Issue 5

Guide on Determining the Market Value of Assets for Capital Gains Tax Purposes

Capital Gains Tax

South African Revenue Service

Guide on Determining the Market Value of Assets for Capital Gains Tax Purposes

Preface

This guide provides general guidance on determining the market value of assets for CGT purposes. It does not go into the precise technical and legal detail that is often associated with tax, and should not, therefore, be used as a legal reference. It is not an "official publication" as defined in section 1 of the Tax Administration Act 28 of 2011 and accordingly does not create a practice generally prevailing under section 5 of that Act. It is also not a binding general ruling under section 89 of Chapter 7 of the Tax Administration Act. Should an advance tax ruling be required, visit the SARS website for details of the application procedure.

For more information you may –

- visit the SARS website at **www.sars.gov.za**;
- visit your nearest SARS branch;
- contact your own tax advisor or tax practitioner;
- contact the SARS National Contact Centre –
  - if calling locally, on 0800 00 7277; or
  - if calling from abroad, on +27 11 602 2093 (only between 8h00 and 16h30 South African time).

Comments on this guide may be emailed to **policycomments@sars.gov.za**.

Leveraged Legal Products
SOUTH AFRICAN REVENUE SERVICE

Date of 1st issue	:	October 2001
Date of 2nd issue	:	February 2006
Date of 3rd issue	:	19 August 2015
Date of 4th issue	:	8 November 2018
Date of 5th issue	:	28 July 2021

Contents

Glossary

In this guide unless the context indicates otherwise –

- **"CGT"** means capital gains tax, being the portion of normal tax attributable to the inclusion in taxable income of a taxable capital gain;
- **"Eighth Schedule"** means the Eighth Schedule to the Act;
- **"Estate Duty Act"** means the Estate Duty Act 45 of 1955;
- **"*GG*"** means *Government Gazette*;
- **"JSE"** means the exchange operated by JSE Ltd which facilitates trade in securities under the style of 'Johannesburg Stock Exchange' and is licensed as an exchange under the Financial Markets Act 19 of 2012;
- **"paragraph"** means a paragraph of the Eighth Schedule;
- **"section"** means a section of the Act;
- **"Tax Administration Act"** means the Tax Administration Act 28 of 2011;
- **"the Act"** means the Income Tax Act 58 of 1962; and
- any other word or expression bears the meaning ascribed to it in the Act.

All guides, forms and tables referred to in this guide are available on the SARS website. Unless indicated otherwise, the latest issue of these documents should be consulted.

1. Introduction

Capital gains tax was introduced in South Africa with effect from 1 October 2001 and applies to the disposal of an asset on or after that date. A South African resident[1] is subject to CGT on the disposal of assets not only in South Africa, but anywhere in the world.[2] A non-resident is subject to CGT on the disposal of –

- any immovable property situated in South Africa held by the person;
- any interest or right of whatever nature to or in immovable property situated in South Africa including rights to variable or fixed payments as consideration for the working of, or the right to work mineral deposits, sources and other natural resources; and
- any asset effectively connected with a permanent establishment through which that non-resident is carrying on a trade in South Africa.[3]

A capital gain or capital loss on disposal or deemed disposal of an asset is determined during a year of assessment by subtracting its base cost from the proceeds. All capital gains and capital losses made on the disposal or deemed disposal of assets are subject to CGT unless specifically excluded. Once the capital gain or capital loss for each asset that is disposed during a year of assessment is determined, all capital gains or capital losses are added together or aggregated.

1 Definition of "resident" in section 1(1).
2 Paragraph 2(1)(*a*).
3 Paragraph 2(1)(*b*).

Section 26A provides that the taxable capital gain must be included in taxable income. CGT is therefore not a separate tax but forms part of income tax. A capital loss cannot be used to reduce taxable income. Such loss can only be set off against future capital gains.

The CGT provisions are mostly contained in the Eighth Schedule, although some are in the main body of the Act, such as those dealing with change of residence, ceasing to be a controlled foreign company or becoming a headquarter company (section 9H), disposals by deceased persons (section 9HA), government grants (section 12P), international shipping (section 12Q) and the corporate restructuring rules (sections 41 to 47).

2. Determining a capital gain or capital loss

The Eighth Schedule contains four key definitions (Asset, Disposal, Proceeds and Base Cost) which form the basic building blocks in determining a capital gain or capital loss. Valuation of an asset is relevant especially in determining its base cost at valuation date or its base cost or proceeds when an asset is deemed to be acquired or disposed of at market value.

A person's capital gain on disposal of an asset is the amount by which the proceeds exceed the base cost of that asset.[4] A capital loss is equal to the amount by which the base cost of the asset exceeds the proceeds.[5]

Example 1 – Determination of a capital gain or capital loss

	Gain R		Loss R
Proceeds	10 000	Proceeds	10 000
Less: Base cost	(5 000)	*Less*: Base cost	(20 000)
Capital gain	5 000	Capital loss	(10 000)

2.1 Asset

An "asset" is widely defined[6] and includes property of whatever nature, whether movable or immovable, corporeal or incorporeal and any right to, or interest in, such property. Any currency is excluded from the definition of "asset", but any coin made mainly from gold or platinum is included. CGT applies to all assets disposed of on or after 1 October 2001 (valuation date), regardless of whether the asset was acquired before, on, or after that date.

Nevertheless, only the capital gain or capital loss attributable to the period on or after 1 October 2001 must be brought to account for CGT purposes.

