

# **Assessing the normal tax implications of a home swap for a resident owning property in South Africa**

by  
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## **ASSESSING THE NORMAL TAX IMPLICATIONS OF A HOME SWAP FOR A RESIDENT OWNING PROPERTY IN SOUTH AFRICA**

The concept of home swapping dates to the 1960s and is therefore an established practice. Participating members exchange reciprocal rights, entitling such members to accommodation (in each other's homes) at predetermined dates for a specific period. The rapid and prodigious strides made in technological advancement have eliminated traditional barriers to international trade. Consequently, the practice of home swaps has been highlighted as a core contributor to the sharing economy. The conventional concept of home swapping has been revised to exploit the upsurge in the current innovative business environment.

Exchanges can be facilitated via points, rights or cash. The essence of such an exchange can be reduced to a short-term rental agreement, with distinction only being made to the recompense: an incorporeal non-cash benefit (points/rights) or cash. Such rights/points fall within the ambit of barter trade, which in turn finds itself within the realm of gross income. However, the South African Revenue Service does not explicitly address the normal tax treatment of the incorporeal non-cash benefit (points or a right) collected. Therefore, the average South African taxpayer, lacking tax expertise, might inadvertently contravene the Income Tax Act No. 58 of 1962 (hereafter referred to as the "ITA"). Contributing to the convoluted nature of assessing the normal tax repercussions for home swaps is the time at which the benefits accrue, the valuation of such benefits, and the influence of cross-border transactions. The principal aim of this study was therefore to address the normal tax implications for a South African resident, in possession of property within South Africa, upon receipt or accrual of the benefit of a successful home swap.

The gross income definition of the ITA, in conjunction with relevant South African case law and legislation, was evaluated to elucidate the recommended normal tax treatment for home swap transactions (hereafter referred to as "swaps"). In addition, the terms and conditions of the two most prominent international home swap programmes, Love Home Swap and Home Exchange, were analysed in the context of the aforementioned legislation and case law. The study concludes with an examination of Australian tax

legislation and case law as a source of counsel from the perspective of the Australian Tax Office.

Home swap benefits, regardless of the currency, were found to be indistinct items of gross income for which no exemption exists in the current ITA. The time at which a normal tax burden arises is dependent on the swap type, the order in which participants consume their benefits and the terms and conditions inherent to affiliation with specific home swap programmes.

Valuation of non-cash benefits is more multifaceted than appraisal where compensation is in cash. Valuation is primarily contingent upon the time at which normal tax is levied and whether the recompense is in cash or kind. An explanatory memorandum or augmentation of the ITA with additional sections, is therefore proposed. Such an addition to the ITA will instruct taxpayers and reduce the forfeiture of tax revenues due to inadvertent non-compliance.

## **EVALUASIE VAN DIE NORMALE BELASTING IMPLIKASIES VAN 'N HUIS-RUIL VIR 'N INWONER WAT EIENDOM IN SUID AFRIKA BESIT**

Die konsep bekend as "huis-ruil" bestaan reeds vanaf die 1960's en is dus 'n gevestigde praktyk. Deelnemende lede verruil 'n wederkerige reg wat elke lid vanaf 'n voorafbepaalde datum vir 'n spesifieke tydperk die reg tot akkommodasie (in mekaar se huise) verleen. Die rasse skrede waarteen die ontwikkeling van tegnologie plaasvind, het reeds die tradisionele struikelblokke wat toetredende tot internasionale handel beperk, uit die weg geruim. Gevolglik het die kollig op huis-ruil as 'n sleutelbydraer tot die deel-ekonomie geval. Die konvensionele metode van huis-ruil is dus hersien en aangepas ten einde hierdie innoverende besigheidsomgewing te ontgin.

Hierdie ruiltransaksies kan met behulp van punte, regte of kontant gefasiliteer word. In wese kan so 'n huis-ruilooreenkoms as 'n korttermyn-huurooreenkoms vereenvoudig word, en die enigste onderskeid wat ten opsigte van vergoeding getref moet word, is 'n ontasbare, nie-likiede voordeel (regte/punte) of kontant. Hierdie regte/punte val binne die reikwydte van ruilhandel, 'n konsep wat deel van die term "bruto inkomste" uitmaak. Die Suid-Afrikaanse Inkomstediens spreek egter nie die normale belastinghantering van hierdie punte/regte-voordeel wat ontvang is, spesifiek aan nie. Dit is dus moontlik dat die gemiddelde Suid-Afrikaanse belastingbetaler vanweë onkunde die Inkomstebelastingwet Nr. 58 van 1962 (hierna die "IBW" genoem) onbewustelik oortree. Die tydstop wanneer die voordeel toeval, die waardasie van die sogenaamde voordeel, en die implikasie van transaksies wat landsgrense oorskry, dra by tot die kompleksiteit rakende die vasstelling van normale belasting vir so 'n huis-ruil. Die sentrale doelstelling van hierdie studie was dus om die normale belastinggevolge te bepaal vir 'n inwoner van Suid-Afrika, wat eiendom in Suid-Afrika besit, wanneer die voordeel van 'n huis-ruil ontvang word of toeval.

Die definisie van bruto inkomste, soos vervat in die IBW, in samewerking met relevante Suid Afrikaanse regspraak en wetgewing, is geëvalueer om lig te werp op die voorgestelde hantering van die voordele van huis-ruil vir normale belasting. 'n Ontleding is bykomend gedoen van die terme en voorwaardes van die twee mees prominente internasionale huis-ruilprogramme, Love Home Swap en Home

Exchange. Hierdie ontleding is binne die konteks van voorgenoemde wetgewing en regspraak onderneem. Die studie is afgesluit met 'n ondersoek na Australiese belastingwetgewing en regspraak as raadgewende bron ten einde huis-ruil vanuit die perspektief van die Australiese belastingkantoor te begryp.

Daar is bevind dat die voordele van huis-ruil, ongeag die kommoditeit van verhandeling, 'n onweerlegbare komponent van bruto inkomste verteenwoordig en dat daar geen vrystelling in die huidige IBW bestaan nie. Die tipe huis-ruil, tesame met die orde waarin die lede hul regte verbruik en die terme en voorwaardes inherent tot die spesifieke huis-ruilprogram, is die bepalende faktore ten einde vas te stel wanneer 'n normale belastingverpligting ontstaan.

Waardasie van nie-likiede voordele is meer ingewikkeld as kontantvergoeding. Waardasie word hoofsaaklik gedryf deur die tydstip wanneer belasting gehef word en of vergoeding in kontant al dan nie geskied. 'n Verduidelikende memorandum of addendum met addisionele artikels as byvoeging tot die huidige IBW, word dus voorgestel. Hierdie byvoeging tot die IBW sal leiding aan belastingbetalers verskaf en die nienakoming van belastingwetgewing, toeskryfbaar aan onkunde, beperk.

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## CHAPTER 1: INTRODUCTION

### 1.1 Background

Tax revenues are the principal source employed to finance public expenditure (Black, Calitz & Steenkamp, 2011:62) and are indispensable in funding government directives worldwide (Muli, 2014:1). Novel means to assess and tax residents, together with eliminating ambiguity from legislation, is an enduring priority in an attempt to decrease budget deficits and increase economic growth (Smith, 2015; Saville, 2015). The convoluted nature of income taxes, in coalescence with continuous amendments and uninformed taxpayers, often has the contrary effect, resulting in inadvertent non-compliance (Muli, 2014:1).

The rapid expansion of the sharing economy, enabled by a global acceleration in electronic commerce, is a grey area which has only recently elicited both the interest of the Australian Taxation Office (hereafter referred to as the “ATO”) and the British tax authorities (ATO, 2017; Woskow, 2014). General guidance on the tax implications of the sharing economy is gradually assigned more prominence as it continues to grow exponentially. Direction from tax authorities, emerging only recently, is however still scant. Combined with the complexity of tax legislation and ignorance of taxpayers, this may potentially result in forfeiting of tax revenue.

Woskow (2014) defines the sharing economy as online platforms permitting people to share property, resources, time and skills. Home swapping is one of the collaborative consumption models on which the sharing economy is built. A traditional home swap agreement is defined as a practice in which the owner of a house allows the use of that property in exchange for the use of another party's home (HS, 2015b). This reciprocal home swap can either coincide or be non-simultaneous. Members of a home swap programme can also exchange using points or through a conventional rental agreement (LHS, 2015a). Hospitality exchanges are optional in selected home swap programmes. A hospitality exchange offers greater flexibility, as exchange partners choose to host each other as guests (HE, 2016c).

Swapping homes with another family in order to enjoy a cost-efficient holiday abroad is not a completely novel concept and was first reported on by Time magazine in 1965 (TIME, 1965). Home swapping, as part of the sharing economy, has however been underscored in the past five years due to an unprecedented acceleration in transactions, enabled by technological advances connecting supply and demand in a trusted environment (Preston, 2014).

The simplicity and cost-effective benefits of home swapping have progressively converted local consumers, and South Africans are catching on with this global trend (Spagnoletti, 2015). An increased interest can be observed in both South African and international sharing economy markets (Geron, 2013; Bloomberg, 2015). The first South African home swap platform was introduced in 2014 (Weber, 2015:35). South African residents' membership of Love Home Swap, one of the largest international home swap programmes, reflected growth of 40% during 2014 (Bryant, 2015a).

The absence of explicit direction by the South African Revenue Service (hereafter referred to as "SARS") on the treatment of home swap benefits, necessitates further analysis of the essence of a home swap agreement. The substance of a home swap agreement is analogous to a traditional short-term rental agreement, with the distinction of performance that entails a right of use instead of cash, positioning this contract within the periphery of a barter transaction. Cambridge Dictionaries Online (2015) defines to barter as "*to exchange goods for other things rather than for money*". The essence of a barter transaction is therefore an exchange of tangible or intangible assets, in a currency other than money. A home swap can consequently be categorised as a barter transaction: the right to utilise one house is exchanged for the right to utilise another.

De Koker and Williams (2016: par.2.16) conclude that the value of property, in whichever shape, received in exchange for an asset, is to be classified as gross income. Exoneration of such a classification will only be available if the asset in question is of a capital nature. In order to address the normal tax implications of home swaps it is therefore elemental to determine whether the right of use received by a home swap member in exchange for the benefit dispensed, is of a capital or of an income nature. Ensuing classification of the nature of the right, the core intricacies surrounding barter transactions must be investigated. The absence of cash and the characteristics of a home swap collectively raise questions regarding the valuation of the right and the time at which the right accrues to the taxpayer.

Barter transactions fall within the ambit of the South African tax net (De Koker & Williams, 2016: par.2.16). The average taxpayer's incomprehension of the South African Income Tax Act No. 58 of 1962 (Republic of South Africa, 1962) (hereafter referred to as "ITA") might however result in an omission from taxable income due to miseducation. The absence of an allotted area on the current tax return for natural persons, prompting the disclosure of a right of use (hereafter referred to as "benefits"), escalates the possibility of non-compliance with the ITA.

There are four supplementary factors significantly contributing to taxpayers' unintentional non-compliance. The first factor being a misconstrued insight of the word "amount", as intended by the SARS with the gross income definition in section 1 of the ITA. The average South African taxpayer might be of the opinion that a right of use does not signify such an amount. Judge Watermeyer, by delivering his judgment in *WH Lategan v CIR* [1926] CPD 213 at 209, 2 SATC 16, established that the value of incorporeal property (such as rights) earned by the taxpayer, is to be included as an amount in taxable income.

The second factor relates to the perplexity of appraising the benefit received. A traditional home swap gives rise to a right of use to another member's house, whereas a point swap endows the member with points which are tradable in exchange for accommodation. The benefit deliberated in a traditional home swap is a right of use, pertaining to a specific pre-determined property. The value of this property might be substantially dissimilar from the value of the property offered and often a swap-partner enjoys residence of a different country. A point swap furnishes a member with a commodity, of which tradability is limited to members of the relevant home swap programme. Vacant points, in the absence of a pre-arranged home swap, cannot be associated with a particular property. This raises the perplexing question of identifying an appropriate method of valuation for the points.

A hospitality exchange entails a home swap akin to accommodation provided by a guesthouse. Participating members will take turns to host each other in their homes. Hospitality exchanges will consequently necessitate the analysis of distinct home swaps, as the extent to which additional services, such as meals and cleaning, are provided, will influence the valuation of the benefit. Rental agreements, an additional means to enable a home swap agreement, are the least complex regarding the valuation of the benefit. A rental agreement is most likely to be negotiated at the market-related daily rate for short-term rentals. Section 102(1)(e) of the Tax Administration Act No. 28 of 2011 places the burden of

proof on the taxpayer. Consequently, the onus of including and substantiating the assessable value for rental recompense per the annual tax return, lies with the taxpayer. The precedent set by *CIR v Butcher Bros (Pty) Ltd* [1945] 13 SATC 21 however determines that the burden of proof with regard to the valuation of the benefit resides with the SARS.

Thirdly, establishing the time at which the benefit is received or accrues to the taxpayer is complex. Home swap transactions are arranged and finalised via online messages. Section 4(1) of the Electronic Communications and Transactions Act No. 25 of 2002 (hereafter referred to as “ECTA”) stipulates that all electronic transactions and data messages fall within the ambit of this act. The nature of the agreement therefore dictates cognisance of the ECTA in order to determine the time at which a valid contract comes into existence. Once a valid contract has been established, the terms and conditions of the specific agreement, in conjunction with the terms and conditions of each home swap programme, must be examined. This step is essential to determine when the right of use accrues to the member, and therefore becomes taxable.

The mere presence of a valid contract does not necessarily impose normal tax on parties to the contract. The precedent set by the *Lategan case (supra)*, in conjunction with the qualification of unconditional entitlement, introduced by *Ochberg v CIR* [1933] 6 SATC 1, prevents a tax liability from arising until all the stipulations prohibiting an immediate claim to performance have been satisfied. The principle of unconditional entitlement as established by the *Ochberg case (supra)* was confirmed by the judgment in *Mooi v SIR* [1972] 2 All SA 57 (A).

The absence of a true condition will however result in an inclusion in gross income once a valid contract is established. This consequently confirms the significance of a meticulous analysis of the terms and conditions of each home swap agreement (hereafter referred to as “home swap”) in order to assess South African members’ tax obligation. The final factor influencing inadvertent non-compliance can be contributed to the uncertainty regarding whether this benefit is capital of nature, or not.

## 1.2 Problem statement

The most prominent contributing influences resulting in the identification of the main problem statement are as follows:

- Miseducation among South African taxpayers;
- The absence of distinct direction by the SARS;
- The complexity regarding the valuation of the benefit;
- Establishing the time of accrual (based on the ECTA); and
- Ambiguity regarding the nature of the receipt.

The main problem statement can therefore be articulated as follows: To assess the normal tax implications for a South African resident, in possession of property within the Republic of South Africa (hereafter referred to as the “Republic”), upon receipt or accrual of the benefit of a successful home swap.

The supervening section expands on the secondary questions identified. The satisfactory resolution of these secondary problems is fundamental in achieving an adequate and comprehensive remedy to the main problem statement.

## 1.3 Research objectives

In order to assess the manner in which members of home swap programmes need to account for the tax implications of these swaps, the following secondary questions have to be answered:

- Which are the most prominent home swap programmes available both in South Africa and internationally and what are their conditions and stipulations?
- Does the benefit received as part of a home swap meet the requirements of the gross income definition in terms of the ITA or is it of a capital nature?
- What is the value of the benefit obtained?
- When does this benefit accrue to the taxpayer?
- Will it be beneficial to investigate the tax treatment for similar transactions of a country in which the tax legislation and practices are homogenous to those of South Africa?

An analytical investigation of the different home swap programmes available (both locally and internationally) will enhance comprehension of the conditions and stipulations of each programme. Such understanding will assist in categorising the disparate types of home swaps per programme to determine the taxability of each type. A comparative investigation between the tax practices and legislation of South Africa and a country of which the legislation and practices are analogous will indicate the appropriateness of South Africa's treatment of home swap benefits.

#### **1.4 Motivation for research**

The sharing economy is unlocking a new generation of entrepreneurs and transforming the traditional business sector (Woskow, 2014). The United Kingdom, a leader in the sharing economy, set up the Sharing Economy UK in March 2015 to regulate this sector and obtain the full benefit of an economy that has grown more than Yahoo, Google and Facebook combined in the past seven years (Growthbusiness, 2015).

The Australian Institute of Public Affairs, renowned for pioneering contributions in the fields of politics, economy and technology, published an article with recommendations to the Australian government in December 2014. Allen and Berg (2014) advocate continuous encouragement of the sharing economy. Additional proposals include a suggestion to eliminate excessive and restrictive government regulations in order to sustain growth in ways beneficial to entrepreneurs and the government alike.

The first South African home swap programme was founded in July 2014 and its listings already include residences in Australia, France and the United Kingdom (HS, 2017a). It has become imperative to examine the tax implications of benefits received to ensure a transparent, fair tax treatment and to avert eluding of fiscal revenue. The absence of explicit guidance from the SARS and the rapid escalation in the popularity of home swapping underscore the importance of such an investigation.

#### **1.5 Research methodology**

The research methodology that was followed in this study mainly consisted of a literature study of purely theoretical aspects. The literature study was comprised of relevant articles written by academics in conjunction with South African legislation and case law of local

courts in the Republic of South Africa. International case law and legislation were considered to aid in addressing the complexities arising with regard to the valuation of the benefit and the timing of accrual.

The study was also comprised of an element of comparative research in order to compare South Africa's tax treatment of the right of use arising from a home swap programme to Australia, a country with tax principles, practices and legislation analogous to that of the Republic. The comparative focused on the treatment of income received in consideration other than cash, in order to aid with recommendations that are well-defined, transparent and fair.

## **1.6 Limitations of scope**

This study was aimed at addressing the implications of a home swap on gross income for natural persons, who are South African residents in possession of property within the Republic, when the benefit is received or accrues. The following fell outside the ambit of this study:

- The tax treatment of the home swap programme itself;
- The deductibility of the expenditure incurred essential to qualify and participate in a home swap programme.

## **1.7 Framework of the study**

The study is arranged in the following chapters:

### **Chapter 2: An analysis of the different categories of home swap programmes and the resulting influence on gross income**

This chapter seeks to answer the following two questions:

- Which home swap programmes are available both in South Africa and internationally and what are their conditions and stipulations?
- Does the benefit received as part of a home swap meet the requirements of the gross income definition or is the benefit capital of nature?

### **Chapter 3: The timing of home swap benefits in accordance with South African legislation and case law**

This chapter entails a discussion on the relevant South African case law and legislation that were investigated to establish the time at which the normal tax liability arises. The significance of an extensive comprehension of the terms and conditions and home swap types available to facilitate a swap are emphasised in this chapter. This approach was deemed essential as the diverse stipulations and principles require disparate tax treatment.

### **Chapter 4: The value of home swap benefits in accordance with South African legislation and case law**

This chapter addresses how the value subject to normal tax can be determined after establishing the time at which such tax arises. Applicable South African case law and legislation were consulted in deliberating the value for inclusion in a resident's gross income.

