oil and Foster's evidence. Suffice it to say that it was a risk, and that over a period the losses might be considerable.

[76] The documents referred to by the Commissioner must of course be considered as part of the factual context in which the transactions were disregarded in the tax years in question. But they must also be weighed against the evidence of the Sasol Oil witnesses as to the reasons for SISL acquiring ownership in the crude oil that it

shipped, advanced by Gird, Loubser and Foster, the expert witness. Although that evidence was labeled as unreliable and not credible by the Commissioner, I consider that evaluation to be unwarranted.

Artificial features of the transactions

[77] The Commissioner contends that several features of the supply agreements between STI, SISL and Sasol Oil have an aura of artificiality, and that there was no commercial justification for them. He argues that the interposition of SISL in the supply chain served no commercial purpose. The requirements of Sasol Oil would have been met had STI continued to supply the crude oil it had procured directly to Sasol Oil. The fact that the crude oil was sold at the same price to SISL and then to Sasol Oil, and SISL made no profit, is also regarded as artificial. And the fact that the effective date of the agreements was agreed to be I July 2001 (which coincided with the introduction of residence based tax) rather than when the agreements were signed, later in that year.

Sasol Oil's response to the argument on substance over form

[78] Sasol Oil refutes all of these contentions as I have already explained in relation to ascertaining the intention of the parties. In addition, Sasol Oil argues that the documents prepared before, and for years after the supply agreements were concluded, demonstrate that there was no artifice in the arrangements. Minutes of board meetings would have to have been falsified and reports to the GEC deliberately disguised. False documentation would have to have been consistently produced from the beginning of 2001 until the end of 2007, the last year of the additional assessments. Financial statements for STI and SOIL would have to have been false and bills of lading fraudulently endorsed. On the Commissioner's contentions, senior staff in a major conglomerate would have been complicit in an elaborate fraud over years.

[79] There is not a shred of evidence that this was the case. The evaluation of Sasol Oil's witnesses as untruthful and unreliable is simply not fair. It is premised on the argument that the key to the whole restructuring in 2001 was the PWC advice in April

2001. Sasol Oil's witnesses denied this. They plausibly explained the genesis of the proposal and its development. And the adoption of PWC's advice is not wrong or dishonest. It was repeatedly put to them that the structure served no purpose other than tax avoidance. They explained why the structure was commercially beneficial and why they intended that SISL would take delivery of the crude oil from STI, then SOIL, and in turn sell and transfer it to Sasol Oil in Durban. It is irrelevant that PWC advised on the transactions in anticipation of their being concluded. And as I have already said, Sasol Oil, until 2005, would not in any event have been liable for residence based tax on income received by STI since it was not a controlled foreign company of Sasol Oil.

[80] In conclusion on the substance over form argument, I consider that Sasol Oil has discharged the onus of proving that the supply agreements between STI (SOIL), SISL and Sasol Oil were genuine transactions, which they implemented from 1 July 2001 through to the years of assessment being 2005, 2006 and 2007. The transactions had a legitimate purpose. There was nothing impermissible about following the PWC advice, and so reducing Sasol Oil's tax liability. The transactions were not false constructs created solely to avoid residence based taxation. There was good commercial reason for introducing SISL into the supply chain, as explained by the witnesses for Sasol Oil, and SISL had, from the beginning of 2001, been envisaged as the oil trader and shipper in the supply chain. The PWC advice was not the trigger for the transactions.

The subparagraph (A) exclusion

[81] Sasol Oil argues that the effect of s 9D(9)(b)(ii)(*aa*)(A) is that its liability for tax on SOIL's net income is excluded. The argument is based on the premise that if SOIL purchased crude oil within its country of residence (the Isle of Man) from any person who was not a connected person in relation to SOIL, the net income of SOIL would not be attributable to Sasol Oil. The Commissioner did not contend that SOIL did not have a foreign business establishment on the Isle of Man. (The Tax Court wrongly held that it did not.) The question that immediately comes to mind is whether SOIL purchased crude oil from Middle Eastern suppliers in the Isle of Man, or in the Middle East. Where were these contracts concluded?

[82] Du Toit, who had taken over the procurement function from Bredenkamp, testified about the contract renewal processes that occurred annually. SISL would indicate to SOIL what was needed by the refinery. SOIL would request a renewal of the contract, specifying the crude oil grades and quantities for the following year. The request could be made at a meeting, or over the telephone, or fax, or telex, and later email. The crude oil producer, if it accepted the request, would issue a new contract to SOIL, and send it by telex or fax to the office in the Isle of Man. Sasol Oil thus argues that the 'goods' were purchased in the Isle of Man, hence the exclusion of liability to tax in the hands of Sasol Oil.

[83] The Commissioner takes the view that the exclusion in para(A) does not apply as Du Toit's evidence as to where the supply contracts were concluded was inconclusive as to where the contract was concluded. Moreover, he contends that the exclusion applies only to goods purchased within the country of residence, not to oil sourced in the Middle East, purchased in the Isle of Man. This interpretation is consistent with the Treasury's explanation of the exclusion, which is that the controlled foreign company must have a nexus with the place in which the goods are produced. It is, however, not necessary to decide this in view of my conclusion that the supply agreements were not simulated.