4 Paragraph 3.
5 Paragraph 4.
6 Paragraph 1.

2.2 Disposal

A wide meaning is given to the term "disposal". The Eighth Schedule provides for both disposals and deemed disposals.[7] A disposal covers any event, act, forbearance or operation of law which results in the creation, variation, transfer or extinction of an asset or any event, act, forbearance or operation of law which is under the Act treated as the disposal of an asset. The following are examples of some events that are disposals or that are treated as disposals:

- Sale of an asset
- Donation of an asset
- Expropriation of an asset
- Loss or destruction of an asset
- Change in the use of an asset
- A company ceasing to be a controlled foreign company otherwise than by way of becoming a resident
- A person ceasing to be a resident
- A company becoming a headquarter company

Certain events are not regarded as disposals, but are not dealt with in this guide.[8]

The Eighth Schedule specifies the time of disposal of an asset.[9] For different types of disposal the timing of the disposal may be different. For example, when an asset is disposed of under an agreement which is subject to a suspensive condition, the time of disposal is when the condition is satisfied. When the agreement is not subject to a suspensive condition, the time of disposal is when the agreement is concluded. The time of disposal is important, since it determines when the capital gain or capital loss must be accounted for.

2.3 Proceeds

The amount received by or accrued to the seller on disposal of an asset or any amount that is treated as having been received by or accrued to the taxpayer (deemed disposal) constitutes the proceeds.[10]

Assets disposed of by donation, for a consideration not measurable in money, or to a connected person at a non-arm's-length price are treated as being disposed of for an amount received or accrued equal to the market value of the asset.[11]

[7] Paragraphs 1 and 11.
[8] See paragraph 11(2) for events that are not a disposal of an asset.
[9] Paragraph 13.
[10] Paragraph 35.
[11] Paragraph 38(1)(*a*).

Proceeds will also be treated as being at market value when specified deemed disposal events occur, such as –

- a person ceasing to be a resident, a company ceasing to be a controlled foreign company otherwise than by way of becoming a resident or a company becoming a headquarter company;[12]
- a deemed disposal of shares by a person holding at least 10% of the equity shares and voting rights in a company ceasing to be a resident, if specified requirements are met;[13]
- the distribution of an asset *in specie* by a company to a holder of its shares;[14]
- a person commencing to be a resident or a foreign company becoming a controlled foreign company;[15]
- an asset ceasing to be part of a non-resident's permanent establishment in South Africa, otherwise than by disposal under paragraph 11;[16]
- conversion of a capital asset to trading stock;[17]
- an asset that becomes a personal-use asset;[18] and
- upon the death of a person.[19]

Amounts included in income or gross income such as a recoupment of capital allowances or dividends constituting a share buy-back are excluded from proceeds.[20]

2.4 Base cost

Broadly, the determination of the base cost of an asset depends on whether the asset was acquired –

- before 1 October 2001;
- on or after 1 October 2001;
- by donation, for a consideration not measurable in money or from a connected person at a non-arm's length price; or
- in consequence of a deemed disposal event such as a distribution of an asset *in specie*, a person ceasing to be a resident, a company ceasing to be a controlled foreign company, a company becoming a headquarter company or the conversion of a capital asset to trading stock.

The date of 1 Oktober 2001 is generally the valuation date (see below).

12 Section 9H(2) and (3).
13 Section 9H(3A).
14 Paragraph 75(1).
15 Paragraph 12(2)(*a*).
16 Paragraph 12(2)(*b*).
17 Paragraph 12(2)(*c*).
18 Paragraph 12(2)(*e*).
19 Section 9HA.
20 Paragraph 35(3)(*a*).

Pre-valuation date assets

The base cost of an asset acquired before valuation date is equal to its valuation date value plus any further allowable expenditure incurred on or after the valuation date under paragraph 20.[21]

The valuation date is generally 1 October 2001 but for certain previously exempt entities it can be a later date, namely when it became partially taxable (that is, when it falls outside paragraph 63).[22]

For example, the valuation date of a public benefit organisation approved by the Commissioner under section 30(3) is the first day of its first year of assessment commencing on or after 1 April 2006.[23] The valuation date of a recreational club which applied for approval under section 30A on or before 31 March 2009 is the first day of its first year of assessment ending on or after 1 April 2007.[24] A recreational club approved under section 10(1)(*d*)(iv) that failed to apply for approval under section 30A by 31 March 2009 will have a valuation date equal to the first day of its first year of assessment ending after 30 September 2010.[25]

Three methods[26] are potentially available for determining the valuation date value of a pre-valuation date asset, namely –

- 20% × (proceeds less allowable expenditure incurred on or after valuation date) (generally used when no records of expenditure incurred before valuation date have been kept and no valuation was obtained at valuation date);
- market value (see **4.**); or
- time-apportionment (this method of calculating the value of the asset takes into account how long the asset was owned before and after valuation date).