### **Chapter 5: Consideration and discussion of the tax treatment of home swap programmes from the perspective of Australian tax legislation**

This chapter presents a comparative study to assess the tax remedy for barter transactions in Australia. An examination of the taxation practices followed by this country for the benefits receivable by home swap members will set a standard to offer direction to South African tax authorities. In the comparative examination, the practices and legislation of Australian tax authorities are emphasised for transactions within the ambit of barter.

### **Chapter 6: Conclusion**

This chapter contains a summative inference after careful consideration of the results reached in the previous chapters. Recommendations to simplify the implementation of a feasible tax system to prevent the benefits arising from home swap programmes to elude the fiscal net are made in the conclusion to this study.

## **CHAPTER 2: AN ANALYSIS OF THE DIFFERENT CATEGORIES OF HOME SWAP PROGRAMMES AND THE RESULTING INFLUENCE ON GROSS INCOME**

### **2.1 Introduction**

This chapter addresses two questions:

- Which are the most prominent home swap programmes available both in South Africa and internationally and what are their conditions and stipulations?
- Do the benefits received as part of a home swap agreement meet the requirements of the gross income definition or are they of a capital nature?

This examination not only illuminates the comprehension of home swap programmes globally, but also positions this collaborative consumption model within a South African context. The rationale for the selection of home swap programmes is discussed alongside the general terms and conditions. An elucidation of the various manners in which a home swap can be facilitated concludes the analysis of home swap categories.

The benefits attributable to a home swap agreement can be of a corporeal or incorporeal nature. Cash, a right of use, or points are obtained in return for the endowment of accommodation. As mentioned in 1.1, De Koker and Williams (2016: par.2.16) conclude that any property, including that of intangible disposition, encompasses gross income, unless the property exchanged was capital of nature. Home swaps facilitated through points or a right of use require the taxpayer to bestow a similar right on the swapping partner. The beneficiary of this right will be eligible to accommodation for a predetermined period. The normal tax implications of home swaps are therefore dependent on whether the inherent nature of the benefit acquired, in exchange for the accommodation dispensed, is capital or income.

### **2.2 Background**

The rapid escalation of collaborative consumption has seen the emergence of a relentless informal economy (Growthbusiness, 2015). Online platforms are established to connect supply and demand in a secure environment. Fundamental changes to traditional commerce are fuelled by continuous technological advances (Given, 2015). Home swaps are one of the cornerstones on which this share economy of collaborative consumption is built. The practice of home swapping, as an alternative to expensive and conventional

accommodation, empowers proprietors to unlock the innate value of assets and utilise their property to travel cost-efficiently.

### 2.3 Definition of a home swap

Investopedia (2015) defines the term 'home swap' as:

*... a practice in which the owners of a home allow the use of that property in exchange for the use of another party's home. A house swap does not involve the sale of a home; rather, it allows a homeowner to 'borrow' someone else's home.*

This definition elucidates the concept by excluding the sale of a house and reducing the transaction in its simplest form to a mutual borrowing of homes.

A traditional home swap programme can therefore be defined as a reciprocal exchange of homes. This exchange can be simultaneous or non-simultaneous. The conventional and more restrictive definition of a home swap is however expanded by innovative means, in order to enhance the accessibility of the programme to an increasing consumer base. Home swaps can also be facilitated by means of a point swap, rental agreement or a hospitality exchange, as previously discussed.

Home swap agreements rarely entail a trade by way of cash. A typical home swap will involve an exchange of either rights (to the mutual use of participating members' homes) or recompense in points. The essence of these transactions is akin to a short-term rental agreement. The right of use, without a change in ownership, is conferred for a pre-arranged period. An exchange of property (i.e. rights or points) without the utilisation of money positions these transactions within the realm of barter trade.

The nature of home swaps demands a simplistic distinction to be drawn between personal rights and real rights. Delpont (1987:7) explains the difference as follows:

*A real right is enforceable against the whole world, that is, against the owner of the property and all other persons who have legal claims to the property by virtue of a contract with the owner or because of the death or insolvency of the owner. A personal right, on the other hand, merely gives the holder the right to claim from a particular person either that he delivers a thing, or performs or refrains from performing a certain act.*

The right of use created between members, participating in a swap, will therefore be a personal right, as its dominion is limited to the natural persons consenting to the swap. Classification of the right as “personal” is validated when the test formulated by *Ex parte Geldenhuys* [1926] OPD 155 at 164 is applied: the right of use does not encumber the property of either swap participant and it cannot be registered over the land. A right of use, for the remainder of the thesis, will therefore refer to a personal right. The home swap programmes elected as subjects for this study are examined next.

## **2.4 Selection of home swap programmes and augmenting concepts**

A multitude of international home swap programmes leave potential members spoilt for choice. Dawnzerly's (2016) non-extensive compilation of home swap websites in July 2015 reflected a selection of 85 active programmes. Different home swap programmes serve dissimilar markets and provide an assortment of ways to swap. The divergent markets accommodate members' preferences by allowing the frugal home owner to swap traditionally or via a hospitality exchange. Home owners in less desirable destinations can participate by swapping commodities that constitute either points or cash. Membership to a South African programme is limited to Houseswap, which was established via Facebook in 2014 (HS, 2015b).

International home swap programmes selected for analysis were, among other things, identified based on size: an extensive property portfolio liberates members to travel far and wide (Dawnzerly, 2016). Popularity among South African residents, and the reputation and maturity of the programme were also considered. Houseswap, the pioneering South African programme, was deliberated due to it being the only equivalent available in the Republic. Subsequently, Love Home Swap and Home Exchange, which are the most dominant participants in the international market, and Houseswap, the forerunner in South Africa, were elected as subjects for this study. The terms and conditions of the distinctive home swap programmes are discussed below.

### **2.4.1 Love Home Swap**

Love Home Swap (hereafter referred to as “LHS”), established in 2009, is one of the two largest programmes, affording exchange opportunities to more than 100 000 homes in more than 140 countries (LHS, 2017d). South Africans’ membership to LHS reflected growth of 40% in 2014, and the Republic holds the ranking as the twelfth most popular destination worldwide (Bryant, 2015a). Members of LHS can elect one of three swap alternatives. A traditional swap, a rental agreement or a point swap can be employed to arrange accommodation (LHS, 2015a).

#### **2.4.2 Home Exchange**

Home Exchange (hereafter referred to as “HE”), endorsed by TripAdvisor and rivalling LHS in size, was founded in the United States of America in 1992 (Anderson, 2014). Membership benefits include exclusive travel discounts from the well-known German airline company Lufthansa. HE is the most established home swap programme and its registry exceeds 65 000 homes in 150 countries (HE, 2016b). Ed Kushins, founding member, indicated that ambitions for 2015 include membership in excess of 100 000 and more collaborative partnerships (Anderson, 2014). A member of HE can embark on a holiday by following the traditional home swap route or by utilising a hospitality exchange (HE, 2016c).

#### **2.4.3 Houseswap**

Houseswap, the sole South African home swap programme, was established in July 2014 and affords members the opportunity to swap traditionally, enter into a rental agreement, or travel by way of a hospitality exchange (HS, 2016b). Houseswap’s listing currently reflects travel opportunities to ten different countries (HS, 2017a). The limited local offering reflects South African residents’ preference to affiliate themselves with international programmes.

### **2.5 The fundamental working principles of a home swap**

Full membership is attained by subscribing, through payment of an annual or bi-annual fee, to an elected home swap programme. The duration of membership varies, but is generally accepted to be for a period of twelve months. Promotional campaigns, such as enrolling at a discount for a limited period, and free membership for trial periods, are used to entice potential members (LHS, 2017b). Full membership is however a prerequisite for concession to the pervasive online communication platform (HE, 2015a).

LHS allows a prospective member to select between three different categories. The membership benefits and pricing progressively increases depending on whether the option selected is categorised as lite, standard or platinum (LHS, 2017b). Unlimited swaps are however a standard benefit of all tiers. HE introduced a gold membership in October 2016, aiming to service the higher end of the market by offering personalised services and added benefits at an additional annual fee of \$350 (HE, 2016d). Unlimited swaps remain invariable regardless of the membership tier (gold or standard) (HE, 2017b). Houseswap does not rank members and benefits and fee structures are homogenous (HE, 2015b; HS, 2015a).

A unique and exhaustive profile is created once a member has enrolled, whether through payment of the subscription fee or by utilising the free trial period (LHS, 2015a). The particulars of this profile include preferred countries and dates for swapping. Additionally, a list of amenities provided to one's swapping partner and personal information about the home owner is disclosed. Furthermore, photos, accompanied by a narrative of one's home, neighbourhood and tourist attractions in the area are fundamental (LHS, 2015d). Unlimited browsing of the home catalogues is permitted by all online home swap programmes. Contact details are however withheld from the profile information in order to prevent "trailing members" or casual online visitors from circumventing the programme (LHS, 2017f; HE, 2015a).

A trialling member enjoys partial benefits of membership for a limited period. A complete online profile presents these hesitant participants with the opportunity to trial the home swap programme. Trialling permits these members to promote their property for a complimentary period, but in the absence of access to instant messaging. The functionality to communicate via the online platform is restricted, confining any home swap negotiations to paying members only (LHS, 2017f; HE, 2015a).

Once a homeowner has paid the subscription fee, exclusive access to a secure online platform is obtained, enabling members to arrange home swaps through fortified instant messages (HE, 2015a). A homeowner can engage in an unlimited number of swaps without any additional charges (LHS, 2016l). Reviews left by previous swap partners provide trustworthy accounts of whether the homeowner's depiction is truthful and accurate (LHS, 2016i). Members have carte blanche to arrange home swaps traditionally, via points, hospitality exchanges, or rental agreements. The terms and conditions can be tailored to suit the participants of a particular home swap. An exhaustive examination of the terms and

conditions of the programmes selected, was pursued (see Chapter 3), as such an examination will determine when a benefit accrues, thus eliciting a possible normal tax implication. The four distinctive home swap methods employed to engage in a home swap are assessed next.

## 2.6 Home swap types

An investigation of LHS and HE, the most prominent programmes, identified four potential methods in which a home swap can be structured:

- A traditional home swap
- A point swap (only offered by LHS as exchange alternative)
- A rental agreement
- A hospitality exchange

Houseswap, the South African equivalent, endows members with three of these methods, omitting point swaps as a travel alternative. The four individual methods in which a home swap can be facilitated require participating members' engagement with disparate commodities.

### 2.6.1 Traditional home swap

This type of swap is the oldest and most popular and is described by LHS as a “*two-way home-exchange*” (LHS, 2015a). Members agree on predetermined dates and the duration of the swap. This type of swap can be either simultaneous or non-simultaneous. A simultaneous swap will result in the parties to the agreement staying concurrently in each other's homes. A non-simultaneous swap can be employed if the parties to the agreement have disparate travel dates. Traditional home swaps can prove to be challenging and fruitless for members of less popular destinations. The limitations set by traditional swaps are addressed by giving members alternative options, as discussed next.

### 2.6.2 Point swap

Points were introduced by LHS to maximise flexibility. HE and Houseswap do not currently accommodate point swaps. Point swaps can be arranged in the absence of a reciprocal interest. This characteristic distinguishes a point swap from a traditional swap, which

requires members to share a mutual interest in each other's homes and countries. Points, ranging in quantity dependent on the membership level (silver, gold or platinum), are received annually when subscriptions are renewed. Alternatively, up to 4 000 points can be borrowed at a predetermined rate. Repayment (of the points borrowed in advance) will transpire when guests are hosted for points within a period of two years (LHS, 2017a).

Points can be employed to compensate another willing member in exchange for accommodation in their home swap property. The points attained by the hosting member can then be redeemed at a preferred time, date and location without limiting them to the property of the member requesting the swap (LHS, 2016h). LHS's points are standardised. All homes enter the market at a minimum of 50 points per night, increasing in intervals of 50 to a maximum of 300 points (LHS, 2015b). The LHS team will recommend an estimated point value per night, but the home owner has sole discretion over a home's final value per night (LHS, 2015b).

Point swaps increase the accessibility of international travel to residents of countries with weaker currencies, as the expenditure of exchange rate inflated accommodation is eliminated. The valuation of these points is however convoluted due to the nature of the commodity being traded. The disparity between property types, seasonality and the popularity of locations gives rise to complexity with regard to the valuation of points. The appraisal of the points, essential to assess the amount eligible for inclusion in gross income, is discussed in Chapter 3.

### **2.6.3 Rental agreement**

This type of swap is for conservative members who prefer to engage in an old-fashioned short-term rental contract: if a host is not interested in a traditional swap or the acquisition of points, a rental agreement can be pursued (LHS, 2015a). A rental agreement, similar to a point swap, offers more flexibility, as no reciprocation is required by the host. The daily rate, as determined by the home owner, will be visible to members perusing the online home swap catalogue. Daily rates are linked to seasonality and steeper prices can be expected over holidays and long-weekends.

### **2.6.4 Hospitality exchange**

Hospitality exchanges are akin to traditional non-simultaneous home swaps with the added benefit of being hosted by one's swapping partner (HE, 2016c). The extent to which additional services such as meals and cleaning are included in the swapping package will be negotiated by the individual swapping partners and is not standardised.

### **2.6.5 Summary of the various home swap types**

The benefits received for the respective home swap types, as discussed, are dissimilar in nature. A member participating in a traditional swap or a hospitality exchange acquires a right of use to the reciprocating member's home, whereas the host of a point swap acquires consideration in a currency only tradable amongst members of the same programme. A rental agreement entitles the hosting member to a pre-determined cash amount.

The normal tax consequences of a rental agreement are the simplest in its interpretation. Cash is a universally accepted commodity and it is evident that the amount should be included in a taxpayer's gross income, as per the principle established by *CIR v Visser* [1937] 8 SATC 271 at 276. The commercial acceptability of points as a method of payment is however limited to a specific programme. Even more limiting in its application is a right of use, as its inherent value is restricted to one specific transaction. This raises the question about whether the benefit received as part of a home swap agreement should be classified as income or capital.

## **2.7 Does the benefit received constitute income or capital?**

*Crowe v CIR* [1930] AD 122, 4 SATC 133 established the principle upheld by South African courts that all amounts are either income or capital. An amount received by a taxpayer can therefore never be a "half-way house" (*Pyott v CIR* [1945] 13 SATC 121 126). This treatment by the SARS prevents an accrual or receipt from falling beyond the government's fiscal jurisdiction, as the ITA requires a designation as either capital or income. This practice implies that an amount will be classified as capital if it fails to comply with the gross income definition of the ITA, and vice versa. The gross income definition is subsequently analysed.

### **2.7.1 Gross income**

Gross income, as defined by the ITA, is comprehensive. It is crucial to apply the different components of the gross income definition, relevant legislation and case law to the benefits

received by home swap members (hereafter referred to as “members”) in order to establish whether such benefits constitute gross income.

The ITA defines gross income in section 1 as follows:

- (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 a person from a source within the Republic,*
- during such a year or period of assessment, excluding receipts or accruals of a capital nature, ...*

The latter part (ii) of this definition was deemed to be superfluous for the purposes of this study. The scope of this investigation was limited to the assessment of the normal tax implications for South African residents who employ owned property, located in the Republic, to engage in home swaps. The various components of part (i) of the gross income definition are considered next, in conjunction with relevant legislation and case law, in order to establish whether the benefits received constitute income or capital.

### **2.7.2 Amount, in cash or otherwise**

A vital issue to address is whether the right of use or points acquired by the member represents an “amount”, as envisioned by the gross income definition. Regardless of the omission of “*in cash or otherwise*” from the definition, the extent of the word “amount”, is sufficient to ensure the inclusion of any property with a monetary value, whether incorporeal or corporeal, in the gross income definition (*Lategan case (supra)*). The precedent established by *Lace Proprietary Mines Ltd. v CIR* [1938] AD 267 requires the market value of such an item to be included in gross income.

Transpiring from case law and the encompassing nature of the gross income definition, there are no exceptions or relief for barter transactions. The right of use and points received will be considered an “amount”, as purported by the SARS. This treatment is corroborated by the precedent set by *CIR v People’s Stores (Walvis Bay) (Pty) Ltd.* [1990] 4 All SA 594 (AD). The judgment in this case established that rights of a non-capital nature which have accrued

and are capable of being valued are to be included in gross income. This principle was confirmed by the ruling in *Cactus Investments (Pty) Ltd. v CIR* [1999] 1 All SA 345 (A).

Subsequently, the right constitutes an amount which should be included in gross income. Points provide an alternative method of home swapping. The adequacy of the currency employed as compensation for accommodation is limited to members of the same home swap programme. The complexity of assigning a value to such a right should not detract from the principle that proceeds with a monetary value are to be included in a taxpayer's gross income (*Lace Proprietary Mines supra*). The ruling in *SARS v Brummeria Renaissance (Pty) Ltd. and others* [2007] 4 All SA 1338 (SCA) further expands the interpretation of the word "amount", to include rights, regardless of whether such rights can be traded or exchanged for cash. The impact on the valuation of points due to the limitations on trade is discussed in Chapter 4.

Points earned by a home swap member as consideration for accommodation offered are included in the scope of the word "amount" as intended by the SARS with the gross income definition. Rental income is the third type of consideration receivable for a successful swap. The rental income is produced by the property utilised for home swaps, which is capital in nature. The rental income therefore reflects the fruit borne by the tree. This principle, established in the *Visser case (supra)*, validates the classification of rental income as an overt item of gross income (Stiglingh, Koekemoer, van Zyl, Wilcocks & de Swardt, 2015:32).

### **2.7.3 Receipt or accrual**

Receipt or accrual of an amount has to transpire before the SARS can levy taxes. The absence of an actual accrual or receipt will leave gross income unaffected (*SARS v Cape Consumers (Pty) Ltd* [1999] (4) SA 1213 (C)). A successful home swap results in the receipt or accrual of either a right of use, points, or rental income, ensuring fulfilment of this condition. There is no definition in the ITA to amplify the intention of the SARS with receipt or accrual. An examination of case law therefore becomes essential to ascertain the objective of tax authorities. Chapter 3 expands on the true denotation of these terms and establishes the timing of accrual and receipt.

### **2.7.4 In favour of the taxpayer**

Section (i) of the gross income definition concludes with “*in favour of such a resident*”, suggesting that a tax burden can only arise once a taxpayer receives the benefit. However, the *Ochberg case (supra)* refuted this school of thought: the appellant was taxed, even though the benefit ensuing from the share transaction in question was trivial.

Tax authorities apply an objective test to assess whether the taxpayer was the beneficiary of an “amount” constituting gross income (Stiglingh *et al.*, 2015:25). This principle becomes critical when a non-cash benefit arising from a home swap transaction has vested, but is yet to be consumed. The lack of a taxpayer’s entitlement to consume the benefit will not disqualify it from being classified as “*in favour*” of the taxpayer. Consequentially, the benefit, whether it constitutes a right of use or points, will be included in gross income, regardless of whether it has been consumed at year-end.