Section 103(1) of the Act

[84] The provisions of s 103(1) of the Act read as follows in the years of assessment.

'Transactions, operations or schemes for purposes of avoiding or postponing liability for or reducing amounts of taxes on income

'Whenever the Commissioner is satisfied that any transaction, operation or scheme (whether entered into or carried out before or after the commencement of this Act, and including a transaction, operation or scheme involving the alienation of property) –

(a) has been entered into or carried out which has the effect of avoiding or postponing liability for the payment of any tax, duty or levy imposed by this Act or any previous Income Tax Act, or of reducing the amount thereof; and

(b) having regard to the circumstances under which the transaction, operation or scheme was entered into or carried out –

(i) was entered into or carried out -

(aa) in the case of a transaction, operation or scheme in the context of business, in a manner which would not normally be employed for *bona fide* business purposes, other than the obtaining of a tax benefit; and

(bb) in the case of any other transaction, operation or scheme, being a transaction, operation or scheme not falling within the provisions of item *(aa)*, by means or in a manner which would not normally be employed in the entering into or carrying out of a transaction, operation or scheme of the nature of the transaction, operation or scheme in question;

(ii) has created rights or obligations which would not normally be created between persons dealing at arm's length under a transaction, operation or scheme of the nature of the transaction, operation or scheme in question; and

(c) was entered into or carried out solely or mainly for the purposes of obtaining a tax benefit,

the Commissioner shall determine the liability for any tax, duty or levy imposed by this Act, and the amount thereof, as if the transaction, operation or scheme had not been entered into or carried out, or in such manner as in the circumstances of the case he deems appropriate for the prevention or diminution of such avoidance, postponement or reduction.'

[85] The Commissioner argues that, even if the supply agreements are found to be genuine, they nonetheless must be disregarded in the assessment of Sasol Oil's income tax liability. For the section to be applied by the Commissioner he must be satisfied that a transaction, operation or scheme has been entered into; if so, did it have the *effect* of avoiding, postponing or reducing the liability for the payment of tax; if so, it must have entered into the transaction, operation or scheme solely or mainly for the *purposes* of obtaining a tax benefit (the purpose requirement) and it must have been abnormal in one of the respects referred to in para (*b*).

[86] If so satisfied, the Commissioner's remedy was to disregard the transaction, operation or scheme, or to determine Sasol's Oil's tax liability in such a way as to prevent the avoidance, postponement or reduction which was the effect of the transaction, operation or scheme. Section 103(4) provided that if it was proved that that the transaction, operation or scheme resulted in the avoidance of liability for tax, it was presumed, until the contrary was proved, that it was concluded solely or mainly for the purpose of avoiding a tax liability. Sasol Oil would then bear the onus of proving

that avoidance of tax was not the sole or main purpose of the transaction, operation or scheme. However, the Commissioner would still bear the onus of showing that the effect requirement was met and that it was abnormal.

[87] The Commissioner contends that the relevant transactions are the supply agreement between SOIL and SISL, and the supply agreement between SISL and Sasol Oil. I shall refer to them as the 'impugned transactions'. Did they satisfy the other requirements of s 103(1)? And if so, which remedy should be invoked?

[88] Sasol Oil argues that the impugned transactions must, in order to fall foul of s 103(1), have the effect of getting out of the way of, escaping or preventing, an anticipated tax liability (*Smith v CIR* 1964 (1) SA 324 (A) at 333E and *Hicklin v SIR* 1980 (1) SA 481 (A) at 492H). Thus it must have anticipated liability for tax, which it avoided through the impugned transactions. If the parties had not entered into the impugned transactions, would Sasol Oil have had a liability for tax that it avoided, or escaped from, by entering into them?

[89] In answering this question one must determine what liability for tax Sasol Oil had avoided by entering into the impugned transactions. The Commissioner stated in his Rule 10 Statement that the impugned transactions 'had the effect of avoiding liability for the payment of tax imposed' under the Act. This was because if the oil had been sold to Sasol Oil by SOIL, the amounts received by or accrued to SOIL from such sales would have been included in determining the net income of SOIL for the purposes of s 9D. Such inclusions would have resulted, in terms of 9D(2), in amounts being included in the income of Sasol Oil for the 2005 year of assessment.

[90] Sasol Oil points out that this proposition is flawed: after the conclusion of the impugned transactions, the controlled foreign company in the Isle of Man was STI; STI was wholly owned by SIH; STI did not sell oil to Sasol Oil directly; even if it had, STI's net income would not have been included in Sasol Oil's income. This is because the shares in STI were held by SIH. Thus Sasol Oil did not have any participation rights in STI. Accordingly, it was not obliged to include the net income of STI in its income for

income tax purposes. In addition, Sasol Oil argues, the foreign business exclusion applied.

