

THE TAXATION OF THE “SHARING ECONOMY” IN SOUTH AFRICA

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ABSTRACT

The research examined whether the services provided by the “sharing economy” platforms are adequately dealt with by the current South African tax systems. In addressing this main goal, the research analysed how the South African tax systems deal with the income and expenses of *Uber*, *Airbnb* and their respective service providers. The research also investigated how South Africa could classify “sharing economy” workers and how this would affect the deductibility of the worker’s expenses. A brief analysis was made of the taxation of the “sharing economy” businesses in Australia and the United States of America. These countries have implemented measures to effectively deal with regulating the “sharing economy” businesses. An interpretative research approach was used to provide clarity on the matter. Documentary data used for the research consists of tax legislation, case law, textbooks, commentaries, journal articles and theses. The research concluded that the current taxation systems have loopholes that are allowing participants in the “sharing economy” to avoid paying tax in South Africa. The thesis recommends that the legislature could adopt certain measures applied in Australia and the United States of America to more effectively regulate “sharing economy” in South African and remedy the leakages the current tax systems suffer, causing SARS to lose potential revenue.

Key words: Income tax; value-added tax; sharing economy; *Uber*; *Airbedandbreakfast* (*Airbnb*); Double Tax Agreements; place of effective management; permanent establishment; employee vs independent contractor; tax opportunism

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CHAPTER 1: INTRODUCTION

1.1 Context of the research and problem statement

Over the past number of years, new models of production and consumption of goods and services have emerged. The “sharing economy” is one such new model that has emerged in recent years, mainly as a result of the Internet.¹ The term “sharing economy” covers a sprawling range of digital platforms and offline activities.² The development of this business model has largely been in response to the weak economic environment and the depressed labour market.³ People unable to find work or needing supplemental income use these platforms to earn income from their labour and assets.

The term “sharing economy” lacks a common definition. According to Codognone, Biagi and Abadie⁴, the term comprises of digital platforms often operating as two-sided markets that match different groups of users and providers and enable the increase in scale and speed of traditional transactions, such as selling, renting, lending, labour trade and the provision of services. In many cases these platforms mediate activities involving peer-to-peer or peer-to-business transactions that are not yet fully regulated. Currently, expressions such as the “sharing economy”, “collaborative economy”, “peer economy”, “on-demand economy”, “collaborative consumption”, “gig economy”, “gift economy”, “circular economy” and “access economy” are used interchangeably to refer to very different digital platforms.⁵ This thesis will use the term “sharing economy”.

According to Schor, “sharing economy” activities fall into four broad categories.⁶ These activities comprise of the recirculation of goods, catering for the exchange of services, sharing

¹ JB Schor and CJ Fitzmaurice “Collaborating and connecting: The emergence of the sharing economy” (2014) 1. In L Reisch & J Thøgersen *Handbook on Research on Sustainable Consumption*. 2014. Cheltenham.UK: Edward Elgar.

² JB Schor “Debating the Sharing Economy” 2014. *Great Transition Initiative*. Available: <http://www.greattransition.org/publication/debating-the-sharing-economy> (Accessed 6 April 2017).

³ D Satyajit “The sharing economy creates a Dickensian world for workers – it masks a dark problem in the labour market” *Independent Voices* 12 February 2017. Available: <http://www.independent.co.uk/voices/sharing-economy-gig-economy-uber-airbnb-workers-rights-a7575856.html> (Accessed 21 June 2017).

⁴ C Codognone F Biagi and F Abadie “The Passions and the Interests: Unpacking the ‘Sharing Economy’” 2016 Available: <http://publications.jrc.ec.europa.eu/repository/bitstream/JRC101279/jrc101279.pdf> (Accessed 9 May 2017).

⁵ R Botsman “Defining the Sharing Economy; What is Collaborative Consumption –And what isn’t?” 2015. Available: https://www.fastcompany.com/3046119/defining-the-sharing-economy-what-is-collaborative-consumption-and-what-isnt?show_rev_content (Accessed 6 April 2017).

⁶ Schor “Debating the Sharing Economy” 4-6.

assets or space and using durable goods and other assets.⁷ Of specific interest in this thesis is the use of durable goods and other assets. The use of durable goods and other assets gained dominance after the 2009 recession in America, when a company named *Zipcar* placed vehicles in convenient urban locations, renting them out at an hourly rate. This approach became more economically attractive and initiatives like that of *Zipcar* proliferated, leading to car rental sites, bicycle-sharing and ride-sharing sites, such as *Uber*, *Uber X* and *Lyft*.⁸ This thesis will focus on vehicle ride-sharing, specifically *Uber* and *Airbedandbreakfast* (referred to as *Airbnb*) in the lodging sector.

Uber Technologies Inc. (with its headquarters in San Francisco, California) is one of the many companies in the relatively new “platform industry”. The company provides a smartphone application (referred to as the “app”) that serves as the intermediary between freelance cab owners and people looking for a lift.⁹ *Uber* itself does not own the cars; all it does is set the fares charged for the rides.¹⁰ In exchange for creating and providing the app-based marketplace for rides, *Uber* takes a portion of the gross fares (usually 20%, although this varies depending on the market) generated by the drivers.¹¹ The drivers have the freedom to decide whether and when to open the *Uber* mobile app and accept ride requests from customers.¹² *Uber* drivers are responsible for their own expenses, including fuel, equipment maintenance and repairs.

Airbnb Inc. (also with its headquarters in San Francisco, California) provides an online hospitality service, enabling people to lease or rent short-term lodging, including vacation rentals, apartment rentals, homestays, hostel beds or hotel rooms.¹³ The app is used in 191 countries, including South Africa. Like the vehicle sharing service, *Airbnb* levies fees or commission from both the guests and the hosts in conjunction with every booking. The property owners, also known as hosts, can rent anything from entire homes, to a room in a house or an

⁷ Codognone *et al* “Unpacking the Sharing Economy”.

⁸ Schor “Debating the Sharing Economy” 5-6.

⁹ S Agarwal “Is *Uber* taking us for a ride?” 2014. Available: <http://thinkbusiness.nus.edu/article/is-uber-taking-us-for-a-ride/> (Accessed 9 May 2017).

¹⁰ *Uber* Newsroom “Insurance for Ridesharing with *Uber*” *Uber Newsroom* 10 February 2014. Available: <https://newsroom.uber.com/insurance-for-uberx-with-ridesharing/> (Accessed 21 June 2017).

¹¹ *Uber* Help “How does *Uber* work?” 2017. Available: <https://help.uber.com/h/738d1ff7-5fe0-4383-b34c-4a2480efd71e> (Accessed 20 April 2017).

¹² *Uberestimate* “So, what is *Uber*?” 2017. Available: <http://uberestimate.com/about-uber/> (Accessed 16 April 2017).

¹³ S Oei and DM Ring “Can Sharing Be Taxed?” (2016) 93 *Washington University Law Review* 989. Available: http://openscholarship.wustl.edu/law_lawreview/vol93/iss4/7 (Accessed 12 April 2017).

air mattress in a living room.¹⁴ Unlike *Uber*, the hosts decide on the price they charge and manage their own personal rental calendar. Renters, by means of the smartphone app or the website, input their travel dates and can then search through host listings based upon price, location and amenities.¹⁵

The “sharing economy” raises fresh issues with respect to tax compliance in South Africa. Firstly, growth of the “sharing economy” has led to an increase in the number of microbusinesses nationwide. This, in turn, has given rise to unique tax compliance challenges. For example, most of these individual earners earn income amounts too small, relatively, to justify the burden of keeping track of such income and expenses.¹⁶ These low-income amounts may cause “sharing economy” workers to pay less attention to the accuracy of their documents when reporting their earnings. The other tax issue relates to the taxation of the commissions earned by *Uber* and *Airbnb*. This leads to the question of what measures the South African Revenue Service (SARS) can put in place to ensure that these microbusinesses and the companies operating these services do not escape reporting and paying tax on their earnings.¹⁷

Another issue that has surfaced in relation to the “sharing economy” is whether its workers are independent contractors or whether they are employees for employees’ tax purposes. The issue has been the subject of intense legal battles worldwide. *Uber* has alleged that its drivers are independent contractors who are responsible for paying self-employment taxes. The distinction between employees and independent contractors in this case has been difficult given that *Uber* drivers do not quite fit into either of the traditional categories.¹⁸ It is submitted that there is a need for this issue to be settled in South African law as this will impact on the responsibility for the payment of the tax that is due by the service provider. Employees’ tax deducted from earnings is a pre-payment of income tax¹⁹, with limitations on the allowable deductions that the employee can claim (section 23(m) of the Income Tax Act²⁰). Independent contractors submit an annual tax return, together with provisional tax returns.²¹ Some authors have even

¹⁴ J Gorey “How to Make Money as an *Airbnb* Host” 2014. Available: <http://www.thesimpledollar.com/how-to-make-money-as-an-airbnb-host/> (Accessed 17 April 2017).

¹⁵ *Ibid.*

¹⁶ Oei and Ring “Can Sharing Be Taxed?” 1008-1009.

¹⁷ *Ibid.*

¹⁸ *Ibid.*

¹⁹ Paragraph 2(1) of Schedule Four to the Income Tax Act, 58 of 1962.

²⁰ Act 58 of 1962.

²¹ Paragraph 19(1) (a) of Schedule Four to the Income Tax Act, 58 of 1962

suggested that it might be time to develop the law by creating a third category of workers who are subject to certain regulations.²²

It is submitted that SARS may be losing tax revenue due to problems that may exist in taxing the “sharing economy”. It is therefore important that an analysis is carried out that investigates whether the application of the current legislation is adequate to deal with the challenges being experienced in taxing the “sharing economy”.

Given the global nature of the phenomenon, taxation of the “sharing economy” elsewhere may provide guidance. A comparative analysis was therefore made of tax law relating to the “sharing economy” in America and Australia. These countries were chosen because of the importance of their contributions on the subject. Several states in America have passed laws to legalise and regulate ride-sharing apps. The new laws require Transport Network Companies such as *Uber* to retain driver and trip records for a period ranging from one to six years.²³ This is assisting the Internal Revenue Service (IRS) check the accuracy of the income declarations that are made by the drivers.²⁴ In the lodging sector, the state of Virginia enacted legislation that regulates *Airbnb* to ensure that users pay tax to the government and to ensure that there is fair competition between *Airbnb* hosts and other accommodation providers.²⁵

Australia is currently implementing an E-tax system that will request information on all payments made from the “sharing economy” companies and the records will be “electronically matched” with the Australian Tax Office’s own information and data holdings to identify those who are not complying with their tax obligations.²⁶ Banks and other financial institutions have started handing over detailed payment information regarding drivers and other users who have not declared their income from using the sharing platforms.²⁷ The Australian tax officials are

²² Oei and Ring “Can Sharing Be Taxed?” 1042-1045.

²³ M Moran, B Ettelman, G Stoeltje, T Hansen and A Pant “Policy Implications of Transport Network Companies” 2017. *Transportation Policy Research Center* 17-70F.

²⁴ KE O’Connor “Along for the Ride: Regulating Transport Network Companies” (2016) 51 *Tulsa Law Review* 2. Available: <http://digitalcommons.law.utulsa.edu/cgi/viewcontent.cgi?article=2988&context=tlr> (Accessed 11 August 2017).

²⁵ E Boehm “*Airbnb* bill passes in Virginia, but won’t take effect until 2017” 2016. Available: <http://watchdog.org/259285/airbnb-virginia-bill-passes/> (Accessed 1 August 2017).

²⁶ N Zhou “Tax office announces crackdown on *Uber* and other ride-sharing services” *The Guardian*. 13 December 2016. Available: <https://www.theguardian.com/australia-news/2016/dec/13/tax-office-announces-crackdown-on-uber-and-other-ride-sharing-services> (Accessed 1 August 2017).

²⁷ R Viellaris “Australian Taxation Office announces crackdown on ride-sharing services *Uber*, *GoCatch* and *Lyft*” *The Courier-Mail* 12 December 2016. Available: http://www.couriermail.com.au/business/companies/australian-taxation-office-announcescrackdown-on-ridesharing-services-uber-gocatch-and-lyft/news_story/c9ac3344651d3d2405053bc80ed2955a (Accessed 11 August 2017).

analysing data from the taxpayers' social media platforms to find out if their declared income matches their lifestyle.²⁸ These developments are helpful for the present study and certain policies can be adopted in South Africa to simplify ways of declaring taxes and help identify culprits who are evading their tax obligations.

1.2 Goals of the research

The main goal of the research is to investigate whether the services provided by the “sharing economy” platforms are adequately dealt with in the current South African tax systems. In achieving the main goal, the research addresses the following sub-goals:

- i. an analysis of how the current tax systems deal with the income and expenses of *Uber*, *Airbnb* and the providers of the underlying services;
- ii. an analysis of how South Africa may classify its “sharing economy” workers for tax purposes;
- iii. a comparative analysis of how Australia and America are taxing the “sharing economy” activities;
- iv. recommendations relating to how the current tax structures can be amended to deal with taxable income from activities in the “sharing economy”.

1.3 Methods, procedure and techniques

Taking the research problem, the goals and sub-goals formulated for the present study into account, a qualitative research style was selected as the most suitable method to analyse how the current tax systems deal with the income and expenses in the “sharing economy”. Consequently, an interpretative research approach will be adopted for the present research as it seeks to understand and describe.²⁹ The research methodology to be applied can be described as a doctrinal research methodology. This methodology provides a systematic exposition of the rules governing a specific legal category (in the present case the legal rules relating to the taxation of the “sharing economy”), analyses the relationships between the rules, explains areas of difficulty and is based purely on documentary data.³⁰

²⁸ *Ibid.*

²⁹ E Babbie and J Mouton *The Practice of social research: South African Edition* 2009.

³⁰ MA McKerchar “Philosophical Paradigms, Inquiry Strategies and Knowledge Claims: Applying the Principles of Research Design and Conduct to Taxation” 2014. Available: http://www.asb.unsw.edu.au/research/publications/ejournaloftaxresearch/Documents/paper1_v6n1.pdf (Accessed 25 June 2017).

Documentary data will be used for the research and will consist of tax legislation, case law, textbooks, commentaries and journal articles. Other sources will include internet sources and academic theses that have investigated and analysed the issue of sharing economies. Non-legal sources will also be consulted, since the topic has more dimensions than simply a legal dimension. Additionally, a comparative research methodology will be used. The comparative research will specifically investigate how developed countries, America and Australia, deal with the “sharing economy” and what legislation they have put in place to regulate this new sector.

The research is conducted in the form of an extended argument, supported by documentary evidence. The validity and reliability of the research and the conclusions will be ensured by:

- 1 adhering to the rules of the statutory interpretation, as established in terms of statute and common law;
- 2 placing greater evidential weight on legislation, case law which creates precedent, or which is of persuasive value (primary data) and the writings of acknowledged experts in the field;
- 3 discussing opposing viewpoints and concluding, based on a preponderance of credible evidence; and
- 4 the rigour of the arguments.

As all the data are publicly available, no ethical considerations arise in relation to the use of the data. Interviews are not conducted, and opinions are considered in their written form.

1.4 Chapter overview

The thesis is divided into five chapters. Chapter one served as an introduction to the thesis. Chapter two discussed the definition of “gross income”, focusing on the concepts of residence, source rules and what constitutes a “receipt” for purpose of “gross income”. Chapter three discussed the deductions *Uber*, the *Uber* driver and the *Airbnb* host can claim. Furthermore, the chapter determined how South Africa may classify its “sharing economy” workers as either “independent contractors” or “employees” and how falling into either group will impact on the deductibility of the workers’ expenses, their tax compliance requirements and the responsibilities of their “employers”. Chapter four investigated the challenges South Africa is experiencing in taxing the “sharing economy” and how these problems can possibly be remedied. In doing so, the chapter analysed approaches that have been adopted by other

jurisdictions, specifically Australia and America, and considered whether the same approaches could be adopted in South Africa. The final chapter, chapter five, concluded the thesis and made recommendations on how the current tax legislation can be amended to more effectively regulate and tax the “sharing economy” in South Africa.

CHAPTER 2: “GROSS INCOME” AND THE “SHARING ECONOMY”

2.1 Introduction

Chapter one described the context in which the research is situated, defined the term “sharing economy”, stated the objectives of the research, discussed the research methodology and briefly outlined the chapters to follow. The present chapter addresses the first research objective: an analysis of how the current South African tax systems deal with the income accruing to *Uber*, *Airbnb* and their respective service providers. In doing so, the definition of “gross income” is briefly discussed, focusing on residence, source rules and what constitutes a “receipt” for purposes of “gross income” when taxing proceeds from the “sharing economy” in South Africa.

2.2 “Gross income”

The calculation of a person’s taxable income commences with determining what constitutes “gross income”.³¹ If a person does not have “gross income” or taxable capital gains, he or she cannot be liable to pay tax.³² The definition of “gross income” makes a distinction between the basis of taxation applied to tax residents and that applied to non-residents. Residents are taxed on their receipts and accruals, irrespective of where it is earned, and non-residents are taxed on income from a source within South Africa.³³

In terms of section 1 of the Income Tax Act “gross income”, in relation to any year or period of assessment, means -

- (i) in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or
- (ii) in the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within the Republic,

during such year or period of assessment excluding receipts or accruals of a capital nature,
...³⁴

³¹ M Stiglingh, A Koekemoer, L Van Schalkwyk, JS Wilcocks, RD de Swardt & K Jordaan *Silke on South African Income Tax* (2015) 13.

³² P Haupt *Notes on South African Income Tax* 36th ed (2017) 17.

³³ Section 1 of the Income Tax Act 58 of 1962.

³⁴ *Ibid.*

In principle, the first step in determining the normal tax liability of any natural person in South Africa is to establish whether the natural person is a resident as defined in section 1 of the Act.³⁵ Therefore, before discussing the definition of “gross income”, the issue of residence will be considered in relation to *Uber*, *Airbnb* and the respective service providers.

2.3 Residence

Since January 2001 South Africa applies a residence-based income tax system. This system taxes South African residents on their receipts and accruals. Non-residents will, however, only be taxed on income from a South African source.³⁶

2.3.1 Residence of natural persons

The residence of a natural person is determined in terms of the definition of “resident” in section 1 of the Income Tax Act,³⁷ as either an individual who is “ordinarily resident” in South Africa in terms of common law or who meets the physical presence test.³⁸ The Income Tax Act does not define “ordinarily resident” and therefore case law applies.

A person will be ordinarily resident in South Africa if he or she meets the common law tests established, *inter alia*, in *Cohen v CIR*³⁹ and *CIR v Kuttel*⁴⁰. In *Cohen v CIR* it was held that a person is ordinarily resident at the “place of his most fixed and settled residence . . . the country to which he would naturally and as a matter of course return from his wanderings . . . his real home”⁴¹. This was upheld in *CIR v Kuttel*, where it was held that a person’s ordinary residence was “where the person was *habitually* and *normally* resident . . .”⁴² A person who is not “ordinarily resident” in South Africa may become ordinarily resident by virtue of the number of days spent in South Africa.⁴³ The definition of “ordinarily resident”, however, excludes any person (whether a natural person or a person other than a natural person) “who is deemed to be exclusively a resident of another country for the purposes of the application of any agreement

³⁵ N Musviba “Ordinary residence and physical presence test” 2017. *South African Tax Guide*. Available: <http://www.sataxguide.co.za/ordinary-residence-physical-presence-test/> (Accessed 1 November 2017).

³⁶ Section 1 of the Income Tax Act 58 of 1962.

³⁷ Act 58 of 1962.

³⁸ *Ibid.*

³⁹ (1946) 13 SATC 362.

⁴⁰ (1992) 54 SATC 298.

⁴¹ (1946) 13 SATC 362.

⁴² (1992) 54 SATC 298.

⁴³ Definition of “ordinarily resident” in section 1 of the Income Tax Act 58 of 1962.

entered into between the governments of the Republic and that other country for the avoidance of double taxation” (a Double Tax Agreement).

Uber drivers or, what is more feasible, *Airbnb* hosts may be residents of a foreign country and also residents in South Africa by virtue of the days present test. As these foreign residents would be earning income from a source in South Africa (see below), the Double Tax Agreements between South Africa and these countries would therefore be relevant. This is discussed below.

2.3.2 Residence of persons other than natural persons

A person other than a natural person (for example companies, close corporations and trusts) is defined as being “resident” if it is incorporated, established, or formed in the Republic, or has its “place of effective management” in the Republic.⁴⁴ This definition is very wide in that all the requirements are alternatives. If the juristic person satisfies one of the requirements it would be regarded as a “resident” of the Republic and it would be liable for tax in South Africa on its world-wide receipts.⁴⁵ *Uber* and *Airbnb* are not incorporated, established or formed in the Republic. They are both incorporated in America but providing their services in South Africa. Therefore, it becomes necessary to see if the companies have a “place of effective management” in the Republic.

The Income Tax Act⁴⁶ does not define what is meant by term “place of effective management”, however, to clarify the meaning SARS issued an Interpretation Note.⁴⁷ The Interpretation Note acknowledges the challenge modern technology presents when establishing a company’s “place of effective management”. For example, “physical meetings of the board are often no longer required or implemented or, alternatively, even when physical board meetings are held in a particular location some, possibly a majority, of the key directors with overriding decision-making powers, are not in the same location as the physical meeting.”⁴⁸ Despite this challenge SARS maintains that the same “core principles” should still apply when establishing a company’s “place of effective management” in the digital economies.

The Interpretation Note states that the test for the “place of effective management” is one of *substance over form*, and it requires the identification of the individuals who are making the

⁴⁴ Paragraph (b) of the definition of “resident” in section 1 of the Income Tax Act 58 of 1962.

⁴⁵ Paragraph (i) of the “gross income” definition in section 1 of the Income Tax Act 58 of 1962.

⁴⁶ Act 58 of 1962.

⁴⁷ Interpretation Note 6 of 2015 of the Income Tax Act of 1962.