A caveat to the taxation of this benefit is unconditional entitlement, which requires a comprehensive investigation of the terms and conditions of individual home swap agreements. Once a taxpayer has become unconditionally entitled, accrual or receipt transpires and accordingly, a tax liability will have to be provided. Chapter 3 addresses the timing of accrual and receipt with deliberation of applicable terms and conditions.

### **2.7.5 Excluding receipts or accruals of a capital nature**

By virtue of the definition assigned to gross income in the ITA, receipts or accruals of a capital nature are excluded (De Koker & Williams, 2015: par.3.1). Subsequently, only receipts and accruals of a revenue nature will fall within the ambit of normal tax, as levied by section 5 of the ITA. The ITA does not assign a definition to capital in nature, which necessitates a conversion back to judicial decisions in order to categorise accruals or receipts as either income or capital (De Koker & Williams, 2015: par.3.1.).

The vast repertoire of judgments in South African case law attempting to distinguish between income and capital emphasises the complexity associated with classification. No single infallible test exists to designate an amount as either income or capital, and the factual circumstances of individual situations have to be analysed. South African courts tend to apply three predominant tests to assess the nature of an amount (Olivier, 2012:172). The tests favoured by the South African judicial system are:

- the presence of a profit-making scheme;
- the fruit versus tree analogy; and
- fixed versus floating capital.

The third test, relating to floating capital, is irrelevant to home swap transactions since the subject of whether an item represents fixed or floating capital implies that the asset has been traded. The nature of a home swap determines that the asset is utilised to generate a return, but ownership remains unaffected. The absence of trade therefore renders the third test extraneous. The first two applicable tests are discussed next.

### **2.7.5.1 Existence of a profit-making scheme**

Firstly, it has to be established whether the taxpayer has embarked on a scheme of profit-making. The pioneering case, according to Olivier (2012:173), is *CIR v Pick 'n Pay Employee Share Purchase Trust* [1992] (4) SA 39 (A). The lack of the taxpayer's intention to generate profit was the crucial factor acquitting it from a designation as income. The majority of the court's finding was based on the absence of facts suggesting that trade or business was being conducted.

The application of this precedent established by *Pick 'n Pay Employee Purchase Trust (supra)* to home swap agreements dictates a breakdown of the essence of such a transaction. Home swap agreements entitle a member to a right of use, points, or a cash amount. This benefit, in whichever currency, is received in exchange for providing accommodation in a property owned by the hosting member. The nature of such a transaction is homogenous to a short-term rental agreement. The benefit, in both instances, arises as a consequence of the utilisation of an underlying asset. Dissimilarity only arises with reference to the currency. Judge Wessels asserted, in delivering judgment in *Commissioner of Taxes v Booyens Estate Ltd.* [1918] AD 576, 32 SATC 10 at 15, that income derived without a change in the underlying ownership of an asset gives compelling evidence of the income nature of an item. Ownership remains unaffected by a home swap agreement, positioning this transaction within the ambit of income rather than capital.

This tax treatment is reinforced when the definition of trade, as intended by section 1 of the ITA, is examined. The word "trade" is given a very extensive meaning and specifically includes "the letting of any property", which is, as discussed previously, fundamentally

similar to a home swap. Dissimilarity only arises with regard to the commodity being traded. According to *Burgess v CIR* [1993] (4) SA 161 (A), the definition accorded by the ITA is not even deemed to be exhaustive, providing seemingly convincing evidence for the inclusion of home swap activities within the ambit of trade.

The absence of a profit-driven operation in *Pick 'n Pay Employee Purchase Share trust (supra)* resulted in an exclusion from gross income. An investigation of the correlation between the treatment in the abovementioned case and the relevance to the taxability of home swaps is vital. Stiglingh *et al.* (2015:39) are of the opinion that the intention of a taxpayer is irrelevant when capital is employed to generate a return. Subsequently, it can be inferred that the motivation behind a home swap does not have to be profit-driven to fall within the ambit of income. The utilisation of the underlying capital asset to generate a return provides sufficient evidence of the revenue nature of such an amount (Stiglingh *et al.*, 2015:39). Rental income is an indistinct item of gross income, regardless of whether the proprietor is pursuing a profit-making scheme (Stiglingh *et al.*, 2015:32). No ambiguity exists regarding its character as income, subject to normal tax. The incorporeal benefit arising from a point or traditional swap is homogenous to rental income and should be treated accordingly. Points or a right of use should therefore also be categorised as indistinct items of gross income (Stiglingh *et al.*, 2015:32).

In contrast with the *Pick 'n Pay Share Purchase Trust (supra)*, home swaps do fall within the scope of trade, which is a compelling argument in favour of income. Additionally, it has been established that the essence of a home swap agreement is undeniably income in nature. The homeowner's property represents an asset which is utilised to yield a return. The application of South African case law, coupled with legislation, establishes the prerogative of the SARS to levy normal tax on the benefits ascribed to a home swap agreement. The second test favoured by courts, comprising of the fruit versus tree analogy, is discussed next.

### **2.7.5.2 Fruit versus tree analogy**

The second fact for consideration, according to Olivier (2012:173), relates to the fruit versus tree analogy. The principle that income is the result of the endeavours of capital employed was established by the court's finding in the *Visser case (supra)*. The fruit and tree analogy can subsequently be applied to the employment of one's property to generate a benefit.

The essence of an incorporeal right tends to infer that it is capital. The extent to which the right gives rise to a recurring benefit has to be considered. A home swap member's right of use to the hosting member's home is once-off. There is no lasting benefit as the right of use perishes once it has been consumed. The benefit arising from a home swap is therefore more comparable to the fruit from the tree, than to the tree itself. The home can potentially facilitate an unlimited number of house swaps, whereas the benefit arising from each individual swap is expendable. The lack of an enduring benefit implies that the right of use should be classified as income (*Palabora Mining Co Ltd v SIR* [1973] 3 All SA 636 22). A capital versus revenue analysis is incomplete without deliberation of the taxpayer's *ipse dixit*, which is considered next.

### **2.7.5.3 Taxpayer's ipse dixit**

According to De Koker and Williams (2015: par.3.1.2), South African case law indicates that the intention with the acquisition and subsequent realisation of an asset has persuasive influence. South African case law concerned with the taxpayer's intention strongly emphasises circumstances dealing with the disposal of an asset. There is no change in ownership of the underlying asset when a home swap is conducted. Instead, the property is treated as a fruit-bearing tree with benefits arising from productively employing the capital. The benefits, whether constituting a right of use, points or rental income, will be treated as income. The property itself is capital in nature and a subsequent sale, unless the Rubicon is crossed, will not affect gross income.

The Rubicon refers to the extent of a taxpayer's activities with regard to an asset. Once the magnitude of endeavours surpasses a certain level, the taxpayer is deemed to trade in that asset (Garven, 2015). Trade revenue falls within the ambit of gross income. Only an apportioned percentage of the return on the sale of a capital asset will be subject to normal tax in accordance with the Eighth Schedule of the ITA. The tax liability arising from the sale of a capital item is therefore significantly more favourable to the taxpayer. The next section concludes on the revenue versus capital analysis.

### **2.7.6 Summary and conclusion for revenue versus capital analysis**

The principle established by South African case law compels the classification of an amount as either income or capital. Classification of an item as gross income subsequently eliminates its ability to be designated as capital and vice versa. South African case law and relevant legislation were examined to ensure the correct classification of home swaps.

Home swaps can be facilitated in one of four ways. Consideration receivable is dissimilar; conditional on the type of swap employed. Traditional swaps and hospitality exchanges give rise to a right of use, whereas alternative considerations encompass points or cash, receivable for a point swap or rental agreement respectively. Cash compensation for a rental agreement is an irrefutable item of gross income. Rental operations are explicitly included in the definition of trade. This in turn identifies any proceeds arising from the trade as gross income, regardless of the taxpayer's intention when the transaction originated.

The right of use or points arising from an alternative swapping method is consideration receivable in a currency other than cash. Similar to cash, the right or points are expendable upon consumption and no lasting benefit is obtained, further substantiating the income nature of these benefits. The disposition of the compensation receivable positions the transaction within the ambit of barter trade. As revenue generated by bartering is within the reach of the ITA's fiscal jurisdiction, the currency of compensation should not result in a differentiation of the normal tax treatment. The essence of all home swap transactions is therefore similar to a short-term rental agreement with dissimilarity arising only with regard to the currency.

An exemption for rental income is not permitted in terms of section 10 of the ITA. As discussed in 2.7.2 (*People's Stores case (supra)*, *Cactus Investments case (supra)*, *Brummeria Renaissance case (supra)*) the Commissioner does not differentiate between receipts in cash or otherwise. The absence of a section absolving the amount included in gross income will consequently result in a normal tax liability. Ensuing is a short review of the fundamental conclusions reached in chapter 2.

## **2.8 Summary and conclusion**

This chapter elucidated the concept of home swaps and the functioning of home swap programmes. The two most prominent international home swap programmes, LHS and HE, and their South African imitator, Houseswap, were elected as subjects of this study. Based

on these programmes' practices and swap types afforded to members, four methods to facilitate a home swap were identified:

- a traditional swap,
- a point swap,
- a hospitality exchange, or
- a conventional rental agreement

Traditional swaps and hospitality exchanges give rise to a reciprocal right of use. Point swaps remove the barriers established by incongruent currencies. Cash as a currency is replaced by points, limiting the commercial viability to members of a specific programme. Consideration receivable for a rental agreement is cash. An illumination of these methods followed, and it was deduced that home swaps are in nature barter transactions. The benefits arising from disparate home swapping methods are dissimilar in nature and a parallel is drawn between short term rentals facilitated through bartering. Regardless of the divergence in the currency, the tax treatment prescribed by the ITA should not differentiate between a receipt in cash or otherwise. The consideration attributable to a home swap should be included in a person's gross income.

Guidance provided by South African case law and relevant legislation were considered, and it was concluded that the benefits arising from a home swap transaction constitutes gross income. The valuation of the non-cash benefit is deliberated in Chapter 4.

In order to ascertain the correct normal tax treatment, it is essential to establish when accrual or receipt transpires. This necessitates an in-depth examination of the terms and conditions of the respective home swap programmes selected. Relevant South African legislation, in conjunction with the stipulations of the individual programmes, was analysed to assess when accrual or receipt occurs. Chapter 3 therefore initiates a shift in focus in an endeavour to address the time at which the benefit accrues to the taxpayer.

## CHAPTER 3: THE TIMING OF HOME SWAP BENEFITS IN ACCORDANCE WITH SOUTH AFRICAN LEGISLATION AND CASE LAW

### 3.1 Introduction and background

Home swaps, as discussed in Chapter 2, are facilitated through one of four methods, depending on the programme with which a member is affiliated. The available methods can be categorised as follows:

- a traditional swap,
- a point swap,
- a hospitality exchange, or
- a conventional rental agreement.

Chapter 2 judiciously analysed the nature of home swap benefits through careful consideration of relevant legislation and South African case law. Benefits received in a divergent currency, such as a right or points, were equated to short-term rental agreements facilitated through barter trade. Dissimilarity in the nature of these benefits does however not impede a uniform compliance with the gross income definition. Residents participating in successful home swaps, regardless of the method, incur a liability for normal tax on the value of the benefit accruing from such a transaction, as no exemption is permitted is permitted for rental income in terms of the ITA.

The nature of non-cash home swaps envelops the value of the taxable benefit in complexity. Augmenting the convoluted nature of the benefit for tax purposes is the issue of establishing when such a benefit accrues or is received by a resident of the Republic (hereafter referred to as “resident”). This chapter consequently addresses the following question:

At what time does the benefit elicit a normal tax burden?

Assessing the terms and conditions established by the elected home swap programmes is an essential component in elucidating the timing of accrual and/or receipt. The prerequisites for membership to LHS and HE will be examined in conjunction with the discerning differences of the respective swap methods. Additionally, deliberating relevant South African

case law and legislation is of paramount importance in establishing the time at which benefits accrue; consequently, this will initiate the discussion.

### 3.2 The meaning of accrual or receipt as established by case law

The gross income definition, which, according to Van Zyl (2015:98) can be seen as the cornerstone of income tax in South Africa, requires accrual or receipt to transpire before an amount is subject to normal tax. Benefits arising from a home swap will therefore only fall within the ambit of the South African tax net once there has been a receipt or an accrual. The wording of the definition is such that an amount will be included in gross income at the earlier of these two events. The simultaneous occurrence of accrual and receipt in the same year of assessment is therefore superfluous (*CIR v Delfos* [1933] 6 SATC 92).

Determining whether receipt has transpired in a specific year of assessment presents little difficulty (De Koker & Williams, 2016: par.2.6). The concept of accrual is however left undefined by the ITA and accordingly judicial precedents are followed to establish when a benefit accrues. Numerous judgments, commencing with the *Lategan case (supra)* in 1926, have purported to interpret the meaning of “*accrued to or in favour of*” as intended by the fiscus with the gross income definition (Van Zyl, 2015:98). The precedent set by the *Lategan case (supra)* ascertained that accrual occurs when entitlement vests, regardless of whether payment is only claimable in a consecutive tax year. In 1990, a unanimous decision by the appeal court in the *People’s Stores case (supra)*, confirmed the precedent established by the *Lategan case (supra)*. Instantaneous collectability of an amount is therefore deemed inconsequential when assessing whether such an amount has accrued and falls within the ambit of gross income (Stiglingh *et al.*, 2015:23).

The qualification to the accrual precedent, as established by the *Lategan case (supra)*, was introduced by the appellate case of *Ochberg (supra)*. This case confined the scope of accrual to unconditional entitlement (Van Zyl, 2015:105). Conditional entitlement will therefore prevent a benefit from accruing and attracting an inclusion in gross income. The more recent *Mooi case (supra)* confirmed the qualification as ascertained by the *Ochberg case (supra)*. It was held, in the *Mooi case (supra)*, that a benefit will only accrue upon fulfilment of all the conditions attached to the right. The contingent right merely “*sets up the machinery for creating the benefit*” (*Mooi case (supra)*). Van Zyl (2015:105) submits that the

contribution of both the *Ochberg case (supra)* and the *Mooi case (supra)* is the confinement of the judiciary meaning of “accrual” to vested rights.

A contingent right, on the other hand, is a “*chance or a possibility of a right*”, as per the judgment of Watermeyer JA in *Jewish Colonial Trust Ltd v Estate Nathan Respondents* [1940] AD 163. The Free Dictionary by Farlex (2016) defines the meaning of “contingent” as “*no present interest or right but only a conditional one which will become effective upon the happening of the designated condition*”. The accrual and ensuing normal tax consequences will therefore be postponed until all the conditions ascribed to the contingent right are fulfilled.

A contingent right is juxtaposed with a mere postponement of the enjoyment of a vested right. A vested right, of which the benefit is delayed, will accrue and induce normal tax. The judgment in the *People’s Stores case (supra)* confirmed this principle and resolved the controversy surrounding the *Lategan case (supra)*. Lategan unsuccessfully disputed the Receiver of Revenue’s (hereafter referred to as the “Receiver”) prerogative to tax amounts that have accrued, but for which collection was deferred to a consecutive tax year. The polemic surrounding the accrual principle as established by the *Lategan case (supra)* was introduced by the majority ruling of the Supreme Court of Appeal in the *Delfos case (supra)* and later in *Hersov’s Estate v CIR* [1957] 21 SATC 106. The school of thought presented by these cases submitted that “accrual” is to be interpreted as both “*due and payable*” (Van Zyl, 2015:105). The unanimous ruling in the *People’s Stores case (supra)* settled the polemic surrounding both the timing and valuation of the meaning of “accrual”. This judgment asserted two things: firstly, that the amount to which a taxpayer obtains unconditional entitlement will be included in gross income, and secondly, that such an amount should be included in gross income at its discounted value.

The timing rule, as established by the *Lategan case (supra)* and upheld by the *People’s Stores case (supra)* was reinforced as legal precedent by the decision in *Cactus Investments (supra)*. The valuation rule introduced by the *People’s Stores case (supra)* was however negated by the promulgation of two provisos to the gross income definition. The first proviso was replaced by the Taxation Laws Amendment Act No.31 of 2013 and the second proviso deleted in its entirety. The remaining revised proviso, as stated in the 2015 edition of the ITA, reads as follows:

*Provided that where during any year of assessment a person has become entitled to any amount which is payable on a date or dates falling after the last day of such year, that amount shall be deemed to have accrued to the person during such year;*

The inference made by De Koker and Williams (2016: par.2.6) is the entrenchment of the accrual principle, as pioneered by the *Lategan case (supra)*, in South African tax law. This principle is qualified only by the introduction of unconditional entitlement (*Ochberg case (supra)*). An amount, which is income in nature, will therefore qualify as an accrual, and subsequently fall within the ambit of gross income once there are no additional obligations inhibiting the taxpayer's right to claim performance. Postponement of consumption of the benefit will not impede accrual.

Home swap programmes employ online platforms to conclude swaps via instant messaging. The ECTA ascertains when a valid and binding contract comes into existence for a South African home swap participant. The nature of swap agreements therefore necessitates deliberation of the interrelation between the ECTA, the ITA and relevant case law. The implications of the ECTA on accrual and receipt, as established by case law, are therefore considered next.

### **3.3 The implications of the ECTA on accrual and receipt**

Predominantly, the moment at which a valid and binding contract is established between home swap participants, has to be identified. Home swap transactions are arranged (via instant online messages) between members who are potentially residents in different countries (LHS, 2016j; HE, 2015a). The nature in which the contract is concluded thus compels a deliberation of the legislation that governs electronic commerce.

The rapid evolution of electronic commerce has necessitated governments worldwide to promulgate and enforce electronic communication acts (Ellipsis, 2016). A home swap agreement between a resident and a non-resident therefore imposes legislation in both countries. The scope of this study is however limited to the normal tax burden imposed on residents by the SARS. The legal inference imposed on residents by the electronic communication act of a foreign state therefore falls beyond the scope of this study. The jurisdiction of the ECTA will consequently be the only relevant legislation to determine the date at which a valid and binding contract comes into existence for a resident.

In accordance with section 22(2) of the ECTA, an agreement “*by means of data messages is concluded at the time and place where the acceptance of the offer was received by the offeror*”. Section 23(b) of the ECTA elaborates on the denotation of the word “received”. This section stipulates that it is at the time that “*the complete data message enters an information system designated or used for that purpose*”. A valid contract is therefore instantaneously established once an addressee accepts the offer electronically.

The mere conclusion of a valid contract does however not suffice to ensure accrual or receipt, as envisioned by the gross income definition in section 1 of the ITA (hereafter referred to as “gross income definition”). A tax liability will only arise once an amount has been “*received by or accrued to or in favour of such resident*”. The ECTA simply dictates the time at which a legally enforceable contract comes into existence. Accrual and/or receipt will consequently have to coincide with the contract date in order for the SARS to invoke normal tax at inception of the contract.

The ECTA is therefore of importance in enforcing legal rights of parties to the contract. Tax consequences are governed by whether accrual or receipt has occurred. As absolute entitlement is a prerequisite to accrual, it was essential to gain a comprehensive understanding of the terms and conditions of the home swap programmes selected for this study (LHS and HE), together with a distinct understanding of the particulars of individually structured transactions.