[91] In July 2001, when the supply chain including SISL was created, Sasol Oil had no anticipated liability for tax based on the application of s 9D. This did not change in 2004 when SOIL was incorporated and took over the procurement function. There was never an intention that SOIL would have sold crude oil to Sasol Oil, and the Commissioner did not prove that there was. If Sasol Oil had done nothing to avoid an anticipated tax liability it would still have not had a tax liability as a result of the application of s 9D. There was no imminent tax liability in respect of SOIL's income anticipated in 2001. And of course there was no evidence as to what was contemplated by the Sasol Group in relation to its restructuring that resulted from the adoption of the Liquid Fuels Charter: we do not know who conceived of the change of shareholding between 2001 and 2004 and how that was implemented.

[92] The Commissioner has not shown that the impugned transactions had the effect of avoiding liability for tax or that there was anything abnormal about them. The fact that STI could have sold the crude oil directly to Sasol Oil does not mean that it was abnormal for STI to sell to SISL and then for SISL to sell to Sasol Oil.

[93] The Commissioner's assessments for the 2005 to 2007 years were based on the incorrect assumption that Sasol Oil had participation rights in STI. It quite simply did not. In 2001 the participation rights in STI were held by SIH. It was only from 2004 and onwards that the participation rights in SOIL were held by Sasol Oil. It is accordingly not necessary to consider the other requirements of s 103(1) in any detail. The application of s 103(1) by the Commissioner in the additional assessments was therefore unfounded.

Interest and penalties

[94] The Tax Court confirmed the imposition of s 76 penalties and s 89*quat* interest on Sasol Oil, having determined that the impugned transactions were simulated. In

view of my findings that the transactions were not simulated and that the application of s 103(1) was ill-founded, it follows that Sasol Oil should not be required to pay these sums.

[95] In the result—

1 The appeal is upheld with the costs of two counsel.

2 The order of the Tax Court is set aside and is replaced with the following order:

'The appeal against the additional assessments issued to the appellant on 30 April 2010 by the Commissioner for the South African Revenue Service for the 2005, 2006 and 2007 years of assessment is upheld and those assessments are set aside.'

C H Lewis
Judge of Appeal

Mothle AJA dissenting (with Makgoka JA)

[96] I have read the judgment of Lewis JA (the first judgment) wherein she upholds the appeal. I am of the contrary view that the supply agreements defining the supply chain for crude oil to Sasol Oil in South Africa are a simulation. I therefore respectfully disagree with the analysis of the evidence and the conclusion reached in that judgment. In my view the appeal should be dismissed with costs.

[97] A summary of the background facts appear in the first judgment and will not be repeated in this judgment. Only the salient points will be referred to for purposes of context.

[98] The litigation giving rise to this appeal concerns additional tax assessments for the years 2005, 2006 and 2007 issued by SARS against Sasol Oil. The total additional tax from the assessment, excluding interest, was R 68 644 584.

[99] It is common cause that Sasol Oil was in the business of acquiring and refining crude oil. Prior to 2001, it received its supply of crude oil from Sasol Trading International Limited (STI), a subsidiary company of Sasol Investment Holdings (SIH). STI was based in the Isle of Man, strategically positioned to purchase crude oil from the Middle East sources for sale to Sasol Oil in South Africa. The transaction was expressed in a Supply Agreement (the original agreement) concluded between STI and Sasol Oil.

[100] The crude oil purchased from the Middle East sellers, was transported by STI with the assistance of a shipping and marketing company, Sasol International Services UK (SISL), another subsidiary of SIH. Both Sasol Oil and SIH were members of the Sasol Group of Companies (Sasol Group). I shall revert to this important relationship later in this judgment.

[101] During the year 2000 and through to 2001, the Sasol Group recognised the need to restructure the foreign based enterprise (FBE) so as to avoid duplication of costs between the subsidiaries, STI and SISL. This duplication was said to be the primary reason for the expenditure of R3 million per year. The restructuring process was driven by Mr Gird (Sasol Oil's trading manager and director of SISL) and Mr Loubser (SISL's director and Sasol Oil's manager: manufacturing, supply and trading). During February 2001 Mr Loubser and Mr Gird produced a restructuring proposal, in which the following is stated:

'Unavoidably there is a duplication of effort between STI, SISL and Sasol Oil on the international oil and products trading side. The cost to these parties to maintain their offices and business contacts in the international oil and products market is simply too high in view of the lack of growth in business as discussed above. It should be mentioned that the cost of an air ticket between Johannesburg and UK is not much higher than a ticket from the Isle of Man to London. It is estimated that rationalising the trading activities could save around R3 million per year cost duplication.'

[102] This proposal was approved by the Sasol Oil board of directors, subject to approval by the Group Executive Committee (GEC), and an opinion on the United Kingdom (UK) tax implications. The GEC approved the proposal. On 7 March 2001 the tax advice was received from Lovells Solicitors, who advised that the proposal would not have any adverse UK tax consequences, other than an increase in SISL's UK tax liability.

[103] I pause here to mention that during the same period, Sasol Group became aware that new tax legislation would apply to the group as from 1 June 2001. It sought advice from PricewaterhouseCoopers (PwC) in this regard. PwC's advice was contained in three letters dated 3 and 18 April 2001 and 16 July 2001. In its letter of 3 April 2001, PwC mentions that towards the end of 2000, it was requested by Sasol Oil to consider and advise on the tax implications of the mooted restructuring. The letter is co-signed by Mr Eric Louw, in his capacity as a tax partner at PwC. Later Mr Louw appears as the addressee of the third PwC letter of 16 July 2001 and referred to as being in the employ of Sasol Limited in the division of Group Tax.