⁴⁸ Interpretation Note 6 (2015) 9.

key management and commercial decisions⁴⁹, as well identifying where the individuals were located when the “decisions were in substance actually made.”⁵⁰ There are several guidelines that assist in determining a company’s “place of effective management”. Some of these factors are briefly discussed below.

a) Head office

The location of a company’s head office is generally a major factor in the determination of a company’s “place of effective management” because it often represents the place where key company decisions are made.⁵¹ The Interpretation Note stipulates that “if a company’s senior management and support staff operate from offices located in various countries, then the company’s head office would be located where those senior managers are primarily based or where they normally return to following travel to other locations, or meet when formulating or deciding key strategies and policies for the company as a whole.”⁵²

Uber has various offices all over the world, including in the Republic. However, none of the offices in the Republic qualify as the head office of the company for purposes of establishing a “place of effective management”. This is because *Uber*’s senior management is primarily based in America where they meet when formulating key strategies and policies for the company as a whole. On the other hand, *Airbnb* does not have any offices in the Republic; the company simply launched its website and “app” that are used in South Africa and it does not have any senior management or support staff located in the Republic. It is submitted that the head offices of *Uber* and *Airbnb* are in America, where the highest level of management and support staff are located.

b) Board

The Interpretation Note states that the location where a company’s board often meets, retains and exercises its authority to govern the company and in substance makes the key management and commercial decisions necessary for the conduct of the company’s business as a whole, may be considered to be the company’s “place of effective management”.⁵³ In relation to *Uber* and *Airbnb*’s board of directors, they would probably meet and make key management and

⁴⁹ *Ibid.*

⁵⁰ N Augustin *Factors to be considered when establishing the place of effective management in a digital economy* (MCom in Taxation, University of Cape Town, 2015).

⁵¹ Interpretation Note 6 (2015) 7.

⁵² *Ibid.*

⁵³ Interpretation Note 6 (2015) 8.

commercial decisions necessary for the conduct of the companies' businesses as a whole in America. Hence, it is submitted that America can be regarded as the "place of effective management" for both *Uber* and *Airbnb*.

c) Operational management versus broader top-level management

The location where operational management and top-level management decisions are made is crucial when establishing a company's "place of effective management".⁵⁴ The Interpretation Note states that operational management generally oversee the day-to-day business operations and activities of a company and their decisions are generally less important when establishing a company's "place of effective management".⁵⁵ On the other hand, top-level management predominantly consists of senior managers who are responsible for key management and commercial decisions; and their decisions are important when establishing a company's "place of effective management".

Decisions by *Uber* or *Airbnb* to launch their business in new countries or to develop new products constitute key management decisions that are likely to be made by senior management in America. The *Uber* managers in South Africa would generally be responsible for the day-to-day business operations of the business, such as attending to matters of repairs at the business premises, implementing the company's human resource policies and similar issues. These decisions indicate that the South African managers would be operational managers, as they are not making key management decisions. On the other hand, *Airbnb* does not have business offices located in the Republic where management can make any decisions or carry out any duties, and thus all the company's decisions are made in America where the company is incorporated. In the light of these factors, it is submitted that persons responsible for the key management and commercial decisions for both companies are located in America.

The factors discussed above establish that *Uber* and *Airbnb* have their head offices, board of directors and highest level of senior management located in America. Since the test for "place of effective management" is one of *substance over form*, the people who are actually "calling the shots" and exercising "realistic positive management" are located in America. Therefore, it is submitted that *Uber* and *Airbnb* do not have a "place of effective management" in the Republic, meaning they are not "resident" for tax purposes. However, considering that the companies are receiving certain income from a South African source, source rules and the

⁵⁴ *Ibid.*

⁵⁵ *Ibid.*

provisions of the Double Tax Agreement (DTA) between South Africa and the United States of America⁵⁶ must be applied.

2.4 Source

The South African tax system changed from source basis to residence basis. Persons who are not resident in South Africa are only subject to tax (in South Africa) on income from a South African source. According to Haupt, the general source of income is where the income has its origins.⁵⁷ In *Liquidator Rhodesia Metals Ltd v COT*⁵⁸ the court suggested that “source” was what a practical man regarded as a real source of income and that it is a question of fact. The principal test used to determine the source of income, where the provisions of section 9 of the Act⁵⁹ do not apply, is the originating cause test. This test was developed in *CIR v Lever Brothers and Unilever Ltd*⁶⁰. In terms of the test, the first step is to determine what gave rise to the income and only after this has been determined can the second question be answered, namely, in which country the activities that gave rise to the income were conducted.⁶¹ As the provisions of section 9 of the Act⁶² do not apply to the “sharing economy” services, this test will be applied to *Uber*, *Airbnb* and their respective service providers.

2.4.1 Source of *Uber* and *Airbnb* companies’ income

The *Airbnb* company receives commission from hosts who use their website and “app” to rent out their homes. The originating cause of the income will be the letting out of property located in South Africa and therefore *Airbnb* must include this income in its South African “gross income”. Similarly, the *Uber* company is earning a commission from the *Uber* drivers who are using its “app”. The originating cause of this commission is the ride services provided by *Uber* drivers in the Republic. For this reason, the income has its origins in the Republic and the non-resident company must include the income in its “gross income”. The provisions of the DTA between South Africa and the United States of America, may, however, override the source rules.

⁵⁶ Convention between the Republic of South Africa and The United States of America for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains (1997).

⁵⁷ Haupt *Notes on South African Income Tax* 30.

⁵⁸ 1938 AD.

⁵⁹ Act 58 of 1962.

⁶⁰ 1946 AD.

⁶¹ L Olivier and M Honiball *International Tax: A South African Perspective* (2005) 44.

⁶² Act 58 of 1962.

2.4.2 Source of income of *Airbnb* hosts and *Uber* drivers

In relation to *Uber* drivers and *Airbnb* hosts, the source of their income is in South Africa. *Uber* drivers are providing their services in the Republic (the “activities” test in *Millin v CIR*⁶³ establishes the source of the income) and the property that the *Airbnb* hosts are letting out is situated in South Africa (the place where the property is situated establishes the source of income, as held in *Liquidator, Rhodesian Metals Ltd v COT*⁶⁴). Therefore, the income that they earn from these activities will be taxed in South Africa, unless the drivers or hosts are non-residents and the DTA between South Africa and their country of residence applies. This is discussed below.

2.5 Double Tax Agreements

Once it has been established that income derived by a non-resident is from a South African source the enquiry then focuses on the existence or non-existence of a DTA. This is because the definition of “resident” states that “any person who is exclusively deemed to be a resident of another country for purposes of the application of a double tax treaty between that country and South Africa is not a resident as defined.”⁶⁵ A DTA is an agreement between two countries aimed at regulating the taxation of income earned in one State and subject to tax in the other State. The principal objective of a DTA is to prevent double taxation because it may happen that an amount received by or accruing to a non-resident may be subject to tax in South Africa in terms of the source rules, while also being subject to tax in the country of residence of the taxpayer.⁶⁶ Section 108 of the Act,⁶⁷ read in conjunction with section 231(4) of the Constitution, provides for relief from such double taxation by enabling the National Executive to enter into an agreement with the government of any other country.⁶⁸ South Africa and the United States of America, as well as a large number of other countries, have DTAs in place and therefore it is necessary to analyse their impact on the source of income.

2.5.1 Double Tax Agreements between South Africa and other countries

As *Uber* drivers and *Airbnb* hosts may be foreign residents earning income from a South African source, the provisions of a DTA between South Africa and their country of residence

⁶³ 3 SATC 170.

⁶⁴ 9 SATC 363.

⁶⁵ Section 1 of the Income Tax Act 58 of 1962.

⁶⁶ Haupt *Notes on South African Income Tax* 36.

⁶⁷ Act 58 of 1962.

⁶⁸ The Constitution of the Republic of South Africa, 1996.

may be relevant. Since it is submitted that most DTAs are drafted using similar language in relation to residence, provisions of the DTA between South Africa and America will be considered. Article 4 of the DTA deals with the issue of residence. The Article states that to determine the residence of the drivers and hosts living in a foreign country the first step is to determine where the individual has a permanent home. “The individual will be deemed to a resident in the State where he has a permanent home available to him; if he has a permanent home available to him in both States, the individual will be deemed resident of the State with which his personal and economic relations are closer.”⁶⁹ If the individual does not have a permanent home in either States or if his personal and economic relations cannot be determined, he will be deemed “resident” of the State in which he has an habitual abode. “If the individual has a habitual abode in both States or in neither of them, he shall be deemed to be resident of the State of which he is a National. If he is a national of both States or neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.”⁷⁰

Given that most of the DTAs entered into by South Africa are based on the OECD Model Tax Treaty⁷¹, the provisions of this treaty are discussed in order to determine which country – South Africa or the foreign country – has taxing rights. The OECD Model Tax Treaty deals with income derived from immovable property in Article 6 and income derived from carrying on a business in Article 7. Article 6 gives the right to tax income from immovable property to the State of source, that is, the State in which the property producing the income is situated.⁷² Article 6 is applicable to *Airbnb* hosts who are foreign residents but are deriving income from immovable property situated in the Republic. In terms of the Article, income derived from the property will be taxed in South Africa.

In terms of the Article 7⁷³, “...profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on a business in the other Contracting State through a ‘permanent establishment’ situated therein.” This Article is applicable to *Uber* drivers who are foreign residents but are deriving income from carrying on their business in the Republic through a permanent establishment. Article 7 allocates the taxing rights attributable to the permanent establishment to South Africa. Where the enterprise does not have

⁶⁹ Article 4 of the DTA between South Africa and America.

⁷⁰ *Ibid.*

⁷¹ The OECD Model Tax Convention on Income and Capital 2010.

⁷² *Ibid.*

⁷³ *Ibid.*

a permanent establishment in the Republic the business profits would be taxed in the foreign resident's country. The definition of a "permanent establishment" is similar in most DTAs and the definition in the DTA between the United States of America and South Africa is discussed below. *Uber* drivers providing their services in South Africa would need to live in South Africa and are likely to provide their services from their homes, and also likely to be South African residents in terms of the relevant DTAs that may apply. Even if they are non-residents in terms of a DTA, they are likely to have a "permanent establishment" in South Africa and in terms of the applicable DTAs would be taxed in South Africa.

2.5.2 The Double Tax Agreement between the United States of America and South Africa

From the discussion above it has been shown that *Uber* and *Airbnb* companies are not residents of South Africa, as they are not incorporated, formed or established in South Africa; nor do they have a "place of effective management" in South Africa. They are therefore residents of America. As *Uber* and *Airbnb* earn income from a South African source, this income received or accruing is subject to normal tax in South Africa, unless the taxability of the income is affected by the DTA between the United States of America and South Africa. Provisions of the DTA that are applicable to *Uber* and *Airbnb* are discussed below.

2.5.2.1 Business Profits

Article 7(1) of the DTA between America and South Africa provides that:

...the profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on a business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.⁷⁴

Under Article 7 the existence of a "permanent establishment" in a Contracting State is necessary, therefore provisions of Article 5 of the DTA will have to be considered. Article 5 defines a "permanent establishment" as a "fixed place of business through which the business of an enterprise is wholly or partly carried on."⁷⁵ To determine which country – South Africa or the United States of America – has taxing rights in respect of the business profits, the provisions of Articles 7 and 5 of the DTA need to be interpreted.

⁷⁴ DTA between South Africa and America (1997) 6.

⁷⁵ *Ibid.*

When interpreting any legislation (including tax treaties), section 233 of the Constitution requires the court to interpret them in a manner consistent with international law.⁷⁶ Oliver and Honiball explain that since “the customary rules of international law form part of international law, section 233 of the Constitution would require the court to interpret the DTA in a manner which is consistent with the customary rules of international law.”⁷⁷ Costa and Stack are of the view that “since the Vienna Convention on the Law of Treaties is regarded as a codification of customary international law, section 232 of the Constitution provides that the Convention should be regarded as law in South Africa.”⁷⁸ This view can be supported by Holmes⁷⁹ who states that DTAs have to be interpreted in accordance with Articles 31 and 32 of the Vienna Convention on the Law of Treaties.⁸⁰ His view can be confirmed by *Krok v CSARS*⁸¹, where the court held that South African courts are bound to apply rules of the Vienna Convention on the Law of Treaties⁸² when interpreting DTAs.

*AB LLC and BD Holdings LLC v CSARS*⁸³ recently interpreted provisions of the DTA between America and South Africa. In the case the court had to determine whether AB LLC and BD Holdings had created a “permanent establishment” in South Africa. In interpreting the provisions of Article 5(1) and 5(2)(k) of the DTA the court did not refer to the rules of interpretation as set out in the Vienna Convention on the Law of Treaties, it simply referred to interpretations as set out in the Technical Explanation of the Convention between the America and South Africa.⁸⁴ The court viewed the Technical Explanation as “offering an insight into the understanding of the signatories of the DTA”, namely South Africa and America.⁸⁵ Although there is no indication in the Technical Explanation itself or in any other document that the Technical Explanation has been adopted in South Africa, it appears that the court took

⁷⁶ D Costa and L Stack “The Relationship between Double Tax Agreements and the Provisions of the South African Income Tax Act” 2014 (7) 2 *JEF* 278.

⁷⁷ L Olivier and M Honiball *International Tax: A South African Perspective* 2008.

⁷⁸ Costa and Stack 2014 (7) 2 *JEF* 278.

⁷⁹ K Holmes *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Application* (2007) 79.

⁸⁰ The Vienna Convention on the Law of Treaties 1969. Available:

<https://treaties.un.org/doc/publication/unts/volume%201155/volume-1155-i-18232-english.pdf> (Accessed 1 January 2018)

⁸¹ 2015 (6) SA 317 (SCA).

⁸² The Vienna Convention on the Law of Treaties 1969.

⁸³ (2015), 77 SATC 349.

⁸⁴ Department of the Treasury “Technical Explanation of the Convention between the United States of America and the Republic of South Africa for the avoidance of Double Taxation and the Prevention of Fiscal evasion with respect to taxes on income and capital gains” (1998) 14.

⁸⁵ (2015), 77 SATC 349.

the view that the Technical Explanation on the DTA under consideration is binding in South Africa.⁸⁶

Commenting on the case, Du Plessis⁸⁷ stated that the court's reliance on the Technical Explanation without sufficient justification is problematic. He is of the view that since Technical Explanations are prepared by American treaty negotiators, they remain only of unilateral authority. It is submitted that Du Plessis' interpretation is correct because Article 31(2)(a) and (b) and 31(3)(a) and (b) of the Vienna Convention on the Law of Treaties all require agreements between the parties to the treaty. Vogel and Rust⁸⁸ and Harris and Oliver⁸⁹ also agree that Technical Explanations cannot be used to interpret a DTA. Therefore, it is submitted that South African courts are required to take the provisions of the Vienna Convention on the Law of Treaties into account when interpreting any legislation including tax treaties, in accordance with section 232 read together with section 233 of the Constitution.⁹⁰

Article 31 of the Vienna Convention on the Law of Treaties contains the general rule of interpretation. It states that "a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and the light of its object and purpose"⁹¹, which are to avoid the same income being taxed twice. Following the approach in Article 31 of the Convention, a plain reading of the wording in Article 7 of the DTA makes it clear that, for the business profits of an American resident to be taxable in South Africa, there must be a business that has been carried on in South Africa and that the business has to be carried on through a "permanent establishment" situated in South Africa.⁹² In terms of Article 5 the term "permanent establishment" means a "fixed" place of business. The ordinary meaning of the word "fixed" is "attached or placed so as to be immovable."⁹³ This means that the "permanent establishment" where the business is conducted must be "a place of management, a branch, an office, a factory, a workshop..." that is immovable.

⁸⁶ I Du Plessis "The Interpretation of DTA: A Comparative Evaluation of Recent South African case law" 2016 (3) *TSAR* 495.

⁸⁷ *Ibid.*

⁸⁸ K Vogel and A Rust *Introduction* in Reimer and Rust (eds) *Klaus Vogel on Double Taxation Conventions* (2015) 42-43.

⁸⁹ P Harris and D Oliver *International Commercial Tax* (2010) 36.

⁹⁰ Costa and Stack 2014 (7) 2 *JEF* 278.

⁹¹ Article 31 of the Vienna Convention.

⁹² DTA between South Africa and America (1997) 6.

⁹³ The Collins Dictionary Online. Available: <https://www.collinsdictionary.com/dictionary/english/fixed> (Accessed 1 January 2018).

In relation to *Uber*, it has business premises in South Africa, located in Johannesburg and Cape Town. Article 5(2) of the DTA⁹⁴ holds that the term “permanent establishment” includes an office; by having offices in these two cities *Uber* qualifies as having a “place of business”. Both offices are “fixed” places of business through which *Uber* carries on its enterprise. Additionally, *Uber* is not excluded from having “permanent establishment” in South Africa by provisions of Article 5(3) of the DTA. Therefore, it is submitted that *Uber* has “permanent establishments” in South Africa. The effect of Article 7(1) of the DTA, read with Article 5, gives South Africa the taxing rights, meaning it may tax *Uber* on profits that it is making in South Africa through a “permanent establishment”.

To date of this thesis, *Airbnb* does not have any premises, facilities or installations from which it carries on its business in South Africa. This means that *Airbnb* fails to satisfy this part of definition of a “permanent establishment”. Therefore, it is submitted that *Airbnb* does not have a “permanent establishment” in the Republic. The effect of *Airbnb* not having a “permanent establishment” in terms of Article 7 of the DTA means that South Africa does not have the right to tax it on commission income earned in South Africa, despite it being from a source within the Republic. Since DTAs take precedence over the Income Tax Act, the profits made by *Airbnb* will be taxed in America.

2.6 Gross income elements

Having established that *Uber*, *Uber* vehicle owners and *Airbnb* owners will be taxed either as residents or non-residents on income from a source within South Africa, the definition of “gross income” will now be briefly discussed.

For an amount to be included in a taxpayer’s “gross income”, all the elements of the “gross income” definition need to be met. If one of the requirements is not satisfied, the amount cannot be “gross income”. Not all elements in this definition are defined in the Act, therefore it is necessary to refer to case law to provide clarity on their meaning.⁹⁵

2.6.1 Amount in cash or otherwise

In *WH Lategan v CIR*, the court held that the word “amount” includes “not only money which has been received by the taxpayer or which has accrued to him, but all forms of property which

⁹⁴ DTA between South Africa and America (1997) 6.

⁹⁵ KT Nyakanyanga *The Taxation of illegal Income in South Africa: The basis on which proceeds from a unilateral taking should be taxed* (MCom (Taxation) mini-thesis, Rhodes University, 2016).

he has received, or which has accrued to him, whether corporeal or incorporeal, which has a monetary value, including debts and rights of action”.⁹⁶ The court in *CIR v Butcher Brothers (Pty) Ltd*, held that the word “amount... must mean an amount having an ascertainable money value”.⁹⁷ This amount must be in cash or otherwise. “Should a taxpayer receive an amount other than in cash, the market value of such asset should be included in the taxpayer’s income.”⁹⁸ In *C:SARS v Brummeria Renaissance (Pty) Ltd*⁹⁹, the court held that a wide interpretation was to be given to the word “amount” in the definition of “gross income”. The Court also stated that the onus of establishing this “amount” lies with the Commissioner.¹⁰⁰

Uber, *Uber* vehicle owners and *Airbnb* owners are recipients of payments in the form of cash or “near cash” and these amounts have a monetary value that is quantifiable. Therefore, receipts flowing from the services provided satisfy this requirement.

2.6.2 The meaning of “received by or accrued to”

Receipt and accrual are the two ways in which an amount may be included in “gross income”. The words “received by” and “accrued to” are not defined in the Act¹⁰¹, therefore case law will be considered. The courts interpret the terms based on the circumstances of each case and the available facts before them.¹⁰²

2.6.2.1 “Received by”

In *Geldenhuis v CIR*, the court had to decide whether the proceeds from the sale of a flock of sheep by a taxpayer who held a *usufructuary* interest in the flock could be included in her “gross income”.¹⁰³ The court held that “received by” means the taxpayer received the amount on his or her own behalf and for his or her own benefit.¹⁰⁴ In this case the taxpayer had not received the proceeds on her own behalf or for her own benefit, but for the benefit of the heirs and therefore the proceeds belonged to the heirs and did not form part of her “gross income”.¹⁰⁵

⁹⁶ 1926 CPD 203, 2 SATC 16

⁹⁷ 1945 AD 301 (318).

⁹⁸ *Lace Proprietary Mines Ltd v CIR* 1938 AD.

⁹⁹ 2007 (6) SA 601.

¹⁰⁰ *Ibid.*

¹⁰¹ Act 58 of 1962.

¹⁰² *Haupt Notes on South African Income Tax* 10.

¹⁰³ 14 SATC 419.

¹⁰⁴ *Ibid.*

¹⁰⁵ *Ibid.*

It follows that money is viewed as “received” when the taxpayer accepts or receives it on his own behalf and for his own benefit.

2.6.2.2 “Accrued to”

It was decided in *Lategan*¹⁰⁶ that “accrual” meant becoming “entitled to” an amount, irrespective of the fact that the amount may only be due and payable in a later year of assessment. After years of debate and deliberations about the meaning of the word “accrual”, *CIR v People's Stores (Walvis Bay) (Pty) Ltd*¹⁰⁷ confirmed the *Lategan* decision that an amount accrues to a taxpayer when he becomes entitled to it. In *Ochberg v CIR*¹⁰⁸ and *Mooi v CIR*¹⁰⁹ the courts held that the taxpayer should be unconditionally entitled to the amount; if there is a condition attached to the right of claim there can be no accrual until the condition is satisfied. Hence, it follows that an amount is viewed as “accrued” when a taxpayer becomes unconditionally entitled to it.

2.6.2.2.1 Receipts from Uber services provided in South Africa

From the discussion above it has been established that “received by” means that the taxpayer must have received the amount on his or her own behalf and for his or her own benefit. Where the driver owns or rents the car being used to provide the *Uber* service, it is safe to assume that the income the driver is receiving is on his own behalf and for his own benefit. The amount received will be included in the driver’s “gross income”. Where a third party was driving the *Uber* vehicle on behalf of the *Uber* vehicle owner, the payments received from the rides will be received by the vehicle owner on his own behalf and for his own benefit. The amount received will be included in the vehicle owner’s “gross income”.

The commission that the *Uber* company charges the *Uber* drivers constitutes an amount that the company “receives” on its own behalf and benefit. Since the *Uber* company becomes unconditionally entitled to the amount, it would have “accrued” it as required by the Income Tax Act. In terms of Article 7 of the DTA between America and South Africa this amount is taxable in South Africa. This means that the amount received will be included in *Uber*’s “gross income”, provided all the other elements of the “gross income” definition are met.

¹⁰⁶ 1926 CPD 203, 2 SATC 16.

¹⁰⁷ 1990 (2) SA 352 (A), 52 SATC 9.

¹⁰⁸ 1933 CPD 256, 6 SATC 1.

¹⁰⁹ 34 SATC 1.