### **3.4 Terms and conditions of home swap programmes elected**

LHS and HE are the two largest international home swap programmes with a collective membership in excess of 135 000 (Tkalčić, 2017; HE, 2016b). Houseswap (hereafter referred to as HS), the first South African home swap programme, was established in mid-2014 (Gqirana & Huisman, 2014). Membership to HS remains trivial in comparison to its international counterparts (HS, 2017a). This is due to residents’ preference for affiliation with international programmes such as LHS and HE. These programmes offer a range of destinations that are significantly more diverse and extensive than the limited, predominantly local listing of HS (HS, 2017a).

The weak South African Rand (Bhoola, 2016) (hereafter referred to as “Rand”) enhances the appeal of non-cash home swap types offered by international programmes. These home

swap types eliminate the automatic handicap experienced by residents reserving accommodation for international travel. Such a swap, agreed between a resident and a member residing in a country other than the Republic (hereafter referred to as “non-resident”), will eliminate the resident’s exchange rate exposure attributable to accommodation in its entirety. The resident’s currency of trade will entail one of three things:

- Reciprocation of the foreign member’s hospitality in the case of a hospitality exchange;
- Dispensation of a right issued by the resident to the foreigner in case of a traditional swap;
- A standardised number of points, dependent on the number of nights agreed, in the case of a point swap.

LHS also allows members to reserve accommodation by way of a rental agreement (LHS, 2016f). As reciprocation is not a prerequisite, this option, even though more flexible, exposes a resident travelling internationally to fluctuations in the exchange rate.

HS’s listing offered access to 148 properties, of which 137 are located in the Republic (HS, 2016a) in 2016. This inability to offer the multiplicity provided by international home swap programmes, such as LHS and HE, significantly inhibits the allure of membership. The most substantial benefit obtained by residents, as discussed above, pertain to the circumvention of the volatility of the Rand when travelling internationally. HS’s lack of international listings might therefore adversely affect growth and sustainability.

Based on membership and popularity, LHS and HE are the unrivalled trailblazers in home swapping. These two international programmes were therefore selected for examination of the terms, conditions and stipulations implemented to govern swaps and protect members. The terms and conditions of HS were not investigated. HS is still a novel and inexperienced contestant to the highly competitive swapping landscape. Membership further reflects this reality (HS, 2017a), contributing to its omission for further analysis. In the sections that follow, the respective terms and conditions of LHS and HE are examined per swap type in order to assess the time at which receipt or accrual transpires and therefore falls within the ambit of gross income.

### 3.4.1 Love Home Swap

LHS provides members with three swap options: a traditional swap, a point swap or a conventional rental agreement can be employed (LHS, 2016a). The scope of this study is limited to the normal tax implications for a resident as imposed by the SARS. As discussed in 3.3., a valid contract, in terms of the ECTA, is concluded once members have agreed, via instant messages, on the details of the trip. This does however not equate to an accrual for normal tax. In the discussion per swap type it is therefore assumed that a valid contract, in terms of the ECTA, was established.

As discussed in 3.2, receipt or accrual, as determined by the coalesced legal precedent set by both the *Lategan case (supra)* and the *Ochberg case (supra)*, has to transpire in order for the SARS to impose a normal tax burden. The taxpayer should thus enjoy a vested right to the benefit arising from the swap agreement. This benefit can encompass a right of use, points or rental income (LHS, 2016a). The validity of the accrual will be unaffected by the postponement of the benefit's enjoyment. The taxpayer's right should however be unencumbered by a future performance to secure absolute entitlement.

The terms and conditions agreed on upon enrolling at LHS will therefore be essential to determine at which time the resident member obtains un-contingent entitlement. An analysis of the general terms and conditions (LHS, 2015c) will initiate the analysis. The member guarantee and conditions (LHS, 2016q) are however so tightly interlaced with the general terms and conditions that a discussion of the one will be incomplete without reference to the other.

#### **Service terms and conditions and member guarantee and conditions**

Paragraph 1.2 of the service terms and conditions states that the utilisation of the website (and its supplementary services) confirms the user's agreement to be bound by the stipulations therein (LHS, 2015c). The service terms and conditions (hereafter referred to as "the terms") distinguish between "exchanges", "rentals" and "swap points scheme". As the terms of engagement and currency of payment are dissimilar depending on the type of swap, the three swap types are subsequently examined separately.

### 3.4.1.1 Exchanges, i.e. traditional swap

An exchange refers to a direct traditional swap (LHS, 2016a). Instead of compensation in a conventional currency, members obtain a mutual right to each other's homes. As explained in 2.6.1, this right can be exercised either simultaneously or non-simultaneously (LHS, 2016a). The member enjoying the benefit of the right to another member's house is the guest. The member extending the right is the host. Traditional swaps therefore operate on the principle that both parties to the agreement will have an opportunity to host and to be accommodated as a guest.

The benefit to which the resident becomes entitled is therefore the right to his/her swap partner's home. The partner extends this right in reciprocation to the resident granting a similar right to his/her home. As this right is an incorporeal asset, receipt will only occur when the resident consumes the right. Accrual, as discussed in 3.2, transpires once the resident becomes unconditionally entitled to this right. Un-contingent entitlement is therefore encumbered until the resident discharges his/her obligation by accommodating the partner.

Subsequently, dependent on whether the resident consumes his/her right prior or subsequent to allowing the swap partner to utilise their right, accrual or receipt will transpire first. The amount will be subject to normal tax at the earlier of these two events. An analysis of the terms is central to addressing the issue of whether accrual or receipt transpires first. An investigation of the basic principles enshrining accrual, as established by case law, will subsequently be pursued.

#### **Accrual applied to swaps as defined by case law**

Accrual equates to an unconditional and un-contingent entitlement. Watermeyer J, in delivering his pronouncement in the *Ochberg case (supra)*, expounded on this principle, as applied by the court in the *Lategan case (supra)*. Any performance or condition impeding the taxpayer's right to claim immediate payment will disqualify an amount from accruing (De Koker & Williams, 2016: par.2.7). The judgment in the *Lategan case (supra)* refers to the uncontested right of the taxpayer to claim recompense in future. In the case of Lategan, his entire harvest was delivered and he had therefore fully discharged all performance obligations. He therefore had an unconditional prerogative to demand payment, even though it was deferred. This situation should be juxtaposed with circumstances where delivery is

incomplete. A definite right to claim payment cannot precede a complete fulfilment of all conditions by the taxpayer (*Mooi case (supra)*). The taxpayer will not be entitled to an amount (of income) until delivery has transpired (De Koker & Williams, 2016: par.2.8).

In order to determine the implications of accrual on traditional swaps, the sequence of events in a traditional swap (hereafter referred to as a “swap”) has to be considered. A contract in terms of the ECTA is established when mutual consent is ascertained. No receipt transpires, as the commodity traded is a reciprocal right that is incorporeal in nature. The benefit of this right can only accrue once the resident has an absolute right unencumbered by any performance or condition.

Essential in assessing the timing of accrual is the distinction between simultaneous and non-simultaneous swaps. In the event of a simultaneous swap, the resident and the swap partner (hereafter referred to as “the partner”) will concurrently consume their mutually bestowed rights. The resident cannot obtain a definite right until the partner has exercised his/her right by inhabiting the home of the resident. Prior to this, the resident has not fulfilled all the conditions attached to the agreement. Accrual will thus be impeded until the partner has occupied the resident’s home in accordance with this agreement. The vesting of unconditional entitlement will therefore coincide with receipt in the event of a simultaneous swap. The resident and the partner will consume their rights (of residing in each other’s homes) simultaneously. The resident’s right therefore becomes absolutely concomitant with consumption of the right bestowed by the partner.

In the event of a non-simultaneous swap, either the resident or the partner will be the first to exercise the mutually exchanged right. The resident will be the recipient of his/her right, should they inaugurate implementation of the swap. Subsequently, receipt will precede accrual (*ITC 1545 [1992] 54 SATC 464*). In this case, as an absolute right is contingent upon discharging the onus imposed by the swap, accrual could not have transpired prior to receipt. However, this sequence will be reversed if the partner is accommodated before the reciprocal right is utilised by the resident. An absolute right vests when the resident fulfils his/her commitments by accommodating the partner. An absolute right equates accrual and the consequential prompting of normal tax. Gross income will thus escalate depending on whether the resident utilises the reciprocal right prior or subsequent to allowing the partner to reside in his/her home.

Non-simultaneous swaps will therefore be included in gross income as follows:

- Upon receipt if the resident exercises the right first;
- Upon accrual if the resident accommodates the partner ahead of utilising the accommodation provided by the partner.

Accrual and receipt will transpire concurrently for simultaneous swaps. The terms are considered next in order elucidate their implication for accrual.

### **Accrual applied to swaps as influenced by the terms**

The terms explicit to traditional swaps are limited to two paragraphs (10.6 and 10.7) (LHS, 2015c). Deliberation of the obligations of members is limited to paragraph 10.7, which reads as follows:

*If an Exchange which has already been accepted and confirmed is cancelled by you, you will be liable for any loss suffered by the other party as a result of such cancellation. If you become part of our Exchange Fee Programme and provided that the value of the loss suffered by the other party as a result of such cancellation does not exceed £2 500, your liability for any such loss may be limited to £250 (plus VAT if applicable) which amount you authorise us to debit from your credit or debit card.*

The first sentence applies to members not affiliated with the Exchange Fee Programme (hereafter referred to as “EFP”). The remainder of the paragraph deliberates the financial indemnity extended (via the EFP) to a member in case of the cancellation of a swap. The EFP is presented as a substitute for personal liability incurred by the party cancelling the swap. The conditions eliciting either a personal liability or the activation of the EFP will therefore be homogenous. The terms and conditions of a traditional swap are limited to paragraph 10.7. The consequences of cancellation are identical, regardless of affiliation with the EFP or the absence thereof. Comprehension of the terms and conditions of the EFP, which is significantly more extensive, is therefore essential to determine when the resident obtains an absolute right.

In the absence of a swap protection pack (automatically issued by electing to participate in the EFP), the member responsible for the cancellation will bear the actual costs incurred by the other participating member (Bryant, 2015b). (Costs qualifying will typically constitute

non-refundable items such as aeroplane tickets and accommodation.) Swap protection therefore merely alleviates the financial burden of the forfeiting party. A resident's loss of right, obtained upon conclusion of a swap, will thus be compensated. Compensation will either be facilitated via the insurance provided by a swap protection pack or recovered directly from the member instigating the repeal (LHS, 2015c; LHS, 2016q).

The particulars of a swap agreement will be specific as to whether the swap envisioned is simultaneous or non-simultaneous and suitable dates will be predetermined and set (LHS, 2016b). The right arising upon conclusion of the swap agreement is conditional upon both parties honouring the stipulations therein. The resident obtains a right supplemented by an obligation (to accommodate the partner) in accordance with the terms of the agreement. As previously discussed in 3.2, a distinction must be drawn between a vested right for which gratification is deferred and a right contingent on a future condition or performance (*Mooi* case (supra)).

Evaluating whether the time at which the right becomes absolute is affected by the terms is therefore crucial in assessing normal tax. De Koker and Williams (2016: par.2.6) hold that the taxpayer's right should be definite and the value convertible into a currency (Van Zyl, 2015:108). A breach of the original swap agreement will result in financial recompense for the offended member. The burden of the compensation will either be borne by the member in contravention of the agreement or by the EFP (LHS, 2015c). Should the swap proceed as planned, a right will be exercisable in future. In case of a breached agreement, the resident will be offered similar accommodation and/or financial recompense for accommodation and actual non-refundable expenditure incurred (LHS, 2015c; LHS, 2016q). Thus, an incorporeal right of analogous value will be exercisable in future, or the equivalent of the right's value will be disbursed. The implication of the terms on accrual can be summarised as follows:

A resident will incur a normal tax burden at the earliest of the following:

- When his/her obligation is discharged in accordance with the agreement (as will be the case in a non-simultaneous swap). The resident has relieved his/her responsibilities of accommodating the partner. The reciprocal right granted by the partner therefore becomes absolute. A subsequent forfeit by the partner will result in financial recompense for the resident.

- When the resident consumes his/her right. This can be in the event of a simultaneous or non-simultaneous swap. The resident receives the right and enjoys its benefit prior to accrual. This will only be applicable to a non-simultaneous swap if the resident is the first to exercise the reciprocally transferred rights.
- When the partner breaches the swap agreement subsequent to conclusion, but prior to either party exercising their rights. Such a cancellation will entitle the resident to cash recompense or a substitute home at no further cost. The resident's performance obligations are deemed fulfilled in such an event. Consequently, a definite right will vest and accrual will transpire.

The right mutually bestowed by participating members is therefore contingent until either party exercises their right (simultaneously or independently) or one party repeals the swap. The resident will either receive the benefit (through consumption) or it will accrue to him/her, conditional on the specific terms negotiated. Dependent on whether accrual or receipt transpires first, the resident's gross income should reflect the value of the right accordingly.

An analysis of the terms relating to swaps will be incomplete without deliberating the impact of a repeal on the time at which an unconditional right vest or is received. A brief consideration of the interrelation between cancellations and accrual or receipt follows. (The essence of HE's swaps and the terms of use governing cancellations are analogous to the traditional swap facility offered by LHS.) The terms of both swap programmes serve as fortification to prevent financial loss due to repeal by one partner. A member revoking an initial swap will be liable to compensate his/her swap partner (LHS, 2015c; HE, 2017b). The impact of a cancellation on the timing of accrual will therefore be congruent, regardless of whether affiliation is with LHS or HE. The ensuing discussion and subsequent conclusions will therefore be relevant to all traditional swaps, whether facilitated by LHS or HE. (Refer to 3.4.2 for a more extensive discussion of HE.)

## **Cancellations**

A swap agreement can be voided either through mutual consent or by either party to the arrangement. An annulment of the swap through reciprocal consent will denote a mutual renouncement of rights prior to the exercise thereof. In this event, the resident's gross income will remain unaffected. The right obtained upon conclusion of the swap is relinquished prior to becoming absolute. As no amount (right) has been received by or has

accrued to the taxpayer, no normal tax burden will arise (*Cape Consumers (supra)*). A breach, initiated by either the resident or the partner, will however elicit financial compensation for the aggrieved party. Identification of the party forfeiting the swap is consequently vital to assess the resident's normal tax implication.

### **Cancellations instigated by the resident**

The resident can repeal the swap prior or subsequent to becoming unconditionally entitled to the right. A cancellation prior to accrual or receipt will result in a forfeit of the right. Subsequently, in the absence of any receipt or accrual, gross income will remain invariable (De Koker & Williams, 2016: par.2.1). The onus to settle non-refundable expenditure incurred by the partner will however be on the resident or the EFP (depending on the option elected).

Section 11 of the ITA governs the extent to which such an expense qualifies for a normal tax reprieve. The stipulations of the general deduction formula are found in section 11(a) of the ITA. A critical prerequisite for such a loss to be eligible for normal tax relief is the carrying on of a trade. The degree to which the practice of participating in home swaps adheres to this criterion exceeds the scope of this study.

A repeal that succeeds the receipt (and consequent consumption) of the right is limited to non-simultaneous swaps. The resident exercises the right prior to accommodating the partner in his/her home. The tax implication of such a cancellation is limited to the recoupment claimable by the partner. The resident's gross income will reflect the value of the right when it is utilised, as it signifies receipt. Consequently, accrual will not transpire, as the resident never discharged the duty of conferring accommodation. As stated in 3.2, the simultaneous occurrence of accrual and receipt is superfluous (*Delfos case (supra)*). Receipt will bestow an indelible right on the SARS to levy normal tax.

### **Cancellations instigated by the partner**

A termination instigated by the partner prior to either party exerting their rights will bestow an absolute right on the resident. The terms require the partner to offer either alternative accommodation or a cash recompense equal to the accommodation's worth (LHS, 2015c). At the time of such a cancellation, the partner surrenders the right extended by the resident.

No performance obligations or conditions remain to be fulfilled by the resident; accrual consequently transpires. Repeal by the partner subsequent to spending his/her right (by residing in the resident's home) will not alleviate the resident's normal tax burden. The resident would have attained an absolute right as his/her obligation in terms of the swap was settled.

Normal tax is imposed at the initial accrual (De Koker & Williams, 2016: par.2.3). Payment due by the partner will therefore just be the actual receipt of an amount already burdened (at the time of accrual) by the fiscus (*Isaacs vs CIR* [1949] 16 SATC 258). (This compensation can be either cash or the proposal of alternate accommodation.) When the recompense entails an offer to substitute the home forfeited, the value of the second property might necessitate a re-visitation of gross income. The nature of such a transaction qualifies it for barter trade (as discussed in 2.3). A right of use is exchanged in reciprocation for a homogenous right. De Koker and Williams (2016: par.2.16) hold that, where accrual precedes receipt and the transaction is facilitated via barter, any excess in the value of the asset eventually received is taxable. Thus, should the right attached to the (second) surrogate home be higher in value, the resident's gross income must escalate accordingly.

### **Conclusion: Traditional swap**

Accrual and receipt always transpire concurrently for simultaneous swaps. In the event of non-simultaneous swaps, the sequence of receipt and accrual is determined by the order in which swap partners consume the right. Receipt will precede accrual if the resident is the first to exercise the right. (The order will however change if accrual precedes receipt in the event of the resident being the first to provide accommodation.)

Three variables govern the impact on the normal tax assessment of a resident in the event of a cancellation:

- the identity of the participant responsible for the termination;
- the timing of the repeal; and
- whether the resident has consumed the right.

Normal tax implications are consequently prompted when a right is consumed (whether the resident or partner is the initiator) or the agreement is rescinded by either one of the parties. The influence of case law and the terms as it relates to rental income, is investigated next.

### **3.4.1.2 Rental**

A rental (in the context of LHS's programme) does not diverge from a conventional rental agreement. The benefit accruing to the hosting homeowner will be the cash receivable in exchange for granting a right to the guest. This benefit, as discussed in 2.7.2, falls within the scope of gross income (*Visser case (supra)*). The terms conducting rentals for hosts are found at 10.9 (LHS, 2015c). Clause (b) reads as follows:

*subject to clause 10.9(c), 10.9(d) and 10.9(e), we will arrange the transfer of the Accommodation Fee due to you (less the Host Fee, if applicable) 48 hours following the start of each Rental. Payment transfers may then take up to 10 days to clear, depending on the Host's bank;*

Prior to discussing the clauses to which 10.9(b) is subordinate, clarification of the meaning of "*the start of each Rental*" is essential. The word "start" in this context refers to the predetermined date from which the guest possesses the right to occupy the property for a prearranged duration (Bryant, 2015b). "Start" does not refer to the date on which a valid contract, in terms of the ECTA, is concluded. The denotation of the word "start", applied in the context of rentals, will therefore signify the meaning ascribed to it. The accommodation fee is released to the host within 48 hours from the date on which the lease started. Receipt will only transpire once the recompense reflects in the host's bank account. Following the elucidation of "start", the implication of the terms on gross income, in the absence of a cancellation, is first examined.