[104] PWC recommended an 'ultimate modus operandi to minimize Sasol's tax liability on its oil trading activities'. This entailed the interposition of SISL in the oil supply chain between STI and Sasol Oil.

[105] From the content of the opinion letter of PwC, it was evident that the advice expressed therein was in response to the anticipated change in tax legislation concerning FBEs. The letter also recommended the establishment of a new company (SUK), with trading functions, to be located in the UK and interposed between STI and Sasol Oil. It also recommended the retention of STI in the Isle of Man and not its transfer (as was the original intent in terms of the proposal by Mr Gird and Mr Loubser). Sasol Oil, through its Board of Directors and the GEC accepted this proposal by PwC. It implemented it by concluding two supply agreements.

[106] The supply agreements provided that STI in the Isle of Man would purchase crude oil from sources in the Middle East and sell it to SISL in the UK with SISL in turn on-selling the crude oil and ensuring its delivery to Sasol Oil in South Africa. The one supply agreement provided for the first leg of the sale transaction between STI and

SISL and the other for the sale and delivery transaction between SISL and Sasol Oil. Unlike before, STI no longer supplied the crude oil directly to Sasol Oil.

[107] This arrangement attracted the attention of SARS. Acting in terms of s 76 of the Income Tax Act 58 of 1962 (the Act), SARS in April 2010, issued the additional assessments against Sasol Oil. Section 9D, quoted in the first judgment, provides in essence that SARS may levy tax in relation to income that is due to a South African resident company, from a controlled FBE, in accordance with the residence-based tax system. By 2005, STI had been replaced by another company in the Sasol Group, Sasol Oil International Limited (SOIL), where STI assigned SOIL the role of purchasing the crude oil from the Middle East sources for sale to SISL.

[108] On 14 July 2010, Sasol Oil raised an objection against the additional assessments, which SARS disallowed on 24 June 2011. Sasol Oil appealed to the Tax Court (Mali J, sitting with two members) which ruled in favour of SARS and upheld the additional assessments. It is against the Tax Court's judgment and orders that Sasol Oil appeals to this Court.

[109] The two main questions raised by SARS as its main contention for consideration by the Tax Court, were:
(a) Whether the substance of the supply agreements differed from their form, in which event whether the relevant amounts were excluded from SOIL's net income for purposes of s 9D, on the basis that the requirements of paragraph (A) of subsection 9(*b*)(ii) were satisfied; and
(b) In the alternative, whether the requirements of s 103(1) were satisfied.

[110] Both the substance over form and the s 103(1) issues depend on SOIL's income being taxable in Sasol Oil's hands in terms of s 9D. Since the Tax Court found that the assessed amounts were included in SOIL's net income, the Tax Court did not deal with the s 103(1) question. The substance over form debate was at the centre of this appeal.

[111] The Tax Court concluded, with reference to the evidence and in answer to the question of substance over form raised by SARS that the interposition of SISL in the

crude oil supply chain from SOIL to Sasol Oil was a sham in that there was no commercial justification for the role of SISL in the supply chain. In arriving at this conclusion, the Tax Court found the interposition of SISL to be an unusual feature in the supply chain as provided for in the supply agreements.

[112] The question whether there was a commercial justification for SISL's role in the supply agreement is best understood within the context of the restructuring alluded to earlier in this judgment.

[113] Before the Tax Court, Sasol Oil presented oral evidence of five factual witnesses and an expert witness. Two of these witnesses were Mr Gird and Mr Loubser, erstwhile employees of Sasol Oil who, as stated already, were central to co-ordinating the restructuring process.

[114] There is no doubt that the genesis of the structure of the FBE of the Sasol Group of Companies, adopted and implemented from July 2001, is found in the written opinion by PwC dated 3 April 2001, referred to earlier.

[115] The structure expressed in the supply agreements conforms to the structure adopted by Sasol Oil save that instead of incorporating a new subsidiary company in the UK (SUK), SISL was clothed with trade functions to be part of the supply chain of crude oil. What is more, the eventual supply agreements concluded between STI and SISL and between SISL and Sasol Oil, copy the narrative of the PwC letters. Another important feature of the opinion letter is a strong recommendation that the company to be interposed between STI and Sasol Oil should be established with a commercial justification.

[116] In essence, the 3 April 2001 letter from PwC, introduced a new approach to the restructuring, which took the Sasol Group in a direction opposite to the initial restructuring that was mooted. The initial restructuring had its intent to eliminate duplication and save costs by collapsing STI, one of the subsidiary companies. The staff and operations of STI in the Isle of Man were to be transferred to SISL in the UK. The proposal by PwC was to the effect that STI should be retained in the Isle of Man and a new company to be interposed between the STI and Sasol Oil in the crude oil

supply chain. Thus, the consequence of the PwC recommendation, which was adopted and implemented, was that instead of having one company in the UK conducting the acquisition and selling of crude oil to Sasol Oil as initially mooted, two companies, both Sasol Group subsidiaries, were recommended for the trade functions.