Post-valuation date assets

The base cost of an asset acquired on or after valuation date is generally equal to the qualifying expenditure under paragraph 20, which includes amongst other things, the cost of acquiring or improving the asset and specified costs of acquisition and disposal.[27] In some situations, however, a post-valuation date asset will be deemed to be acquired at market value, such as when it is –

- acquired by donation, for consideration not measurable in money, or at a non-arm's length price from a connected person;[28]
- acquired by inheritance from a deceased estate on the date of death of the testator;[29]
- acquired by inheritance if the asset is treated as having been disposed of by a deceased person under section 9HA(1) and is transferred directly to an heir or legatee of that person;[30]

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21 Paragraph 25.
22 Definition of "valuation date" in paragraph 1.
23 Definition of "valuation date" in paragraph 1 read with paragraph 63A.
24 Definition of "valuation date" in paragraph 1 read with section 30A.
25 Definition of "valuation date" in paragraph 1 read with section 30A. See the *Comprehensive Guide to Capital Gains Tax* in Chapters 4 and 8 for detailed commentary in this regard.
26 Paragraph 26.
27 See paragraph 20(2) for expenditure that is not included in base cost.
28 Paragraph 20(1)(*h*)(vi) (acquisition from non-resident) and paragraph 38.
29 Paragraph 20(1)(*h*)(v) (acquisition from non-resident deceased estate) and section 25(3)(*b*).
30 Section 9HA(3).

- acquired by a creditor from a debtor that reduces or discharges a debt owed by the debtor to the creditor by disposing of the asset to the creditor;[31]
- an asset that is held by a person otherwise than as trading stock, which commences to be held by that person as trading stock;[32] and
- acquired by distribution *in specie* from a company.[33]

3. Meaning of market value

Paragraph 29 contains special rules for determining the market value of specified assets on valuation date (see **4.**). These special rules do not cover all assets and are essentially an anti-avoidance measure aimed at selected assets whose values are susceptible to manipulation.

The term "market value" is defined in paragraph 1 and means –

> "market value as contemplated in paragraph 31".

Paragraph 31 provides the general rules on how "market value" as defined is to be determined in respect of those assets not covered by paragraph 29 as well as in other situations (see **5.**).

The market value of an asset is the best price at which an interest in the asset would have been sold unconditionally for a cash consideration on the date of valuation assuming –

- a willing seller (under no duress at all);
- that, before the date of valuation, there had been a reasonable period (having regard to the nature of the asset and the state of the market) for the proper marketing of the interest and for the sale to be concluded;
- that no account is taken of any additional bid by a prospective purchaser with a special interest;
- a sale either –
  - ➢ of the asset as a whole for use in its working place; or
  - ➢ of the asset as a whole for removal from the premises of the seller at the expense of the purchaser; or
  - ➢ of individual items for removal from the premises of the seller at the expense of the purchaser; and
- that both parties to the transaction had acted knowledgeably, prudently and without compulsion.

[31] Paragraph 34 applies with effect from 20 January 2021.
[32] Paragraph 12(2)(*c*).
[33] Paragraph 75.

4. Market value of assets on valuation date

Paragraph 29 contains a number of transitional measures which apply to the valuation of assets on 1 October 2001. To the extent that paragraph 29 does not apply, the provisions of paragraph 31 will apply (see **5.**).

4.1 Time limit for performing valuations and circumstances when market value may be applied

Paragraph 29(4) stipulates that for the purposes of paragraphs 26(1)(*a*) and 27(3), a person may only adopt or determine the market value as the valuation date value of an asset if specified requirements are met.

Under paragraph 29(4)(*a*)(i) valuations as at 1 October 2001 were required to be carried out by 30 September 2004.[34] A public benefit organisation or recreational club may not adopt or determine the market value of an asset unless it has valued the asset within two years from the valuation date.[35]

Failure to comply with the time periods for performing valuations means that the market-value method cannot be used to determine the valuation date value of the asset.

The asset must have been valued according to the factors prevailing on valuation date such as its condition at the time and prevailing economic conditions.

The requirement to value assets by 30 September 2004 does not apply to those assets whose prices as at 1 October 2001 were published in the *Government Gazette* such as shares listed on the JSE and participatory interests in collective investment schemes.[36] A company is required to use these prices and therefore does not need to determine its own values for these assets. The prices are also available on the SARS website.[37] Similarly, public benefit organisations and recreational clubs are not subject to a time limit for valuing financial instruments listed on a recognised exchange or participatory interests in collective investment schemes in securities or property.[38]

A person may adopt or determine the market value as the valuation date value of that asset if that person acquired that asset from that person's spouse under section 9HB and the transferor spouse had adopted or determined a market value in terms of this paragraph, and for this purpose the transferee spouse must be treated as having adopted or determined that same market value.[39]

4.2 Persons who may perform valuations

The Act does not prescribe who may perform valuation of assets. This task is the responsibility of the taxpayer and the onus of substantiating a valuation rests with the taxpayer (see **4.6**). The taxpayer may, however, appoint a professional person to assist with a valuation.

34 This deadline was originally 30 September 2003 but was extended to 30 September 2004 by the Minister of Finance in *GG* 26026 of 20 February 2004.
35 Paragraph 29(4)(*b*)(i).
36 Paragraph 29(4)(*a*)(ii).
37 Prices supplied in *GG* 23037 of 25 January 2002.
38 Paragraph 29(4)(*b*)(ii).
39 Paragraph 29(4)(*a*)(iii).

4.3 Methods to be adopted in valuing specified assets

The table below sets out the methods stipulated in paragraph 29 for valuing assets on valuation date.