2.6.2.2.2 Receipts from Airbnb services provided in South Africa

SARS states that the rental of residential accommodation includes holiday homes, bed-and-breakfast establishments, guesthouses, sub-renting part of your house, dwelling houses and other similar residential dwellings.¹¹⁰ Income earned by individuals from letting out their property on the *Airbnb* website or “app” qualifies as rental income.

If the *Airbnb* host is the owner or lessee of the property, the income that accrues will be for his or her own behalf and benefit as required by the definition of “gross income”. This amount will be included in owner’s or lessee’s “gross income”. If a rental agency acts on behalf of the *Airbnb* owner, the payments that accrue from letting out the homes will be taxed in the hands of the *Airbnb* owner, since the amounts accrue on his own behalf and for his own benefit. This rental income “received or accrued” by the *Airbnb* owner from the agent should be included in the owner’s “gross income”.

The commission that the *Airbnb* company receives from its website or “app” constitutes an amount “received” by the company on its own behalf and for its own benefit. However, in terms of Article 7 of the DTA, this commission cannot be included in the taxpayer’s South African “gross income” as discussed above. This is because DTAs take precedence over the Income Tax Act.¹¹¹

2.6.3 The “receipt or accrual” must not be capital in nature

The final component of the definition of “gross income” excludes receipts or accruals of a capital nature. Capital receipts will not be included in “gross income”, unless a special inclusion requires a specific type of capital receipt to be included in “gross income”. The Act does not define the term “capital” so guidance on the meaning is drawn from case law. To ascertain the nature of a receipt, the court will decide each case on its own merits. The burden of proving that an amount is of a capital nature rests upon the taxpayer, because an amount may be capital in the hands of one taxpayer but revenue in the hands of another.¹¹² Various tests and guidelines have been formulated by our courts to help distinguish whether receipts and accruals are capital or revenue in nature. The most important guideline established by the courts is the involvement of the taxpayer in a scheme of profit making. In *C:SARS v Capstone*

¹¹⁰ SARS “Tax on Rental Income” 2016. Available: <http://www.sars.gov.za/TaxTypes/PIT/Pages/Tax-on-rental-income.aspx> (Accessed 2 August 2017).

¹¹¹ PJ Hattingh *Elimination of International Double Taxation* in De Koker A and E Brincker (eds) *Silke on International Tax* (2010) paragraph 36.14.

¹¹² Section 102 of the Tax Administration Act 28 of 2011.

556 (Pty) Ltd¹¹³ the court, referring to *Samril Investments (Pty) Ltd v C:SARS*,¹¹⁴ commented on what constitutes a scheme of profit making. The court held that a mere intention to profit is not conclusive, there must be an operation of business in carrying out a scheme for profit making for a receipt to be income.¹¹⁵ In relation to *Uber* drivers and *Airbnb* hosts the main reason they registered on the *Uber* and *Airbnb* platforms was so that they could make a profit by carrying on a business. The profit is therefore revenue in nature. In relation to the *Uber* company, its main reason for developing the “app” was to receive commission or fees in carrying on its business. This income is therefore revenue in nature.

2.7 Conclusion

Based on the factors discussed above, it is submitted that the amounts “received by” or “accruing to” the *Uber* vehicle owner, *Airbnb* owner and *Uber* (the company) have satisfied all the elements of the “gross income” definition and amounts each received or that accrued to each of them will be included in their “gross income”.

This chapter discussed the concepts of residence and source, focusing on whether *Uber* and *Airbnb* have a “permanent establishment” in South Africa. It was demonstrated that, whilst *Uber* has “permanent establishment” in South Africa, *Airbnb* does not. As a result, South Africa has exclusive taxing rights on proceeds made by *Uber* from its “permanent establishment”, whereas for *Airbnb*, America has the exclusive taxing rights in accordance with the DTA between South Africa and America. The chapter further dealt with the “gross income” definition, focusing on what constitutes “receipts” for purposes of “gross income” when taxing proceeds from the “sharing economy”. It was established that proceeds derived by *Uber*, *Uber* drivers and *Airbnb* hosts satisfy all the requirements of “gross income” and the amounts each of them receives or accrues will be included in their “gross income”.

The next chapter will investigate the deductibility of expenses incurred by *Uber*, *Uber* vehicle owners and *Airbnb* owners.

¹¹³ 2006 ZASCA 2.

¹¹⁴ 2002 (65) SATC 1.

¹¹⁵ *Ibid.*

CHAPTER 3: THE GENERAL DEDUCTION FORMULA AND THE “SHARING ECONOMY”

3.1 Introduction

The preceding chapter established that South Africa has taxing rights on the business profits made by *Uber*, whereas the profits made by *Airbnb* will be taxed in America in accordance with the provisions of the DTA between South Africa and America. The deduction of expenses that *Airbnb* may incur will therefore not form part of this discussion. The present chapter discusses the deductibility of expenses incurred by *Uber*, *Uber* drivers and *Airbnb* hosts. In doing so, the second part of the first research goal is addressed: to analyse the deductibility of expenses incurred by the “sharing economy” participants. Furthermore, the chapter analyses whether workers in the “sharing economy” should be classified as employees or independent contractors and how falling into either category will affect the deductibility of their expenses, thus addressing the second goal of the research: an analysis of how South Africa may classify its “sharing economy” workers for tax purposes. The chapter concludes by briefly outlining the duty of the taxpayers to register for tax, how and when they may be required to pay provisional tax and the period for which they must retain records.

3.2 Deductions

Having established the “gross income” of *Uber*, the *Uber* vehicle owner and the *Airbnb* owner, as there are no applicable exemptions, their “gross income” will constitute “income” as defined in the Act¹¹⁶. The next step in the calculation of taxable income is to deduct from the “income”, all amounts allowed as tax deductions in terms of the Act.¹¹⁷ Most of these deductions are granted in terms of the “general deduction formula” which is contained in the preamble to section 11 and section 11(a), read with sections 23(f) and 23(g) of the Act.¹¹⁸ In the absence of a specific deduction allowed under the Act, the general deduction formula will apply.

The preamble to and section 11(a) provides as follows:

For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deduction from the income of such person so derived –

¹¹⁶ Act 58 of 1962.

¹¹⁷ Haupt *Notes on South African Income Tax* 111.

¹¹⁸ Act 58 of 1962.

- (a) expenditure and losses actually incurred in the production of income, provided such expenditure and losses are not of a capital nature...

As is evident from the preamble to section 11, taxpayers may not claim a deduction in terms of section 11 unless they are “carrying on a trade”. The term “trade” is defined in section 1 as including “...every profession, trade, business, employment, calling, occupation or venture, including the letting of any property . . .”¹¹⁹. From this definition, the activities of “letting of property” by an *Airbnb* host and providing ride services by an *Uber* vehicle owner would fall within the definition of “trade”, but the question is whether their activities constitute “carrying on trade”. This is discussed below.

3.2.1 Can the activities performed in the “sharing economy” be defined as “carrying on a trade”?

Whether the taxpayer is “carrying on a trade” is a question of law that must be decided after a fact-based enquiry. “Carrying on a trade” usually requires that the taxpayer must have the intention to make a profit¹²⁰, but this is not decisive. In terms of the Income Tax Act, profit-making is not a requirement in determining whether the taxpayer is “carrying on a trade”. The court in *De Beers Holdings (Pty) Ltd v CIR* made it clear that absence of a profit does not necessarily mean that the taxpayer’s transactions do not constitute the “carrying on of a trade”.¹²¹ However, in circumstances where there is no reasonable expectation of a profit, this indicates that the presence of profit is a positive indicator that the taxpayer is “carrying on a trade”.

For *Uber*, the main purpose for which it developed the “app” was to receive an income (commission) from service providers using its technology. For *Uber* drivers and *Airbnb* hosts the main purpose for downloading the apps, registering with the website and accepting the ride and accommodation requests is to earn an income. It can be argued that the driver, host and *Uber*’s long-term objective of engaging in the trades is to generate a profit. This intention to make a profit may indicate that they are “carrying on of a trade”. Additionally, *Uber*, the driver’s and the host’s motive to earn an income is likely to be real and based on a reasonable

¹¹⁹ Act 58 of 1962.

¹²⁰ NR Tshikororo *A Critical Analysis of the Concept of Carrying on Trade in the South African Income Tax Act* (LLM, mini-thesis, University of Johannesburg, 2014) 16.

¹²¹ 47 SATC 229.

possibility, as is required by *ITC 1292*.¹²² This indicates that the participants may have the intention to “carry on a trade”.

Whilst the intention to make a profit is a good indication of the existence of a trade, Tshikororo cautions that this is not necessarily a decisive factor.¹²³ Thus, it is necessary to have regard to other elements and examine the all relevant factors.

The activities of a taxpayer are also considered in deciding whether they resemble a taxpayer who is “carrying on a trade”. The court in *ITC 1467*¹²⁴ held that ““carrying on a trade’ involves some active steps, something more than watching over existing investments which are not intended or expected to be income-producing during the year of assessment in question.” Applying this factor to the activities of the service providers in the “sharing economy” indicates that most of them are actively involved personally in providing their services. This is because the “sharing economy” business model is centred on the peer-to-peer exchange of goods or services on a personal level. For example, an *Uber* driver personally drives the customers to their intended destination and a host provides the letting service. It can be accepted that participants in the “sharing economy” play an active role in providing their services. This active role may indicate that the service providers are “carrying on a trade” (*ITC 1467*¹²⁵ – trading presupposes active steps).

Continuity of the transactions is another element that can be looked at to determine whether a taxpayer is “carrying on a trade”.¹²⁶ In *CSARS v Van Blerk*, the court held that the sale of sand by the taxpayer on a regular basis was an indication that the taxpayer was conducting a trade pursuant to a scheme for profit-making.¹²⁷ An analysis of the activities carried on by the drivers, hosts and *Uber* indicates that most are involved in the same repetitive business operations. This may indicate that the taxpayers are “carrying on a trade”.

The approach of SARS to the question of when a trade is being carried on is dealt with in Interpretation Note 33.¹²⁸ What can be deduced from the Interpretation Note is that “in South Africa the absence of productive assets has been found to be an indicator of the absence of

¹²² 41 SATC 163.

¹²³ Tshikororo *Concept of Carrying on Trade* 16.

¹²⁴ 52 SATC 141.

¹²⁵ *Ibid.*

¹²⁶ *Ibid.*

¹²⁷ 2000 (2) SA 1061 (C) 1021.

¹²⁸ SARS Interpretation Note 33 “Assessed Losses: Companies. The trade and income from trade requirements” (2005) paragraph 4.

trading activity.”¹²⁹ This approach was applied in *ITC 697*, where Price J stated that “if the taxpayer has no asset with which he can trade then he cannot be trading”.¹³⁰ A similar approach was also followed in *C:SARS v Contour Engineering (Pty) Ltd*¹³¹, where the court found that the respondent had no premises, no equipment, no stock, no staff and, save for book debts, no assets. The court held that this is clearly indicative of a company which is not trading. Therefore, it follows that where a taxpayer has no income-producing assets, it is taken as an indicator that there is no “carrying on of a trade”.

Applying this to the *Uber* vehicle owners and *Airbnb* owners, they will be regarded as “carrying on a trade” if an asset fundamental to their trade is in existence, in this case the property or a motor vehicle, without which the envisaged trade income cannot be earned. Additionally, if the *Uber* vehicle owner or the *Airbnb* owner has acquired the operating assets specifically for the type of business they are engaged in, it would be viewed as “carrying on a trade”. An example of this would be an *Airbnb* owner acquiring asserts such as furniture and fittings for the rooms or apartment he or she plans to let out. This view is supported by Tshikororo¹³² who pointed out that a taxpayer will be regarded as “carrying on a trade” when the taxpayer’s property is actively available to produce income.

The cumulative factors above indicate that the activities in the “sharing economy” can be regarded as “carrying on trade” for purposes of the preamble to section 11 of the Act. However, given the “sharing economy” business model, certain host participants may only let their property to others occasionally, it is crucial to discuss what level of activity is necessary for a taxpayer to be regarded as “carrying on trade”. This aspect is discussed in sub-section 3.3.6 below, in relation to section 23(g).

The next step is to determine whether the activities of *Uber* and the respective service providers meet all the requirements of the general deduction formula in order for them to claim the deductions.

3.3 Other requirements of the general deduction formula

The general deduction formula includes section 11(a), which provides for what may be deducted, and section 23(g), which stipulates what may not be deducted. Section 11(a) is made

¹²⁹ Interpretation Note 33 (2005) 7.

¹³⁰ (1950) 17 SATC 93.

¹³¹ (1999) 61 SATC 447.

¹³² Tshikororo *Concept of Carrying on Trade* 30.

up of various elements, all which must be satisfied before the deduction can be claimed.¹³³ Failure to meet any one of the requirements results in disallowing part of or the whole deduction claimed.¹³⁴ Elements of the general deduction formula are discussed below.

3.3.1 Expenditure and losses

Section 11(a) refers to both “expenditure and losses”.¹³⁵ In *ITC 1783* the court stated that the word “expenditure” had to be given its ordinary meaning, which is the spending of money or its equivalent.¹³⁶ In *CSARS v Labat* the court had to grapple with the question of whether the issue by a company of its own shares in consideration for a trade mark constituted “expenditure actually incurred” by the company.¹³⁷ The Commissioner contended that no expenditure had actually been incurred by the taxpayer in acquiring the trade mark as required by the Act. The court held that “expenditure” refers to the action of spending funds; disbursement or consumption; and hence the amount of money spent.¹³⁸ The court found that in the context of the Act “expenditure” would also include the disbursement of other assets with a monetary value. The case stated that “expenditure” requires a diminution (even if only temporary) or at the very least movement of assets of the person who expends.¹³⁹ In *Joffe and Co Ltd v CIR* the court stated that in relation to trading operations “loss” usually refers to an involuntary deprivation.¹⁴⁰

In relation to “expenditure or losses” incurred by participants in the “sharing economy”, it is submitted that, based on the meaning of the words, money expended, or losses incurred from such activities can clearly be regarded as complying with either of the meanings.

3.3.2 Actually incurred

Expenditure must be “actually incurred” for a taxpayer to claim a deduction in terms of section 11(a). In *Caltex Oil (SA) Ltd v CIR*¹⁴¹, the court held that expenditure “actually incurred” means all expenditure for which liability has been incurred during the year, whether or not the liability

¹³³ Act 58 of 1962.

¹³⁴ *Tshikororo Concept of Carrying on Trade 30*.

¹³⁵ Act 58 of 1962.

¹³⁶ 66 SATC 373.

¹³⁷ (669/10) (2011) ZASCA 157.

¹³⁸ *Ibid.*

¹³⁹ *Ibid.*

¹⁴⁰ (1946) 13 SATC 354.

¹⁴¹ 37 SATC 1, 1975 (1) SA 665.

has been discharged.¹⁴² *Edgars Stores Ltd v CIR* added that there must be an unconditional legal obligation during the year of assessment for the expense to be regarded as “actually incurred”.¹⁴³

It follows that expenses from “sharing economy” activities will be “actually incurred” if they result in an unconditional legal obligation to pay the amount during the year of assessment. For example, costs of maintaining the motor vehicle by an *Uber* driver when he changes oil or replaces brake linings are costs that are “actually incurred” because they place an obligation on the driver to pay once the maintenance has been carried out. The same is true for an *Airbnb* host, who would incur municipal costs, cleaning and other maintenance costs and *Uber* in respect of salaries, rent of premises and running costs; if an unconditional legal obligation to pay the amount exists, the expenses are regarded “actually incurred”.

3.3.3 During the year of assessment

Section 11(a) does not specifically provide that the expenditure incurred in one year of assessment must be claimed in that year of assessment; however, the courts have held that deductible expenditure is restricted to that incurred in the year of assessment.¹⁴⁴ The expenses incurred by *Uber*, the *Uber* vehicle owner and the *Airbnb* owner can only be claimed in the year they are “actually incurred”, provided all the other requirements of section 11(a) have been met.

3.3.4 In the production of income

For a taxpayer to successfully claim a deduction, the expenditure must be incurred “in the production of income”.¹⁴⁵ “This element requires a link between the act giving rise to the expenditure and the earning of income”.¹⁴⁶ In the *Port Elizabeth Electric Tramway Co Ltd v CIR*¹⁴⁷, the court laid down the test for determining whether an expense has been incurred in the production of income. The test is in the form of two questions, namely: (1) was the act, to which the expenditure is attached, performed in the production of income? (2) how closely is the expenditure linked to the production of income?¹⁴⁸

¹⁴² *Ibid.*

¹⁴³ 1988 (3) SA 876 (A).

¹⁴⁴ *Stiglingh et al Silke* 146.

¹⁴⁵ Section 11(a) of the Income Tax Act 58 of 1962.

¹⁴⁶ Goldswain *Master of Commerce (Taxation): Module 4* (2016) 30.

¹⁴⁷ 1936 CPD 241, 8 SATC 13.

¹⁴⁸ 1936 CPD (241) 245.

To satisfy this element participants in the “sharing economy” must show that there is a link between the expenditure incurred and the trade that is being carried on. For example, an *Airbnb* host must show that the internet costs, DSTV subscriptions and electricity charges are expenses that are closely connected with the business and are necessary for its efficient performance. The same is true for the *Uber* driver, who must prove that the costs of vehicle registration, car washes, the fuel bill, or the cost of refreshments for his customers, were a necessary concomitant of the business.¹⁴⁹ In relation to *Uber*, it would have to show that the rental expenses for their offices, businesses insurance, wages and salaries and other miscellaneous expenses are closely connected to the business and necessary for its performance. If it is proved that a link exists between what gave rise to the expenditure and the earning of the income, *Uber* and the respective service providers would have satisfied this requirement.

3.3.5 Not of a capital nature

Capital expenses are not deductible in terms of section 11(a) even if they are incurred in the production of income.¹⁵⁰ The Act does not define what is meant by “capital”, hence reliance is placed on the court’s interpretation of the word. There are several case-derived tests that assist in determining whether an expense is capital in nature. Some of the tests are discussed below.

The true nature of the transaction is a test used by our courts to determine whether an expense is of a capital nature or not. In *New State Areas Ltd v CIR*, the court held that where a person incurs an expense to acquire an asset for his or her business, this is a strong indication that the cost of such a purchase is capital in nature and may therefore not be deducted in terms of section 11(a).¹⁵¹ An example of this type of purchase for an *Uber* driver would be the cost of buying a motor vehicle with the intention of using it to produce income; it forms part of the income-producing structure. The cost would not be deductible under section 11(a) of the Act,¹⁵² although a wear and tear allowance could be claimed in terms of section 11(e). Where a driver rents the motor vehicle he uses for trade purposes, the rental costs would be expenses required for the day-to-day functioning of the driver’s business. These rental expenses would be deductible in terms of section 11(a), as they are will not be capital in nature, since they do not form part of the driver’s income-producing structure. Where the driver acquired the car under a financial lease, he or she acquires ownership of the motor vehicle. The driver would have

¹⁴⁹ The principle of “necessary concomitant” was established in *Joffe & Co (Pty) Ltd v CIR* (1946 AD).

¹⁵⁰ Act 58 of 1962.

¹⁵¹ 14 SATC 155.

¹⁵² Act 58 of 1962.

acquired the motor vehicle with the intention of using it to produce income, therefore the vehicle will form part of the driver's income-producing structure. The cost of this acquisition would not be deductible under section 11(a), as the expense will be capital in nature.

The enduring benefit test is another test used to determine the capital or revenue nature of an expense. The test was established in the English case, *British Insulated and Helsby Cables Ltd v Atherton*¹⁵³, where the court held that "when an expenditure is made not only once and for all, but with the view to bring into existence an asset or advantage for the enduring benefit of a trade, ...there is a very good reason... for treating such an expenditure as properly attributable not to revenue but to capital". In terms of the test, expenses incurred by an *Airbnb* owner to acquire property (a fixed capital asset) for business use are of a capital nature because the asset will endure for a substantial period. This means that the expense will not be deductible in terms of section 11(a).

Another test established by the courts is whether a sufficient link exists between an expense and the income-earning operations of a taxpayer. *SIR v Cadac Engineering Works (Pty) Ltd* held that there must be a sufficiently close link between the expenditure and the taxpayer's income-earning operations in order to warrant the conclusion that it formed part of the cost of performing the taxpayer's income-earning operations, rather than the cost of expanding his income-producing structure.¹⁵⁴ "If the expenditure is more closely related to the taxpayer's income-earning structure than to his income-earning operations, it is capital expenditure."

The payment of salaries to staff by an *Airbnb* host or *Uber* will be money closely linked to the income-earning operations of the taxpayer and would therefore not be of a capital nature. This type of expenditure would be deductible under section 11(a) of the Act.¹⁵⁵ Expenses incurred by the drivers and hosts when they use the "apps", in the form of mobile data, are costs closely linked to the income-earning operations of the taxpayers. This is because the mobile data costs do not create an asset or improve or add anything to the driver's or host's existing assets. The mobile data costs will be incurred on a regular basis and they do not create an enduring benefit. This type of expenditure is revenue in nature and it would be deductible under section 11(a) of the Act.

¹⁵³ 1926 AC.

¹⁵⁴ 1965 (2) SA 511 (A).

¹⁵⁵ Act 58 of 1962.

If it is proved that the expenses are not of a capital nature; *Uber*, the *Uber* vehicle owner and the *Airbnb* owner would have satisfied this requirement.

3.3.6 To the extent “not laid out or expended for the purpose of trade”

Section 11(a) is read together with section 23(g) and 23(f) of the Act to determine whether the expense will be deductible.¹⁵⁶ Section 23(g) prohibits the deduction of “any monies, claimed as a deduction from income derived from trade, to the extent to which such monies were not laid out or expended for the purposes of trade”, whilst section 23(f) effectively prevents a deduction of expenditure in respect of amounts received or accrued which do not constitute “income” as defined.¹⁵⁷ The words “expended for the purpose of trade” in section 23(g) were interpreted to mean “for the purpose of enabling a person to carry on and earn profits in the trade”.¹⁵⁸

Several cases have dealt with the deductibility of expenses not laid out or expended for the purposes of trade (as the prohibition previously applied). In *ITC 881*¹⁵⁹, the taxpayer and his family occupied a house that was acquired by a company that the taxpayer had formed. The company claimed deductions for certain expenses, which the Commissioner refused to allow. The court placed the taxpayer in the same position as any person who purchases a house for personal occupation and held that the expenses could not be said to have been expended for purposes of trade, therefore, they could not be claimed as deductions in terms of section 12(g) [now section 23(g)] of the Act.¹⁶⁰ In *Reef Estates Ltd v CIR*¹⁶¹, the taxpayer sought to deduct expenses on property rates for a property that it held but had not brought into use. The court held that in terms of section 12(g) [now section 23(g)] the expenditure had not been incurred for the purpose of trade. The expense was therefore not deductible.¹⁶²

In *ITC 1385*, the taxpayer purchased a dwelling in Pretoria in February 1982 and took occupation in May 1982.¹⁶³ After failing to obtain a tenant for the dwelling, the taxpayer concluded an agreement with an estate agent who undertook to pay him a rental for the dwelling. On 1 July 1983 the appellant took personal occupation of the dwelling and moved in

¹⁵⁶ Act 58 of 1962.