#### **Accrual and receipt of a successful rental**

In the absence of a termination, the accommodation fee cannot accrue to the host prior to the guest residing in the rental home. Depending on the cancellation policy favoured by the host, entitlement to a fixed percentage of the total accommodation fee accrues gradually as time to the start of the rental decreases. Accrual can however not be absolute, as the host

has not discharged the onus of delivery (*Mooi case (supra)*). The host's entitlement can therefore not be absolute before the obligation to provide accommodation has been relieved.

Once the guests take up residence, accrual transpires gradually as the resident fulfils the performance obligation. Each day of accommodation discharges the conditions upon which vesting is contingent. The host's right to the specific day's accommodation fee becomes definite. Accrual might precede receipt, depending on the number of days hosted, as the transfer of the cash might take 2–10 days after guests take up residence (LHS, 2015c). Receipt of the accommodation fee in its entirety prior to complete fulfilment of the aforesaid conditions will however elicit normal tax on the full amount (*Delfos case (supra)*).

Whether accrual or receipt transpires first will only hold relevance if the period of accommodation exceeds the host's year of assessment. In such an event, the aggregate accommodation fee will be subject to tax if has been collected in full. Receipt of the lump sum subsequent to year-end will induce normal tax on the accrued amount, i.e. the number of days expired before year-end.

In the event of a successful rental, both accrual and receipt are deferred until the guest takes up residence in the host's home. An inclusive comprehension of rentals however requires a discussion of the clauses to which 9.10(b) of the terms is subject.

### **Cancellation clause 10.9(c)**

This clause governs incidents where a guest terminates a confirmed rental. The terms prevent the host from collecting any consideration prior to the cancellation (LHS, 2015c). In such an event, the host's policy determines the amount due. One of four cancellation policies can be elected (LHS, 2017c), namely:

- strict
- firm
- moderate
- relaxed

All cancellations must be made by 12:00 midday Central European Time (hereafter referred to as "CET") on the appropriate day.

The guest surrenders the right to occupancy but forfeits a fixed percentage of the total accommodation fee (LHS, 2015c). The host becomes unconditionally entitled to the percentage forfeited by the guest as no encumbering conditions remain. Unconditional entitlement of the amount due, based on the assumption of cancellation by a guest, will vest as follows:

### **Strict policy**

- 57.5% of the rental fee more than two months before the start of the stay;
- the balance of 42.5% (or 100% of the cumulative accommodation fee) less than two months before the start of the stay.

### **Firm policy**

- 15% of the rental fee more than two months before the start of the stay;
- 42.5% of the rental fee (or 57.5% of the cumulative accommodation fee) more than one month but less than two months left before the start of the stay;
- 42.5% of the rental fee (or 100% of the cumulative accommodation fee) at 12:01 CET on the final day before the booking is due in less than one month.

### **Moderate policy**

- 15% of the rental fee more than one month before the start of the stay;
- 42.5% of the rental fee (or 57.5% of the cumulative accommodation fee) more than one month but less than two weeks left before the start of the stay.
- 42.5% of the rental fee (or 100% of the cumulative accommodation fee) at 12:01 CET on the final day before the booking is due in less than two weeks.

### **Relaxed policy**

- 15% of the rental fee at 12:01 CET on the final day before the booking is due in less than two weeks;
- 42.5% of the rental fee (or 57.5% of the cumulative accommodation fee) when there is more than one week but less than two weeks left before the start of the stay;
- 42.5% of the rental fee (or 100% of the cumulative accommodation fee) at 12:01 CET on the final day before the booking is due in less than one week.

Un-contingent entitlement equates accrual, as previously discussed. The accommodation fee, in its entirety or in part, therefore accrues to the host at the time of termination by the guest.

### **Cancellation clause 10.9(d)**

Clause 10(9)(d) deals with a cancellation instigated by the host. The host will forfeit any claim to the accommodation fee but the applicable expenditure incurred by LHS on the host's behalf will still be recouped from the host (LHS, 2015c). As the accommodation fee is only released within 48 hours of the start of the rental, no reimbursement by the host will be required. LHS will simply withhold the amount sacrificed and the host will receive no disbursement. As repeal precedes accrual or receipt and void the host's right to claim any further compensation, gross income will remain unaffected.

### **Cancellation clause 10.9(e)**

This clause governs instances where the rental home becomes uninhabitable during the guest's stay. The host forfeits the accommodation fee for the number of days that the house was unavailable to the guest (LHS, 2015c). In the event that LHS had already disbursed the accommodation fee, a liability would arise to the host to reimburse LHS for the number of days forfeited. The duration of the rental agreement will direct the manner in which the recoupment is structured. One of two potential scenarios will arise (LHS, 2015c):

- In the event of a longer rental period, the host might already have collected the entire accommodation fee prior to the house becoming uninhabitable. Receipt will precede accrual in such an instance.
- In the event of a shorter rental period, LHS disburses the net accommodation fee, after penalising the host for uninhabitable days. The forfeited balance will neither have been received, nor have accrued.

Longer rental periods therefore elicit a cash outflow for the host, whereas a diminished net cash inflow is the corollary of a shorter rental period. The normal tax treatment of the respective rental periods is discussed below.

## Longer term rental

The recoupment of the accommodation fee can transpire in the same or an ensuing tax year; however, this does not limit SARS's prerogative to levy normal tax on the total accommodation fee initially collected by the host. The definition of "gross income" requires inclusion of the "*total amount*" that was received during the year. The Free Dictionary by Farlex (2016) defines "gross" as "*exclusive of deductions*". Case law further substantiates the legal sentiment. In the *Pyott case (supra)* a potentially refundable deposit was included in gross income, as the appellate court found that it was received for the benefit of the taxpayer. The customer was under no obligation to return the empty cookie tin (which was the subject of dispute) and the deposits (collected by the merchant) were not ring-fenced from other income. The potential for recoupment did not defer the imposition of normal tax. The accommodation fee, at the time of its receipt, has no preordained reimbursement terms. The host is at liberty to expend the entire amount immediately. The requirements of the word "receipt", applied within the context of the gross income definition, are thus adequately met to provoke normal tax (*Delfos case (supra)*). In the event of a claim instigated by LHS against the host, the taxpayer's sole remedy is to appeal to section 11 of the ITA. The deductibility of such expenditure exceeds the scope of this study and is not pursued.

## Shorter-term rental

The accommodation fee forfeited neither will have accrued nor have been received, as the host has not discharged the full performance obligation. Subsequently, the Receiver's prerogative to charge normal tax will be limited to the accommodation fee excluding the penalty for days forfeited.

## Conclusion: Rental

The duration of a rental will determine whether accrual or receipt elicits normal tax. Accrual will transpire in intervals as the host fulfils the conditions of the rental by accommodating the guest. The entire accommodation fee will therefore only accrue upon expiry of the rental. Receipt will however precede accrual in the event of longer-term rentals, as the total accommodation fee is transmitted within 48 hours of the guests taking occupation of the host's home. Whether accrual or receipt is the first to prompt normal tax is however irrelevant if the rental concludes within a single tax year. Cancellations are to be considered

independently when a host's normal tax obligation is assessed. The time at which a point swap elicits normal tax is considered in the subsequent section.

### 3.4.1.3 Swap points scheme

Swap points (hereafter referred to as "points") as alternative currency are a relatively novel concept in the home swapping community. LHS pioneered the points model in 2013 (O'Hear, 2013). LHS prescribes the following structure for point swaps (LHS, 2016h):

- The points charged per property per night range from 50 to 300.
- The homeowner is at liberty to assess the number of points per night.
- LHS provides each host with a recommendation in the "Points" section of "My homes" of their personal profile.
- The number of points is determined in correlation to the value of the property.
- Points due are calculated automatically when travel dates are submitted.
- Once the trip has been confirmed by the host, the points are immediately credited to the host's account (LHS, 2016g).

The benefit receivable by the host is therefore the number of points earned in return for providing the guest with accommodation. The classification of these points as an "amount", as envisioned by the SARS with the definition of gross income in the ITA, was established in 2.7.2.

### Accrual and receipt in the context of a point swap

Receipt transpires immediately after the point swap agreement (hereafter referred to as "point swap") has been concluded (LHS, 2016g). In *Geldenhuis v CIR* [1947] 14 SATC 419, the court ascertained that the receipt of an amount is included in gross income if it was "*received by the taxpayer on his own behalf for his own benefit*". Consequently, the physical receipt of the points does not ensure that the amount falls within the ambit of "received by", as envisioned by the gross income definition (De Koker & Williams, 2016: par.2.5). The resident host (i.e. the recipient of the points) will therefore only be liable for normal tax if the points are received for his/her benefit.

In order to comprehend the intended meaning of benefit in this context, points are compared to rental income. The nature of the transaction simulates a prepayment of rental income. The host provides accommodation for a set period at a predetermined date in exchange for consideration. The consideration is instantaneously credited to the host's account, but the member requesting accommodation will only enjoy the right of use in future. A traditional rental agreement and point swap are dissimilar merely in terms of the trade currency. The points transferred by the guest are for the benefit and immediate consumption of the host (LHS, 2016g). The host is therefore at liberty to expend the points upon receipt, similar to a cash advance on a rental property.

The directive provided by the SARS for rental income received in advance can therefore be applied to points received in advance. The SARS will levy normal tax on rental income in the year that it accrues or is received (SARS, 2016b). *ITC 1545 (supra)* accentuated the use of the word "or" in the gross income definition of the ITA. The court held that the inference denotes the validity of a receipt in the absence of an accrual (Stiglingh *et al.*, 2015:21). Based on the precedent set by case law, Stiglingh *et al.* (2015:22) conclude that an amount will be considered as received if the taxpayer intended, upon receipt, to collect the amount for his/her benefit. Acquisition of membership sufficiently establishes the intent of the host. The mandate of LHS is to afford its members with cost-effective holiday options (LHS, 2017e). Membership therefore signifies intent to benefit through participation in the programme.

The intent of the host was attested and the points are received at the time the agreement is concluded. A receipt, within the ambit of the gross income definition in the ITA, transpires at the time the point swap is consented to by both the guest and the host. Mutual consent, facilitated by the online platform provided by LHS, suffices as proof for a valid contract in terms of the ECTA. The host will therefore become liable for normal tax upon agreement of the point swap (via LHS's online platform). As receipt precedes accrual and an amount is included in gross income at the earlier of these two events, the timing of the accrual of the points is not examined.

Acquaintance with the terms is fundamental to ensure accurate and comprehensive elucidation of the time at which receipt transpires and elicits normal tax. Cancellation clauses and their resulting influence on normal tax are discussed separately below.

## **Cancellation clause 10.11**

Clause 10.11 deals with the guest's rights and responsibilities. The ramification for a guest relinquishing the initial swap agreement is a reimbursement of points spent. LHS debits points against the host's account and restores the balance of the guest partially or completely. The following formula is applied (LHS, 2016p):

- Up to 48 hours after agreeing the trip: 100% of points are returned.
- four or more months before the start of the trip: 75% of points are returned.
- two to four months before the start of the trip: 50% of points are returned.
- one to two months before the start of the trip: 25% of points are returned.
- Fewer than 30 days before the start of the trip: no points are returned.

In the spirit of endorsing the benefits of points, LHS credits the guest's account with points calculated in accordance with the policy above, without seeking any reparation from the host (LHS, 2015c; Sekher, 2016). The host therefore has the autonomy to deal with the points without the limitations imposed by a retention period. The conclusion of the point swap coincides with the transfer of the points. The host therefore becomes the unconditional beneficiary of the points upon receipt; thus, a liability for normal tax on the value of these points arises.

## **Cancellation clause 10.12**

This clause deals with cancellations instigated by the host. Two potential situations and the accompanying ramifications are discussed next.

### **Cancellation clause 10.12(b)**

Clause 10.12(b) presides over cancellations due to unforeseen circumstances beyond the host's "*reasonable control*". The host will forfeit all points awarded for the specific point swap and LHS debits the account accordingly to reflect the adjustment. In the event of the host's point balance being insufficient to recover all or a portion of the points, LHS can require the host to re-pledge the home for a period equivalent to the worth of the points expended (LHS, 2015c). A distinction must be drawn between whether the points were expended or whether they could be recouped (in accordance to the policy set out) (LHS, 2016p).

### **The implication of clause 10.12(b) if points have been spent**

In the event of the points already disbursed, the normal tax treatment will simulate the tax treatment prescribed for a successfully completed point swap. Whether the cancellation transpires in the same or ensuing tax year, the host received and consumed the benefit. Subsequently, the resident will be subject to normal tax in the year of receipt (*ITC 1545 (supra)*).

### **The implication of clause 10.12(b) if points are recouped**

Points have been equated to rental income, of which the currency is divergent. The normal tax implication when points are recouped will therefore imitate the remedy discussed under cancellation clause 10(9)(e). The host's gross income must reflect the full value of the gross points received. A recoupment, whether transpiring in the year of the initiating agreement or an ensuing year, will not encumber the Commissioner of Revenue's (hereafter referred to as the "Commissioner") claim to normal tax on the value of the total points collected. The availability of tax reprieve in the event of a cancellation (and consequent recoupment) exceeds the scope of this study.

### **Cancellation clause 10.12(c)**

Clause 10.12 (c) governs cancellations in the absence of "*events or circumstances beyond your reasonable control*". A cancellation of this nature warrants an immediate suspension or cancellation of such a host's account (LHS, 2015c). LHS reserves the right to exercise discretion in ascertaining whether a cancellation is deliberate or due to unforeseen circumstances. Death, natural disaster and terminal illness are a few of the instances for which a host will not be penalised (Sekher, 2016).

The normal tax treatment will equate the treatment prescribed by clause 10.9(e) and 10.12(b). Termination subsequent to receipt does not deter the imposition of normal tax on the value of total points collected. The host's inability to spend points prior to termination does therefore not deflect from its inclusion in gross income.

## **Cancellation clause 10.10**

Clause 10.10 governs the host's eligibility to enjoy the benefit procured through points. This is the final clause for consideration in assessing the recipient of points' tax position. Clause 10.10 disqualifies any host from utilising his/her points in the event that they are no longer subscribed to LHS. Cancellation, as previously discussed (in clause 10.12(b) and 10.12(c)), will not encumber the prerogative of the SARS to include the full value of points collected (at initiation of the point swap) in gross income.

Similar to rental agreements and traditional swaps, remedy is offered for actual losses, other than accommodation, suffered by guests (LHS, 2015c). The host can elect to limit liability to £250 by obtaining membership to the EFP. Alternatively, the host will have to reimburse the guest for actual losses suffered (LHS, 2015c). Whether recourse is administered by way of the EFP or the host itself, damages cannot be claimed in excess of £2 500 (LHS, 2015c).

### **Points: Conclusion**

Points are a virtual currency for which receipt always precedes accrual. The resident's gross income will reflect an amount (equating the value of the points) in the tax year that the point swap was concluded. A point swap can be annulled by either the guest or the host. Gross income is not affected by a subsequent repeal, regardless of the party initiating it or the year of assessment in which it transpires. The disposition of the fiscus towards the deduction of expenditure incurred by the host exceeds the scope of this study and is not investigated.

### **3.4.2 Home Exchange**

HE, the second home swap programme to be examined, is Love Home Swap's most prominent rival, contending with listings in more than 150 countries worldwide (HE, 2016b). HE offers two swap options (HE, 2016C):

- traditional swap; or
- hospitality exchange.

The principles governing the two swap options are homogenous to a traditional swap offered by LHS (these swaps can thus be simultaneous or non-simultaneous). The benefit to which

such a member becomes entitled is therefore a right congruent to the one extended in a traditional swap governed by LHS. (As the recompense for both sub-categories is similar, no distinction is drawn between these exchanges in assessing the time at which the resident becomes liable for normal tax.) A third option allows the owner of a designated bed and breakfast establishment (hereafter referred to as a “B&B”) to list their property on HE (HE, 2017b). The arrangement is made outside the parameters and protection provided by HE. Thus, the tax consequences for members operating B&Bs exceed the scope of this study and are not examined.

The principles considered in 3.4 concerning the validity of a contract and accrual or receipt remains invariable. HE, similar to LHS, hosts an electronic online platform to facilitate secure online messaging. This platform aids members in the engagement and conclusion of contracts. The ECTA governs the validity of contracts. As discussed in 3.3, a valid contract does not necessarily equate to accrual and/or receipt. Assuming that a valid contract, adhering to the ECTA, has been established is therefore presupposed in conducting the discussion.

A critical analysis of the terms of use, as with LHS, will be vital to assess the timing of accrual and/or receipt. Un-contingent entitlement and the absence of any conditions of further performance will result in accrual (*Lategan case (supra)*; *Ochberg case (supra)*) and consequently an inclusion in gross income. Accrual is conditional upon the resident discharging his/her liability by accommodating the partner in accordance with the agreement. Once the resident has obliged, the right to use the partner’s home vests, and accrual transpires (De Koker & Williams, 2016: par.2.8). Receipt might precede accrual if the resident exerts this right prior to hosting the partner (in a non-simultaneous swap). An analysis of the terms of use is indispensable to ensure an inclusive interpretation of the time at which the swap provokes normal tax.

### **Code of conduct**

Enrolment with HE requires consent to be bound by the terms of use. Members will be entitled to enjoy the benefits and rights bestowed, but will also bear the responsibility to engage in swaps in accordance with the stipulations (HE, 2017b). The code of conduct (hereafter referred to as “the code”) governs the terms on which members engage with each other, present their homes and ultimately the ramifications in the event of a cancellation. A

cancellation, whether justified or not, will impose an obligation on the forfeiting member to *“pay reasonable compensation for such accommodation if necessary, and/or by reimbursing your partner for non-refundable travel expenses”*. A failure to comply with these stipulations might result in a permanent and non-refundable termination of membership (HE, 2017b).

The terms of engagement are therefore analogous with the stipulations of LHS for traditional swaps. The normal tax treatment is contingent firstly on the type of swap, i.e. simultaneous or non-simultaneous. Secondly, the order in which a non-simultaneous swap is structured will directly influence the time at which a normal tax liability arises for the resident.

The comprehensive discussion of traditional swaps in 3.4.1 therefore applies to swaps facilitated through HE. The time at which accrual or receipt transpires can subsequently be summarised as follows:

- The right granted to the resident under a non-simultaneous swap will become subject to normal tax upon receipt if the resident exercises his/her right prior to reciprocation.
- The reciprocal right transferred cannot accrue to the resident prior to utilisation by either participant, as all the conditions upon which an absolute right is contingent have not been satisfied.
- Accrual will however precede receipt if, in the event of a non-simultaneous swap, the partner is the first to expend the right. Accommodating the partner discharges the resident's obligation in terms of the agreement. The resident's right to performance becomes definite.
- Simultaneous swaps will only elicit normal tax when the mutually bestowed right is consumed. Accrual and receipt will transpire concurrently. The resident will exercise his/her right whilst simultaneously accommodating the partner.