Table 1 – Market values on 1 October 2001

Paragraph 29	**Type of asset**	**Market value**
(1)(*a*)(i)	Financial instruments listed on a recognised exchange in South Africa[40]	Prices supplied in *GG* 23037 of 25 January 2002 and on SARS website. Price based on five business days preceding 1 October 2001.
(1)(*a*)(ii)	Foreign financial instruments listed on a recognised exchange outside South Africa[41]	The ruling price on that recognised exchange on the last business day before 1 October 2001.
(1)(*b*)(i)	Participation rights and property shares in South African collective investment schemes	Average "sell" price for the last five trading days before 1 October 2001. Prices supplied in the *Government Gazette.*
(1)(*b*)(ii)	Participation rights in foreign collective investment schemes	Same as for South African collective investment schemes, except based on last trading day before 1 October 2001. If no price quoted, the price which could have been obtained upon a sale of the asset between a willing buyer and a willing seller dealing at arm's length in an open market on 1 October 2001.
(1)(*c*)	Any other asset	The market value determined under paragraph 31 (see **5.**).
(2) and (3)	Controlling interest in a listed company	Control premium / discount determined on disposal and applied to listed price at 1 October 2001 (see conditions below and Example 1 in the Annexure).

40 Definition of "recognised exchange" in paragraph 1. Currently JSE, ZARX (Pty) Ltd (ZAR X), 4 Africa Exchange (Pty) Ltd (4AX), A2X Markets (Pty) Ltd (A2X) and Equity Express Securities Exchange (Pty) Ltd (EESE) are licenced under the Financial Markets Act 19 of 2012.

41 Definition of "recognised exchange in paragraph 1. The list of recognised exchanges in countries outside South Africa was published in Government Notice R 997 in *GG* 22723 of 2 October 2001 and Government Notice 1088 in *GG* 30484 of 16 November 2007 and is also available on the SARS website.

Valuing a controlling interest in a listed company under paragraph 29(2)

A holder of shares must value a controlling interest in a company in the manner described in paragraph 29(2) if –

- the company is listed on a recognised exchange;
- the entire controlling interest is disposed of to a person who is not a connected person in relation to the seller and the acquirer acquires the entire controlling interest; and
- the controlling interest comprises more than 35% of the company's equity shares.[42]

A controlling interest in a listed company usually gives the shareholder the right to appoint the board of directors, pass resolutions and generally control the direction of the company. A person acquiring such an interest will usually pay a premium for the privilege, though in some instances it can happen that the shares will be disposed of at a discount. If such an interest were to be valued according to the normal prices quoted on an exchange, the result in most situations would be that the base cost of the shares would be understated. In order to avoid the problems inherent in valuing such an interest on valuation date, the premium or discount must be determined at date of disposal by comparing the actual selling price with the price quoted the day before the announcement of the disposal. This premium or discount is then applied to the base cost of the shares disposed of.

It is not a requirement of paragraph 29(2) that the holder of shares must hold the controlling interest on valuation date. For example, a person may hold an interest of 25% on valuation date and acquire a further 11% interest after that date. In such event the adjustment to the valuation date market value must be applied to the pre-valuation date interest of 25%. The base cost of the post-valuation date interest of 11% remains unaffected by this adjustment, being determined under paragraph 20 or 38.

Valuing a controlling interest in an unlisted company under paragraph 31(3)

The market value of a controlling interest in an unlisted company must be determined in accordance with paragraph 31(3), namely, the price a willing buyer would pay a willing seller with both parties dealing at arm's length in an open market, but disregarding any transferability restrictions or valuation method stipulations, and taking into account any preferential entitlement upon winding-up (see **5.** and **6.**).

Identical assets (paragraph 32)

Paragraph 32[43] contains the rules for determining the base cost of assets forming part of a group of similar assets (identical assets).[44] Such assets are sometimes referred to as fungible assets. When an asset of this nature is sold, it may not be possible to physically identify the particular asset that is being disposed of. Hence, it is necessary to lay down identification rules. Examples include Krugerrands, participatory interests in portfolios of collective investment schemes and shares.

42 Definition of "controlling interest" in paragraph 29(3).
43 See the *Comprehensive Guide to Capital Gains Tax* in Chapter 8 for detailed commentary on identical assets.
44 Definition of "identical assets" in paragraph 32(2).

As far as pre-valuation date assets are concerned, it is important to understand the relationship between the asset identification methods in paragraph 32 and the methods prescribed for determining valuation date values in paragraphs 26, 27 and 28. Paragraph 32, apart from specifying identification methods, also prescribes a valuation date value method, namely, weighted average. The relationship can be summarised as follows:

Table 2 – Asset identification methods that can be used with selected valuation date value methods

Valuation date value method	Permissible Identification method
Market value	Specific identification or FIFO[45]
Time-apportionment base cost	Specific identification or FIFO[46]
20% × (proceeds less allowable expenditure incurred on or after valuation date)	Not applicable – identification of pre-CGT costs is not required for this method
Weighted average	Weighted average. On valuation date the result is the same as the market-value method. Once additions take place after valuation date, the two methods yield different results.

4.4 Submission and retention requirements in specific cases

The requirements for submission of the prescribed valuation forms (CGT 2L if completed after 30 September 2004 or CGT2 if completed before that date) and related particulars are set out in paragraph 29(5) and (6).

High value assets [paragraph 29(5)]

For specified assets the valuation forms were required to be lodged with the first return of income submitted after 30 September 2004, irrespective of whether the relevant assets had been disposed of. If not so submitted, market value may not be used as the valuation date value for these assets. These categories of assets are set out in the table below (see also Example 2 in the Annexure).

Table 3 – Submission requirements for high value assets

Type of asset	Applies	Market value exceeds
Intangible assets (such as goodwill and trade marks)	Per asset	R1 million
Unlisted shares	All shares held by the person in the company	R10 million
All other assets	Per asset	R10 million

45 First-in-first-out.

46 See above.

Other assets [paragraph 29(6)]

It is not required that the valuation form be submitted with the return of income reflecting the disposal of the asset mentioned above or any other asset which has been valued. Proof of the valuation must, however, be retained and submitted when called upon by SARS to do so.