¹⁵⁷ *Ibid.*

¹⁵⁸ *Tshikororo Concept of Carrying on Trade* 28.

¹⁵⁹ 23 SATC 237.

¹⁶⁰ *Ibid.*

¹⁶¹ 1954 (2) SA 593 (T), 19 SATC 153.

¹⁶² *Ibid.*

¹⁶³ 46 SATC 111.

with his family. The taxpayer sought to deduct the amount of R1 836,74 being the difference between the sums of R4 830,96 rental received during the tax year in issue and R6 667,70 expended on the dwelling that year. The Commissioner submitted that the expenditure in issue could not qualify as having been expended for purposes of trade.¹⁶⁴ Evidence before the court showed that the appellant purchased the dwelling with mixed motives, namely as his future residence to be leased in the meantime. The court held that the expenditure incurred has not been laid out for purposes of trade.¹⁶⁵

In addition to the provisions of section 23(g), section 23(a) and (b) prohibit the taxpayer from deducting certain expenditure. Section 23(a) prohibits as a deduction, costs incurred in the maintenance of any taxpayer, his family or establishment.¹⁶⁶ Section 23(b) provides that domestic or private expenditure that includes the rent, cost of repairs, or expenditure in connection with any premises not occupied for purposes of trade, or of any dwelling-house or domestic premises except in respect of such part as may be occupied for the purposes of trade, will not be allowed as a deduction.¹⁶⁷ The effect of section 23(b) is that if an *Airbnb* host uses part of his or her house for the purposes of trade, expenditure relating to that part occupied for trade purposes may qualify for a deduction.¹⁶⁸ The part of the dwelling will be deemed to be occupied for purposes of trade if it is specifically equipped for purposes of the trade and if it is regularly and exclusively used for that purpose.

Because the “sharing economy” business model is centred on the idea of sharing resources, it is very common for assets to be used for both business and personal use, sometimes predominantly for personal use. Thus, apportionment of expenses becomes relevant. The Income Tax Act does not expressly provide for the apportionment of expenditure that has been incurred to produce both taxable and exempt income. However, many authors agree that the amendment of section 23(g) after *Solaglass Finance Company (Pty) Ltd v CIR*¹⁶⁹ led to the official sanctioning of apportionment by the Act.¹⁷⁰ Guidance on how to apportion has been provided by the courts.¹⁷¹ De Koker and Williams contend that apportionment is only appropriate where a single, indivisible expense appears to have been incurred for a dual

¹⁶⁴ *Ibid.*

¹⁶⁵ *Ibid.*

¹⁶⁶ Act 58 of 1962.

¹⁶⁷ *Ibid.*

¹⁶⁸ *Ibid.*

¹⁶⁹ 1991 (2) SA 257 AD.

¹⁷⁰ Act 58 of 1962.

¹⁷¹ RC Williams *Income Tax Act in South Africa: Cases and Materials* 3rd ed 2009.

purpose.¹⁷² This is because separately identifiable amounts incurred for different purposes do not require to be apportioned, as their deductibility can be judged on their individual merits.¹⁷³

In *CIR v Nemojim*, the taxpayer company had incurred costs for a dual purpose, to acquire shares in a company, declare the reserves as exempt dividends and then sell the shares, in that way generating a loss to be set off against its other income.¹⁷⁴ The issue before the court was whether the total cost of the shares was deductible in terms of section 11(a), or whether part of the cost was not deductible by virtue of section 23(f), which does not permit a deduction for expenditure incurred in respect of amounts received or accrued which do not constitute “income” as defined.¹⁷⁵ The court held that the expenditure in issue failed to satisfy the requirements of section 11(a) and section 23(f) of the Act. The court concluded that it was appropriate to apportion the expenditure between the purposes, thus it only allowed a portion of the cost of shares to be deducted.

In *MTN (Pty) Ltd v C:SARS* the taxpayer sought to deduct the expenditure incurred in respect of the auditing and training fees.¹⁷⁶ SARS disallowed the training fees entirely and allowed between 2% and 6% of the audit fees to be deducted, based on the ratio of the taxpayer’s interest income to its exempt dividend income. The taxpayer objected but SARS disallowed the objection and the taxpayer then appealed.¹⁷⁷ The Supreme Court of Appeal, in *C:SARS v Mobile Telephone Networks Holdings (Pty) Ltd*¹⁷⁸, confirmed that the audit fees had been incurred for a dual purpose. The court concluded that it was appropriate to apportion the expenditure between the two purposes. A 10% deduction of the audit fees was held to be fair and reasonable for all parties concerned.¹⁷⁹ In relation to the training fees, the court held that due to the inadequacy of the evidence adduced by the taxpayer’s general manager, it was impossible to determine if the fees had been incurred in the production of income or whether the fees were capital or revenue in nature. The court held that the Commissioner was correct in disallowing the training fee in its entirety.

¹⁷² A De Koker and RC Williams *Silke on South Africa Income Tax* (Online) 2017.

¹⁷³ *SIR v Guardian Assurance Holdings (SA) Ltd* (1976) 38 SATC 111.

¹⁷⁴ (1983) 45 SATC 241.

¹⁷⁵ *Ibid.*

¹⁷⁶ (2011) 73 SATC 315.

¹⁷⁷ *Ibid.*

¹⁷⁸ (966/12) [2014] ZASCA 4.

¹⁷⁹ D du Ploy *An analysis of the Apportionment of Damages Act 34 of 1956 in South African Law* (LLM thesis, University of Pretoria, 2015).

In relation to *Airbnb*, where the host uses his or her property as a bed-and-breakfast establishment, for example, and for personal occupation for the family, he or she must apportion the expenses he or she incurs. The courts use the number of days the property is let out or the floor area let out to apportion the expenses.¹⁸⁰ Applying the former method, the owner of the property will be entitled to claim a percentage of these expenses equal to the number of days the property was rented out, divided by 365 days in the tax year.¹⁸¹ With the floor area method the owner would measure the area let out and express it as a percentage of the total area of the house, and then apply that let out percentage to the expense incurred.¹⁸² Both apportionments may apply where part of a dwelling is let out.

In relation to *Uber*, if the vehicle owner uses the motor vehicle for a dual purpose, he or she must apportion the expenses between whatever relates to the *Uber* business and private use. Assuming all the other section 11(a) requirements are met, only the portion of total motor vehicle expenses relating to business use will be deductible.¹⁸³ Apportionment will be based on the actual kilometres travelled. This would require the driver to maintain a logbook in which he or she keeps track of personal use kilometres and business use kilometres. When maintaining this logbook for travel expenses, the driver must record the kilometres travelled for the different business purposes, including exact details of what the business travel pertains to.¹⁸⁴ In recording these expenses, the following costs must be included: depreciation, fuel, insurance, licences, oil, parking fees, registration, repairs, tyres and toll road levies.¹⁸⁵ The expenses will then be apportioned, based on the kilometres, with the business portion being deductible.¹⁸⁶

Uber, *Uber* drivers and *Airbnb* hosts will generally only be allowed to deduct expenditure or a loss, if it was incurred after the commencement of a trade. However, section 11A of the Act allows for a deduction for qualifying expenditure and losses incurred before the

¹⁸⁰ *Ibid.*

¹⁸¹ M Fisher-French "Beware the potential tax pitfalls of earnings through Airbnb" 2017. Available: <https://mayaonmoney.co.za/2017/12/beware-potential-tax-pitfalls-earnings-airbnb/> (Accessed 12 January 2018).

¹⁸² *Ibid.*

¹⁸³ Anonymous "Why Sole Traders must submit logbooks to claim travel expenses" 2016. ICBA. Available: <https://www.icba.org.za/betty-bookkeeper-explains-why-sole-proprietors-must-submit-logbooks-to-claim-travel-expenses-december-2016> (Accessed 7 August 2017).

¹⁸⁴ Anonymous "Must an independent contractor keep a travel logbook to get a deduction for travel expenses?" 2015. SAIT. Available: <http://www.thesait.org.za/news/219454/Must-an-independent-contractor-keep-a-travel-logbook-to-get-a-deduction-for-travel-expenses-htm> (Accessed 7 August 2017).

¹⁸⁵ *Ibid.*

¹⁸⁶ *Ibid.*

commencement of that trade, once a trade is carried on.¹⁸⁷ A pre-trade expense qualifies as a deduction against the income from the trade to which it relates, subject to four requirements in section 11A(1). Firstly, the trade in respect of which the pre-trade expenditure was incurred, must have been commenced by the taxpayer. Secondly, the pre-trade expense must have been incurred before the commencement of and in preparation for carrying on that trade. Thirdly, the pre-trade expense must qualify as a deduction in terms of section 11, had it been incurred after the commencement of trade to which it relates. Fourthly, the pre-trade expense must not have been allowed as a deduction in that year or any previous year of assessment.

If *Uber*, the *Uber* driver or *Airbnb* host meets these requirements, the pre-trade expense will be allowed as a deduction under section 11A(1) in the year of assessment in which the trade to which it relates commences. For *Uber* and an *Airbnb* host, examples of pre-trade expenses they might incur are costs of salaries and wages, staff training, electricity and water, insurance, rates and taxes, telephone costs and other similar costs. For an *Uber* driver pre-trade expenses can include telephone, insurance and other related costs.

Section 102(1)(b) of the Tax Administration Act places the burden of proving that an amount is deductible on the taxpayer.¹⁸⁸ To discharge this onus *Uber*, the *Uber* vehicle owner and the *Airbnb* owner would have to satisfy all the requirements of the general deduction formula. As shown by the cases above, expenditure or loss incurred for a non-trade purpose, will not be deductible in terms of section 11(a), read with sections 23(f) and 23(g) of the Act.¹⁸⁹ Because the business model of the “sharing economy” is centred on sharing resources, where an expense was incurred for a dual purpose the service provider will have to discharge the onus of proving the reasonableness of the method used to apportion the expenses.¹⁹⁰ In this regard, keeping a logbook for the kilometres travelled or records of the actual number of days that the house was in use for trade or providing measurements of the part of the house used for letting, will suffice to discharge the onus.

3.4 Special deductions

Apart from the deductions allowed under the general deduction formula, the Act sets out certain special deductions in section 11(c) to (w).¹⁹¹ “The purpose of the special deductions is to permit

¹⁸⁷ Act 58 of 1962.

¹⁸⁸ Act 28 of 2011.

¹⁸⁹ Act 58 of 1962.

¹⁹⁰ *Ibid.*

¹⁹¹ Act 58 of 1962.

deductions that would not ordinarily be deductible under the general deduction formula, either because they are of a capital nature or because they cannot satisfy the restrictive test that the expenditure must be incurred in the production of income.”¹⁹² Some of the special deductions relating to *Uber*, the *Uber* driver and *Airbnb* host are discussed below.

3.4.1. Repair costs

In terms of section 11(d), repairs will be deductible if they are actually incurred during the year of assessment for purposes of the taxpayer’s trade.¹⁹³ The Act does not define the word “repair”, but in *CIR v African Products Manufacturing Co Ltd*¹⁹⁴ the court held that a repair is restoration by renewal or replacement of a subsidiary part of the whole. In order for an asset to be repaired, there must be damage or deterioration to a part of the original asset or structure and the intention of the taxpayer must be to restore the asset or structure to its original condition.¹⁹⁵ If the expenses incurred do not prolong the useful life of an asset or replace the asset, they are deductible as a repair.¹⁹⁶

For an *Uber* driver, repairs would include replacing worn-out car parts, fixing paint scratches, rotating tyres, replacing the car battery and similar costs. In the case of *Airbnb* hosts, repair costs would include replacement of a leaky roof, a cracked foundation, clogged gutters, and similar costs. For the *Uber* establishment, repairs to the business premises would include replacing worn-out carpets, fixing ventilation and air conditioning and other similar costs. Where these repairs are carried out, the related expenses will be “actually incurred” because there will be an obligation on the taxpayer to pay for them. Section 11(d) requires that for repairs to rank as a deduction they must have been carried out on the property occupied or used “for the purpose of trade”.¹⁹⁷ Therefore, where these repairs are incurred for a dual purpose, apportionment becomes necessary.

If *Uber* and the respective service providers incurred the repair costs for purposes of trade or apportioned the costs to deduct part of the cost relating to the business, the repair costs (or the portion) will qualify as a deduction in terms of section 11(d).

¹⁹² Haupt *Notes on South African Income Tax*.

¹⁹³ Act 58 of 1962.

¹⁹⁴ 1944 TPD 248, 13 SATC 164.

¹⁹⁵ *Ibid.*

¹⁹⁶ Anonymous “*Airbnb* General guidance on the taxation of rental income “(2017) 10. Available: <http://assets.airbnb.com/eyguidance/us.pdf> (Accessed 18 July 2017).

¹⁹⁷ Act 58 of 1962.

3.4.2 Wear and tear allowance

Section 11(e) of the Act provides a deduction if the value of the movable capital asset being used for purposes of trade has diminished because of wear and tear.¹⁹⁸ The section does not apply to any asset that is subject to a special depreciation allowance in any section of the Act and this is done to avoid double deductions.¹⁹⁹

An *Uber* vehicle owner or an *Airbnb* host will qualify for the wear and tear allowance if he or she satisfies the Commissioner that he or she is the owner of the asset or acquired the asset under an instalment credit agreement and the asset is being used to carry on the trade. In terms of section 11(e) the *Uber* driver can claim the deduction on the motor vehicle, cellular phone and other assets used for purposes of the trade. For the *Uber* company and *Airbnb* hosts, the assets on which they can claim a deduction include television sets, furniture and fittings, computers and other similar costs. The host and the *Uber* company must make sure that the asset in respect of which the deduction is being claimed is not so integrated into a building or structure or work of a permanent nature that it loses its own separate identity.²⁰⁰

Section 11(e) only allows deductions to the extent that a qualifying asset is used for purposes of trade. Therefore, where the driver or host uses the assets for both business and private use, only the portion of the allowance in respect of the asset used in carrying on the trade will be allowed as a deduction.²⁰¹ The Commissioner will grant the taxpayer a deduction that he regards as just and reasonable as representing the amount by which the value of the asset has diminished during the year because of the wear and tear.²⁰²

In terms of paragraph (vii) of the proviso to section 11(e), where *Uber*, the *Uber* driver or the *Airbnb* host acquired the movable capital asset by way of inheritance, donation or distribution from a connected person, the market value can be used as the “cost”.²⁰³ The taxpayer will have the burden of proof to show what the market value is.²⁰⁴ If the taxpayer acquired the movable asset from a connected person before 1 January 2013, the provisions of the deleted section 23J would still be applicable to them.²⁰⁵ Section 23J limits the amount in respect of which the

¹⁹⁸ Act 58 of 1962.

¹⁹⁹ *Ibid.*

²⁰⁰ Haupt Notes on South African Income Tax 176.

²⁰¹ *Ibid.*

²⁰² Haupt Notes on South African Income Tax 175.

²⁰³ Act 58 of 1962.

²⁰⁴ Interpretation Note 47 (Issue 3)

²⁰⁵ Haupt Notes on South African Income Tax 176.

taxpayer may claim wear and tear. Were *Uber*, the *Uber* vehicle owner or an *Airbnb* host claimed repair costs under section 11(d), this must be taken into account when determining the wear and tear allowance.²⁰⁶

3.5 Other deductions

3.5.1 Capital allowance on residential accommodation

The Income Tax Act provides for capital allowances in respect of immovable property, depending on the use of the property.²⁰⁷ A capital allowance allows a taxpayer to deduct a portion of the cost of an asset against income over a certain period of time.²⁰⁸ Section 13sex allows developers, investors or purchasers of residential property to claim a “write-off” of the building or improvement costs they incurred as a tax deduction, provided that they comply with the requirements of the section.²⁰⁹ This allowance is not claimable if an allowance on the residential unit can be claimed under any other section in the Act.²¹⁰

In terms of the section, the taxpayer, who in this context is the *Airbnb* host, may claim an annual allowance of 5% or 10% of the cost of the building, provided he or she meets the requirements of the section.²¹¹ The percentage that the *Airbnb* owner can claim is dependent on whether the residential unit is a residential unit that qualifies for a 5% allowance or a low-cost residential unit that qualifies for a 10% allowance. The allowance is only applicable to the building, not the whole property, therefore a value needs to be assigned to the building.²¹²

To qualify for the deduction, the *Airbnb* owner must have acquired the residential unit, erected the unit or made improvements to it on or after 21 October 2008.²¹³ Secondly, the residential unit or the improvement must be new and unused.²¹⁴ Thirdly, the *Airbnb* host must own the unit, as the allowance cannot be claimed on improvements made to property that the taxpayer

²⁰⁶ Act 58 of 1962.

²⁰⁷ *Ibid.*

²⁰⁸ Anonymous “Tax loopholes for property investors” 2017. *Oneproperty*. Available: <https://oneprop.co.za/tax-loopholes-for-property-investors/> (Accessed 23 October 2017).

²⁰⁹ Act 58 of 1962.

²¹⁰ Section 23B(3) of the Income Tax Act 58 of 1962 provides that where a deduction is granted under a specific provision which imposes a limitation on the amount of the deduction, no portion of the deduction will be allowed under the general rules (for example under section 11(a)).

²¹¹ *Ibid.*

²¹² J Maree “Section 13sex example” 2015. Available: http://jadepm.co.za/file/ms_website/w5/file/repository/Section_13_sex_example.pdf (Accessed 23 October 2017).

²¹³ *Ibid.*

²¹⁴ Section 13sex(1).

occupies as a tenant. Fourthly, the section requires that the residential unit or the improvement must be used by the taxpayer solely for the purposes of a trade that he or she carries on. Additionally, the residential unit must be situated in South Africa.²¹⁵ Lastly, the *Airbnb* host must own at least five residential units in South Africa (they need not be in the same place), which must be used for the purposes of carrying on trade by the taxpayer.²¹⁶

The “sharing economy” is based on the concept of sharing idle resources and promoting micro-entrepreneurship by encouraging the use or trading of the resources with those who want or need them in return for a financial value. Therefore, whilst some *Airbnb* hosts let out an entire property, most hosts let out free rooms or even sleeping spots in their living rooms, and therefore it is unlikely that they will be able to satisfy the requirements that:

- they own and let at least five residential units in South Africa; and
- the residential unit or the improvement is used solely for the purposes of a trade that he or she carries on.

Failure to satisfy all the requirements means that section 13*sex* will not be applicable to the host.

3.5.2 Insurance

Insurance premiums in respect of loss of or damage to assets have generally been permitted as deductions under section 11(a) of the Income Tax Act.²¹⁷ This is because premiums are revenue in nature since they are recurring expenses and closely linked to the taxpayer’s income-earning operations.²¹⁸ Premiums in respect to the insurance of the *Uber* establishment, the *Uber* vehicle or *Airbnb* host’s property against loss or damage to the assets is therefore, deductible. However, this is only to the extent that the expense was incurred for the purposes of trade. Due to the nature of the “sharing economy” business model, the insurance premiums paid by the *Uber* driver or *Airbnb* host are may be incurred for a mixed purpose and therefore apportionment of the expenditure becomes necessary.

²¹⁵ Section 13*sex* (1)(b).

²¹⁶ Section 13*sex*(1)(c).

²¹⁷ Act 58 of 1962.

²¹⁸ J Wessels *The Tax Implications of Non-resident Sportspersons performing and Earning an income in South Africa* (MCom in Taxation, mini-thesis, Rhodes University, 2007) 34.

3.5.3 Assessed losses

Section 20(2) of the Act defines an assessed loss as the amount by which the deductions exceed income in respect of which these deductions are admissible.²¹⁹ Section 20 of the Act allows a taxpayer to set-off against the income derived by him from carrying on a trade, the balance of assessed loss brought forward from the previous year of assessment that has been carried forward from the preceding year of assessment.²²⁰ Section 20 has been made subject to the provisions of section 20A of the Act²²¹, which provides that the assessed loss incurred by a natural person in the carrying on of certain trades may not be set-off against the income from his or her other sources under certain circumstances. If the loss is “ring-fenced” in terms of section 20A, it can only be set-off against the income derived from the trade concerned. Since an assessed loss is not automatically ring-fenced, a determination must be made when considering whether to ring-fence it.²²² This determination is made using the four steps discussed below.

3.5.3.1 Maximum marginal tax rate requirement

In terms of section 20A(2),²²³ the ring-fencing is only applicable to individuals whose taxable income for the year of assessment is equal to or greater than the level of taxable income at which the maximum rate of tax applies (R1 500 000 for 2018). Where the *Uber* driver and *Airbnb* host’s adjusted taxable income falls below the level at which the maximum marginal rate of tax becomes payable, the assessed loss will not be ring-fenced and section 20A is not applicable. Where the vehicle owner or the host reaches the maximum marginal rate, he or she satisfies the pre-requisite to potential ring-fencing and the other steps of section 20A must be applied to determine whether the assessed loss must be ring-fenced.

3.5.3.2 Potential ring-fencing pre-requisites

A taxpayer will be subject to potential ring-fencing if either section 20A(2)(a) or section 20A(2)(b) applies.²²⁴

²¹⁹ Act of 58 of 1962.

²²⁰ Anonymous “When can you utilise an assessed tax loss?” 2010. *ENSAfrica*. Available: <https://www.ensafrica.com/news/when-can-you-utilise-an-assessed-tax-loss?id=90&STitle=tax%20ENSight> (Accessed 24 October 2017).

²²¹ Act 58 of 1962.

²²² Haupt *Notes on South African Income Tax* 305.

²²³ Act 58 of 1962.

²²⁴ *Ibid.*

i) *The “three-out-of-five-years” pre-requisite*

Section 20A(2)(a) states that an assessed loss will be subject to potential ring-fencing if the taxpayer has, during a five-year period ending on the last day of the tax year, incurred an assessed loss in the relevant trade in at least three years of assessment.²²⁵ This section may be applicable to *Uber* drivers because their job of transporting customers to their destinations is not listed as a suspect trade (see below).