The normal tax implications for a resident affiliated with HE will therefore be dependent on the timing and type of swap. The benefit associated with non-simultaneous swaps will fall within the ambit of gross income at either accrual or receipt, contingent on the swap order. Accrual and receipt will transpire concomitantly in the event of a simultaneous swap.

HE's terms are significantly simpler and more concise than those of LHS. There is no further elucidation concerning consequences in the event of forfeiture by either party to a swap agreement. The most severe penalty is termination of membership. (In the event of such a

termination, the user's listing will be removed from the website and HE will retract the offer of any services (HE, 2017b). The participant repealing the original swap will also be liable to reimburse the partner for non-refundable travel expenditure and subsidise substituted accommodation (HE, 2017b). The ramification of such a cancellation, whether instigated by the resident or the partner, is examined independently to determine its result on gross income.

## **Cancellations**

Either a resident or a partner can instigate a cancellation. The characteristics of traditional swaps, independent of the home swap programme with which a member is affiliated, are consistent. The nature, conditions for engagement and repercussions in the event of repeal are congruent for all traditional swaps, regardless of whether a member is affiliated with LHS or HE. The consequences elicited by cancellations are discussed comprehensively in 3.4.1.

### **3.5 Conclusion: Receipt and accrual in the context of home swap programmes**

The analysis of case law and South African tax legislation, in conjunction with an exploration of the terms and conditions of LHS and HE, ascertained the time at which receipt and/or accrual transpire for a resident. Timing is however influenced by numerous variables:

- The swap method;
- whether a non-cash swap is simultaneous or non-simultaneous; and
- the implication of cancellation policies.

Identifying whether there has been a receipt is significantly simpler than establishing the time at which accrual transpires. Accrual requires an unequivocal claim to an amount in the absence of any conditions encumbering such a right. The Commissioner's prerogative to levy normal tax is not deterred if accrual and receipt do not transpire in the same tax year. The principles that can be applied to successful swaps to determine the time at which a tax liability arises are discussed below.

Accrual will precede receipt for short-term rentals as collection of the accommodation fee succeeds expiry of the accommodation. In the event of a long-term rental, receipt will precede accrual as cash is collected before the accommodation agreement has run its full

term. Once receipt has transpired, the full amount falls within the ambit of gross income. A delay in the transmission of the accommodation fee will result in accrual eliciting normal tax prior to receipt. Drawing a distinction between accrual and receipt is only significant if a rental swap extends over two tax years. Adherence to the abovementioned principles will then be critical to assess gross income.

Traditional swaps and hospitality exchanges (hereafter collectively referred to as “traditional swaps”) entail the trading of reciprocal rights. An obligation to reciprocate encumbers the resident’s unconditional right to the partner’s home. A simultaneous traditional swap will prompt accrual and receipt to transpire concurrently. A non-simultaneous traditional swap will elicit normal tax at either accrual or receipt, depending on whether the resident consumes his/her right prior to or subsequent to accommodating the partner. Receipt transpires if the resident is the first to exert the right conferred by the partner. A reversal of this order (i.e. if the resident is the first to offer accommodation) will result in accrual to precede receipt.

Point swaps offer members the opportunity to circumvent the disparity between exchange rates and employ a virtual currency to conclude a rental agreement. Points are credited to a member’s account upon conclusion of the agreement in exchange for accommodation. The host’s absolute right to the points is precluded by fulfilment of the point swap conditions. Receipt however transpires immediately and its validity to be included in gross income is not incapacitated by the absence of accrual. The host’s gross income should consequently reflect the value of the points in the year of receipt of the points.

Cancellations require a separate assessment, per swap type and conditional on the terms and conditions ascribed to such a swap. In this chapter, the time at which accrual and/or receipt transpires has been elucidated. The value attributable to the currency traded (whether cash or non-corporeal in nature) has however not been established. Based on legislation and relevant case law, the value to be reflected in gross income is assessed in Chapter 4.

## CHAPTER 4: THE VALUE OF HOME SWAP BENEFITS IN ACCORDANCE WITH SOUTH AFRICAN LEGISLATION AND CASE LAW

### 4.1 Introduction and background

Chapter 3 investigated the time at which accrual or receipt transpires in the case of a resident actively participating in home swaps. Relevant case law, legislation and the terms and conditions of home swap programmes such as LHS and HE, in conjunction with cancellation clauses, were scrutinised and considered. The four different home swap methods were analysed independently to ascertain the time at which the fiscus attains a prerogative to levy normal tax.

The gross income definition, as envisioned by the legislator in section 1 of the ITA, reads to include *“the total amount, in cash or otherwise”*. This phrase implies that the condition attached to a receipt and accrual is its classification as an amount. In Chapter 2 (see 2.7.2) the conformance of the benefits receivable, whether in cash or otherwise, to the word “amount” as applied within the context of gross income was ascertained. Ascribing a value to the amount is of critical importance, as gross income is the result of a calculation. Normal tax cannot be levied in the absence thereof. The currency of exchange that is potentially employable by a guest residing in a host’s home is divergent in nature and can consist of points, a right or cash (LHS, 2015b; HE, 2016c). In this chapter, each method of payment is examined separately in terms of relevant case law and legislation – ensuring its accurate and appropriate inclusion in gross income.

The simplicity and ease offered by online platforms encourages home swaps between residents and international partners (Spagnoletti, 2015). Consequently, two issues are raised: 1) conversion of the recompense collected and 2) the relevant tax jurisdiction. Residents collect compensation in a foreign currency and rights and benefits are created in both the Republic and another country (LHS, 2015c; HE, 2017b). A reconnaissance of the value ascribable to these benefits will therefore be incomplete without reference to the mechanisms of taxation presiding over such transactions. Section 25D of the ITA governs the timing and rate of conversion of such amounts. Section 6quat of the ITA offers relief to residents liable for tax imposed by the government of another country on income from a source outside the Republic. It is therefore essential to ensure a holistic overview of valuation by deliberating on the influence that double tax agreements, section 25D and

section 6quat, will have on the normal tax burden of a resident. Section 43 of the Eighth Schedule of the ITA is the final section requiring cognisance. This section administers the acquisition and disposal of capital assets in a foreign currency. The scope of this study is however confined to gross income, rendering any further investigation regarding capital gains redundant.

Chapter 4 therefore purports to ascribe a value to the non-cash benefits or the cash disbursement in the tax year in which accrual and/or receipt transpires. This discussion commences with a general discourse to indicate compliance of non-cash benefits to the word “amount”. An in-depth analysis emphasises the valuation and the hindrances encountered in appraising non-cash benefits. In conclusion, tax relief offered by section 6quat and double taxation agreements are considered.

#### **4.2 Compliance of non-cash benefits with the word “amount” as applied within the gross income definition**

Designating a non-cash benefit as an “amount” is not an unfamiliar concept to the Receiver. Watermeyer J, in the *Lategan case (supra)*, was one of the first to enunciate judgment on this. In delivering the court’s unanimous decision, he assigned a more expansive meaning to the word “amount”, and included any form of property (whether corporeal, incorporeal, debt or a right) earned by the taxpayer and to which a fiscal value can be ascribed.

Judge Watermeyer’s sentiment was validated by Chief Justice Wessels, in the Appellate Division’s split judgment in 1933 in the *Delfos case (supra)*. The court held that something which cannot be “*turned into money*”, cannot constitute income. In 1990, the case of *People’s Stores (supra)*, offered the courts the opportunity to revisit the pronouncement in the *Delfos case (supra)*. Hefer JA upheld the pronouncement of Watermeyer J in the *People’s Stores case (supra)*. Debt, which was the point of contention, was merited to be gross income, as its nature permits the allocation of a value, in monetary terms, to the debt. In *Stander v CIR* [1997] (3) SA 617 (C) the court held the opinion that a subjective view is to be taken in order to assess whether a receipt constitutes an amount for a particular taxpayer. As the benefit awarded to Stander could not be encashed by him, the court rejected its designation as an amount. The majority decision of the Appellate Division in the *Ochberg case (supra)* is juxtaposed by the ruling in the *Stander case (supra)*. Ochberg argued that the lack of benefit from the receipt disqualified the amount from constituting

gross income. In pronouncing the majority ruling, Chief Justice De Villiers rejected this interpretation and enunciates the following at 97:

*“Whether and to what extent the person may have benefited by the receipt of the income is irrelevant ...”*

He further opines, at 98, that receipts are all either income or capital in nature. Thus, classifying an amount as income (as opposed to capital), is sufficient to place it within the ambit of gross income.

Smit (2008:15) submits that a two-tier approach was followed by the majority of the court in the *Ochberg case (supra)*. The first tier of inquiry, once accrual or receipt has been established, is to determine whether the benefit comprises cash or something other than cash. Once the nature of the receipt or accrual *in casu* has been ascertained to be incorporeal, the second question remains to be addressed. This necessitates the designation of a monetary value to the right or other non-cash receipt (Smit, 2008:15). An inability to value the non-cash benefit will defer its inclusion from gross income, as it will not constitute an amount. Convolution in attaching a monetary value to such a non-cash item should however not detract from its inclusion in gross income (*People’s Stores case (supra)*).

The court’s verdict in the 2007 case of *Brummeria (supra)* contrasts starkly with legal precedent preceding this case. Interpretation note: No 58 (Issue 2) (SARS, 2012) (hereafter referred to as “IN 58”) places a non-cash accrual or receipt within the ambit of gross income, regardless of whether such a benefit can be encashed or disposed; hereby further widening the ambit of “amount”. The courts’ rulings in prior contentions (*Delfos case (supra)*, *People’s Stores case (supra)* and *Stander case (supra)*) favoured the taxpayer who could not turn the incorporeal right into cash. The enunciation in the *Brummeria case (supra)* juxtaposes these pronouncements.

De Koker and Williams (2016: par.2.9C) opine that the standard established by the *Brummeria case (supra)* confers a right to the Receiver to tax any non-monetary benefit that is of an income nature. The extent to which such a non-monetary benefit is convertible into cash is therefore deemed superfluous. Even though IN 58 does not elaborate on the subject of the appraisal of such a right, the legacy of the *Brummeria case (supra)* requires the

inclusion of this non-monetary item in gross income at its market value (De Koker & Williams, 2016: par.2.9C).

Non-cash swaps offer three methods of exchange, but in essence encompass one of two things. A mutual exchange of rights, via a traditional swap or hospitality exchange, entitles participants to take up residence in each other's homes. Alternatively, swap points are pledged and in reciprocation, accommodation is reserved for a fixed period commencing on a pre-determined date. Though divergent, the benefits, in both instances, are of a non-cash nature. Subsequently, the characteristics of these transactions squarely position it within the ambit of the principles established by the *Brummeria case (supra)*. The income nature of the benefit was established in Chapter 2 and the encashment principle, previously observed in case law, was annulled by the enunciation of the *Brummeria case (supra)*.

Membership is an essential qualification to ensure that the inherent value of these non-cash benefits is sustained (LHS, 2016c; LHS, 2016o). Tradability of points is reduced to mutual affiliation with a home swap programme (LHS, 2015b). A mutually exchanged right is only esteemed by the participants to the specific transaction. The impediment imposed by both the prerequisite of membership and the customised nature of transactions would, preceding the enunciation in the *Brummeria case (supra)*, have exonerated the taxpayer from inclusion of these values in gross income. The non-cash benefit's inability to be turned into money would have disqualified it from eligibility as an "amount".

The precedent of the *Brummeria case (supra)*, however, enshrined the Receiver's prerogative to designate a non-capital, non-cash benefit in the absence of the encashment principle, as gross income. Designation as gross income does however not ascribe a value to the benefit. Ensuing authentication of non-cash benefits (rights and points) as an "amount", will be an exposition to assign a value to these benefits, as proposed by case law and legislation.

### **4.3 The valuation of non-cash benefits as prescribed by case law and legislation**

Non-cash benefits are to be included in gross income at the value for which they can be sold on the open market employing a reasonable method to do so (*Lace Proprietary Mines (supra)*; *ITC 1375 [1982] 45 SATC 207 at 210*). De Koker and Williams (2016: par.2.13)

voice the opinion that the true market value is of the essence when determining the “amount” for inclusion in gross income. This prompts five further questions:

- What will constitute a fair market value for which the rights or points can be sold?
- Is the value determined at the time of accrual or receipt?
- How does seasonality influence the valuation?
- How does the collection of consideration from a non-resident influence the assessment of the market value?
- What is the implication of cancellations on a fair market value?

These five questions will elicit divergent answers, depending on whether the swap method constitutes a point swap or a traditional swap. Preceding the resolution of these questions is a deliberation of whether the non-cash benefits must elicit a tax treatment analogous to its cash counterpart.

There can be no misgivings regarding the Commissioner’s intent to levy normal tax on all benefits in kind. The gross income definition explicitly includes the phrase “*in cash or otherwise*” to eradicate any uncertainty regarding the taxability of barter trade. Precedents established by numerous instances of case law, of which the *Brummeria case (supra)* is the most recent and controversial, further enshrine the commitment of the fiscus to disallow any “amounts” from eluding the normal tax net.

Case law proposes appraisal to equate the value for which such an item could have been traded in the market place (*Lace Proprietary Mines (supra)*; *ITC 1375 (supra)*). Prominent former case law, such as the *Delfos case (supra)* and the *People’s Stores case (supra)*, dealt with non-cash elements which were freely exchangeable should the taxpayer have favoured the pursuit of such a possibility. Traditional swaps do not offer the option to trade, as the particulars of the agreement are limited to two members for specific dates and homes. Points command more influence as a virtual currency. Acceptance as a means to trade and acquire accommodation is however reduced to members of the same swap programme. A reservation therefore arises with regard to whether subjecting this incorporeal right/points to normal tax at their full value is fair and equitable.

Canadian authorities favoured the taxpayer in *Linett v Minister of National Revenue* [1985] 2 C.T.C. 2037 (TCC) by consenting to assign a lesser value to credits obtained in a barter

transaction. Linett argued that the credits he acquired in affiliation with an accredited barter system held less appeal than conventional cash and therefore devalued it as a currency. The court acknowledged this argument and reduced the amount for inclusion in gross income accordingly. There has however been no indication from existing South African case law that tax authorities will follow suit.

Van Zyl (2015:110) submits that the purposive approach, mandated by the Constitution, empowers taxpayers to question the canons of taxations with more boldness than permitted in the pre-democratic regime. Evidence in the furtherance of this cause is found in the Receiver's commitment to "*equity and fairness*", as envisioned in the 2013-2014 Annual Report of the SARS (SARS, 2014). The credence of a claim to reduce the value assessed for gross income and the tax courts' inclination to deliver judgments favouring the taxpayer will however only be resolved once such a matter is contended in court. However, the five primary questions are reverted to below in order to elucidate the appraisal of non-cash benefits. The first question to be addressed is the matter of assessing a fair market value.

#### **4.3.1 What constitutes a fair market value?**

Paragraph 31(1)(g) of the Eighth Schedule sheds some light on the concept of market value and defines it as "*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*".

Paragraph 38(1)(a) of the Eighth Schedule fortifies the significance of the term "market value". This paragraph compels the taxpayer to regard a disposal of which the "*consideration [is] not measurable in money*" as at its market value, regardless of whether the transaction transpires at an arm's length value or not. This paragraph is applicable to certain disposals of capital assets, but can be used as guidance for normal tax purposes. The Free Dictionary (2016) defines market value as "*the amount that a seller might expect to obtain for merchandise, services, or securities in the open market*".

The "merchandise", in the event of a non-cash benefit, constitutes either points or a right of use. A right of use will always be affiliated with a specific home, as it entails a reciprocal exchange for the right to be established. This right cannot be sold, as two individuals have acquiesced to the terms of the agreement and its subsequent conditions, and such an

agreement relates to explicit homes and countries. The *Brummeria case (supra)* negated this as a counter-argument to avert the inclusion of the right's market value in gross income. However, if one considers a hypothetical sale, the market value of this right will equate the consideration collectible if the same home (to which a right is obtained) were to be pledged in exchange for rental income. Elements further influencing the market value of rental income will be:

- the inference of seasonality;
- exchange rates; and
- whether valuation is to be performed at the time of accrual or receipt.

These elements are discussed in greater detail in 4.3.2. The basic calculation to assess the value of the right for normal tax will therefore be performed as follows:

rental income per day x number of days of occupation x appropriate exchange rate  
(if applicable)

A point swap might however prove slightly more convoluted, depending on the disposition thereof at the end of the year of assessment. The value for which points can be sold is inextricably linked to the home for which the points are pledged. The learned Judge President referred to the Special Court ruling of Conradie J in *ITC 701 [1950] 17 SATC 108* in delivering his verdict in the *Brummeria case (supra)*. Conradie J rejected the stance favoured by the *Delfos case (supra)* and the *Lategan case (supra)*. He abridged the concept of the word "amount" by advocating a straightforward consideration of what the market would have paid for such a non-cash item. Points which have been spent can be attached to a specific home, for which a rental fee (based on market sentiment) is calculable. Unspent points will however necessitate more caution in the appraisal thereof.

As discussed in Chapter 2, homeowners will assign a number of points per night to their house. This can range from 50 points, increasing in intervals of 50, to a maximum of 300 points (LHS, 2016h). The number of points are to resemble the inherent value of the property (LHS, 2016h). This calculation is however a subjective exercise and depends on the home owner's discretion. LHS will offer a guiding opinion, but the ultimate decision remains with the home owner (LHS, 2016k). The prejudice to which points are exposed disqualifies it, in the author's opinion, from being used as the sole measure to assess the value thereof. There

is no single objective benchmark to warrant that the number of points ascribed to a home accurately and fairly represents its rank among the catalogue of other available homes. Market sentiment is also not authentically reflected, as the final assessment is the sole discretion of the home owner.

Further ineligibility results from the restriction that points introduce. The multiplicity of homes available on home swap programmes varies from villas in France to ski chalets in Austria and apartments in New York (LHS, 2017g; HE, 2017a). Thus, rental values fluctuate substantially. The limitation of points (ranging from 50-300) to accurately disclose the inherent rental value of properties further disqualifies it as an appropriate and reliable measure to assess a value for gross income.

Precision will consequently only be attained once the points have been disbursed to secure residence in a specific home. The rental value of such a home will be a true reflection of the value obtained through the expended points. Disbursed points can be attached to a specific home, of which the rental value is ascertainable. The value to be assigned to the points, and thus constituting the amount to be included in gross income, can be calculated as follows:

rental income per day x number of days of occupation x appropriate exchange rate  
(if applicable)

In assessing the worth of unspent points at the end of the tax year, the current author submits the following: a calculation of which the formula simulates the principles applied to calculate the doubtful debt allowance permitted by section 11(j) of the ITA. This section permits a deduction, subject to the Commissioner's discretion, of amounts previously included in gross income (Stiglingh *et al.*, 2015:355). The ambit of this respite only extends to include an amount which would have qualified for a deduction if it had become bad debt. The allowance deducted in the previous year will however be included in the gross income of the taxpayer in the ensuing tax year. Pursuit of the basic principles of the aforementioned legislation will ensure a more accurate, transparent and fair value that is ultimately subjected to normal tax – ethical principles to which the SARS is committed (SARS, 2014). Points represent a taxable benefit, whereas the doubtful debt allowance denotes a deduction. The proposition is merely an application of the methodology employed and the manner in which the amount is calculated.