Retention of documents

The periods for which the valuation forms and any related valuation documentation must be retained are set out in section 29 of the Tax Administration Act.

A person who has submitted a return of income reflecting a capital gain or capital loss must retain records, books of account or documents supporting the determination of that capital gain or capital loss for a period of five years from the date of submission of the return.

A person who is required to submit a return but has not done so will have to retain the relevant records for at least five years after the date on which the return is eventually submitted.

A person who is not required to submit a return under the criteria set out in the annual notice to furnish returns, for example, because a resident natural person had capital gains or capital losses during the 2021 year of assessment which did not exceed R40 000,[47] must retain the records pertaining to any capital gain or capital loss for at least five years from the end of the year of assessment in which the asset was disposed of.

4.5 Loss limitation rules

Paragraphs 26 and 27 contain rules to limit losses when the market-value method is used to determine the valuation date value of an asset. Paragraph 26 deals with valuation date value when proceeds exceed expenditure or when expenditure relating to an asset cannot be determined. Paragraph 27 deals with the valuation date value when proceeds do not exceed expenditure. These rules are designed to prevent the creation of phantom losses arising from inflated valuations, but apply equally when the valuation is realistic and the market value exceeds the proceeds. For more information see the *Comprehensive Guide to Capital Gains Tax* in Chapter 8.

4.6 Burden of proof

Under section 102(1)(*e*) of the Tax Administration Act, the taxpayer bears the burden of proving that a valuation is correct.

The fact that a valuation was done by a qualified valuer will not prevent the Commissioner from verifying or auditing the valuation. The Commissioner may, if dissatisfied with a valuation –

- request further information or documents relating to the valuation;[48] or
- adjust the valuation.[49] The Commissioner's right to adjust the valuation is subject to objection and appeal.[50]

47 See the annual notice to furnish returns. The notice for the 2021 year of assessment was published in Government Notice 419 in *GG* 44571 of 14 May 2021.
48 Paragraph 29(7)(*a*).
49 Paragraph 29(7)(*b*).
50 Section 3(4)(*h*).

The following are some common examples of the information which the Commissioner may require:

Residential property

- Valuer's valuation, including basis of the valuation and calculations
- Physical address
- Size of property
- Details of improvements to the property
- Plans of the property as at 1 October 2001
- Details of recent property sales in the same area
- Municipal valuation of the property
- Any other information which may be relevant

See **6.** for commentary on Case Law dealing with the valuation of a residence.

Farming property

- The detail requested in the Land Bank questionnaire used for valuing immovable property on which *bona fide* farming operations are carried on is a useful aid when farm land is valued using the market-value method.
- As from 1 February 2006, Land Bank valuations no longer apply and the market value must be the fair market value as per paragraph (*b*) of the definition of "fair market value" in section 1(1) of the Estate Duty Act, namely, the price that could be obtained between a willing buyer and willing seller dealing at arm's length in an open market, less 30% (see also **5.** and the *Comprehensive Guide to Capital Gains Tax* in Chapter 8).

Mineral rights

- Valuer's valuation, including basis of valuation and calculations
- The description of the mineral right and its registered number at the Deeds Office
- Type of mineral
- Location and extent of mineral right
- Exploitation of mineral right as at 1 October 2001
- Original cost of mineral right
- Quantification of reserves still to be mined
- Remaining life of mine
- If exploitation has not commenced, details and results of prospecting undertaken as at 1 October 2001
- Department of Minerals and Energy valuation
- Any other information which may be relevant

A mineral right is a capital expense to a mining company but a revenue expense to a prospecting or exploration company. Only companies involved in mining activities, or which intend mining any areas covered by mineral rights which they possess, are required to value their mineral rights for CGT purposes.

Unlisted shares

- Valuer's valuation, including basis of valuation and calculations

  The method used will depend on, amongst other things, the degree of control which the particular block of shares enables the holder to exercise over the affairs of the company, which may vary from full control to a small or non-existent influence.

  Possible valuation methods include the following:

  - Dividend-based valuations may be used for minority holdings when the company has a history of paying dividends.
  - Earnings-based minority holding valuations may be used in cases of influential minority holdings (concentrating on net earnings per share and price earnings ratios).
  - Earnings-based whole company valuations for majority holdings (concentrating on maintainable pre-tax profits, a capitalisation factor and a discount which takes cognisance of the size of the shareholding).
- Proof of shareholding.
- Full description of the business carried on by the company.
- The company's annual financial statements for the last three years before the valuation date.
- If there are different classes of shares, documentation proving the rights of each class, in particular those concerning voting, dividends and distributions on liquidation of the company.
- Any other information which may be relevant.

See also **6.** for commentary on Case Law dealing with the valuation of unlisted shares.

5. Market value of assets otherwise than on valuation date

The permanent market valuation rules, as opposed to the transitional market valuation rules on valuation date, are contained in paragraph 31 and are summarised in the table below.