If an *Uber* driver who meets the maximum marginal rate requirement incurs assessed losses in the first three years of assessment in which the trade is carried on, he or she will be subject to potential ring-fencing in the third year, since even if profits will be derived in year four and five the requirements of the pre-requisite will have been met.²²⁶ This means that the *Uber* driver’s assessed losses incurred in the current year of assessment may not be set-off against income from another trade he carries on. However, the *Uber* driver can escape this ring-fencing if the “escape clause” provided for in section 20A(3) of the Act applies (see below).²²⁷

ii) *The “suspect trade” pre-requisite*

In terms of section 20A(2)(b), where an assessed loss arises from any one of the eight suspect trades listed it will be subject to potential automatic ring-fencing.²²⁸ The section lists the rental of residential accommodation as a suspected trade, and hence this section could apply to *Airbnb* hosts using the *Airbnb* platform.²²⁹

For the *Airbnb* host’s letting activities to be excluded as a suspect trade and to have his or her assessed loss set-off, he or she must satisfy two requirements in section 20A(2)(b)(iii).²³⁰ The requirements are that at least 80% of the residential accommodation should be used by persons who are not relatives of the taxpayer and this must be for a period of at least six months during the year of assessment. In determining whether the 80% is met, the floor area of the accommodation will be considered. If the host can satisfy these two requirements, the assessed loss will not be ring-fenced, and the taxpayer will be allowed to set-off the loss against income from other trades he or she carries on.

²²⁵ Act 58 of 1962.

²²⁶ SARS: Guide on the Ring-fencing of Assessed Losses Arising from certain trades conducted by individuals (2010) 9.

²²⁷ Act 58 of 1962.

²²⁸ SARS: Guide on the Ring-fencing of Assessed Losses 9.

²²⁹ Act 58 of 1962.

²³⁰ *Ibid.*

Given that the “sharing economy” business model is based on sharing idle resources, the 80% requirement might be difficult for most hosts to satisfy since they only let out part of the house in which they live with their families. Many of the hosts will fail to satisfy this requirement and they will not be allowed to set-off their assessed losses against income from other trades they carry on, unless they can show that there is a reasonable prospect of making a profit within reasonable period.

3.5.3.3 Facts and circumstances test or the “escape clause”

The provisions of section 20A do not apply if the trade carried on by the person constitutes a business in respect of which there is a reasonable prospect of deriving taxable within a reasonable period.²³¹ Therefore, a determination should be made whether there is a reasonable prospect of the taxpayer deriving a taxable income within a reasonable period. To determine this, section 20A(3) provides an objective test that consists of factors which must all be considered.²³² These factors are discussed below.

- *The proportion of gross income derived from a specific activity in relation to the allowable deductions incurred in carrying on the specific trade*

SARS views the claiming of large amounts as deductions, despite deriving a relatively small amount of “gross income” as a negative factor.²³³ For the host’s or driver’s deductions to be viewed favourably they should be small in relation to the “gross income”.

- *The level of activities carried on by the taxpayer or the amount of expenses incurred in respect of advertising, promotion or selling in carrying on the specific trade*

When compared to “traditional” forms of service provision, *Uber* vehicle owners and *Airbnb* hosts do not require the same level of advertising and promotion to produce income. For an *Airbnb* host, registering and posting pictures of the house and room or space that is being let out is sufficient advertising and promotion to show a serious intention to conduct trade. For the *Uber* driver, registering with *Uber* is enough for the taxpayer to generate income as the platform will advertise for him or her.

²³¹ Act 58 of 1962.

²³² *Ibid.*

²³³ Haupt Notes on South African Income Tax 307.

- *The trade must be carried on in a commercial manner, taking into account certain considerations*

The number of full-time employees employed for the purpose of trade will be considered. The “sharing economy” business model is structured in a way that it requires that the services are rendered personally by the taxpayer. Even those service providers who employ people are not likely to employ many people. Therefore, this factor will not be very helpful in assessing if the trade is being carried on in a commercially viable manner.

The commercial setting of the premises where the trade is carried on, is another factor that SARS takes into account. This factor relates to an enquiry into whether the physical location of the suspect trade is likely to promote or hinder the production of income. Where it is found that the location promotes the production of income SARS will view this favourably. An *Uber* driver is unlikely to work from business premises and probably works from home. An *Airbnb* host would also be working from his or her private home. These are not commercial settings and the driver or host would not satisfy this criterion.

The extent of the equipment used exclusively for the purposes of carrying on that trade, is also considered. Therefore, where assets are used exclusively for purposes of the suspect trade, SARS will view this as a favourable factor as compared to when the host or driver uses the asset for mixed purposes.

The time that the person spends at the premises conducting that business will also be taken into account. For example, where the *Uber* driver or host provides the service on a full-time basis, he or she would spend a lot of time and effort in carrying on the trade and this would be regarded as likely to render the trade commercially viable, when compared to a driver or host claiming a deduction in respect of an assessed loss incurred from carrying on trade on a part-time basis.

- *Number of years of assessment in which assessed losses were incurred in carrying on the trade in relation to the total number of years that the taxpayer has conducted the specific trade, taking into account any expected events giving rise to any of the assessed losses.*

Incurring a loss because of circumstances that were beyond the taxpayer’s control will be considered in determining the number of years in which assessed losses have been incurred. For example, if a flood damages a host’s house or if the driver’s car is involved in an accident,

these events will be viewed in a favourable way by SARS in determining if the business has a reasonable prospect of deriving taxable income within a reasonable period.

- *The business plans of the taxpayer as well as any changes thereto, to ensure that taxable income will be derived from carrying on that trade in future*

“The presence of a business plan could be relevant in considering whether the activity has a reasonable prospect of deriving taxable income within a reasonable period.”²³⁴ Favourable consideration is given to taxpayers who have business plans. An *Uber* driver and an *Airbnb* host would be unlikely to have a business plan and would fail to satisfy this requirement.

- *The extent to which assets attributable to the specific trade are used or are available for use by the taxpayer or any relatives for private use*

The driver and the host, must show that the relevant asset is not generally available for personal use, in a business in respect of which an assessed loss has been claimed. This will be viewed in a positive light by SARS. The driver and host may use the assets for their personal purposes and would fail to satisfy this requirement.

If the facts and circumstances referred to above, when considered as a whole, indicate that the taxpayer is conducting a business in respect of which there is a reasonable prospect of deriving a taxable income within a reasonable period, the trade will not be ring-fenced, and the taxpayer will be able deduct the assessed loss from the trade, from income from other trades. If the facts and circumstances show otherwise, then the trade will be ring-fenced in terms of section 20A.

3.5.3.4 “Six-out-of-ten-years” or the catch-all provision

In terms of section 20A(4), the “escape clause” does not apply in respect of suspect trades where the taxpayer has, during a ten-year-period ending on the last day of the tax year, incurred assessed losses in at least six of those years (before utilising the balance of any assessed loss brought forward).²³⁵ This means that in the year of assessment in which the rule applies, the assessed loss will be permanently ring-fenced.²³⁶ Where the host or driver is subject to this provision, their assessed loss must be carried forward and will only be available for set-off against future income from the same trade.²³⁷

²³⁴ SARS: Guide to Ring-Fencing of Assessed Losses 20.

²³⁵ Act 58 of 1962.

²³⁶ Haupt *Notes on South African Income Tax* 308.

²³⁷ *Ibid.*

An *Uber* driver or an *Airbnb* host can therefore claim a deduction of assessed losses provided he or she does not fall within the highest tax bracket for individuals, or although he or she falls within the highest bracket and it is a suspect trade, the trade constitutes a business in respect of which there is a reasonable prospect of deriving a taxable income within a reasonable period.

If the driver or host is issued with an assessment that ring-fences an assessed loss, he or she has the right to object to the assessment if not satisfied with the decision made by SARS.²³⁸ If the objection is disallowed fully or in part, the driver or the host has the right to lodge an appeal against such full or partial disallowance.²³⁹

The discussion above has established that, if participants met all the elements of the general deduction formula, the expense will be deductible in terms of 11(a). Apart from the deductions allowed in terms of section 11(a), it was shown that participants in the “sharing economy” may claim special deductions in terms of section 11(c) to (w). In this regard it was shown that *Uber*, an *Uber* driver and an *Airbnb* host may claim deductions for repairs and wear-and-tear expenses. The discussion also established that certain capital assets (such as the houses or apartments used by the *Airbnb* owner), if they fulfil the requirements listed in the Act, will qualify for capital allowances and can be written off for tax purposes over a period of time. It was also shown that an *Uber* driver or an *Airbnb* host can claim a deduction for assessed losses in terms of section 20, provided the loss is not ring-fenced in terms of section 20A of the Act.²⁴⁰

What follows is an analysis of the status of the workers in the “sharing economy” and how it affects the deductibility of their expenses.

3.6 Worker status and the deductibility or non-deductibility of expenses

The employment status of workers in the “sharing economy” has been a subject of debate, not only in South Africa, but globally. Businesses in the “sharing economy” classify their workers as “independent contractors” to avoid costs that are related with employer-employee relationship. The Act does not define an “independent contractor” and in this regard reference on its meaning is drawn from case law (see below). The Fourth Schedule of the Act defines an “employee” as “any person (other than a company) who receives any remuneration or to whom any remuneration accrues”; and an employer as “any person...who pays or is liable to pay to

²³⁸ SARS: Guide to Ring-Fencing of Assessed Losses 22.

²³⁹ *Ibid.*

²⁴⁰ Act 58 of 1962.

any person any amount by way of remuneration, ...”²⁴¹ The Schedule defines “remuneration” as “any amount of income which is paid or payable to any person by way of any salary, wage, commission ..., whether in cash or otherwise and whether or not in respect of services rendered ...”.²⁴² In relation to *Uber*, it pays its drivers a commission on a weekly basis for services rendered. *Airbnb* pays the hosts a commission as well, 24 hours after a guest’s scheduled check-in-time. It is submitted that the commission earned by the drivers and hosts from rendering their services constitutes “remuneration” as defined in the Fourth Schedule.

The distinction between an “employee” and an “independent contractor” is important as section 23(m) of the Act²⁴³ limits deductions that may be claimed by employees and office holders against their employment income, unless their income is earned mainly in the form of commission. Therefore, an analysis of the status of the workers in the “sharing economy” is relevant as it affects the deductibility of their expenses.

3.6.1 Are “sharing economy” workers “employees” or “independent contractors”?

In July 2017, the Commission for Conciliation, Mediation and Arbitration (CCMA) ruled on the status of seven *Uber* drivers in *Uber South Africa Technological Services (Pty) Ltd v NUPSAW, SATAWU*.²⁴⁴ *Uber* had “deactivated” the drivers from the “app” for a variety of reasons and the drivers referred their unfair dismissal disputes to the CCMA.²⁴⁵ *Uber* objected to the CCMA’s jurisdiction in the unfair dismissal cases, claiming that the drivers were not employees of *Uber* but were independent contractors who had contracted their services to *Uber*. The CCMA ruled that the *Uber* drivers were full-blown employees and not independent contractors.²⁴⁶ *Uber* made it clear that the CCMA’s ruling was only applicable to the seven individuals.²⁴⁷ To date of this thesis, *Uber South Africa Technological Services (Pty) Ltd* is still reviewing this ruling before the Labour Court of South Africa.²⁴⁸

²⁴¹ Section 1 of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁴² *Ibid.*

²⁴³ Act 58 of 1962.

²⁴⁴ [2017] ZACCMA 1.

²⁴⁵ E Mabuza “CCMA says SA’s *Uber* drivers are employees, but *Uber* still disagrees” *Business Day* 25 July 2017. Available: <https://www.businesslive.co.za/bd/companies/transport-and-tourism/2017-07-25-ccma-says-sas-uber-drivers-are-employees-but-uber-still-disagrees/> (Accessed 16 October 2017).

²⁴⁶ [2017] ZACCMA 1.

²⁴⁷ Anonymous “*Uber* clarifies that Labour Ruling in South Africa only applies to seven of its driver partners and not all of them” *IAFRIKAN NEWS* 17 July 2017. Available: <https://www.iafrikkan.com/2017/07/17/uber-clarifies-and-says-that-the-labour-a-ruling-in-south-africa-only-applies-to-7-of-its-driver-partners-and-not-all-of-them/> (Accessed 17 October 2017).

²⁴⁸ *Ibid.*

In the case the CCMA only ruled on the status of the workers from an employment law perspective and there is no indication that the ruling extends to tax. However, this decision is extremely important given it is the first South African case to rule on the status of *Uber* drivers. A discussion on the status of workers in the “sharing economy” is therefore, still relevant. What follows is an analysis of the South African tests for categorising workers as either “employees” or “independent contractors” and these tests will be applied to *Uber* drivers and *Airbnb* hosts.

3.6.1.1 Tests developed by the courts

Drawing a distinction between an “employee” and an “independent contractor” has always been a difficult question in our law. Despite the difficulties, the South African courts have formulated various tests to be applied in drawing this distinction. These tests are discussed below.

a. The control test

The control test was formulated in *Colonial Mutual Life Assurance Society Ltd v Macdonald*, where the court held that “the relationship of master and servant could not exist where there is total absence of the right of supervising and controlling the workman under the contract.”²⁴⁹ In terms of this test, the difference between an employee and an independent contractor is that the employer has no legal right to prescribe the manner in which the independent contractor achieves the desired result.²⁵⁰ On the contrary, in an employer-employee relationship, the employer will exercise a fair amount of control over the activities of the employee, telling him or her what to do, when to do it, and the manner in which the employee must perform the tasks.²⁵¹ “However, with the advent of highly skilled employees who are given a relatively free hand when performing their work, courts no longer insist on *de facto* control, but recognise that a right to control is sufficient.”²⁵²

Applying the test to *Uber* drivers, they are responsible for choosing their hours of work and they may accept, decline or ignore a ride request. However, *Uber* controls the drivers to the extent that they can only transport the customers when requested to do so by *Uber*.²⁵³ The drivers cannot initiate a request, they can only refuse or accept rides, therefore they do not have

²⁴⁹ 1931 AD 412.

²⁵⁰ J Grogan *Workplace Law* 10th Ed (2011) 17.

²⁵¹ AC Basson, MC Christianson, A Dekker, C Garbers, PAK Le Roux, C Mischke and EML Strydom *Essentials of Labour Law* 5th Ed (2009) 26.

²⁵² *Ibid.*

²⁵³ *Ibid.*

complete control over their work. The same is true for an *Airbnb* host. He or she can only refuse or accept the request. In *Uber South Africa Technological Services*, the court maintained that, although there is no physical supervision, control is exercised through technology (that is through the “app”), to the extent that the driver has no say over the fare and is not aware of the destination until the passenger is picked up.²⁵⁴ *Uber* is in control of the whole operation because the driver has minimal knowledge of the passenger’s personal details and is prohibited from further contact in terms of the service agreement.

Uber and *Airbnb* control the way workers perform their tasks by setting standards and performance requirements, such as those contained in the deactivation policies.²⁵⁵ In relation to *Uber*, it supervises the drivers through the GPS system on their smartphone.²⁵⁶ If the driver’s satisfaction ratings fall below 4.6 out of 5 the driver can be effectively dismissed. *Airbnb* also monitors the host’s reviews and it can deactivate the host’s account if he or she has unsatisfactory reviews from customers. *Uber* and *Airbnb* may immediately, without notice, terminate the agreement if the host or driver has materially breached any obligations.

Based on these factors, it is submitted that the companies have sufficient control over the workers, telling them what to do, when to do it and how they must perform their tasks. Hence, the workers may be regarded as “employees” of *Uber* and *Airbnb*.

b. The organisation test

Dissatisfaction with the control test led the courts in *R v AMCA Services*²⁵⁷ to experiment with another test – the organisation test. This test is based on the assumption that being a servant does not rest on submission to orders, but it depends on whether the person is part and parcel of the organisation.²⁵⁸ In *SABC v McKenzie* the court held that “...a person is an employee if he is part and parcel of the organisation..., whereas the work of an independent contractor although done for business, is not integrated into it but is only an accessory to it...”²⁵⁹ By implication, if a person is sufficiently related to the organisation of the employer, that person will be regarded as an employee, even though the employer might exercise little control.²⁶⁰

²⁵⁴ *Ibid.*

²⁵⁵ [2017] ZACCMA 1.

²⁵⁶ *Ibid.*

²⁵⁷ 1959 (4) SA 207.

²⁵⁸ *Ibid.*

²⁵⁹ [1999] 1 BLLR 1 (LAC) 5.

²⁶⁰ Basson *et al Essentials of Labour Law* 18.

Applying this test, without the drivers and the hosts, *Uber* and *Airbnb* would not have any means of satisfying their customers' requests. *Uber South Africa Technological Services* case held that the smartphone "app" is a tool to request and provide rides, but it is the drivers who provide the riders with what they want.²⁶¹ What the customers want are rides and accommodation, not the "app". In this regard the drivers and the hosts are so integrated into the business of the companies and their roles are so central to the companies' operations as to be regarded as forming part and parcel of the companies. The major challenge in applying this test is that it is impossible to know the degree of integration that would be sufficient for the *Uber* driver or the *Airbnb* host to qualify as "employees". It is submitted, however, that the drivers and hosts form part and parcel of the companies, thus they may be regarded as "employees" of the companies.

c. The multiple or dominant impression test

Deficiencies in the control and organisation tests led the court to approach the question of whether a particular relationship is one of employment, by viewing the relationship between the parties as a whole and drawing a conclusion from the entire picture."²⁶² To obtain the dominant impression, the court takes the following factors into account: "the right to supervision, whether the worker provides his or her own tools and equipment, whether the employer has the right to discipline the worker, whether the worker is paid according to a fixed rate or by commission, whether the employee is allowed to work for anyone else, the extent to which the worker depends on the employer in the performance of duties, whether the worker is required to devote a specific time to his work and whether he is obliged to perform the duties personally."²⁶³ The court will weigh up all the relevant factors and then determine whether or not it obtains the dominant impression that the person performing the duties is an "employee" or "independent contractor".²⁶⁴ Accordingly, there is no single factor that decisively indicates the presence or absence of an employment relationship.

Applying the factors of the dominant impression test to *Uber* drivers and *Airbnb* hosts, they are subordinate to the will of the companies in the manner they perform their duties, and this is generally the case for employees. Support for this is found in *SABC v McKenzie*, where the court held that an independent contractor is not under the supervision or control of the

²⁶¹ [2017] ZACCMA 1.

²⁶² *Ibid.*

²⁶³ Basson *et al Essentials of Labour Law* 27.

²⁶⁴ Basson *et al Essentials of Labour Law* 28.

employer, nor is he under any obligation to obey any orders of the employer regarding the manner in which the work is to be performed.²⁶⁵ Another factor is that the drivers and the hosts are solely dependent on *Uber* and *Airbnb* giving them access to the “app” and providing them with the ride or accommodation requests. Without *Uber* and *Airbnb* authorising these requests the drivers and hosts would not be able to perform their duties. This level of dependency on the employer in the performance of the worker’s duties indicates an employer-employee relationship.

Additionally, *Uber* requires the driver to render the services personally and he or she may not out-source the duties to someone else without prior approval by *Uber*. This is generally the case with employees and support for this is found in *Uber South Africa Technological Services (Pty) Ltd case*²⁶⁶, where the court held that workers are “employees” where a principal imposes restrictions on the delegation of duties, whereas with “independent contractors”, it does not really matter who does the work provided the job gets done. Another factor is that *Airbnb* and *Uber* have the right to discipline the workers by “deactivating” their accounts for breach or bad reviews. Other factors are that the drivers and the hosts are required to provide their own tools and equipment, they are paid on a commission basis and are not required to devote a specific time to their work. This is generally the case for independent contractors. It is submitted, however, that all these factors form a dominant impression that the workers are “employees” of the companies and not independent contractors.

Considering all the tests discussed above, it is submitted that the workers in the “sharing economy” may be classified as “employees” because the companies (*Uber* and *Airbnb*) exercise sufficient control over the workers, telling them what to do, when to do it and the way in which they must perform their tasks. In addition, the companies grant the drivers and the hosts a limited, non-exclusive, non-sublicensable, revocable, non-transferable license to use their “app” and website and they also retain the right to terminate the agreement at any time. This demonstrates that, although the companies do not have physical control over the workers, they exercise sufficient control through technology. The workers’ roles in the companies was also found to be of such paramount importance as to be regarded as forming part and parcel of the businesses.

²⁶⁵1999 (1) BLLR 1 (LAC).

²⁶⁶ [2017] ZACCMA 1.

It is submitted that the cumulative effect of these factors is persuasive for a conclusion that the workers are “employees” of *Uber* and *Airbnb* and not independent contractors. This “employee” status may affect the taxpayer’s ability to deduct certain expenses and this is discussed below.

3.6.2 Effects of the “employee” status on the deductibility of expenses

Section 23(m) of the Act states that an “employee” or a holder of office who is remunerated mainly by way of a salary is denied any deduction of expenditure incurred in the course of earning the remuneration and claimed in terms of section 11 of the Act, other than those classes of expenditure specifically listed in section 23(m).²⁶⁷ The prohibition in section 23(m) only applies to expenditure or a loss that relates to remuneration as defined in the Fourth Schedule.²⁶⁸ The discussion above established that the *Uber* drivers and *Airbnb* hosts earn a commission which constitutes “remuneration” as defined in the Fourth Schedule. Therefore, it becomes necessary to examine if the drivers or hosts are prohibited from deducting their expenses in terms of section 23(m).

In relation to commission earners, section 23(m) provides that, if the commission earned by the taxpayer relates to any employment, the deduction of expenditure will only be allowed if the remuneration is mainly derived in the form of commission based on his or her performance.²⁶⁹ In this instance, “mainly” means more than 50% of the monthly total remuneration. It is submitted that, in the case of an *Uber* driver or *Airbnb* host, his or her commission would constitute 100% (thus more than 50%) of the total remuneration earned from *Uber* and *Airbnb*. Therefore, the prohibitions in section 23(m) would not apply to the driver or host. The driver or host would, however, still need to comply with the requirements of the “general deduction formula”.

Other tax-related consequences of the “employee” status are that *Uber* and *Airbnb* would be required to register with SARS as employers and withhold or deduct employees’ tax (pay-as-you-earn (PAYE)) from the employee’s remuneration and pay it over to SARS (see below). SARS might seek to recover employees’ tax on all payments that were previously made to “sharing economy” workers. Additionally, it would mean the workers would be entitled to employment rights, such as holiday pay and sick leave. *Uber* and *Airbnb* might also have to

²⁶⁷ Act 58 of 1962.