Both the allowance for doubtful debts and the points are enshrined in uncertainty. Ambiguity with regard to the valuation of both amounts will be resolved by the occurrence of a future event. Trade debtors will either forfeit or pay outstanding debt and a point swap will be arranged, establishing an exact value for the points by attaching it to a specific home. In both events, there is significant uncertainty with regard to a precise value at the end of the tax year. The abstruseness is however resolved in the ensuing tax year.

The author suggests that the SARS could establish a matrix ascribing a general Rand value to every 50 points. At the end of the year of assessment this matrix can be utilised to obtain an approximation of the amount to be included in gross income. In the subsequent tax year, when the points are utilised in an actual point swap, the prior year's estimate can be reversed and the actual amount included. This method will reduce the administrative burden and complexity accompanying the valuation of passive points at the end of the tax year. The value of unreserved points to augment gross income at the end of the tax year will be calculated as follows:

$$(\text{number of points}/50) \times \text{Rand value ascribed to 50 points}$$

The ideal home swap member will continuously amass and disburse points – either in the current or consecutive tax years. Cognisance of two more unusual scenarios is however required: Points can either expire due to termination of membership or remain unspent for several years.

Expiry of points essentially annuls the right to utilise those points as a trade currency to acquire accommodation. As the paradigm for the proposed valuation of unspent points are based on the principles of section 11(j) of the ITA, a reversion to the methodology prescribed by this section offers guidance. The estimated amount, subject to normal tax in a preceding tax period, is reversed. There is however no actual value to include in taxable income: expired points are devoid of value and cannot convey any right. The taxpayer's net position is consequently neutralised: deduction of the amount previously burdened by the SARS provides relief in the year of its expiration. Termination of membership with an existing balance of unspent points is however an extremely uncommon occurrence (Napier, 2017) and is consequently not analysed in greater depth.

Points that remain unspent for several tax years requires a more liberal interpretation of the methodology prescribed by section 11(j) of the ITA. In order to eliminate complexity and alleviate the administrative burden, the author proposes the following: unspent points, previously taxed, should not alter normal tax in consecutive years, until it has been disbursed. (The value of an annual adjustment of unspent points to the taxpayer's gross income will be inconsequential whilst amplifying the governmental burden and jeopardising accuracy.) The appraised value of the points will consequently augment gross income in the year of its acquisition. Once these points are expended, the estimated amount will be reversed and a precise value included in gross income. Refer to figure 1 for a graphic representation of the progressive steps to determine the normal tax implication of points in a specific tax year.

There are however matters compelling further deliberation in order to ascertain that the market value assigned to the non-cash benefit is fair, accurate and in abidance with legislation. The inferences of rules explicitly governing the time at which non-cash benefits fall within the ambit of gross income, and cancellations, are two of the questions to be resolved. The implication of seasonality for valuation and the treatment of rental fees denominated in foreign currencies further contributes to this discussion.

#### **4.3.2. Factors influencing the market value of non-cash benefits**

The four main issues influencing assessment of non-cash benefits' market value are as follows:

- Is the value determined at the time of accrual or receipt?
- How does seasonality influence the valuation?
- What is the impact on valuation if consideration is collected from a non-resident?
- What is the implication of cancellations on market value?

Each item is subsequently discussed separately in order to establish its effect on the value of the non-cash benefit.

#### 4.3.2.1. The time at which valuation is determined

De Koker and Williams (2016: par.2.17) submit that case law prescribes the valuation of a benefit in kind at the time of its accrual. Judgments in both the *Mooi case (supra)* and *Lace Proprietary Mines (supra)* substantiate this submission. In his Appellate Division judgment of the *Mooi case (supra)*, Ogilvie Thompson CJ, at 11-12, held that accrual, relevant for valuation, transpired when all conditions attached to the agreement were discharged and the taxpayer's right therefore vested. Share options, which constitute the subject matter in the *Mooi case (supra)*, were exercised subsequent to the accrual of the shares. The court, however, maintained its initial enunciation and the option value (to assess gross income) was appraised at the date of accrual.

The view proposed by the *Caltex Oil (SA) Ltd v SIR* [1975] 37 SATC 1, and shared by the *Lategan case (supra)*, suggests the valuation of a non-cash benefit at the end of the year of assessment. De Koker and Williams (2016: par.2.17) however contest this view. In *ITC 1375 (supra)* the Special Court for Hearing Income Tax Appeals (now the Tax Court) sided with the precedent as established by the *Mooi case (supra)*. This affirms that the valuation of a non-cash item (in determining its worth for gross income) is dictated by the date on which the taxpayer acquires an absolute right. The provisos to traditional swaps and point swaps however demand that a distinction is drawn between the two methods.

#### Special timing considerations for traditional swaps

The currency of exchange for traditional swaps is limited to rights (LHS, 2016a; HE, 2016a). The time at which normal tax is elicited is dependent on whether the traditional swap occurs simultaneously or non-simultaneously (refer to 3.4.1.1 for a comprehensive discussion). The difference can be summated as follows:

Non-simultaneous swaps will augment gross income:

- Upon receipt if the resident exercises the right first;
- Upon accrual if the resident accommodates the partner ahead of utilising the accommodation provided by the partner (*Mooi case (supra)*).

Simultaneous swaps are simpler in comparison to their non-simultaneous counterpart - accrual and receipt will transpire concurrently.

Establishing whether the date of accrual or receipt is used to assess the value of the right is significant for two reasons. Firstly, the “value” is fixed to the rental fee of the house for which the right is granted; thus, fluctuations due to seasonality will manipulate the value. Secondly, rental fees for homes of non-residents will be designated in foreign currencies and exchange rates will have to be considered. Reverting to the *Mooi case (supra)*, the court held, at 11-12, that accrual transpired when the “*option became exercisable*”. The rights in the aforementioned case were contingent on fulfilment of the option’s conditions, after which entitlement became absolute.

The nature of a non-simultaneous swap however requires a more holistic interpretation of the word “right”, as envisioned by the court in the *Mooi case (supra)*. Merriam-Webster (2016) defines the word “right” as “*the power or privilege to which one is justly entitled*”. A valid and mutually consented swap agreement precedes consumption of the reciprocally bestowed right by the resident. The terms and conditions of such a swap explicitly confer the right on the resident to initiate the swap by being the first to utilise this right. The resident is therefore justly entitled to occupy his/her swap partner’s home at the time of taking up residence, as it simply constitutes the due claim of a right bestowed in terms of the swap agreement.

The analogy of the *Mooi case (supra)* can thus be applied to support the assertion that, should receipt precede accrual, the authoritative date for valuation should be that of receipt. This view is further validated by its relevance when considering its interrelation to the gross income definition. An amount is to be included at the earlier of receipt or accrual. Furthermore, the redundancy of both events transpiring in the same tax year has been established in Chapter 3 (*Delfos case (supra)*). An austere and inflexible application of the *Mooi case (supra)* will therefore contradict the gross income definition in a tax year where receipt has transpired, but accrual is deferred to an ensuing tax year.

In support of advocating a more holistic approach to determine the time of appraisal, Interpretation note No. 63 (SARS, 2011) (hereafter referred to as “IN 63”) is instrumental. The aforementioned note explicitly deals with the translation of amounts measured in foreign currencies. Even though the matter at hand does not relate to such conversions, the leniency exerted by the SARS in the translation of amounts denominated in currencies other than Rand offer some insight.

Section 6.2 of IN 63 (dealing with section 25D(1)) allows for a single rate to be applied for a short period. Section 8.2 (dealing with section 25D(3)) permits natural persons to apply an average rate to ascertain a value at the end of the tax year. This section sanctions the taxpayer to elect the rate which will be most advantageous when gross income is calculated. Consistent application for all transactions denominated in foreign currency for a relevant tax year is however a qualifying condition to benefit from this permission. Inferred from this is a more forthcoming stance by the SARS when difficulty arises with regard to identifying an exact time to establish valuation. Henceforth, the Receiver's concern with ensuring the inclusion of a value in gross income can be deduced. Less crucial is attaching a precise value to it, if an inaccuracy will not result in a material misrepresentation. A more exhaustive review of IN 63 is performed in 4.3.2.3.

Accrual and receipt can however also both occur in the same tax year. Whether the taxpayer elects to follow the more confined principle enshrined by the *Mooi case (supra)* and to ascertain the value at the date of accrual, or apply the broader interpretation by assessing the value at the date of receipt, the net result should not differ substantially. Seasonality and oscillation in the exchange rate will be the only factors driving the divergence. The variance attributable to performing the valuation on either the date of accrual or receipt should not be substantial and is therefore unlikely to be of any concern to the fiscus. The taxpayer, in the event of a single swap, will however be at liberty to select the rate which will affect gross income most beneficially.

### **Special timing considerations for point swaps**

The nature of a point swap constitutes a barter trade: points are exchanged for time in the resident host's home. The resident host (hereafter referred to as "the host") receives points instantaneously at conclusion of the point swap (LHS, 2015c). Accrual will be delayed until the host has provided residence to the guest. Receipt will, as in the case of a non-simultaneous swap initiated by the resident, precede accrual. These points can either be expended or passive at the end of the year of assessment.

Passive points have been received but cannot be attached to a specific home. Depending on whether the guest has been accommodated by the host before the end of the tax year, the host's right to the points might be definite. The rental income and relevant exchange rate

can therefore be reduced to the specific date or a limited range of dates during which the partner was accommodated, as accrual will transpire concomitant with accommodation.

The diction of the gross income definition however requires the inclusion of points at receipt, regardless of whether accrual has transpired in the same year of assessment (*Lategan case (supra)*). Valuation of these points, for which the performance conditions are incomplete, has however to be judged on autonomous criteria.

The matter of passive points for which accrual has not yet transpired is yet to cross the periphery and obtain the status of non-contingent entitlement. Existing case law (as seen in the *Mooi case (supra)*, *Lace Proprietary Mines (supra)* and *ITC 1375 (supra)*), is found to be inadequate in providing conclusive guidance in the valuation of these passive points. The factual circumstances of the *Mooi case (supra)* set a precedent for valuation where accrual explicitly transpires. Reversion to the *Caltex Oil case (supra)*, even though disputed by De Koker and Williams (2016: par. 2.17) due to it giving rise to difficulties, might however bring elucidation.

De Koker and Williams (2016: par.2.17) draw an analogy between the judgment in the *Caltex Oil case (supra)* and the valuation of non-cash benefits received. Botha JA, in delivering judgment in this Appellate Division case, held that it only becomes imperative to value benefits in kind on the last day of the year of assessment. This principle, when applied in conjunction with the valuation method proposed for unpledged points in 4.3.1, will ensure an edified estimation for inclusion in gross income. A gross over- or underestimation can be remedied in the ensuing year when the points have been attached to a specific house.

Points can also be expended by the time that the tax year concludes. One of two potential situations must be considered:

- Points can be collected and disbursed in a single tax year.
- Points assembled in a preceding tax year could have been expended in the current year of assessment.

The preferable progression for successful membership will constitute a continuous cycle of accumulating and disbursing points. In the event of points being assembled and spent in a single tax year, the presence of accrual cannot be overlooked. Unconditional entitlement

ensues when the resident concedes to the partner residing in the home for which points have been pledged. This absolute right equates to accrual and thus a date for the valuation of the points is established. Disbursement ascertains that an explicit rental value is discernible, as points can be ascribed to a specific home.

Conscientious application of the valuation principle submitted by the *Mooi case (supra)* will require the valuation to be completed in the following manner: the daily rental fee of the home on which the points was spent must be ascertained at the date of accrual, as established by the suggested rubric of the gross income definition. This daily rate will then be multiplied by the number of days for which the points were transmitted.

Points can also be expended before accrual has transpired (LHS, 2015c). The absence of accrual disqualifies the application of the *Mooi case (supra)* as its working is prompted by the vesting of the taxpayer's absolute right. As previously submitted, De Koker and Williams (2016: par.2.17) propose a feasible solution by paralleling the principles of the *Caltex Oil case (supra)* with the valuation of non-cash benefits. The central contention of the aforementioned case advocates the valuation of consideration in kind on the last day of the year of assessment (which is discounted by De Koker and Williams).

A more inclusive interpretation of the aforementioned *Caltex Oil case (supra)* however offers resolution in the absence of an accrual. De Koker and Williams (2016: par.2.17) suggest that the principle established by the *Caltex Oil case (supra)* will concede valuation during the year if the item received or accrued is disposed prior to the last day of the tax year. As the non-cash benefit is no longer in the possession of the taxpayer at the conclusion of the fiscal period, valuation on the last day will be impractical and inaccurate. Gross income will, in such an event, be adjusted with the proceeds of the disposal. The points collected in exchange for extending a right of use (swap 1), is disposed of in return for residence in a third home swap member's home (swap 2). Points can be attached to a specific home, simplifying the appraisal of the amount to include in gross income. The daily rental fee for which the resident disbursed previously earned points will be multiplied by the number of days for which accommodation was secured.

Points that are only expended in a supervening tax year would, if the fiscus follows the recommendations as set out in 4.3.1 of including an approximation in gross income, have been subject to normal tax in a preceding year of assessment. The author proposes a

remedy of which the principles emulate the treatment of allowance for doubtful debts in section 11(j) of the ITA.

The SARS will, in the event of favouring the author's recommendation, include an approximation of the benefit in gross income at the end of tax year 1. The influence on normal tax in the subsequent tax year will be twofold. Gross income in tax year 2 will reflect an accurate amount based on actual information. Once the points have been pledged in exchange for a specific home, the computation can be performed with exact and actual information. Subsequently, the estimated amount, previously included in gross income (in tax year 1), can be revised and a deduction applied to arrive at taxable income.

De Koker and Williams (2016: par.2.3, par.2.16) opine that the fiscus is eligible to revise gross income in the event of barter trade where the following conditions are present: receipt and accrual did not coincide and the value of the non-cash item, when received, varies from the value that was taxed as an accrual in a previous tax year. This further strengthens the Receiver's commission to guarantee that normal taxes are levied on the accurate and full value of a benefit in kind.

The extent to which the SARS is obligated by case law and legislation to allow relief for formerly taxed amounts, when the actual amount is assessed in a succeeding tax year, exceeds the scope of this dissertation. However, it is deemed necessary to address consideration of the nature of the deduction. The deduction originates from an amount previously burdened by the Commissioner and not from an expenditure for which relief is claimed. Refusal to allow this deduction will breach the commitment of the SARS to their values and core outcomes of being "*equitable and fair*" (SARS, 2014). Acceptance of this proposed treatment will at the very least provide assurance that normal tax is accounted for on the benefit in kind, even if the accuracy is encumbered by the estimation. Efficacious implementation will warrant that the taxpayer's gross income reflects the correct value.

### **Special timing considerations: Conclusion**

Prominent case law advocates that benefits in kind are to be valued at the time of their accrual. A rigorous application of this proposed method however obfuscates the assessment of a non-cash item's value when pertaining to home swaps. The terms and conditions upon which accrual is contingent have repeatedly been the subject of contention, but never as

they pertain to the minutiae of home swaps. Consequently, existing case law and legislation do not offer explicit guidance. The time of accrual remains the most prominent indicator to determine the time at which the benefit in kind is to be valued. An austere execution of this rule will however conflict with the decree of the gross income definition that compels inclusion of a value at the earliest of accrual or receipt.

The nature of swaps therefore necessitates a more liberal understanding of case law to allow for valuation at the date of receipt, should accrual only transpire in an ensuing tax year. Points which have not been expended at the end of the tax year further convolute the valuation of the non-cash benefit for gross income and this matter requires a separate appraisal. Seasonality's inference on the appraisal of the benefit's value is discussed next.

#### **4.3.2.2 Seasonality**

Rental income oscillates depending on the desirability of a home at different times of year (Eurostat, 2017). The valuation of non-cash home swaps is contingent upon rental income – it should equate to cash consideration as if the transaction was concluded on conventional terms. Payment consists of either a right or points instead of cash. The valuation is thus unequivocally linked to the daily rental fee of the home in which the taxpayer will reside (regardless of whether the right was obtained via a mutual exchange or purchased with points).

Rental fees fluctuate cyclically, based on seasonal demand or exclusive local events such as festivals or sporting events (LHS, 2016d; Airbnb, 2016). As discussed in 4.3, the time at which the benefit in kind falls within the ambit of gross income does not necessarily equate to the time prescribed to appraise this benefit. In accordance with legislation and case law, the date established for valuation will thus be pivotal in determining the daily rental fee assigned to the home for a specific period.

#### **4.3.2.3 Consideration from non-residents**

Residents are attracted by home swaps facilitated traditionally or via points as the disproportion experienced due to the undervalued Rand is eliminated (Preuss, 2015; Bisseker, 2016). Barter trade significantly improves the accessibility of accommodation

denominated in a foreign currency. Rands are not traded and the resident participating in a swap is therefore placed on equal footing with a foreign counterpart.

The benefit acquired constitutes the rental income of the home which the resident will occupy in terms of the swap agreement. The daily rental fee will be presented in either US dollars, pounds, euros or Australian dollars (Sekher, 2016). A resident's taxable income is determined in Rand. Legislation governing the translation of foreign currencies will consequently also require consideration. Income denominated in a foreign currency has to be converted into Rand in order to appraise it as part of gross income (De Koker & Williams, 2016: par.2.18). Section 25D, as discussed in 4.3.2.1, governs the translation of amounts denominated in foreign currency.

Section 25D (1) encompasses the principal rule to this section. Submission to its requirements will compel conversion of foreign amounts *"by applying the spot rate on the date on which that amount was so received or accrued"*. Section 3.1 of IN 63 defines spot rate as *"the appropriate quoted exchange rate at a specific time by any authorised dealer in foreign exchange for the delivery of currency"*. Thus, it refers to the rate required to convert another currency to its Rand equivalent on a specific date. This section is however acquiescent to certain subsections. In the event of a single statute containing both a general and a specific provision, relating to the same situation, the general provision will defer to the specific provision.

Section 25D (3), overriding the core rule in section 25D (1), permits residents to convert amounts denominated in a foreign currency at the average rate for the fiscal period. The SARS offers further aid by providing exchange rates for a single date or range of dates on their website (SARS, 2016a). Consistency is a prerequisite for the application of Section 25D. The resident is at liberty to elect adherence annually to either Section 25D (1) or 25D (3). A resident's choice, once made, has to be applied unfailingly to all foreign amounts relevant to the particular tax year (IN 63, 2011).

The mere nature of point and traditional swaps layers the transaction with tiers of intricacy. In order to value the benefit, the underlying home's rental value has to be assessed. Such an appraisal requires contemplation of the time at which such valuation is to be performed, i.e. at the time of accrual or receipt. The impact of seasonality on this valuation adds further nuances of convolution. The author proposes election, annually exercisable, of the

exchange rate which would result in the lesser Rand amount – effectively reducing the resident's normal tax burden. Cancellations, which add another nuance of intricacy to the concept of valuation, are discussed next.