These rules apply to the following:

- Pre-valuation date assets not covered by the transitional valuation rules [paragraph 29(1)(*c*)].
- Specified events or deemed acquisitions (see **2.4**) or deemed disposals (see **2.3**) at market value, such as the following:
  - A person ceasing or commencing to be a resident. Persons that become resident are deemed to dispose of and reacquire their assets (except specified assets that were subject to tax in South Africa before they became resident) at market value under paragraph 12(1). Paragraph 24 contains rules which limit the base cost so arrived at in order to prevent phantom losses. Paragraph 24 applies when a person becomes a resident on or after 1 October 2001 and disposes of an asset acquired before that person became a resident.
  - Death of a person (paragraph 9HA).
  - Donation of an asset, an asset disposed of for a consideration not measurable in money or connected person transactions at a non-arm's length price [paragraph 38(1)].

- Assets acquired or disposed of by distribution *in specie* (paragraph 75).

Table 4 – Market values otherwise than on valuation date

Paragraph 31	**Type of asset**	**Market value**
(1)(*a*)	Financial instrument listed on a recognised exchange	The ruling price at close of business on the last business day before disposal.
(1)(*b*)	Long-term insurance policy[51]	Greater of – • surrender value; and • insurer's fair market value (assume policy runs to maturity).
(1)(*c*)(i)	Participation right in a portfolio of a collective investment scheme in securities or property carried on in South Africa	Management company's repurchase price.
(1)(*c*)(ii)	Participation right in a foreign collective investment scheme which is comparable to a collective investment scheme in participation bonds or securities	Management company's repurchase price or, if not available, selling price based on willing buyer, willing seller dealing at arm's length in an open market.
(1)(*d*) read with (2)	Fiduciary, usufructuary and other like interests	Present value of future benefits discounted at 12% a year over the life expectancy[52] of the person entitled to the asset or a lesser period of enjoyment. The Commissioner may approve less than 12% if justified (see Example 3 in the Annexure).
(1)(*e*)	Property subject to a fiduciary, usufructuary or other like interest	Market value of full ownership, less the value of the fiduciary, usufructuary or other like interest as determined above
(1)(*f*) read with (4)[53]	Immovable property on which a *bona fide*	• Market value less 30% [paragraph 31(*f*)(i)];[54] or

51 Definition in section 1 of the Long-term Insurance Act 52 of 1998.
52 See paragraph 31(2)(*b*).
53 See the *Comprehensive Guide to Capital Gains Tax* in Chapter 8 for detailed commentary on paragraph 31(1)(*f*) and (4). The purpose of paragraph 31(4) is to ensure that the method used for determining the consideration received or accrued on disposal of an asset under section 9HA or paragraph 38 is the same as the method used in determining its base cost under section 25 or paragraph 26, 27 or 38.
54 As determined under paragraph (*b*) of the definition of "fair market value" in section 1(1) of the Estate Duty Act.

Paragraph 31	Type of asset	Market value
	farming undertaking is carried on	• Price based on willing buyer, willing seller dealing at arm's length in an open market [paragraph 31(*f*)(ii)]. As from 1 February 2006 the value in paragraph 31(*f*)(i) must be the fair market value as per paragraph (*b*) of the definition of "fair market value" in section 1(1) of the Estate Duty Act, namely, the price that could be obtained between a willing buyer and willing seller dealing at arm's length in an open market, less 30%. In the case of a farm acquired before valuation date and disposed of by way of death, donation or non-arm's length transaction on or after 1 February 2006, the Land Bank value on 1 October 2001 must be used as the valuation date value if "market value less 30%" is used to determine proceeds [paragraph 31(4)(*a*)]. Paragraph 31(4)(*b*) applies to farming property acquired on or after valuation date which is disposed of by way of death, donation or non-arm's length transaction. Market value less 30% may be used to determine the consideration received or accrued under section 9HA or paragraph 38 only if the property was acquired by way of inheritance, donation or non-arm's length transaction at Land Bank value (before 1 February 2006) or "market value less 30%" (on or after 1 February 2006).
(1)(*g*)	Any other asset	The price which could have been obtained upon a sale of the asset between a willing buyer and a willing seller dealing at arm's length in an open market.
(3)	Unlisted shares	The price which could have been obtained upon a sale of the share between a willing buyer and a willing seller dealing at arm's length in an open market subject to the following: • No regard shall be had to any provision – ➢ restricting the transferability of the shares, and it shall be

Paragraph 31	Type of asset	Market value
		assumed that those shares were freely transferable; or ➢ whereby or whereunder the value of the shares is to be determined. • If upon the winding-up of the company that person would have been entitled to share in the assets of the company to an extent that is not in proportion to that person's holding of shares, the value of the shares held by that holder of shares must not be less than the amount to which that holder of shares would have been so entitled if the company had been in the course of winding-up and the said amount had been determined as at valuation date. The valuation may reflect the extent to which a potential buyer of the shares can control or influence the company. To determine the market value of different classes of shares held in an unlisted company, the facts of each case have to be considered. Factors to be considered are, amongst others, the preferences, rights, limitations or other terms of a class or classes of shares, as set out in a company's Memorandum of Incorporation which is issued or amended under the Companies Act 71 of 2008, or if not so issued or amended under that Act, as set out in the Company's Memorandum of Incorporation, Articles of Association, shareholders agreements and resolutions issued, amended or entered into under the Companies Act 61 of 1973 or 46 of 1926, directors' resolutions and previous distributions of dividends.

