

VAT implications of using the 'middle man'

Not all of us have the talent for the art of marketing and selling a product to a client. For this reason, an agent, or the proverbial 'middleman', is sometimes used to get the product from the producer to the buyer.



Questions that commonly arise:

What are the VAT implications of selling to the client through an agent if the producer is registered for VAT? What are the implications in the event that the agent is paid commission?

Let's look at the following example:

Fertiliser (Pty) Ltd produces fertiliser for the use of agricultural purposes by other persons (possibly persons involved in farming operations).

Fertiliser (Pty) Ltd uses Distributor (Pty) Ltd to sell their products to farmers because Fertiliser (Pty) Ltd feel that they do not possess the necessary knowledge, contacts and information with respect to prospective buyers in the market.

Though Distributor (Pty) Ltd does not include an extra levy for the product sales, they are entitled to a 2% commission on the sales.

What would the VAT implications of the above transaction between Fertiliser (Pty) Ltd and Distributor (Pty) Ltd be considering a product sold to the value of R100 under the conditions stated above? Let's suppose that both entities are registered for VAT.

VAT implications for Distributor (Pty) and Fertiliser (Pty) Ltd

Unless any other law is mentioned, all of the sections contained below will be applicable with reference to the Value-Added Tax Act No.89 of 1991.

1. If Distributor (Pty) Ltd acts on behalf of Fertiliser (Pty) Ltd, the underlying delivery to (or by) Distributor (Pty) Ltd will be deemed to be to (or by) Fertilizer (Pty) Ltd (s 54(1) and 54 (2)).
2. Fertilizer (Pty) Ltd will therefore be entitled to claim input tax and be liable to charge output tax. If goods are imported, it will also be deemed to be imported by Fertilizer (Pty) Ltd (s 54(2)(a)).
3. Any invoices received by Distributor (Pty) Ltd (or issued to farmers) should be in the name of Fertilizer (Pty) Ltd.
4. It is also possible for Distributor (Pty) Ltd to receive (or issue to farmers) documents in its own name (provisions of ss 54(1) and 54(2) and 54(2A)(a))
5. If a document is received in Distributor (Pty) Ltd's own name (or issued to the farmers), Fertilizer (Pty) Ltd must be notified in writing of the deliveries and Distributor (Pty) Ltd must keep sufficient records so that Fertilizer (Pty) Ltd's name, address and VAT number can be determined (a 54(3)).



6. However, in the case mentioned in point 5 above, it is not a requirement that the details of Fertilizer (Pty) Ltd appear on the underlying documents of the deliveries, but only that it be kept by Distributor (Pty) Ltd.
7. All VAT effects will still be accounted for by Fertilizer (Pty) Ltd and not by Distributor (Pty) Ltd. Fertilizer (Pty) Ltd will be entitled to claim input tax if Fertilizer (Pty) Ltd has the following required documentary evidence:
 - a tax invoice in the name of Fertilizer (Pty) Ltd (s 16(2)(e)), or
 - a statement from Distributor (Pty) Ltd (a Distributor (Pty) Ltd statement) on which deliveries to Distributor (Pty) Ltd are made on behalf of Fertilizer (Pty) Ltd (s 16(2)(e)), or
 - a transire (or other customs and excise duties) kept by Distributor (Pty) Ltd for which Fertilizer (Pty) Ltd received a Distributor (Pty) Ltd statement (s 16(2)(dA)).
8. The primary relationship between Distributor (Pty) Ltd and the farmer at the time of the fertilizer or product transaction is a very important element in the VAT chain.
9. Referring to the Supreme Court of Appeal ruling in 2005 between SARS and British Airways (www.justice.gov.za): Although the primary relationship between British Airways and the passenger existed, and not between Airports Company Limited and the passenger, the court was not affected by its ruling in the British Airways case. Airports Company Limited therefore had to levy VAT on the passenger service fee. SARS believed that Section 8(15) was applicable to the airplane ticket and that each part involved was a separate delivery. SARS held that the passenger service fee was a standard rate delivery. The court found that British Airways is not required to account for VAT on a service that it does not provide.
10. The principle described in the British Airways case determines that if Distributor (Pty) Ltd is reimbursed by Fertilizer (Pty) Ltd for any expenses incurred on behalf of Fertilizer (Pty) Ltd, Distributor (Pty) Ltd will not be liable for any resulting VAT because it is merely an expense that is being recovered for services rendered by another.
11. Distributor (Pty) Ltd will only have to pay VAT on any commission earned because such compensation is not earned on behalf of Fertilizer (Pty) Ltd, but in its own capacity.
12. Distributor (Pty) Ltd, if registered for VAT, will however be liable for output tax in respect of the R2 (2% commission fee charged on the R100 sales to the farmer) for services rendered to Fertilizer (Pty) Ltd as such services are in own capacity and not on behalf of Fertilizer (Pty) Ltd.
13. The output tax calculated will be R 0.26 (R2 x 15/115), and Fertilizer (Pty) Ltd will then charge input tax equal to R0.26 charged by Distributor (Pty) Ltd as output tax on the commission.