²⁶⁸ SARS Interpretation Note 13 (Issue 3) “Deductions: Limitation of deductions for Employees and Office holders” (2011) 4.

²⁶⁹ Act 58 of 1962.

give the drivers and hosts back-pay for unpaid benefits. If the appeal of *Uber South African Technological Services* is overturned, it would mean that the host or driver as an “independent contractor” may claim deductions on all expenses incurred in the production of income. As independent contractors there would be no withholding of any taxes from their compensation and they would not be entitled to any employee benefits.

3.7 Miscellaneous tax issues

Having established that the *Airbnb* owner, *Uber* driver and *Uber* are liable for “income tax” it becomes necessary to discuss issues relating to tax registration, payment of provisional tax and retention of records. This is discussed below.

3.7.1 Tax Registration

When a taxpayer becomes liable for “income tax”, he or she is required to apply to the Commissioner to be registered as a taxpayer.²⁷⁰ Individuals whose income exceeds the threshold amounts are obliged to register as taxpayers. *Uber* drivers or *Airbnb* hosts whose income exceeds R75 750 if they are under 65 years; R 117 300 if they are 65 years and older and R131 150 if they are 75 years and older, are obliged to register as taxpayers.²⁷¹ The application for registration as a taxpayer must be made within 21 business days of the date on which the person becomes liable for “income tax”.²⁷² In relation to *Uber*, as a company, it is required by law to be registered with SARS for income tax.²⁷³

3.7.2 Provisional tax

Where an *Airbnb* host or an *Uber* vehicle owner earns a taxable income from the platforms that exceeds R30 000 per year, he or she will be required to register as a provisional taxpayer with SARS and to submit provisional tax returns on a bi-annual basis in August and February of each tax year.²⁷⁴ The onus is on the taxpayer to register as a provisional taxpayer within 30 days after the date on which he or she qualifies as a provisional taxpayer.²⁷⁵ In relation to *Uber*, paragraph 23 of the Fourth Schedule states that all companies are provisional taxpayers. Therefore, *Uber* must make the first provisional tax six months before its year end and the

²⁷⁰ Act 58 of 1962.

²⁷¹ Haupt *Notes on South African Income Tax*.

²⁷² Section 67 of the Income Tax Act 58 of 1962, read with section 22 of the Tax Administration Act 28 of 2011.

²⁷³ Haupt *Notes on South African Income Tax*.

²⁷⁴ SARS “Provisional Tax” 2017. Available: <http://www.sars.gov.za/TaxTypes/PT/Pages/default.aspx> (Accessed 4 August 2017).

²⁷⁵ *Ibid*.

second payment by the end of its year of assessment.²⁷⁶ Non-compliance can result in the levying of interest and penalties, and even imprisonment.²⁷⁷

3.7.3 *Uber* and *Airbnb*'s responsibilities as employers

The discussion above established that *Uber* drivers and *Airbnb* hosts may be regarded as employees for tax purposes, making *Uber* and *Airbnb* their employers. As employers, *Uber* and *Airbnb* are required to apply to the Commissioner for registration within 14 days after becoming employers, or within such further period as the Commissioner may approve.²⁷⁸ In terms of paragraph 2 of the Fourth Schedule, *Uber* and *Airbnb* have an obligation to deduct and pay over employees' tax, unless the Commissioner has granted authority to the contrary.²⁷⁹ This deduction of employees' tax is made in respect of the employees' liability for normal tax. *Uber* and *Airbnb* may, however, deduct more employees' tax if they receive a written request to do so from an employee.²⁸⁰ Where the remuneration is paid or payable to a married person and the remuneration is deemed to be income of the employee's spouse under section 7(2) of the Income Tax Act, the deduction is to be made in respect of the normal tax liability of the employee's spouse.²⁸¹

The amount of employees' tax that *Uber* and *Airbnb* deduct or withhold must be paid to the Commissioner within 7 days after the end of the month during which it was deducted.²⁸² The liability to deduct employees' tax is deemed to be discharged if the employer made payment of the outstanding employees' tax to the Commissioner. Subject to the provisions in paragraph 6, if *Uber* and *Airbnb* fail to deduct the full amount of employees' tax as provided in paragraph 2, the Commissioner will hold them personally liable for the amount that they fail to deduct or withhold.²⁸³ *Uber* and *Airbnb* can, on application in the prescribed form and manner by the Commissioner and if he is satisfied that there is a reasonable prospect of ultimately recovering the tax from the employee, be absolved from the employer's personal liability if the failure was not due to an intent to postpone the payment of tax or to evade their obligations as employers.²⁸⁴

²⁷⁶ Paragraph 23 of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁷⁷ E Bell "There are many pitfalls when it comes to provisional tax" 2013. *SAIT*. Available: <http://www.thesait.org.za/news/118861/There-are-many-pitfalls-when-it-comes-to-provisional-tax.htm> (Accessed 5 August 2017).

²⁷⁸ Paragraph 15 of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁷⁹ *Ibid.*

²⁸⁰ Paragraph 2 of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁸¹ *Ibid.*

²⁸² *Ibid.*

²⁸³ Paragraph 5 of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁸⁴ *Ibid.*

Paragraph 5(3) gives *Uber* and *Airbnb* the right to recover any tax they pay in terms of paragraph 5(1) from the employee in such manner as the Commissioner, on application in the prescribed form and manner by the employer, decides.²⁸⁵ However, any amount that *Uber* and *Airbnb* pay in terms of paragraph 5(1) but not recovered from the employee, shall, for purposes of section 23(d)²⁸⁶ be deemed to be a penalty due and payable by the employer and therefore not deductible for income tax purposes. If *Uber* and *Airbnb* fail to pay any employees' tax for which they are liable within the period allowed, the Commissioner will impose a penalty of 10% of the amount due. If this non-payment of the employees' tax was an intent by either of the companies to evade tax obligations, the Commissioner will hold them liable to pay a penalty not exceeding an amount equal to twice the amount of employees' tax which it so failed to pay.²⁸⁷ Additionally, in terms of paragraph 30(1) of the Fourth Schedule, read with section 75 of the Act, *Uber* and *Airbnb* can be liable, on conviction, to a fine if either of them fails to deduct and pay employees' tax within the prescribed period. Furthermore, interest at the prescribed rate, as well as penalties, may be imposed on *Uber* and *Airbnb* in respect of the late payment of any outstanding employees' tax.

Paragraph 13 requires *Uber* and *Airbnb* to deliver an employee's tax certificate to each employee or former employee to whom remuneration had been paid or has become payable by them. Furthermore, *Uber* and *Airbnb* must within 60 days from the end of each tax year, render a return to the Commissioner for each employee indicating the name and address of the employee, the total remuneration paid to the employee and the total amount of taxation deducted from the employee's remuneration.²⁸⁸ Therefore, *Uber's* and *Airbnb's* obligation to withhold or deduct employees tax is absolute. Thus, any agreement between *Uber* or *Airbnb* and their employees not to deduct or withhold employees' tax will be void.²⁸⁹

3.7.4 Retention of records

Uber and the respective service providers must retain records relating to their business operations for a certain number of years. Since *Uber* is liable for VAT, as will be shown in chapter 4, it must keep records of supporting information such as bank statements, stock lists,

²⁸⁵ *Ibid.*

²⁸⁶ Section 23(d) prohibits the deduction of any tax imposed or interest or penalty imposed under the Act administered by the Commissioner.

²⁸⁷ Paragraph 5 of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁸⁸ Paragraph 14(3) of the Fourth Schedule of the Income Tax Act 58 of 1962.

²⁸⁹ Paragraph 7 of the Fourth Schedule of the Income Tax Act 58 of 1962.

paid cheques and invoices for a period of five years.²⁹⁰ An *Uber* driver or *Airbnb* host must also retain records of income, liabilities and assets owned for a period of five years. These records may be retained electronically, provided they can be reprinted.

3.8 Conclusion

This chapter discussed the deduction of expenditure incurred by *Uber* and the respective service providers. The discussion established that expenses or losses incurred from “sharing economy” activities can be regarded as “expenditure and losses” contemplated in section 11(a) of the Act. Furthermore, the discussion indicated that expenses from “sharing economy” activities will be incurred if they result in an unconditional legal obligation to pay the amount during the year of assessment. The “sharing economy” participant must show that there is a link between the expenditure incurred and the trade that is being carried on. Proving this link would satisfy this element of the general deduction formula. Additionally, expenses incurred from the “sharing economy” activities must be expended for purposes of trade and be of a revenue nature, to be deductible in terms of section 11. Where expenses are incurred for a dual purpose, *Uber*, the driver or host must apportion the expenses between business and personal use, with the business portion being deductible. Thus, if a participant meets all the requirements of the general deduction formula, the expense will be deductible in terms of the section 11(a).

It was established that *Uber*, the *Uber* driver and *Airbnb* host may claim deductions for wear and tear, repairs, insurance and other non-capital business expenses. The driver and host may also claim a deduction of assessed losses in terms of section 20 of the Act, unless ring-fencing in terms of section 20A applies. Additionally, an *Airbnb* host may, under certain circumstances, claim a capital allowance in terms of section 13*sex*.

The chapter established that a “sharing economy” worker’s status may affect the deductibility of his or her expenses, due to provisions of section 23(m) of the Act, which limits deductions that can be claimed against employment income. The chapter analysed the status of “sharing economy” workers, specifically *Uber* drivers and *Airbnb* hosts, and concluded that the workers may be regarded as “employees” for tax purposes. From the analysis it was shown that the *Uber* driver’s and *Airbnb* host’s remuneration is mainly derived in the form of a commission and thus the limitations of section 23(m) are not applicable to them.

²⁹⁰ *Ibid.*

Having established that *Uber*, and possibly the *Airbnb* owner and *Uber* driver, are liable for “income tax”, the chapter concluded by explaining that they have a duty to register as taxpayers with the Commissioner, retain records for certain periods of time and, where applicable, pay provisional tax.

The following chapter will analyse the challenges that presently exist in taxing the “sharing economy” in South Africa and what measures can be taken to address these problems. In this regard, legislation in Australia and America will be analysed to see how these challenges are dealt with.

CHAPTER 4: COUNTRY COMPARATIVE ANALYSIS

4.1 Introduction

In the preceding chapters, the concept of the “sharing economy” was discussed, and it was established that *Uber*, the *Uber* driver and the *Airbnb* host are subject to the current South African tax system. Having established this, chapter 4 will investigate how South Africa and two other selected countries deal with taxing the “sharing economy”. The chapter will examine problems of the South African tax system in effectively regulating *Uber* and *Airbnb* and investigate how the same challenges are addressed in Australia and America, thus addressing the third objective of the thesis – a comparative analysis of how Australia and America are taxing the “sharing economy” activities. The chapter will also assess whether the measures applied in the two countries could be adopted in South Africa. This will address the final research objective – recommendations relating to how the current South African tax system could be amended to deal with taxable income from activities in the “sharing economy”.

4.2 South Africa

Uber and *Airbnb* services have become part of everyday life in South Africa, but their presence has not been without difficulties.²⁹¹ This is because the technologically advanced “sharing economy” business model had not been contemplated by the existing tax laws.²⁹² The main problem that South Africa is facing in ensuring tax compliance is that the “sharing economy” businesses are engaging in “tax opportunism”. Tax opportunism describes a situation where, “in determining how and whether to comply with existing laws and regulations, ‘sharing economy’ businesses have the propensity to pick a favourable regime if there is ambiguity as to which regime applies.”²⁹³ When engaging in the opportunistic behaviour, the “sharing economy” businesses make a tax compliance choice that provides them with a regulatory advantage as compared with the alternative reporting compliance position.²⁹⁴ While this phenomenon is not new, in the “sharing economy” it presents a unique challenge. Some of the tax compliance issues, exacerbated by the “sharing economy’s” opportunistic behaviour in South Africa are discussed below.

²⁹¹ A Johnston “*Uber, Airbnb and the problem with South Africa’s sharing economy*” 2017. Available: <https://datacentrenews.eu/story/uber-airbnb-and-problem-south-africas-sharing-economy/> (Accessed 18 January 2018).

²⁹² *Ibid.*

²⁹³ Oei “Can Sharing be Taxed” 1027.

²⁹⁴ *Ibid.*

4.2.1 Non-declaration of income

One of the problems that SARS is experiencing is that the current legislation has loopholes that have enabled participants in the “sharing economy” to avoid paying tax in South Africa. The current tax regime was developed in the last century when the Internet was not yet in common use; therefore, the system is failing to effectively regulate these new platforms. The tax system’s failure to respond to these innovations will be illustrated by an analysis of how *Uber* works.

Assuming an *Uber* customer has requested a ride, which will cost R100. The fare is charged through the customer’s credit card and then sent across national borders into an account of the company in Netherlands, *Uber BV*.²⁹⁵ This company collects the fare electronically, through *Raiser Operations BV* and sends R80 (80% of the fare) to the driver’s account.²⁹⁶ The remaining R20 (20% of the fare) enters a complicated network of Dutch offshore companies. The R20 is transferred to *Uber International CV* by *Uber BV*, through an “Intangible Property License Agreement”.²⁹⁷ In the terms of the agreement, *Uber BV* keeps a small portion of the fare to cover the costs of operation and administration expenses.²⁹⁸ The rest of the profit is then sent to *Uber International CV* as a royalty.

Under Dutch law, that royalty payment is not taxable because it lies in a grey area between national tax authorities.²⁹⁹ This royalty income will be legally off the grid and it is not taxed in South Africa, in the Netherlands or in the United States.³⁰⁰ This strategy of using two Netherlands companies connected by a license agreement is referred to as the “Double Dutch”. The process helps *Uber* to avoid paying tax because there is no recorded income for *Uber* in South Africa. The process makes *Uber*’s income invisible to SARS, even though the R20 gross profit is from a South African source. This process can – in a simplified form – best be illustrated as follows:

²⁹⁵ Anonymous “How *Uber*, *Google*, *Facebook* and other Tech giants avoid paying billions in taxes” 2017. *Dconstrct*. Available: <https://dconstrct.com/how-uber-google-facebook-and-other-tech-giants-avoid-paying-billions-in-tax/> (Accessed 18 August 2017).

²⁹⁶ *Ibid*.

²⁹⁷ B O’Keefe and M Jones “How *Uber* plays the tax shell game” 2015. Available: <http://fortune.com/2015/10/22/uber-tax-shell/> (Accessed 18 August 2017).

²⁹⁸ *Ibid*.

²⁹⁹ *Ibid*.

³⁰⁰ Anonymous “Tech giants avoid paying billions in taxes” 2017.

Figure 4.1: Uber royalty payment process

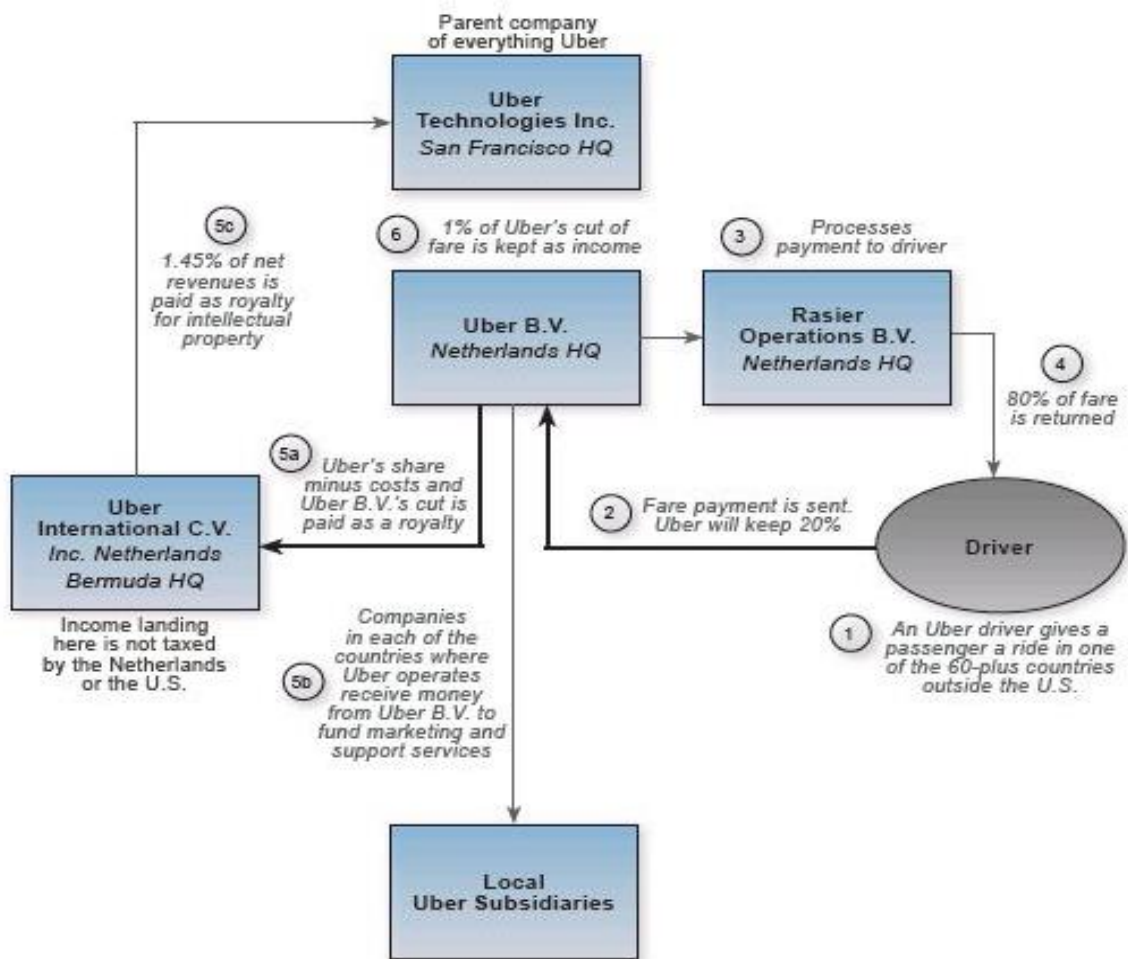


Diagram credit: B Erwin and AF Karaman³⁰¹

As a non-resident company, *Uber* is subject to normal tax in South Africa, since it receives income or income accrues to it from a South African source. This tax is imposed on businesses incorporated under the laws of South Africa or which derive income through a branch or “permanent establishment” within South Africa.³⁰² It was established in chapter 2 that *Uber* has a “permanent establishment” in South Africa and therefore the normal tax payable is calculated at a flat rate of 28% on its taxable income.³⁰³ A key allegation, however, is that

³⁰¹ B Erwin and AF Karaman “The sharing Economy part 1: New Business Models + Traditional tax rules don’t mix” 2017. Available: <http://www.mondaq.com/unitedstates/x/647460/tax+authorities/The+Sharing+Economy+Part+1New+Business+Models+Traditional+Tax+Rules+Dont+Mix> (Accessed 26 January 2018).

³⁰² N Musviba “Corporate Income Tax” 2017. Available: <http://www.sataguide.co.za/corporate-income-tax/> (Accessed 18 January 2017).

³⁰³ *Ibid.*

Uber is not declaring any income to SARS as illustrated by the example above.³⁰⁴ The “Double Dutch” system may be depriving SARS of millions of Rand in tax.

Furthermore, *Uber* and *Airbnb* classify their respective service providers as “independent contractors”. This means that the drivers or hosts are running their own businesses and are paying *Uber* or *Airbnb* a small fee to use their platform.³⁰⁵ In terms of South African law, independent contractors are responsible for paying their own taxes, instead of employees’ tax being deducted. Many of these drivers and hosts may not be declaring their income to SARS. This may be because many of the participants in this industry may be new to the payment of taxes and not fully aware of how to declare their income.³⁰⁶ Even the drivers and hosts who are aware of how to declare their income, may not be doing so because they know that SARS has no means of effectively ascertaining whether they are complying with their tax obligations. This constitutes tax evasion and, in the process, may be depriving the *fiscus* of potential tax revenue.

4.2.2 Non-payment of VAT

Uber classifies itself as a technological company, rather than a transport company.³⁰⁷ *Uber* views itself as merely connecting consumers to drivers and earning a 20% commission, based on the fare calculated using their app.³⁰⁸ In South Africa, all fare-paying transportation services are exempt from VAT in terms of section 12(g) of the VAT Act.³⁰⁹ *Uber* does not qualify for the exemption as it is, by its own statement, not a transport provider. Therefore, in terms of South African tax law, *Uber* must charge its customers 14% VAT on the fare charge and then pay this over to SARS. However, *Uber* is not charging any of its customers with VAT, arguing that each of its drivers is a separate business, but each too small to register for VAT.³¹⁰ This opportunistic behaviour allows *Uber* to provide cheaper services when compared to other providers.

This same loophole is used by other multi-national companies, such as *Google* and *Facebook*, to avoid VAT on certain transactions involving small businesses, but the benefit is more

³⁰⁴ L Gedye “*Uber’s* competitors cry foul” 2015. *SAIT*. Available: <http://www.thesait.org.za/news/217498/> (Accessed 18 August 2017).

³⁰⁵ Anonymous “SA misses opportunity to tax foreign e-services-PwC” 2016.

³⁰⁶ *Ibid.*

³⁰⁷ *Ibid.*

³⁰⁸ *Ibid.*

³⁰⁹ *Ibid.*

³¹⁰ Gedye “*Uber’s* competitors cry foul”.

important for *Uber* since the fees it charges drivers are its main source of income.³¹¹ *Uber* is exploiting loopholes in law to avoid paying VAT and in the process depriving the *fiscus* of tax revenue.³¹²

4.2.3 Unfair competition

Uber's success has triggered an outcry from taxi service providers as they believe *Uber* is a threat to their viability. In 2016 and 2017 there was an escalation of violence between *Uber* and metered taxi drivers, which reached proportions that threatened peace and stability in the Republic.³¹³ The reason for the “wars” was that *Uber* was not complying with the transport laws in relation to obtaining licenses and operating permits, despite the Minister of Transport announcing that they need to do so.³¹⁴ Many have argued that by failing to comply with the traditional regulatory requirements that burden taxi companies, *Uber* is engaging in unfair competition.³¹⁵ The “war” resulted in murder, attempted murder, arson, assault, assault with intent to do grievous bodily harm, theft, robbery, hijacking of vehicles and verbal intimidation.³¹⁶

In relation to *Airbnb*, South Africa is by far its biggest market in Africa, accounting for almost half the listings on the continent.³¹⁷ The *Airbnb* community boosted the South African economy with an estimated R2,4 million in 2016 and this grew to R197 million in 2017.³¹⁸ There has been a growing concern, however, over the service’s non-compliance with the law. For example, it was revealed that many of Cape Town’s *Airbnb* rentals are “illegal” as the city’s municipal by-laws do not permit the renting out of entire homes or apartments on a short-term

³¹¹ A Churchyard “Know when to charge VAT on passenger transport or face 200% penalties” 2014. Available : <http://fspbusiness.co.za/articles/vat/know-when-to-charge-vat-on-passenger-transport-or-face-200-penalties-6431.html> (Accessed 19 August 2017).