[117] The purpose was clearly to avoid Sasol Oil from having to purchase crude oil from STI, as was the case prior to the restructuring. In that instance, the supply and sale would have been taxable at the hands of STI's holding company, SIH, a residence based company in South Africa. The interposed UK Company would ensure that there would be a distance between Sasol Oil and STI in order to ensure that the supply chain should fall outside the ambit of s 9D.

[118] Consequent to the PwC letters, the following developments emerged. First, no new company was incorporated in the UK. SISL was introduced and clothed with trading functions to be the interposed company. Secondly, Sasol Oil contended that for a dishonest transaction to take place there would have had to be a conspiracy involving a number of officials and companies. In my view, that consideration does not find application in this case, for the following simple reason. Both STI and SISL were subsidiaries of SIH. In turn, SIH was a member of the Sasol Group. In the final analysis, all these companies were members of the Sasol Group. Sasol Group and its GEC were in effective control of the affairs of each of its subsidiaries. Thus, all it took was a meeting of its Sasol Group's GEC to approve the recommended structure. The question of the need for commercial justification was included in the PwC opinion but there is no evidence that the meeting of 5 July 2001 expressed itself on how that question should be addressed. That being so, there is no basis to conclude, in the absence of evidence, that it would require a conspiracy not to address the question of commercial justification. Thirdly, on the documents submitted and the evidence presented before the Tax Court, and contrary to a strong and repeated recommendation by PwC, there is no explanation as to the commercial justification of SISL in the new supply chain structure. Fourthly, as recommended by PwC, the supply agreements were put in place, one providing for the purchase and sale of crude oil between STI and SISL and the other between SISL and Sasol Oil, to streamline the supply chain.

[119] The supply agreements present unusual features of independent trading companies. Firstly, the agreements provide that the crude oil acquired by STI was intended to be sold to SISL and to no other third party. Similarly, the crude oil purchased by SISL from STI, was intended to be sold to Sasol Oil and to no other external party. Secondly, the agreements ensured that the purchase price remained constant in that, from STI to Sasol Oil, there was no room to change the price, by either STI or SISL, with a view to making a profit. In essence therefore, SISL traded by purchasing crude oil only from STI and on- selling it only to Sasol Oil without making any profit. Thirdly, the sale of crude oil by STI to SISL does not result in transfer of ownership in the sale transactions involving SISL. SARS contends that this is a sham. I agree. The absence of transfer of ownership, though not necessarily invalidating the transaction, would within the context of the two supply agreements, be one of the relevant factors indicative of a simulated transaction.

[120] As stated already, historically, and prior to July 2001, Sasol Oil purchased crude oil directly from STI in terms of an agreement concluded between the parties in 1998. Thus, only STI performed the function of buying and selling term crude oil. SISL performed only a shipping service. The supply agreement in terms of which SISL's functions would include the buying and selling of crude oil, had to be commercially justified.

[121] In all three letters (of 3 April 2001, 18 April 2001 and 16 July 2001) PwC emphasised the need for sufficient commercial justification for SISL's interposition in the supply chain to sell crude oil. For example, in the 16 July 2001 letter, the following is explained:

'However, we need to stress that sufficient commercial justification must exist for now using SISL to sell the crude oil to Sasol Oil and to undertake the shipping of such crude oil. If not, the use of SISL could be seen as a scheme to avoid tax in SA and the new structure could be disregarded for SA tax purposes.'

[122] It must be borne in mind that Sasol Oil bore the onus to establish a commercial justification for the interposition of SISL in the supply chain. It thus fell upon the witnesses testifying for Sasol Oil to explain to the court such commercial justification. Did Sasol Oil, through its witnesses, discharge that onus? In this regard, it is important

to have careful regard to the contemporaneous documents and the evidence. As a general observation, it is instructive that in the contemporaneous documents, including correspondence between PwC and Sasol Oil, no such commercial justification is recorded, other than the duplicated costs under the existing structure. The closest Sasol Oil comes to identifying such justification, is recorded in a letter dated 22 November 2001. There, Mr Gird, in a submission to SISL, projected the adoption of the PwC structure as a normal part of the Sasol Group's Business. But it was not. The main purpose of the PwC structure was tax avoidance, of which there is nothing wrong in principle. But, in any event, this letter was written months after the Sasol Group had decided to implement the PwC structure. What is more, apart from the duplication of costs, there is no discernible problem recorded or identified with the existing structure. Startlingly, the PwC structure, instead of doing away with duplication, entrenches it by the interposition of SISL in the buying and selling of crude oil. It makes no commercial sense at all.

[123] The documentary evidence demonstrates that the initial motivation for restructuring was intended to collapse STI and end up with only one company doing all the trade for the acquisition and supply of crude oil. When it became evident on the advice of PwC, that that approach would attract the imposition of tax in terms of s 9D, the Sasol Group accepted the PwC model which entrenched the duplication by imposing SISL in the supply chain between STI and Sasol Oil.