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14. Also note that in terms of Section 191 of the Tax Administration Act, the amount claimed from SARS is not considered repayable if it is less than R100, but the amount must be transferred to Fertilizer (Pty) Ltd's account.
15. Fertilizer (Pty) Ltd will also be entitled to claim input tax in respect of the delivery of any subcontractor used by Distributor (Pty) Ltd, on condition that Distributor (Pty) Ltd, upon receipt of the invoices, provides Fertilizer (Pty) Ltd with a Distributor (Pty) Ltd statement (s 54(2)).
16. The Distributor (Pty) Ltd statement will also serve as documentary proof of payment of input tax, regardless of the fact that the subcontractor's invoice is in the name of Distributor (Pty) Ltd.
17. Also note that Section 11(1) stipulates which delivery of goods will qualify as zero-rate deliveries.
18. In terms of Section 11(1)(g), the delivery of goods used for agricultural and other farming purposes, such as fertilizer, seeds, fodder, manure, etc., will be considered as zero-rate supplies.
19. Zero-rate deliveries are taxable supplies and a company can reclaim the input tax in respect of such deliveries.
20. Although VAT is levied at 0% by Fertilizer (Pty) Ltd on the delivery of fertilizer to farmers, the input tax may be claimed in respect of the deliveries.

The Delinquent Director

When consulting a dictionary, the word "delinquent" echoes words like "committing crimes", "lawless", "lawbreaking", "criminal", "offending" and "failing one's duty" – these are certainly not words we would want to use in the same sentence with "director". Therefore, it is vital for South African directors to take cognisance of the impact of Section 162 of the Companies Act, in order to not open themselves to the possibility of being declared a delinquent.

Who is a delinquent director? / What are the grounds for delinquency?

The Act provides for grounds on which applications may be brought to have someone declared a delinquent. If just one of the following criteria is met, the court has no discretion - a court must declare someone a delinquent director:

1. If the person has consented to serve as a director while being ineligible or disqualified of being such.

Examples are where the director: is an unrehabilitated insolvent; has been removed from office on the grounds of dishonesty; or has been convicted of crime, theft, fraud, forgery or any other conduct involving fraud, misrepresentation or dishonesty.

2. If, while under an order of probation, a person has acted as a director in a manner that contravenes that order.

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Up to this point one may think that these conditions are quite obvious, and that directors who subject themselves to this kind of conduct should not be directors. But the section continues to include some instances that may not be as obvious. A court must further also declare a director a delinquent if he/she has repeatedly been personally subject to a compliance notice or similar enforcement mechanism for substantially similar conduct in terms of any legislation. Another instance is in the case where the court is satisfied that the declaration of delinquency is justified, having regard to the nature of the contravention.

Effect/consequences of being a Delinquent Director

A declaration of delinquency may either be unconditional and will then subsist for the lifetime of the person OR a court may make it subject to any conditions the court considers appropriate, including a condition to limit the application to only certain categories of companies. This will depend on the grounds of delinquency.

Who may apply to court?

A company, shareholder, director, company secretary or prescribed officer of a company, a registered trade union, or any other representative of the employees of the company may apply to a court for an order to declare a director delinquent. In some instances, organs of state may also bring an application.

Oddly, creditors do not have the power to apply to a court to have a director declared delinquent.

It must also be kept in mind that a delinquent director is not prohibited from being a shareholder. Therefore, unfortunately, delinquents may still have influence in a company.

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