³¹² G McGlashan “Opinion: *Uber*- The Wolf in Sheep’s Clothing” 2015. Available: <http://bandwidthblog.com/technology/mobile/uber-wolf-in-sheeps-clothing/> (Accessed 19 August 2017).

³¹³ J Gerber “Gauteng to clamp down on illegal *Uber* and metered taxis” *News24* 17 September 2017. Available: <https://www.news24.com/SouthAfrica/News/gauteng-to-clamp-down-on-illegal-uber-and-metered-taxis-20170917> (Accessed 1 January 2018).

³¹⁴ S Mabena “Permits a must for *Uber*, says Minister” *Times Live* 11 July 2017. Available: <https://www.timeslive.co.za/politics/2017-07-11-permits-a-must-for-uber-says-minister/> (Accessed 19 January 2018).

³¹⁵ *Ibid.*

³¹⁶ *Ibid.*

³¹⁷ K Douglas “How big is *Airbnb's* business in Africa?” 2017. Available: <https://www.howwemadeitinafrica.com/big-airbnbs-business-africa/58243/> (Accessed 19 January 2017).

³¹⁸ T Mhlanga “Tourists- and South Africans – discover Soweto *Airbnb*” *Mail&Guardian* 1 December 2017. Available: <https://mg.co.za/article/2017-12-01-00-tourists-and-south-africans-discover-soweto-airbnb> (Accessed 19 January 2018).

basis.³¹⁹ Furthermore, most hosts are not using appropriately zoned properties and they are not applying for consent to let out the properties from the city's development management department.³²⁰ Additionally, non-regulation of *Airbnb*, has had a direct impact on hotel industry performance – for example, most hotels have had to undercut their services considerably.³²¹

At present separate laws apply to similarly situated companies, products and services and this is resulting in unfair competition. *Uber*, *Airbnb* and their service providers are operating outside tax laws that traditional taxi services and hotels are subject to. This is causing the *fiscus* to lose potential tax revenue due to the lack of proper regulation of the “sharing economy”. Therefore, it is important to draw solutions from other jurisdictions that have faced similar problems and found ways to deal with them. What follows is a discussion of the approach taken by Australia and America to tax “sharing economy” businesses.

4.3 The “sharing economy” in Australia

Uber and *Airbnb* are the most prominent “sharing economy” businesses raising issues in Australia. According to Baldassarre³²² the value of Australia's “sharing economy” is expected to reach \$55 billion in the next five years, having risen from \$14.5 billion to over \$15.1 billion in six months. The Australian Government Productivity Commission's 2016 Research Paper identified that sharing economies have a disruptive business model that moves faster than legislation can be created, and this has caused friction between businesses operating in the “sharing economy” and their various stakeholders, such as the government, employees, consumers and unions.³²³ As these technology-driven businesses continue to grow, there continue to be regulatory and policy issues across cities and towns in Australia.³²⁴ Some of the regulatory issues are discussed below.

³¹⁹ A Haden “Many of Cape Town's *Airbnb*'s are illegal- here's why” 2017. Available: <https://www.thesouthafrican.com/many-of-cape-towns-airbnbs-are-illegal-heres-why/> (Accessed 24 January 2018).

³²⁰ *Ibid.*

³²¹ *Ibid.*

³²² G Baldassarre “Value of Australia's sharing economy hits \$15 billion, while concerns around future of work grow” 2017. *Startupdaily*. Available: <http://www.startupdaily.net/2017/02/value-australias-sharing-economy-hits-15-billion-concerns-around-future-work-grow/> (Accessed 05 October 2017).

³²³ Australian Government Productivity Commission Research Paper *Digital Disruption: What do governments need to do?* 2016

³²⁴ J Penn and J Wihbey “*Uber*, *Airbnb* and consequences of the sharing economy: Research roundup” 2017. Available: <https://journalistsresource.org/studies/economics/business/airbnb-lyft-uber-bike-share-sharing-economy-research-roundup> (Accessed 4 October 2017).

4.3.1 Non-payment of goods and services tax

Just as in South Africa and other parts of the world, *Uber* was avoiding paying Goods and Services Tax (GST – the local equivalent of VAT) in Australia. *Uber* alleged that its Australian business did not pay tax because it did not generate any revenue, since the drivers keep 75% of the customer’s fee and the other 25% goes to Netherlands.³²⁵ *Uber* further alleged that it should not be forced to pay GST because it was not a taxi company, but a technological company.³²⁶ This tax avoidance strategy by *Uber* led to the Australian Tax Office (ATO) losing potential tax revenue it could have collected and used. It also created unfair competition between *Uber*, its similar competitors and the traditional taxi operators, who had to pay GST. This gave *Uber* the advantage of providing cheaper services when compared to the traditional taxi services.

To ensure tax compliance and to promote fair competition the ATO took *Uber* to court requesting that they pay GST.³²⁷ The court classified *Uber* as a taxi service, liable for GST. The court accepted that there was a deficiency in the GST Act that allowed “ride-sharing” to slip through a legal loophole.³²⁸ To close this tax loophole, the ATO now requires any driver earning income from the ride-sharing apps to register for tax and it has introduced a 10% GST rate on each ride. The court ruling gave the ATO wide-ranging powers to access documents and collect information to apply and administer the GST.³²⁹ These powers allow the ATO to request information in relation to drivers and fares received from *Uber* or similar companies.³³⁰ Additionally, the ATO introduced penalties for failure to comply with these requests and for failing to pay GST.

South Africa could take note of this approach by Australia, where GST (the VAT equivalent) is directly withheld by the driver who in turn remits it to the ATO. Requiring the drivers to charge and collect the VAT on behalf of SARS would promote fair competition between the

³²⁵ R Chirgwin “*Uber* Australia is broke: We don’t pay tax because we don’t generate revenue” 2015. Available: https://www.theregister.co.uk/2015/11/18/uber_australia_is_broke_we_dont_pay_tax_because_we_dont_generate_revenue/ (Accessed 27 August 2017).

³²⁶ *Ibid.*

³²⁷ *Uber B.V. v FC of T* [2017] FCA 110.

³²⁸ F Chung “*Uber* drivers must pay GST, court rules” 2017. Available: <http://www.news.com.au/finance/business/travel/uber-drivers-must-pay-gst-court-rules/news-story/cc95dad277da68532609bc93cdd03760> (Accessed 27 August 2017).

³²⁹ [2017] FCA 110.

³³⁰ K Bain “GST and ride-sharing: why the ATO believes *Uber* must pay” 2015. *The Conversation*. Available: <https://theconversation.com/gst-and-ride-sharing-why-the-ato-believes-uber-must-pay-42114> (Accessed 27 August 2017).

“sharing economy” businesses and the traditional businesses that already charge VAT on the supply of goods and services. SARS could also have an agreement with *Uber*, which allows it access to driver and fare information when checking for compliance. Alternatively, SARS could task *Uber* to withhold VAT and pay it over to SARS. This would be a more favourable approach because requiring drivers to do so might prove to be difficult, given that many of the participants in the “sharing economy” may be new to the need to collect and pay over VAT. Charging VAT would ensure compliance with tax provisions and it would increase the tax base and consequently address the leakage in the current tax system.

4.3.2 Non-declaration of income

Another problem that the ATO was facing was that taxpayers were not declaring their earnings from these “sharing economy” platforms. In terms of Australian Tax law, *Airbnb* hosts, *Uber* drivers and any other online service providers are required to include earnings from the platforms in their tax returns. However, thousands of drivers and hosts engaged in these online businesses were not declaring their income to the ATO.³³¹ This non-compliance led to the Australian government losing tens of thousands of Australian Dollars in tax.

To ensure compliance, the ATO found a way to ensure that *Uber* drivers and *Airbnb* hosts do not evade declaring their income tax. The ATO introduced a new data-matching program where banks (including overseas banks), other financial institutions, employers and health insurance funds will hand over to the ATO detailed information on payments to taxpayers using “sharing economy” platforms and other online services.³³² This new data-matching program is helping the tax office to identify any drivers or hosts who have ignored their tax registration, lodgement, reporting and payment obligations.³³³ For those caught not complying, the ATO is applying back-payment of taxes, plus fines, and in some cases back-payment of interest charges.³³⁴

The data collected by the system allows the tax office to get directly into touch with the drivers and hosts offering services to make sure that they are aware of their tax obligations. This communication happens through letters, text messages and phone calls.³³⁵ The data-matching program enables the ATO to put together a picture of what a person’s assessable income should

³³¹ *Ibid.*

³³² Anonymous “The ATO says it’s coming after *Uber* drivers who evade the GST” 2017. Available: <http://poweredbyg.nu/The-ato-says-its-coming-after-uber-drivers-who-evade-the-gst> (Accessed 26 August 2017).

³³³ *Ibid.*

³³⁴ *Ibid.*

³³⁵ Viellaris “ATO announces crackdown on ride-sharing services” 2016.

be. If something does not look quite right, the data-matching program sends a red flag to the ATO and they will investigate further.³³⁶ By June 2017, this data matching program had successfully identified more than 60 000 *Uber* drivers who had not complied with their tax obligations, prompting the ATO to send out communications alerting them to the need to honour their obligations.³³⁷ This data-matching program has been a success and it has improved the quality of data held in the ATO's database, increased revenue collection and voluntary compliance.³³⁸

Furthermore, the ATO has gone a step further by employing a team of data-mining specialists who analyse a taxpayer's social media posts, private school records and immigration data for data-matching purposes. These data specialists are analysing information from social media sites like *Facebook*, *Twitter* and *Instagram*, which they believe could be used to identify tax misreporting and dodgy deductions.³³⁹ The specialists will match the data in the taxpayer's tax returns, the lifestyle he or she is living and the pictures or videos of holidays that might have been claimed as work-related expenses.³⁴⁰

This approach is commendable and could be considered by South African regulators when drafting laws to deal with "sharing economy" businesses. Developing and implementing a data-matching program like the one in Australia is likely to be successful as knowledge of the existence of the program would encourage the declaration of income and deter tax evasion. It would also ensure that the correct amount income is declared, protect public revenue through the identification of non-compliance and promote public confidence in the integrity of the tax system.

Analysing social media platforms to find cases of people's declared income not matching their lifestyles could also be a useful strategy for SARS to adopt. It is a reality of the present age that there is more and more information publicly available through social media. Therefore, using social media platforms could help SARS to fill in gaps, where a taxpayer's information does not make sense. In developing this data-matching program, SARS could also collect

³³⁶ *Ibid.*

³³⁷ N Khadem "ATO writes to 60,000 *Uber* and other ride-sharing drives asking them to get tax affairs in order" 2017. Available: <http://www.smh.com.au/business/ato-writes-to-60000-uber-and-other-ridesharing-drivers-asking-them-to-register-for-gst-20170629-gx12xb.html> (Accessed 22 January 2018).

³³⁸ Data Matching Program- Parliament of Australia, 25.

³³⁹ B Squires "ATO tracking your Facebook posts" 2017. Available: <http://www.oversixty.com.au/finance/money-banking/2017/03/the-ato-is-stalking-your-facebook-posts/> (Accessed 27 August 2017).

³⁴⁰ *Ibid.*

information from a range of public and private sources, such as motor vehicle registries, the stock exchange and other online selling platforms. The legislature could ensure that banks, employers and government agencies are obliged to report information to SARS when requested to do so. Adopting such a sophisticated system could lead to a significant drop in tax avoidance. While it will take time, the South African legislature could start investigating ways to develop and implement such an E-tax data-matching program.

In relation to income declaration by *Uber*, the ATO had no idea how much *Uber* was earning from its activities in Australia. This is because any revenue collected by *Uber*, gets routed back to its overseas head subsidiary.³⁴¹ *Uber's* use of the “Double Dutch” made it difficult for the ATO to track exactly how much it was earning. It was alleged that, after paying its drivers, no revenue was coming back to Australia and that *Uber* was syphoning off 100% of its profits to offshore countries.³⁴² Thus, in 2016, *Uber* was requested to lodge its financial statements with the Australian Securities and Investment Commission. This gave the Australian government a clear indication of how much tax was due and how much *Uber* paid. Submission of the statements to the Australian Securities and Investment Commission ensures that *Uber* operates efficiently, honestly and fairly.

To deal with non-payment of corporate tax by *Uber* in South Africa, SARS could request it to lodge its financial statements. As in Australia, this would provide SARS with information on how much *Uber* is earning and then levy the appropriate corporate tax on that amount.

4.4 The “sharing economy” in America

In 2010, America’s sharing systems had an estimated market volume of US\$100 billion.³⁴³ Since then the “sharing economy” market volume has continued to grow. Li *et al*³⁴⁴ attributes the sharing economy’s growth to the lower consumption costs it offers and the convenience and ease of use. The Internal Revenue Services (IRS) identified that the “sharing economy” increased the efficiency of underutilized assets and it accelerated technological progress in the economy.³⁴⁵ However, the law is unable to keep up with taxing the “sharing economy” and its

³⁴¹ N Khadem “*Uber* pays \$2,5 million tax in Australia, says company is not under ATO audit” *The Sydney Morning Herald* 3 November 2016. Available: <http://www.smh.com.au/business/the-economy/uber-pays-25million-tax-in-australia-says-company-is-not-under-ato-audit-20161103-gsh37e.html> (Accessed 23 January 2018).

³⁴² *Ibid.*

³⁴³ M Mohlmann “Collaborative consumption: determinants of satisfaction and the likelihood of using a sharing economy option again” *2017 Journal of Consumer Behavior* 14.

³⁴⁴ W Li, M Nirei and K Yamana “Sharing Economy in Japan and the United States” 2017.

³⁴⁵ *Ibid.*

continuous growth is causing regulatory challenges. Some of these challenges are discussed below.

4.4.1 Non-payment of sales tax

Just as in South Africa and Australia, many States in America are having trouble with applying and collecting sales taxes (the VAT equivalent).³⁴⁶ Most often, American tax laws place the burden of collecting taxes on the individual suppliers in the “sharing economy” rather than on the company that facilitates the “peer-to-peer” transactions. This results in most individual suppliers not collecting the taxes because it is burdensome for them to file the appropriate tax return and remit the tax to the State.³⁴⁷

In most States both taxi fares and rides from ride-sharing sites are exempt from sales tax.³⁴⁸ With the growth of the service sector and tax enforcement methods improving, the costs of exempting these services came to outweigh the benefits. This led to eight States applying sales taxes to taxi fares and rides from ride-sharing sites, namely Georgia, Hawaii, New Mexico, Ohio, Rhode Island, South Dakota, Washington and Wyoming.³⁴⁹ Although the sales tax was applied to the fares, companies such as *Uber* and *Lyft* were not collecting the tax, claiming that the law does not apply to them.³⁵⁰ The matter went before the Rhode Island State’s Division of Taxation where it was held that “an entity ... that uses a digital network to connect transportation network company riders to transportation network operators who provide pre-arranged rides” must collect sales tax.³⁵¹ Regardless of this court ruling, the ride-sharing companies in some States are still not collecting tax.³⁵²

To avoid disputes with these ride-sharing companies on whether they are subject to sales tax, some States are now levying taxes specifically tailored to the ride-sharing industry. Massachusetts is one such State that has just signed into law a \$0.20-cent tax per trip on *Uber*

³⁴⁶ JL Kerner “Challenges of Taxing the Sharing Economy” 2015. *LexisNexis*. Available: <https://www.lexisnexis.com/lexis-practice-advisor/the-journal/b/lpa/archive/2015/11/25/challenges-of-taxing-the-sharing-economy.aspx> (Accessed 5 October 2017).

³⁴⁷ *Ibid.*

³⁴⁸ Z Schiller and C Davis “Taxes and the On-Demand Economy” 2017. *Institute on Taxation and Economic Policy*. Available: <https://itep.org/taxes-and-the-on-demand-economy/> (Accessed 4 October 2017).

³⁴⁹ *Ibid.*

³⁵⁰ A Patrick, “*Uber* says it has paid Rhode Island sales tax” 2015. *Providence Journal*. Available: <http://www.providencejournal.com/article/20150429/NEWS/150429139> (Accessed 4 October 2017).

³⁵¹ *Ibid.*

³⁵² *Ibid.*

and *Lyft* rides.³⁵³ This \$0.20-cent tax is split, with \$0.05-cents designated for taxis, \$0.05-cents designated for a state transportation fund and the \$0.10-cents going to cities and towns.³⁵⁴ This \$0.20-cent tax is charged to the ride-sharing companies and the State has explicitly barred the companies from passing on the tax to the riders or the drivers. The State of Nevada imposes a 3% excise tax on such rides, while South Carolina imposes a 1% fee on each ride. In Pennsylvania, the State law requires the ride-sharing company to pay a 1.4% gross receipt tax, but only on rides originating in the city of Philadelphia.³⁵⁵

As an alternative to charging of VAT, South Africa could adopt a similar measure and introduce a tax that is specific to the ride-sharing industry. Placing an obligation on *Uber* and similar ride-sharing businesses to collect and remit this tax to SARS could further reduce the leakage in the current tax system. This would also be favourable as it might prove to be challenging for the individual drivers to collect and pay over the tax to SARS. It would also be less burdensome for SARS to monitor the company than having to monitor thousands of small transactions by individual drivers using these platforms. It is submitted that introduction of this tax as an alternative to charging VAT is likely to be successful and it could increase the tax base and promote fair competition in the transportation industry.

4.4.2 Non-declaration of income

The IRS noticed that the *Uber* drivers and *Airbnb* hosts are not always aware of their tax reporting and filing obligations, which also leads to a substantial loss in tax revenues. In 2016, the IRS attempted to resolve this issue by launching the “Sharing Economy Tax Center”.³⁵⁶ The website provides education and resources relevant to the taxation of the “sharing economy”, so that individuals earning income through platforms like *Uber* and *Airbnb* can comply with their filing obligations.

³⁵³ AJ Hawkins “Massachusetts becomes the first state to tax *Uber* and *Lyft*” 2016. *The Verge*. Available: <https://www.theverge.com/2016/8/22/12585976/massachusetts-uber-lyft-tax-taxi-ride-hail> (Accessed 26 August 2017).

³⁵⁴ B Hunter “*Uber* and *Lyft* Slapped with Taxi Tax in Massachusetts” 2016. Available: <https://fee.org/articles/uber-and-lyft-slapped-with-taxi-tax-in-massachusetts/> (Accessed 26 August 2017).

³⁵⁵ A Coulombis “Wolf signs bill making *Uber*, *Lyft* legal in Philly”. *The Inquirer Daily News* 4 November 2016. Available: http://www.philly.com/philly/news/politics/20161105_Wolf_signs_bill_making_Uber_Lyft_legal_in_Philly.html (Accessed 4 October 2017).

³⁵⁶ Thomson Reuters Tax & Accounting “New guidance for taxpayers in the sharing economy on how to meet their tax responsibilities” 2016. Available: <https://tax.thomsonreuters.com/media-resources/news-media-resources/checkpoint-news/daily-newsstand/new-guidance-for-taxpayers-in-the-sharing-economy-on-how-to-meet-their-tax-responsibilities/> (Accessed 19 January 2018).

South Africa could consider developing a similar website. This would help active participants in the “sharing economy” to be aware of the income tax consequences associated with their earning activities. The website could include information for individuals, such as payment of tax, depreciation, business expenses, self-employment taxes, and so on. The website could also offer guidance for companies providing the services in the “sharing economy” with respect to employment tax issues and tax requirements for these companies. As the “sharing economy” continues to grow, a website like the “Sharing Economy Tax Center” would be a valuable starting place for taxpayers to understand the tax consequences associated with the “sharing economy” and it would help with resources to enable them to meet their tax obligations.

4.4.3 Unfair competition

Airbnb and similar online home-sharing services are rapidly taking market-share away from traditional hotels. According to a report backed by the American Hotel and Lodging Association, companies like *Airbnb* are providing a platform for individuals to run illegitimate, unregulated and often illegal hotels in communities across the country.³⁵⁷ The report showed that, for the period October 2015 to September 2016, hosts generated an estimated \$5,7 billion in revenue through *Airbnb* in America.³⁵⁸ Of this \$5,7 billion, approximately 81% was earned by hosts offering an entire-home unit.³⁵⁹ The report showed that revenue for entire-home multi-unit hosts increased at a greater rate than all other *Airbnb* host types.³⁶⁰ An argument was put forward by hotel industry officials that revenue from whole-unit rentals, where that owner is not present, was not home-sharing, but a business and that *Airbnb* was evading the law to avoid paying the taxes and fees other companies have been subject to for decades.³⁶¹

To close the illegal hotel loophole of home-sharing under the guise of *Airbnb* and to hold other short-term rental companies accountable, most States in America have put in place a “primary residence rule.”³⁶² This rule requires that a host cannot offer multiple listings that are not his or her primary residences. The rule was put in place to discourage commercial multiple host

³⁵⁷ CBRE Hotels’ American Research “Hosts with Multiple Units -A Key Driver of *Airbnb* Growth. A Comprehensive National Review Including a Spotlight on 13 U.S. Markets” 2017.

³⁵⁸ CBRE Hotels’ American Research 5.

³⁵⁹ *Ibid.*

³⁶⁰ *Ibid.*

³⁶¹ R Sager “*Airbnb* making millions from ‘illegal hotels’, hotel industry report claims” *Fox News* 13 March 2017 Available: <http://www.foxnews.com/travel/2017/03/13/airbnb-making-millions-from-illegal-hotels-hotel-industry-report-claims.html> (Accessed 21 December 2017).