[124] I hasten to add that there was nothing untoward about what at that time appeared to be a tax avoidance scheme. Much has been written about tax avoidance schemes. In *Helvering v Gregory*,[1] the court, per Judge Hand, said as follows:

'Anyone may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes.'

Later, Judge Hand, expanded on this in his dissent in *Commissioner v Newman*[2], and stated:

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[1] *Helvering v Gregory* 69F.2d 809,810 (2d Cir 1934) affd 293 US 465 (1935).
[2] *Commissioner v Newman* F.2d 848.841(2d Cir 1947).

‘Over and over again the Courts have said that there is nothing sinister in so arranging one’s affairs to keep taxes as low as possible. Everybody does it, rich and poor and all do right, for nobody owes any public duty to pay more than the law demands.’

[125] These sentiments have since been echoed in a line of decisions[3] in South Africa, including the seminal judgment of *Commissioner of Customs and Excise v Randles Brothers and Hudson Ltd* 1941 AD 369. In that case the court contrasted the two scenarios of tax avoidance and tax evasion as follows:[4]

‘A transaction is not necessarily a disguised one because it is devised for the purpose of evading the prohibition in the Act or avoiding liability for the tax imposed by it. A transaction devised for that purpose, if the parties honestly intend it to have effect according to its tenor, is interpreted by the Courts according to its tenor, and then the only question is whether, so interpreted, it falls within or without the prohibition or tax.

A disguised transaction in the sense in which the words are used above is something different. In essence it is a dishonest transaction: dishonest, in as much as the parties to it do not really intend it to have, *inter partes*, the legal effect which its terms convey to the outside world. The purpose of the disguise is to deceive by concealing what is the real agreement or transaction between the parties. The parties wish to hide the fact that their real agreement or transaction falls within the prohibition or is subject to the tax, and so they dress it up in a guise which conveys the impression that it is outside of the prohibition or not subject to the tax. Such a transaction is said to be in *fraudem legis*, and is interpreted by the Courts in accordance with what is found to be the real agreement or transaction between the parties.’

[126] The courts have equally not hesitated to express a strong view against disguised transactions, as in the English case of *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* [1992] 2 All ER 275 (HL) at 295, where the House of Lords expressed a view thus:

‘Unacceptable tax avoidance [which] typically involves the creation of complex artificial structures by which, as though by the wave of a magic wand, the taxpayer conjures out of the air a loss or a gain, or expenditure, or whatever it may be, which otherwise would never have existed. These structures are designed to achieve an adventitious tax benefit for the taxpayer, and in truth are no more than raids on the public funds at the expense of the general body of taxpayers, and as such are unacceptable.’

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[3] Some of which would include *Mackay v Fey NO & another* 2006 (3) SA 182 (SCA) and *CSARS v Bosch & another* [2014] ZASCA 171; 2015 (2) SA 174 (SCA).

[4] *Commissioner of Customs and Excise v Randles Brothers and Hudson Ltd* 1941 AD 369 at 395-396.

[127] SARS contended that the evidence presented by Sasol Oil is inconsistent with the stated intention of the transactions. It argued, with reference to *CSARS v Bosch & another* [2014] ZASCA 171; 2015 (2) SA 174 (SCA) para 40, that in determining whether the transactions were genuine or simulated, the court stated thus:

'. . .The true position is that the "court examines the transaction as a whole, including all surrounding circumstances, any unusual features of the transaction and the manner in which the parties intend to implement it, before determining in any particular case whether a transaction is simulated.'"

[128] In this case, one needs to examine the evidence of the PwC letters of 3 and 18 April 2001 and the transfer pricing documents. These documents, including reports and minutes of SIH, reveal undisputed evidence, some of which, according to SARS's contention, finds expression in the following documents: (a) The 2003 and 2004 Sasol Limited filings with the USA Security and Exchange Commission refers to SISL consistently as a 'service company' and STI is referred to, correctly so, as a trading company; (b) SIH's Board minutes of 22 November 2002 and 28 February 2003, state that SISL's main business is to act as a 'service company' while STI's business is to act as a trading company; (c) SISL's transfer pricing report (2002/2003) by KPMG states that SISL's 'primary function is to provide shipping services' and that it 'takes on a small level of risk in connection with the provision of these services'. KPMG further reports that SISL had only one employee (based in the UK) who is responsible for 'facilitating the shipment of oil to [SA]'; (d) The transfer pricing study of Sasol Limited dated 30 June 2003, repeats that 'SISL's primary function is that of arranging shipping of oil to Sasol Oil'; and (e) The Sasol Oil resolution dated 14 May 2004 in which the main object of SOIL (which took over from STI) is described as: '[t]o act as an international trading company mainly for Sasol Oil'.

[129] SARS further refers to instances where the description of the role of SISL in the supply chain was sharply contradicted and irreconcilable with the role as described in the supply agreements and the oral evidence presented by Sasol Oil's witnesses in the Tax Court. Sasol Oil made no effort to explain these glaring contradictions and inconsistencies. While these instances, when individually considered, might not say much, their cumulative effect reveals, in the Sasol Group's own words, the true nature

and identity of SISL's function as shipping, and never the buying and selling of crude oil.