6. Case law

Valuation of unlisted shares

In *C: SARS v Stepney Investments (Pty) Ltd*[55] the taxpayer company had disposed of a 4,37% interest in a company in two tranches during the 2002 and 2003 years of assessment. The taxpayer had used the market-value method to determine the valuation date value of the shares. Since the proceeds on disposal of the shares were less than the market value established by the taxpayer, a capital loss had arisen which was eliminated by paragraph 26(3). All shares in the company had been valued by the taxpayer using the "discounted cash flow" basis with the market value of its holding being determined by multiplying the total value by the percentage holding. The Commissioner adjusted the market value of the shares disposed of under paragraph 29(7)(*b*) to nil. The Memorandum of Incorporation of the company in which the shares were held described its main object as developing, owning, operating and conducting the business of casinos, hotels and related leisure ancillary activities. The company was awarded a casino licence on 21 October 2000 by the KZN Gambling Board which gave it an exclusive right to operate a casino for 15 years in the Richards Bay area. After the licence was awarded, a religious group objected to the proposed location of the casino and the company obtained an alternative temporary venue in Empangeni for which it was granted a temporary licence on 4 October 2001. The objection brought by the religious group did not succeed after valuation date. The Commissioner valued the shares on the net asset value basis, arguing that the shares had a value of nil. The Commissioner's valuation took into account the various uncertainties that existed on valuation date. Having lost in the tax court the Commissioner took the matter on appeal to the Supreme Court of Appeal (SCA). In the SCA the Commissioner conceded that the net asset value method was inappropriate but challenged the taxpayer's valuation as being defective on a number of grounds. It then fell to the SCA to evaluate the conflicting opinions of the experts called by SARS and the taxpayer. On the question of relying on the evidence of experts the court cited the following dictum of Wessels JA in *Coopers (SA) (Pty) Ltd v Deutsche Gesellschaft Für Schädlingsbekämfung MBH*:[56]

> "As I see it, an expert's opinion represents his reasoned conclusion based on certain facts [or] on data, which are either common cause, or established by his own evidence or that of some other competent witness. Except possibly where it is not controverted, an expert's bald statement of his opinion is not of any real assistance. Proper evaluation of the opinion can only be undertaken if the process of reasoning which led to the conclusion, including the premises from which the reasoning proceeds, are disclosed by the expert."

The court also cited Addleson J in *Menday v Protea Assurance Co Ltd*:[57]

> "It is not the mere opinion of the witness which is decisive but his ability to satisfy the Court that, because of his special skill, training or experience, the reasons for the opinion which he expresses are acceptable . . . the Court, while exercising due caution, must be guided by the views of an expert when it is satisfied of his qualification to speak with authority and with the reasons given for his opinion."

55 2016 (2) SA 608 (SCA), 78 SATC 86.
56 1976 (3) SA 352 (A) at 371 F–H.
57 1976 (1) SA 565 (E) at 569B–E.

Next, the court proceeded to examine the various assumptions underpinning the valuation:

- The future forecast free cash flows – The valuation was performed in 2004 but the taxpayer had relied on estimates submitted to the Gambling Board around 2001 despite being aware that the earlier estimates were substantially overstated. The valuer also disregarded a letter dated 20 March 2003 submitted to the Gambling Board which painted a bleak picture of the company's profitability. The court rejected the taxpayer's argument that to take into account subsequent events would have amounted to valuing the shares with hindsight. It noted that a valuer cannot just blindly accept figures presented to him or her and has a duty to assess their reasonableness and correctness. The valuer was duty bound to evaluate the soundness of management's projections and it was wrong not to take the later information into account.
- Starting date for valuation – The valuer used 1 March 2002 instead of 1 October 2001 which had an adverse impact on the valuation.
- Tax estimates – Incorrect figures had been used by the valuer.
- Projected capital expenditure – The projected capital expenditure was significantly understated.
- Terminal value – The terminal value had been based on discounting into perpetuity while the licence had a lifespan of 15 years. The risk of non-renewal or the costs of submitting a renewal application should have been taken into account.
- Discount factor – The discount rate used of 20,86% was used in valuing all the entities in the group and did not take into account the specific circumstances of the casino in question which was a start-up and not an established business.

In the result the court found that the valuation was fatally flawed in respect of the matters listed above. It noted that a court is entitled to reject a valuation if it is not satisfied with the investigations underpinning it and cited the following words of Denning LJ in *Dean v Prince*:[58]

> "For instance, if the expert added up his figures wrongly, or took something into account which he ought not to have taken into account, or conversely, or interpreted the agreement wrongly, or proceeded on some erroneous principle – in all these cases, the court will interfere."

The court upheld SARS's appeal and referred the matter back to SARS for further investigation and assessment.

In *C: SARS v Executors Estate Late Sidney Ellerine* [59] the court had to consider the valuation of preference shares held by the deceased on the date of death under paragraph 40(1).[60]

The deceased held 112 000 7% redeemable non-cumulative preference shares of R1 each on date of death in Sidney Ellerine Trust (Pty) Ltd. The company's share capital also included 600 ordinary shares held by a number of trusts. Each of the preference and ordinary shares carried one vote with the result that the deceased held 99,5% of the voting rights in the company (112 000 / 112 600 × 100).

58 1954 (1) All ER 749 at 758.
59 [2018] JOL 40193 (SCA), 80 SATC 389.
60 Paragraph 40(1) provided for a deemed disposal of the deceased's assets at market value on the date of death. For persons dying on or after 1 March 2016 this deemed disposal is now contained in section 9HA.