³⁶² Z Jamasi “Regulating *Airbnb* and the Short-term Rental Market: An overview of North American regulatory frameworks” (2017) 5. *Canadian Centre for Policy Alternatives*.

operations and to safeguard the housing market by discouraging hosts from purchasing investment properties to be used only for short-term rentals.³⁶³

In the State of Virginia, the law went a step further by enacting a Bill that applies to all Virginians who rent out their homes or bedrooms on platforms like *Airbnb*.³⁶⁴ To effectively regulate home-sharing businesses this Bill requires the hosts to identify all owners of the adjacent residential dwellings and notify them, in writing, about their intention to rent out a bedroom or space in their house.³⁶⁵ Secondly, the taxpayer must request and obtain permission from the local municipality to offer a residential dwelling unit for short-term rental. This permission is only granted when the host or taxpayer agrees to pay all the applicable taxes related to the short-term rental transaction.³⁶⁶

The taxpayer offering a residential dwelling for short-term rental must also maintain a minimum of \$500,000 in commercial premises liability insurance that covers all renters, third parties, and for purposes of any damage that might be caused by a renter, persons and property immediately adjacent to the residential dwelling unit.³⁶⁷ If the local municipality prohibits the short-term rental of residential dwelling units, any person or entity, including a hosting platform, that advertises or promotes such rental in the area shall be subject to a \$10 000 fine for each violation, payable to the local municipality. Moreover, the Bill requires *Airbnb* hosts who operate over a period of 90 days or more in a calendar year to obtain a business licence.³⁶⁸ The Bill addresses problems that many States in America still face.

A similar enactment is something that South Africa could consider. This would clearly outline the boundaries within which all South Africans renting out their homes or bedrooms on platforms like *Airbnb* should operate. It would be helpful for the hosts to know how to register, what licences they need to hold, what taxes they should pay, how they should pay them, what fines and penalties are charged and for what offences. The limitations in terms of noise hours, number of days the house can be let, the number of visitors they may host could be clearly specified and zoning laws could be identified that they should be aware of. In adopting such a

³⁶³ *Ibid.*

³⁶⁴ Boehm “*Airbnb* nil passes in Virginia”.

³⁶⁵ Virginia Senate Bill 1579.

³⁶⁶ *Ibid.*

³⁶⁷ *Ibid.*

³⁶⁸ JR Blackwell “McAuliffe signs legislation to enable local regulation of short-term rentals such as *Airbnb* in Va.” *Richmond Times Dispatch* 27 March 2017. Available: http://www.richmond.com/business/local/mcauliffe-signs-legislation-to-enable-local-regulation-of-short-term/article_e6fe0bd8-4f3f-55df-af0f-af471ac71a18.html (Accessed 10 February 2018).

measure, SARS could make sure it includes the “primary residence rule” so as to discourage hosts from purchasing investment properties to be used for short-term rentals only, unless they register as bed-and-breakfast business. Requiring that hosts with multiple listings register as businesses would ensure equity between the hosts and hotels. In addition, it is submitted that the protection of third parties, such the neighbours of *Airbnb* hosts, could also be included to make sure that they are protected from risk. Setting such rules would create trust and collaboration between users and guarantee the safety of third parties and their properties.³⁶⁹

Alternatively, the legislature could consider creating a comprehensive law to encompass all sharing practices, instead of creating a separate law for each “sharing economy” model, such as ride-sharing, apartment-sharing, or other similar businesses when they come into existence. Otherwise, separate laws will need to be continuously amended whenever a new “sharing economy” business emerges. Since neither *Uber* nor *Airbnb* fit neatly into the existing tax laws, a comprehensive law could lead to an effective regulatory regime. Creating a comprehensive law for this new class of “services” eliminates the need to find a place for “sharing economy” within existing laws.

4.5 Conclusion

This chapter explored the challenges that South Africa is experiencing in taxing the “sharing economy” and investigated how other jurisdictions have dealt with the same challenges. The discussion established that most *Uber* drivers and *Airbnb* hosts are not declaring their income to SARS. To deal with this issue Australia developed a data-matching program that will identify culprits and alert the ATO. The discussion indicated that if South Africa adopts a similar data-matching program, it is likely to be successful and it would improve the efficiency and effectiveness of the current tax system in the Republic.

Another problem identified by the research was that *Uber* is not paying VAT for the goods and services that it is offering in the Republic. In solving this problem, Australia and America adopted similar measures, where they now levy taxes specifically tailored to the ride-sharing industry. Since *Uber* classifies its self as a technology company and not a transport company, SARS could therefore adopt a similar measure to ensure that *Uber* withholds the tax and remits it to SARS.

³⁶⁹ Z He “Risks and Regulations of the Sharing Economy” 2017. *Chicago Policy Review*. Available: <http://chicagopolicyreview.org/2017/08/26/risks-and-regulations-of-the-sharing-economy/> (Accessed 26 January 2017).

The research also identified that the growth of the “sharing economy”, without proper regulation, can cause problems in South Africa, such as high rental prices and shortages in long-term rentals throughout Cape Town, as well as an increase in illegal hotels, under the guise of *Airbnb*. To deal with similar problems, most States in America have put in place the “primary residency rule”, which prohibits hosts from offering multiple listings that are not their primary residences. The recommendation was made that the adoption of a similar rule by South Africa could resolve the issues of high rentals and shortages in long-term rentals for residents in certain locations. Furthermore, an enactment like the one passed in Virginia would be commendable because it would clearly outline what the law is regarding the service. Such a law could also clarify what licences are needed, how to acquire them, what taxes must be paid, what fines and penalties are applied, and for what offences.

The chapter demonstrated that the current tax legislation has leakages that are causing SARS to lose potential revenue and this calls for regulation of the “sharing economy” businesses. Adopting the measures used in Australia and America could remedy the leakages in the system. Therefore, the legislature could start investigating ways to improve the tax and regulatory systems. Although the development of the necessary systems may prove to be costly, particularly in the early stages, the tax revenue gain should compensate for this over time. It would also send a message that tax evasion will be detected and penalised and, possibly, help to ease the present tensions between the “sharing economy” participants and traditional providers of these services.

The following chapter will provide a conclusion for the research.

CHAPTER 5: CONCLUSION

5.1 Introduction

Over the past three years there has been increased growth of the “sharing economy” in South Africa. The term “sharing economy” lacks a shared definition, but the research identified that the term comprises of digital platforms that operate as two-sided markets that match different groups of users and providers who want to share assets or services in exchange for a fee, typically by means of the Internet. “Sharing economy” activities comprise of several categories, however this thesis focused on “sharing economy” activities that involve the use of durable goods and other assets. *Uber*, *Airbnb* and their service providers in the Republic were the subjects of the investigation into the tax consequences of their business activities.

The research identified the problems being experienced in South Africa in effectively regulating participants in these new markets, based on current tax legislation. Additionally, the “sharing economy” business model moves faster than legislation can be promulgated, and this creates the opportunity for many of the participants in the “sharing economy” to slip through a legal loophole and avoid paying their taxes. It was acknowledged that the problems in taxing the “sharing economy” may be causing SARS to lose potential tax revenue. This motivated the research, and the primary goal was therefore to determine whether the services provided by the “sharing economy” platforms are adequately dealt with by the current South African tax systems.

This chapter will summarise the conclusions reached on chapters two to four as well as link these conclusions to the research goals.

5.2 “Gross income and the “sharing economy”

Chapter two involved an analysis of how the current tax systems deal with income accruing to *Uber*, *Airbnb* and their respective service providers. Chapter two briefly discussed the “gross income” definition in section 1 of the Income Tax Act, focusing on residence, source rules and what constitutes a “receipt” for purposes of “gross income”, in relation to taxing the proceeds from the “sharing economy” in South Africa. From this analysis the findings were that *Uber* drivers and *Airbnb* hosts who are ordinarily resident in the Republic will be “resident” for income tax purposes in South Africa in terms of the definition of a “resident” in section 1 of the Income Tax Act. The research indicated that it is possible that drivers and hosts may be residents of a foreign country, as well as residents in South Africa, based on the “days present”

test incorporated in the definition of a “resident”, and earning income from a South African source. The analysis established that in such cases the provisions of a DTA between South Africa and this foreign country would be relevant.

In the case of the residence of persons other than natural persons, it was established that *Uber* and *Airbnb* are not formed, established or incorporated in the Republic and do not have a place of effective management here. The discussion indicated that the people in *Uber* and *Airbnb* who are “calling the shots” and exercising “realistic positive management” are located in America and therefore the companies are “resident” in America. However, since *Uber* and *Airbnb* earn income from a South African source, this income was found to be subject to normal tax in South Africa, unless the right to tax the income is affected by the DTA between America and South Africa.³⁷⁰

The chapter analysed Article 7 and 5(2) of the DTA between South Africa and America. The research identified that Article 7 read with Article 5(2) of the DTA, gave South Africa the taxing rights on the profits *Uber* is earning in South Africa through a “permanent establishment” in South Africa. This is because *Uber* has a fixed “place of business” in the Republic, as it has offices located in Johannesburg and Cape Town. However, *Airbnb* does not have any premises or facilities from which it carries on business in South Africa. Thus, it is submitted that, since *Airbnb* does not have a “permanent establishment” in the Republic, South Africa does not have the right to impose tax on the commission income earned, despite it being from a South African source. The commission earned will be taxed in America.

Having established that *Uber*, *Uber* vehicle owners and *Airbnb* owners will be taxed either as residents or non-residents on income from a source in South Africa, the chapter examined the “gross income” definition, focusing on whether the amounts received constitute “receipts or accruals” for purposes of “gross income” as defined in section 1 of the Act. It was established that where the driver or host owns or rents the asset being used to provide the service, the driver or host would receive the income (or it would accrue) on his or her own behalf and benefit. This amount would therefore be included in the driver’s or host’s “gross income”, provided all the other elements of the “gross income” are satisfied. Where a person drives on behalf of the *Uber* vehicle owner, the payments received from the rides will be received by the vehicle owner on his own behalf and benefit. Where a rental agency acts on behalf of the *Airbnb* owner,

³⁷⁰ DTA between South Africa and America (1997) 6.

payments received from letting out the homes will be taxed in the hands of the owner, as they are received on his or her behalf and benefit.

Regarding the commission that *Uber* charges the drivers, the research ascertained that *Uber* receives this amount on its own behalf and for its own benefit as required by the definition of “gross income”. Additionally, in terms of Article 7 of the DTA, this amount is taxable in South Africa and the amount received is included in *Uber*’s “gross income”. In relation to the commission that *Airbnb* receives from hosts using its website and “app”, the research established that it is “received” for *Airbnb*’s own behalf and benefit. However, in terms of Article 7 read with Article 5(2) of the DTA, this commission will not be included in *Airbnb*’s South African “gross income” because the company does not have “permanent establishment” in the Republic. It is submitted that this commission will be taxed in America. The research also established that *Uber*, *Uber* drivers and *Airbnb* hosts are recipients of “amounts” that have a monetary value that is quantifiable. This “amount” received will be included in the driver’s or host’s “gross income”.

Having established the “gross income” of *Uber*, *Uber* drivers and the *Airbnb* hosts, the research concluded that there are no exemptions that would apply and therefore the “gross income” will constitute “income” as defined in the Income Tax Act.

5.3 The general deduction formula and the “sharing economy”

Chapter three sought to examine how the current income tax system deals with the deduction of expenses incurred by *Uber*, *Uber* drivers and *Airbnb* hosts and how “sharing economy” worker status affects deductibility of their expenses. Deductions are granted mainly in terms of the “general deduction formula”, which is set out in the preamble to section 11 and section 11(a), read with sections 23(f) and 23(g) of the Act.³⁷¹ In terms of the preamble to section 11, a person cannot claim a deduction unless they are “carrying on a trade”. The discussion established that the activities performed in the “sharing economy” can be regarded as “carrying on a trade” for purposes of section 11 of the Act.

Having satisfied this prerequisite, elements of the general deduction formula were analysed. The findings were that expenses or losses incurred from “sharing economy” activities can be regarded as “expenditure and losses” contemplated in section 11(a). The discussion indicated that *Uber*, *Uber* drivers and *Airbnb* hosts will be able to deduct expenses that are actually

³⁷¹ *Ibid.*

incurred, during the year of assessment, in the production on income, and are not of a capital nature, to the extent that they are laid out or expended for the purpose of trade. It was shown that *Uber*, the *Uber* driver and the *Airbnb* host may also claim the deduction of the cost of repairs and capital allowances on the property used to provide the services. Furthermore, it was shown that the driver and host may deduct assessed losses that they incur in carrying on their trades from taxable income in later years of assessment. In the case of natural persons and under certain circumstances, losses incurred by participants in the sharing economy may be “ring-fenced” in terms of section 20A of the Act.

Due to the “sharing economy” business model, which is based on the sharing of resources, expenses are often incurred for both business and personal purposes. The research established that where dual-purpose expenditure is incurred, the taxpayer must apportion the expenses, in terms of section 23(g), between business and personal use, with the business use portion being deductible.

Having established that the expenditure of the participants in the “sharing economy” may satisfy all elements of the general deduction formula, it became necessary to analyse the status of workers in the “sharing economy”. Their status may affect the deductibility of their expenses, their possible need to register as taxpayers and to pay provisional tax. The possible status of the participants as employees would imply that their “employers” would have responsibilities regarding employees’ tax. The chapter briefly discussed and applied tests used by our courts to distinguish between an “employee” and an “independent contractor” in relation to the service providers. From this analysis the control test demonstrated that *Uber* and *Airbnb* have sufficient control over the workers, instructing them what to do, when to do it and how they must perform their tasks. The “organisation” test established that the drivers and hosts are so integrated into the business of the companies as to be regarded as part and parcel of the companies. The test also established that the roles of the service providers are central to the operation of the companies, to an extent that the workers may be regarded as “employees” of the companies. The “dominant impression” test established that the drivers and hosts are subordinate to the will of the company in the manner they perform their duties and that the workers are solely dependent on the companies giving them access to the “app” and providing them with the ride or accommodation requests. The “dominant impression” test indicated that the workers are employees of the companies. It was found that the cumulative effect of these tests is persuasive for a conclusion that the workers are “employees” of *Uber* and *Airbnb* and

not independent contractors. *Uber* and *Airbnb* would therefore be required to register as employers and comply with the associated responsibilities.³⁷²

Having determined this employee status, the research discussed section 23(m) of the Act³⁷³, which prohibits employees receiving only salaries from claiming any expenditure other than those specifically listed in section 23(m).³⁷⁴ However, the research established that both *Uber* drivers and *Airbnb* hosts earn commission from the companies. In terms of section 23(m), if the commission earned by the taxpayer relates to any employment, the deduction of expenditure will only be allowed if the remuneration is mainly derived in the form of commission based on his or her sales.³⁷⁵ The research established that an *Uber* driver's or *Airbnb* host's income would probably constitute 100% of their total remuneration, meaning the prohibitions in section 23(m) would not apply to the driver or host. The driver or host would, however, still need to comply with the requirements of the "general deduction formula" to claim deductions. Finally, the chapter established that the *Airbnb* owner, *Uber* vehicle owner and *Uber* are liable for "income tax" in South Africa.

Being liable for "income tax", the chapter established that *Uber*, *Uber* drivers and *Airbnb* hosts must register as taxpayers with the Commissioner. The research established that, in terms of paragraph 23 of the Fourth Schedule, *Uber* is required to register as a provisional taxpayer with SARS, whereas the driver or host will only be required to register as a provisional taxpayer when his or her taxable income exceeds R30 000 per year. As was shown in chapter 3, *Uber* is liable for VAT, as a result it must keep records of supporting information for a period of five years. The *Uber* drivers and *Airbnb* hosts, like all other taxpayers, must retain records of income, dividends declared, assets owned and liabilities for a period of five years. The research established that non-compliance can result in the imposition of interest and penalties, and even imprisonment.³⁷⁶

5.4 Comparative analysis and the "sharing economy"

The chapter examined the problems South Africa is experiencing in taxing the "sharing economy", specifically the activities of *Uber*, the *Uber* driver and the *Airbnb* hosts. The chapter also made recommendations regarding the approach that could be applied in South Africa,

³⁷² Part II of the Fourth Schedule to the Income Tax Act 58 of 1962.

³⁷³ *Ibid.*

³⁷⁴ *Ibid.*

³⁷⁵ Fourth Schedule to the Income Tax Act 58 of 1962.

³⁷⁶ Bell "There are many pitfalls when it comes to provisional tax" 2013.

based on how Australian and American legislators dealt with the tax problems arising from the “sharing economy”. The research established that *Uber* is allegedly not paying corporate tax in South Africa. This because *Uber* is using of a “Double Dutch” system that renders its income invisible to SARS, even though the income is from a South African source. To remedy this, the research recommended that South Africa could adopt an approach like that applying in Australia, where SARS could request *Uber* to lodge its financial statements so that SARS has adequate information on how much profit *Uber* is earning and then levy the appropriate corporate tax on the amount.

Another problem identified by the research was that many of the drivers and hosts in South Africa may not be declaring their income to SARS. To remedy this, the research recommended that South African regulators could consider developing and implementing an E-tax data-matching program like the one used in Australia. Such a program is likely to be successful as the information would enable SARS to identify non-declarers and, furthermore, the knowledge of the existence of the program would encourage the declaration of income and help to prevent tax evasion. The second recommendation was that SARS could consider creating a website like the one used in America to help active participants in the “sharing economy” to be aware of the income tax consequences associated with their earning activities. It was found that such a website would be a valuable starting place for taxpayers and that it would help them with resources to understand their tax responsibilities.

A third problem identified by the research is that *Uber* is not charging its customers VAT on the fare charge, arguing that each of its drivers is a separate business, but each too small to register for VAT. It was established that *Uber* is exploiting loopholes in the law to avoid paying VAT and in the process depriving the *fiscus* of tax revenue. To remedy this, the research recommended that SARS could require the drivers to charge and collect the VAT on its behalf. SARS could also adopt the American approach of charging a tax specific to the “ridesharing” industry. Alternatively, SARS could task *Uber* to withhold VAT and pay it over to SARS. It was found that adopting similar measures would ensure compliance with tax provisions and would increase the tax base and consequently remedy the “leakage” in the current tax systems.

The research found that, in South Africa at present, taxation laws and other regulations apply differently to similarly situated companies, products and services and this results in unfair competition. *Uber* is engaging in unfair competition by not complying with the transport laws in relation to obtaining licences and operating permits. In relation to *Airbnb*, hosts are not using

appropriately zoned properties or applying for consent to let out the properties from the city of Cape Town's development management department and that *Airbnb's* non-regulation has a direct impact on the competing hotel industry performance. It was found that lack of proper regulation of the "sharing economy" in South Africa is causing the *fiscus* to lose potential tax revenue.

To remedy this problem a recommendation was made that South Africa could consider adopting legislation like that used in Virginia. This would clearly outline the boundaries within which all South Africans renting out their homes or bedrooms on platforms like *Airbnb* should operate. In adopting such legislation, SARS could include a "primary residence rule" to discourage hosts from purchasing investment properties to be used for short-term rentals only, unless they register as a bed-and-breakfast business. Alternatively, it was suggested that the South African regulators could consider creating a comprehensive law to encompass all sharing practices, instead of creating a separate law for each "sharing economy" model, such as ride-sharing, apartment-sharing, or other similar businesses which may come into existence in the future. It is submitted that creating a comprehensive law for this new class of "services" eliminates the need to find a place for "sharing economy" within existing laws.

Adopting the measures used in America and Australia could help to remedy the leakages the current tax systems suffer from that are causing SARS to lose potential revenue. The research also established that such measures could help to ease the present tensions between the "sharing economy" participants and traditional providers of these services.

5.5 Concluding remarks

It is clear that SARS may experience problems in implementing the above suggested proposals. Firstly, tax collection across all categories has slowed down in the past two years due to weak economic growth, administrative challenges and increased tax avoidance, leading to SARS experiencing revenue shortfalls.³⁷⁷ These revenue shortfalls have had a significant impact on SARS's budget and the Treasury has had to borrow to meet the shortfall.³⁷⁸ Since 90% of SARS's budget comes from revenue collection³⁷⁹, this means that SARS might experience financial difficulties in implementing the proposals to deal with the "sharing economy". For example, the thesis proposed the implementation of an E-tax data matching technology system,

³⁷⁷ S Menon SARS misses tax collection target 2018. Available: <http://www.heraldive.co.za/business/2018/04/03/sars-misses-tax-collection-target/> (Accessed 4 April 2018).

³⁷⁸ *Ibid.*

³⁷⁹ *Ibid.*

this system will require large sums of money, but with the current shortfalls such a system might not be developed and implemented soon.

Besides the financial issues, for the past two years SARS has suffered a “brain drain”, losing 39 senior managers and hiring 21 new senior managers.³⁸⁰ However, none of these new managers have any tax experience and this might be a challenge when trying to implement some of the suggested proposals. For example, implementing the E-tax data matching technology would require a highly skilled team and proper planning. Hiring unexperienced members of the SARS’s executive committee is therefore a disadvantage that might hinder or delay the development and installation of the proposed E-tax system. Inadequate qualifications by the executive committee can also negatively impact the proposed launching of a “sharing economy” tax centre and can result in a poorly drafted Bill, as the executive committee might fail to fully analyse possible issues that have to be included in the Bill. Additionally, these new appointments on the SARS executive committee might lead to failure by SARS to fully maintain their current operations and continually modernise tax laws that are required for SARS to remain a world class tax collection agency that is needed in South Africa today.³⁸¹

Despite the regulatory challenges and the difficulties that SARS might experience in trying to implement the suggested proposals, the “sharing economy” provides a wide range of benefits to the consumers and suppliers of the services. For workers the “sharing economy” may yield benefits relative to traditional employment in terms of ease of finding employment and greater flexibility to choose jobs and working hours. The “sharing economy” also provides opportunities to generate income when circumstances do not accommodate traditional full-time or full-year employment. The “sharing economy” has introduced ways to save money by eliminating costs associated with ownership; the business model focuses more of providing access to assets. The “sharing economy” business model has made it possible for individuals to secure valuable financial support for new businesses that may not have been fundable otherwise. In addition, the “sharing economy” also contributes to new experiences, new acquaintances, and the most importantly, the ability to get the service or good at a convenient time and in a convenient location.

³⁸⁰ F Haffajee “SARS Special Report: An Institution in Crisis as South Africa faces junk status 2017. Available: https://www.huffingtonpost.co.za/2017/04/03/sars-special-report-an-institution-in-crisis-as-south-africa-fa_a_22024086/ (Accessed 4 April 2018).

³⁸¹ M le Cordeur “Two more senior managers leave SARS, DA claims” 2017. News24. Available: <https://www.fin24.com/Economy/two-more-senior-managers-leave-sars-da-claims-20170417> (Accessed 5 April 2018).

While the “sharing economy” is still in its infancy, the potential it holds is substantial. With proper regulation, the “sharing economy” is a valuable addition to the economy of the South Africa.

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