[130] The Tax Court found that some of the witnesses presented by Sasol Oil were not credible in that they resorted to denials and obfuscation when required to explain the commercial justification for SISL's role in the supply chain, considering that prior to July 2001, STI was able to solely conduct the supply directly to Sasol Oil. One such witness was Mr Gird, who testified that the restructuring he had proposed could not have been informed by tax considerations as he is not a tax expert. However, there is evidence that he commissioned an opinion on the tax implications of the initial proposed structure from Lovell. In addition, he received the PwC report from Ms Van Wyk, a fact he did not deny. He was thus alive to the possible impact of tax issues on any mooted restructuring.

[131] Similarly Mr Loubser was confronted, during cross-examination, with a copy of the minutes as evidence of his presentation to the Board at its meeting of 5 July 2001. The minutes of the meeting stated the following:

'A presentation by Mr Henri Loubser emphasised the need to review Sasol's structure in light of certain legislative changes. The proposal was to cease the contract between STI and Sasol Oil and move it to Sasol International Services. *This would optimise the tax regime.*' (My emphasis.)

Mr Loubser's answers in cross-examination on this aspect were most unsatisfactory. He sought to distance himself from the clear minutes of the meeting by stating that because he is not a tax expert, but an engineer, he could not have referred to the legislative changes or the tax regime. The suggestion of course was that the minutes incorrectly attributed those remarks to him. This assertion was disingenuous to the Tax Court. Up to the point in the trial when he was confronted with these minutes, there is no suggestion that he had ever sought to correct that which he claims had been wrongly attributed to him. Further, there is neither evidence that the tendency to attribute reports to officers who knew nothing of the subject was common place at Sasol Oil, nor was there any plausible reason as to why it would occur.

[132] Messrs Gird and Loubser were not candid with the Tax Court in their attempt to explain the commercial benefit of SISL in the supply chain. During cross-examination

on this point, Mr Gird referred to a 14 June 2001 presentation by Mr Bredenkamp, who was responsible for the STI operations in the Isle of Man, as outlining the commercial justification for the interposing of SISL in the supply chain. A careful reading of that presentation indicates that it is a repeat of the PwC opinion and fell woefully short of providing an explanation for the commercial justification of SISL. In the absence of such commercial justification, what would have been a tax avoidance scheme, as PwC cautioned, resulted in it being a tax evasion scheme.

[133] The evidence of Mr Harvey Foster, an expert witness, who testified for Sasol, focused on the international practice in the shipping trade to utilise different companies in line with their expertise. He further testified that it would be normal 'for international crude oil trading companies to buy crude oil on an FOB [Free On Board] basis and supply it on a delivered outturn basis' or 'conclude contracts on a back-to-back basis'. Such practice he opines, would be aimed at minimising the losses, regard being had in particular to the risk inherent in the transportation of oil. In general, it seems there would be nothing untoward with such arranged structures. As counsel for Sasol Oil correctly submitted, it is a choice that companies are free to make.

[134] Turning to this case, Mr Foster's evidence could not assist in explaining the role of SISL. During cross-examination, Mr Foster was confronted with evidence of a study conducted by KPMG, an audit firm, undertaken for the Sasol Group. The study found that in this particular case, the risk of losses during transit were minimal because SISL was insured. The shipping fees earned by SISL were justifiably low, less than 0.5 per cent of the volume of oil transported. Whatever risk there was, was covered by insurance. The question thus still remained: What was the commercial justification for the interposing of SISL, a shipping service company, as a trading company with powers to procure and sell crude oil as provided for in the supply agreements?

[135] From the record it is evident that Messrs Gird and Loubser as witnesses repeatedly asserted that their original proposal of restructuring never changed but was the same and consistent with the one adopted in July 2001. This is not borne out by the common cause facts. It is undisputed that the original proposal entailed the collapse of STI in the Isle of Man and transfer of both staff and operations to the UK based SISL, so as to bring an end to duplication, all of which made commercial sense.

At the risk of repetition, the PwC structure perpetuated duplication, with the identified inherent risk of absence of a commercial justification.

[136] It is trite that an appeal court is bound by the trial court's findings of credibility, unless they were found to be affected by a material misdirection or to be clearly wrong. The appeal court will only reverse these findings where it is convinced that the findings are wrong. I am unable to find any misdirection by the Tax Court in regard to the finding of credibility and contradictions on the part of Sasol's witnesses, in particular Messrs Gird and Loubser.

[137] On the conspectus of the evidence I would find that Sasol Oil failed to demonstrate to the Tax Court the commercial justification for interposing SISL in the supply chain. The role of SISL as stated in the supply agreements was a simulation. The continued reference to SISL, well beyond the adoption of the supply agreements, as a company with shipping functions and providing a service instead of trade functions, exposes its real role in the supply chain. No explanation could be provided to the Tax Court by Sasol Oil as to why it now had to take two companies to conduct a trade function that was initially handled by one company. I would therefore agree with the finding by the Tax Court that the interposing of SISL was not with the intention to avoid duplication and reduce costs, it was initially set out to achieve, but resulted in an entrenched duplication of trade functions by two subsidiary companies, clearly to evade the clutches of s 9D of the Act. The failure to provide commercial justification for SISL, revealed the absence of *bona fides* behind the transactions and as such the additional assessments were justified.