In the deceased's return of income up to date of death the proceeds on the deemed disposal of the shares were shown as R112 000, being their par value, which was the same as their redemption value. By contrast, SARS had assessed the deceased on proceeds of R563 million on the basis that the deceased could have converted the preference shares to ordinary shares. The preference shares should thus have been valued as if they were ordinary shares. The issue before the court was whether the right to convert the preference shares to ordinary shares should be taken into account when valuing the preference shares. The crux of the matter was whether the consent of the ordinary shareholders was required before the preference shares could be converted to ordinary shares. The Articles of Association of the company provided that any variation in the rights of shares of a particular class required the consent of 75% of the shareholders in that class. The respondent argued that the conversion of the preference shares to ordinary shares would result in the variation of the rights in the ordinary shares because it would result in a drastic decrease in their value, and hence the consent of 75% of the ordinary shareholders would have been required. The court noted that English law supported the view that a variation of rights occurs when the rights which attach to shares are varied and not when they become commercially less valuable. The court cited various authorities which confirmed that this principle applied equally in South Africa. In the result the court held that the deceased could have converted the preference shares to ordinary shares without the consent of the ordinary shareholders. The appeal was accordingly upheld, with the court finding that the shares should have been valued at R563 million.

Valuation of a residence

In Tax Board Case 0110[61] the appellant had disposed of a residence for proceeds of R3,2 million in 2003. The valuation date value of the residence had been determined at R4 million on the market-value basis by a professional valuer using the comparable sales method in which three comparable sales were selected. The valuation of R4 million was actually done for mortgage bond purposes at the instance of a bank and therefore carried out conservatively. A larger property was sold in the same road by public auction for only R2,3 million a month after valuation date but was in poor condition and disposed of under a forced sale. It was therefore not accepted by the chairman as a comparable property for valuation purposes. The chairman noted that for non-expert criticism to be accepted as evidence above the testimony of experts is not easy. In summing up the evidence he noted that –

> "[w]e are left with a valuation done by an impartial valuator with many years' experience who valued the property conservatively. No evidence was produced to counter either his valuation or his methodology. The evidence produced by cross-examination, which was the only actual evidence adduced by the respondent, did not assist the respondent in any way".

In the result the chairman found in favour of the appellant.

61 Durban Tax Board, 23 August 2007, unreported.

Annexure – Examples

Example 1 – Valuation of a controlling interest in a listed company

Facts:

Company A acquired 51% of the shares in Company B, a company listed on the JSE, in 1990. On 1 October 2020 Company A disposed of its entire holding of 3 million shares in Company B to Company C.

The prices for the Company B shares were as follows:

Last buying price for each Company B share on 30 September 2020	R1,95
Last selling price for each Company B share on 30 September 2020	R2,05
Price for each Company B share under the sale agreement	R2,20
Price for each Company B share as at valuation date per *GG* 23037	R1,50

Result:

Step 1 – Calculate market value on valuation date

Valuation date market value (3 million shares × R1,50)	R4 500 000

Step 2 – Calculate control premium or discount

Average last price quoted (R1,95 + R2,05) / 2	R2,00
Control premium (R2,20 – R2,00) / R2,20	10%

The control premium is determined by deducting the price per share per the sale agreement from the average last price quoted on the JSE and dividing the result by the selling price per the sale agreement.

Step 3 – Determine base cost

	R
Valuation date market value (3 million shares × R1,50)	4 500 000
Control premium (R4 500 000 × 10%)	450 000
Base cost	4 950 000

Step 4 – Determine capital gain

	R
Proceeds (3 million shares × R2,20)	6 600 000
Less: Base cost	(4 950 000)
Capital gain	1 650 000

Example 2 – Submission requirements for valuations of assets

Facts:

Individual A holds 10 shares in Company B, an unlisted company. Company B's financial year ends on 31 August. Individual A's accountant valued the shares in Company B on 31 August 2003 at R1,5 million each as at 1 October 2001.

The market values of the assets of Company B was as follows at 1 October 2001:

	R
Fixtures and fittings (small items, each valued at less than R200 000)	10 000 000
Goodwill	2 500 000
Trade mark	1 700 000
Liquor licence	800 000

Company B submitted its return for the 2003 year of assessment on 31 August 2004 and the return for the 2004 year of assessment on 31 August 2005.

Individual A submitted the return for the 2004 year of assesment on 1 October 2004.

Individual A and Company B adopted the market value basis for all their assets.

Result:

Proof of valuations of the following assets had to be submitted to SARS with the returns for the 2004 year of assessment (see Note 1):

Asset	**Reason**	**Proof to be submitted with return for year ending:**
Individual A		
Shares in Company B	MV > R10 million	28 February 2004
Company B		
Goodwill	MV > R1 million	31 August 2004
Trade marks	MV > R1 million	31 August 2004

Notes:

(1) The returns submitted by Individual A and Company B for the 2004 year of assessment were the first returns submitted after 30 September 2004.

(2) The furniture and fittings and liquor licence do not fall within paragraph 29(5) because their individual values do not exceed R10 million. The prescribed valuation form for these assets must be retained for five years from the date of submission of the return for the year of assessment during which the assets are disposed.

Example 3 – Valuation of an usufruct

Facts:

The market value of Individual A's farm less 30% is R800 000. Individual A donated a usufruct over the farm to Individual B for the rest of Individual B's natural life. Individual B is 30 years of age.

Result:

The market value of the usufruct is determined as follows:

- Annual value: R800 000 × 12% = R96 000
- According to the life expectancy tables for males, Individual B's life expectancy is 38,48 years.
- Present value of R1 capitalised at 12% a year for 38,48 years = R8,22694

Market value of usufruct:

R96 000 × 8,22694 = R789 786