[138] In light of the conclusions I have reached, in line with that of the Tax Court, I deem it unnecessary to deal with SARS' alternative ground of attack based on s 103 of the Act. In this regard, I agree with the view expressed in the first judgment concerning s 103 debate and conclusion.

[139] I also agree with the Tax Court's decision on the interest and penalties payable to SARS on the additional assessments.

[140] In the circumstances I would dismiss the appeal with costs.

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S P Mothle

Acting Judge of Appeal

Ponnan JA (Lewis and Cachalia JJA concurring)

[141] On whether or not the transactions in question were simulated, my colleagues, Lewis JA and Mothle AJA, disagree. Lewis JA concludes (a conclusion with which I align myself) that they are not. Mothle AJA takes the view that 'the supply agreements defining the supply chain for crude oil to Sasol Oil in South Africa are a simulation.' In arriving at that conclusion, he states: 'I am unable to find any misdirection by the Tax Court in regard to the finding of credibility and contradictions on the part of Sasol's witnesses, in particular Messrs Gird and Loubser'.

[142] We are not concerned here with a dispute between the parties to the agreements. It is a third party – the Commissioner – who contends that the parties did not really intend the agreements to have, *inter partes*, the legal effect which its terms convey to the outside world. As Lewis JA points out, no evidence was led for the Commissioner. She adds 'but that is hardly surprising as it would not have had access to the internal workings of the Sasol Group'. Whilst that may be so, the fact that no evidence was led for the Commissioner is not without its consequence. It means that there was nothing to gainsay the evidence of Sasol Oil's five factual witnesses and one expert witness. It is unclear to me why the Tax Court took the view that the evidence of Sasol Oil's witnesses fell to be rejected. The criticism of their evidence was not only unduly generalized, but also rather severe. The rejection of the evidence of senior employees, two of whom were retired, absent any countervailing evidence, is disquieting. They had no motive to lie in order to save tax for Sasol Oil. No ready answer presents itself as to why these professional persons would perjure themselves. There thus appears to be no reason to question the reliability of their evidence (either

individually or collectively), much less their integrity or to brand them untruthful or evasive witnesses.

[143] However, a finding that the evidence of those witnesses did not survive scrutiny, is hardly the end of the enquiry. One would have to go much further. For the written agreements to have been a sham would have required the most extensive and elaborate fraud, stretching over a period of many years. It would have required the involvement of the persons participating directly, as well as the boards of directors of not just Sasol Oil, but also their related companies. The conduct of the parties and the documents generated before, at the time of and subsequent to the conclusion of the agreements belies that. There is not the slightest hint or suggestion in the wide array of documents introduced into evidence, such as letters of credit, bills of lading, invoices and certificates of quantity and quality, that the transactions were a sham or disguise. What is more, the financial statements of the relevant companies were entirely consonant with the supply agreements. The conclusion that such a sham was intended would mean that the production of these documents would have involved an elaborate fraud on the part of the authors of the documents and the members of the boards of directors of the relevant companies, as also their auditors. When one has regard to the history and background, the genesis and conclusion of the agreements in accordance with their terms, makes perfect sense.

[144] It goes without saying that the evidence must be looked at holistically. The Tax Court approached the evidence piecemeal. It appears to have focused rather too intently upon selected pieces of evidence to support its conclusion that the transactions were simulated. As it was put in *S v Hadebe & Others* 1998 (1) SACR 422 (SCA) at 426 f-h (citing with approval from *Moshephi and Others v R* (1980-1984) LAC 57 at 59F-H):

'The breaking down of a body of evidence into its component parts is obviously a useful aid to a proper understanding and evaluation of it. But, in doing so, one must guard against a tendency to focus too intently upon the separate and individual part of what is, after all, a mosaic of proof. Doubts about one aspect of the evidence led in a trial may arise when that aspect is viewed in isolation. Those doubts may be set at rest when it is evaluated again together with all the other available evidence. That is not to say that a broad and indulgent approach is appropriate when evaluating evidence. Far from it. There is no substitute for a detailed and critical examination of each and every component in a body of evidence. But,

once that has been done, it is necessary to step back a pace and consider the mosaic as a whole. If that is not done, one may fail to see the wood for the trees.'

Here, a proper consideration of the entire evidential mosaic, leads me to the conclusion that the alternative hypothesis sought to be advanced by the Commissioner, namely that the agreements are simulated, is without a proper factual foundation and remains but a speculative and conjectural one.

[145] In my view, it is clear that the relevant agreements were genuine agreements and truly intended by the parties in accordance with their terms. There was no simulation or, more particularly, dishonest intention by the parties to deceive by concealing the real agreements. There is accordingly no basis for finding that the ostensible agreements were a pretense or that there was any secret or unexpressed agreement, at odds with the apparent agreements. I am accordingly in respectful disagreement with Mothle AJA. For the rest, I agree with Lewis JA.

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V M Ponnan

Judge of Appeal

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