#### **4.3.2.4 Cancellations**

Chapter 3 (specifically 3.4.1.1, 3.4.1.2 and 3.4.1.3) comprises a comprehensive discussion on the influence cancellations have on receipt and accrual of gross income. Cancellations are the exception to the rule and not a common occurrence (Sekher, 2016; Cavalli, 2016). The infrequency of cancellations consequently validates a succinct examination of its implication on valuation (Shetabi, 2016b). The time at which the fiscus can impose normal tax might be revised in the event of such a termination. The terms instigated by LHS and HE govern cancellations and the correct tax treatment will be contingent upon the stipulations contained therein. The following discussion explores the impact which termination of the home swap has on the valuation of gross income. A distinction is drawn between traditional and point swaps.

##### **Cancellations: Traditional swaps**

A traditional swap can be terminated by either parties to the agreement. A repeal by the resident will however not result in a modification to gross income. A termination by the swap partner will however augment gross income. The swap partner might rescind the swap agreement at one of two stages:

- prior to either parties having exercised their rights of use; or
- subsequent to consuming the reciprocally bestowed right (in the event of a non-simultaneous swap).

The ramifications of cancellations on the timing of accrual and/or receipt are exhaustively explicated in 3.4. Accrual transpires in both events at the time the swap partner rescinds the swap agreement. Appraisal will subsequently coincide with the date of accrual, as advocated by case law (*Mooi case (supra)*; *Lace Proprietary Mines (supra)*).

## **Cancellations: Point swaps**

A resident will be penalised for repealing a point swap by rescinding the points credited to the account. The resident therefore loses the benefit acquired at the time the point swap was concluded. Termination can transpire in the same or an ensuing tax year. Should the initiating swap agreement and the cancellation eventuate in the same tax year, gross income will remain unaffected (3.4.1.3). The concept of valuation will consequently be redundant.

A repeal (of unspent points) can however also transpire in an ensuing tax year. Enactment of the author's commendation would have seen an estimated amount included in the taxpayer's gross income at the end of tax year 1 (refer to 4.3.2.1). A cancellation in tax year 2 will forever preclude the points from being allotted to a specific home. Consequently, gross income will not be modified by a suitable and exact amount. Application of the principles of section 11 of the ITA, as proposed, will however result in a reversal of the estimated benefit, taxed in the preceding tax year. Valuation for a termination does therefore not deviate from the method proposed for a successful point swap, as the valuation remains unaffected and the impact of an annulment (on normal tax) exceeds the scope of this discussion. This concludes the examination of non-cash swaps; the appraisal of rental income is deliberated on next.

## **4.4 Rental income**

LHS offers its members the flexibility to travel by means of a conventional rental agreement (LHS, 2016a; LHS, 2016e). The valuation of cash as compensation eliminates many of the complexities associated with non-cash benefits. The issue therein that requires to be addressed is the selection of an appropriate exchange rate.

As discussed in 4.3.2.3, section 25D of the ITA governs the conversion of amounts denominated in a currency other than Rand. Section 25D(1), the central provision contained within this statute, prescribes translation at the date of accrual or receipt, by applying the relevant spot rate. An extensive discussion on accrual and receipt of rental income was submitted in chapter 3.4.1.2 To sum up: accrual and receipt for rental income generally transpire as follows:

- at the time of accrual in the event of a successful short-term rental;
- at the time of receipt in the event of a successful long-term rental; or

- at the time of accrual in the event of a cancellation by the guest.

Accrual precedes receipt when the nature of a rental agreement is short term; the host collects the cash subsequent to conclusion of the rental. Meticulous abidance of Section 25D(1) will compel each day's rental fee to be translated at the spot rate for that day. The SARS is however aware of the practical difficulties accompanying such exact execution. As discussed in 4.3.2.3, IN 63 permits the taxpayer to convert foreign receipts at an average rate for short periods. This exception is contingent upon the stability of the exchange rate and a consistent application of the elected method.

Receipt of the rental fee prior to the completion of the guest's occupation (in the case of a long-term rental) simplifies translation. Section 25D(1) prescribes conversion of the entire amount at the relevant date on which receipt transpires. A rental agreement terminated by the guest will entitle the resident host to a percentage of the total rental fee, depending on the cancellation policy elected. Conversion of the entire balance at the relevant exchange rate congruent with the date of accrual is, in such an event, recommended by Section 25D(1). However, as stated in 4.3.2.3, the resident host is at liberty to elect the concession offered by section 25D(3). (This section sanctions the resident to apply an average rate to all foreign income and expenditure consistently in a specific year of assessment (SARS, 2011).)

Rental income's complexity is opportunely limited to election of a suitable exchange rate, whether it be the spot rate (in compliance with section 25D(1)) or an average rate (in adherence to section 25D(3)). Technical expertise, due to the Commissioner's leniency in election of a conversion rate, is not a prerequisite and will therefore not impede accuracy and recoverability. In the ensuing section, the potential dualistic nature of a tax resulting from international trade, in conjunction with its supplementary remedies, is deliberated.

#### **4.5 Double tax agreements**

Residency in the Republic is the nexus endowing the fiscus with the power to levy taxes on worldwide accruals and receipts. A resident's income, realised from a home swap, will thus fall within the ambit of gross income, regardless of such a property's location. The nature of home swaps requires that these transactions are concluded across international borders. Consequently, income that is subject to tax in the Republic might also enter the tax

jurisdiction of another country. Tax treaties are therefore established to facilitate the appraisal of tax dominion in such an event. The scope of this dissertation is however restricted to a resident's tax liability, inflicted by the SARS, as it pertains to property owned within the Republic. Consequently, the state of residence and source are the same and an analysis of the principles of double tax agreements are consequently superfluous.

The nature of home swaps between residents and non-residents also requires consideration of section 6quat of the ITA. Consequently, the relevance of this section to the valuation of benefits derived from home swaps is investigated.

#### **4.6 Section 6quat**

Section 6quat intends to offer relief to South African citizens with a dualistic tax burden. The prerequisite, as listed in section 6quat(1)(a), is that such income must be from "*any source outside the Republic*". As discussed in 4.5, the scope of this thesis excludes income from a foreign source, deeming section 6quat irrelevant for the purpose of this dissertation.

After careful consideration of the numerous dynamics influencing the valuation of home swap benefits, the following section encapsulates the most substantial conclusions.

#### **4.6 Conclusion: Valuation of home swaps**

The investigation reflected in Chapter 4 sought to ascertain the value attributable to the benefits collected by a resident participating in a home swap. All home swaps, with the exception of rental agreements, transpire in the absence of cash exchanging hands. Barter trade is therefore an essential component to home swap agreements. Appraising the worth of this benefit is directly related to the rental fee of the house to which a right of use is obtained. The mere disposition of the recompense therefore convolutes the valuation. The market value of the home's rental fee (and therefore of the benefit in kind) is affected by several elements: timing, seasonality, exchange rates, impediments to tradability and tax relief are all components potentially influencing the valuation.

Existing authoritative case law regards accrual as the authoritative event to determine a date for the valuation of non-cash recompense. Receipt may however precede accrual and transpire in a separate year of assessment. An austere application of the principles

enshrined by case law will therefore, in such a context, contradict the gross income definition. The nature of home swaps therefore necessitates a more extensive interpretation, allowing for events where receipt precedes accrual in succeeding tax years. A distinction should however be drawn between traditional swaps (which include hospitality exchanges) and point swaps.

The valuation of traditional swaps is more clear-cut, as a benefit will always be directly ascribable to a specific house. Points can however not always be explicitly assigned. The author proposes, in the absence of points pledged to an exact home, an approximation emulating the principles of section 11(j) of the ITA.

Traditional rental agreements facilitated by home swap programmes are less complicated. Intricacy is reduced to the election of an appropriate exchange rate. The issue of home swaps with international partners raises queries regarding the translation of rental fees, whether in cash or otherwise. Section 25D governs the conversion of amounts in foreign currency and is further aided by IN 63. The resident is at liberty to elect applying either the spot rate or an average rate. International trade necessitates reference to section 6quat and DTAs. Neither of these mechanisms are however relevant, as the source of the income is established within the Republic. Furthermore, no clemency is extended for the trade restraints imposed by the nature of non-cash recompense. There is no existing historical South African case law indicating that SARS is susceptible to considering a tax reprieve by devaluating the amount for inclusion in gross income.

The Receiver's leniency with regard to the translation of foreign amounts denotes a disposition inciting compliance rather than rigorous enforcement to ensure gross income reflecting an exact amount. A resident will therefore establish the value (for gross income) with reference to the house in which accommodation was acquired. The valuation will be performed at either the date of accrual or receipt, depending on the order in which it transpires and with cognisance of all the elements influencing a home swap.

In Chapter 5 the treatment prescribed for home swap programmes by the tax authorities of Australia is deliberated. This chapter will deal more comprehensively with the congruent factors considered in ascertaining eligibility of this country for comparative analysis. Furthermore, Chapter 5 aims to offer insight into the policies and methods applied by the Australian government when dealing with the sharing economy. The acumen attained will

be valuable in measuring the aforementioned practices against those employed by the SARS.

## **CHAPTER 5: CONSIDERATION AND DISCUSSION OF THE TAX TREATMENT OF HOME SWAP PROGRAMMES FROM THE PERSPECTIVE OF AUSTRALIAN TAX LEGISLATION**

### **5.1 Background and introduction**

The preceding chapters explicated the nature of home swaps and established the innate nature thereof as gross income. The multifaceted characteristics inherent to home swaps necessitated an examination of the timing (Chapter 3) and valuation (Chapter 4) relevant to the assessment of normal tax. The case law and tax legislation of countries with tax systems congruent to that of the Republic are valuable aids in assessing areas of ambiguity in the tax milieu (Brink, 2010).

This chapter appraises the tax legislation and case law of Australia, specifically as it pertains to home swap programmes. The rationale for this selection is multifarious and is discussed in 5.2. This chapter of the thesis is structured as follows:

- 5.2. Motivation for selecting Australia as subject to allow a comparative study
- 5.3. Background to the Australian Income Tax Assessment Act
- 5.4. Application of the Australian Income Tax Assessment Act to home swap programmes
- 5.5. Conclusion

### **5.2 Motivation for selecting Australia as subject to allow a comparative study**

Australia, a developed country with a resilient economy (Jericho, 2016), is listed as a country of the first world (Nationsonline, 2016). Membership of the Organisation for Economic Co-Operation and Development (hereafter referred to as "OECD") reinforces its status as one of the world's most advanced countries (OECD, 2016b).

Both South Africa and Australia are former British colonies. A strong British influence can therefore be detected in the tax legislation of both these countries (Willemse, 2010). The Republic's first Income Tax Act (No. 28 of 1914), introduced in 1914, originates from the New South Wales Act of 1895 (Australian Income Tax Act) (Huxham & Haupt, 2010:6). Furthermore, both South Africa and Australia are members of The Commonwealth (The Commonwealth, 2016a). The Commonwealth is committed to the advancement of

democracy, good governance and continuous innovation in areas of “*social and economic development*” (The Commonwealth, 2016b).

Australian tax authorities impose tax on the worldwide income of residents, regardless of its source (Woellner, Barkoczy, Murphy, Evans & Pinto, 2013:66). Residency as nexus to levy normal tax is also employed by the Commissioner (De Koker & Williams, 2016: par.1.8). Based on the factors deliberated, it was considered appropriate to elect Australia as subject to conduct a comparative study. The following is an abridged overview of the Australian Income Tax Assessment Act.

### **5.3 Background to the Australian Income Tax Assessment Act**

The Australian Tax Acts consist of the Income Tax Assessment Act 1997 (hereafter referred to as “ITAA 97”), the Income Tax Assessment Act 1936 (hereafter referred to as “ITAA36”), the Fringe Benefits Tax Assessment Act 1986, the Taxation Administration Act 1953 and the Goods and Services Tax Act 1999. The only legislation of relevance for the purpose of this study was ITAA 97 and ITAA 36. These two acts are intimately entwined and operate in conjunction with each other (Woellner, Barkoczy, Murphy & Evans, 2004:53). The relevant sections in each of these acts are subsequently considered.

#### **5.3.1 Relevant sections of Australian Tax Acts**

The previous chapters established the income nature of home swap benefits, the time at which a tax burden arises and the assessable value thereof. South African case law, ranging from the *Lategan case (supra)* to the more recent *Brummeria case (supra)*, is unequivocal about the income nature of non-cash home swap benefits. The ITA does however not devote a specific section proffering direct counsel on the characteristics, timing and appraisal of non-cash benefits. Australian Tax Acts are therefore deliberated on to appraise the merit of a section offering more explicit guidance.

Section 21 of ITAA 36 (hereafter referred to as “Section 21”) governs receipts in kind and assigns the “money value” to such a benefit. The legislative authority of this section is limited to the function of appraisal. Section 21, if operating in isolation, cannot decree an amount to be ordinary income (Woellner *et al.*, 2013:115). *FC of T v Cooke & Sherden* [1980] 80 ATC 4140 confined a non-cash business benefit’s aptitude to provoke tax to the extent of its

liquidity. Section 21A of ITAA 36 (hereafter referred to as “Section 21A”) was however instituted in 1988 to counteract the deficit exposed by the *Cooke & Sherden case (supra)*. Non-cash benefits, in the context of business relationships, are deemed ordinary income by this section, regardless of whether such benefits can be encashed (Woellner *et al.*, 2013:120).

Ordinary income is defined by section 6.5(1) of ITAA 97 as “*income according to ordinary concepts*”. The second paragraph of this section expands the dominion of the Australian Taxation Office (hereafter referred to as the “ATO”) to all ordinary income collected by residents, emulating the residence-based principle enforced by the Commissioner. Ordinary income, based on the principles instituted by case law, is conventionally divided into three categories, namely income from personal exertion, property or business (Woellner *et al.*, 2013:109). Assessable income is however more comprehensive than ordinary income as its scope extends to include both ordinary and statutory income (amounts included due to specific tax legislation) in terms of the ITAA 97 (Australia, 1997).

Section 21 therefore sets the value of a non-cash benefit, but only bears influence subject to qualification by section 21A. Taxation Ruling No. IT 2668 (hereafter referred to as “IT 2668”) (Australia, 1992), released in 1992 and updated in 2008 (IT 2668A), illuminates the tax legislator’s intent with regard to barter transactions. IT 2668A aids in ascertaining which barter trade transactions induce tax and assist in establishing the monetary value originating as a consequence.

Home swaps entitle participants to collect benefits through employment of their property. In the event of the benefit being in kind, it has been compared to rental income (refer 2.3), which in turn serves as a common example of income from property (Woellner *et al.*, 2013:166). The nature of the transaction therefore classifies it as (ordinary) income from property. Australian tax legislation prescribing the treatment of barter trade is examined next in conjunction with statutes governing income from property.

#### **5.4 Application of the Australian Tax Act to home swap programmes**

The currency of exchange for home swaps can be divided into two main categories: a benefit in kind and cash. Benefits in kind denote barter trade, where points or rights are exchanged;

traditional rental agreements, on the other hand, are settled in cash. The vital issues that have been addressed in the previous chapters of this study can be summated as follows:

- Whether the benefit collected in a successful home swap constitutes assessable income;
- Once the benefit's nature has been affirmed in the positive, the time at which the benefit elicits income tax needs to be established; and
- The need to determine the value ascribable to such a benefit.

As cancellations are inconsequential and an exceptional occurrence (Shetabi, 2016a), their impact on the timing and valuation of assessable income is not investigated. A distinction is to be drawn between the two primary categories (benefits in kind and cash).

Cash recompense is limited to rental agreements (LHS, 2016f). Woellner *et al.* (2013:166) list rental income as a common example of income from property. This stance is substantiated by the case of *Adelaide Fruit and Produce Exchange Co Ltd v DFCT* [1932] 2 ATD 1, which pronounced rent, by its very nature, to be ordinary income. The undisputable nature of rental income as gross income in the Republic has been discussed in 2.7.2 (*Visser case (supra)*). As no ambiguity exists with regard to rental income in cash, this chapter focuses on guidance pertaining to non-cash compensation. The vital issues, catalogued above, are addressed per category, based on Australian tax legislation and relevant case law.

#### **5.4.1 Benefits in kind**

The eligibility of benefits in kind (constituting either points or a right) as ordinary income, is governed by section 21A (Woellner *et al.*, 2013:113) and IT 2668A. The ITA does not contain explicit provisions to assist residents in applying the correct tax remedies to non-cash benefits. An evaluation of section 21A can therefore offer valuable insights in deliberating a potential implementation of similar legislation in the Republic. Section 21A and IT 2668A are closely interwoven, necessitating a conjoint analysis to comprehend and apply their interplay correctly.

Application of section 21A is confined to compliance with the following requisites (Woellner *et al.*, 2013:230):

- A non-cash business benefit must exist.
- The benefit must constitute income originating from carrying on a business with the intent to generate assessable income.
- The assessable value of non-cash business benefits must exceed A\$300 in a specific tax year.
- The cost derived as a result of the benefit must not qualify as a non-deductible entertainment expenditure.

The conformance to each requisite, as it pertains to non-cash home swaps, is subsequently assessed independently to establish the extent of its compliance to this section.

#### **5.4.2.1 Existence of a non-cash business benefit**

In order to examine and understand the first condition, the following definitions as per section 21A are crucial:

A “non-cash business benefit” is *“property or services provided ...*

*(a) wholly or partly in respect of a business relationship; or*

*(b) wholly or partly for or in relation directly or indirectly to a business relationship”.*

A “business relationship”, which is the crux upon which this criterion is poised, is however left undefined. Section 995.1 of ITAA 97 includes in the definition of “business” *“any profession, trade, employment, vocation or calling, but does not include occupation as an employee”*. This definition, similar to the definition of trade in the ITA, is very broad and inclusive. Case law offers insight and illuminates the concept of “business” as intended by the ATO. Five predominant factors indicative of a business, as identified by Woellner *et al.* (2013:199), are discussed independently:

##### **a) The degree to which the taxpayer’s activity is characterised by system and organisation**

A diminutive scale of operations, if organised and conducted in a business-like fashion, will not avert an affirmative classification. In the cases of both *Ferguson v FC of T* [1979] 79 ATC 4261 and *FC of T v JR Walker* [1985] 85 ATC 4179 the degree of the ventures was

trivial. (Ferguson farmed part-time with five cows, whilst Walker's operation was comprised of a single goat.) The courts were however content with the mere presence of a system and organisation, even in the absence of operating profitably (*JR Walker case (supra)*), in order to classify it as a business (Woellner *et al.*, 2013:200).

- Membership to a home swap programme ensures that the entire process is simple, systematic and highly structured (Costello, 2013; HE, 2016d).
- Affiliation with LHS or HE is thus indicative of a taxpayer's resolve to participate in home swaps conducted in an orderly and methodical way.
- As the scale of operations will not disqualify an operation as a "business", members listing only a single property with limited home swaps will not be exonerated.

In *IR Commrs v Livingston* [1927] 11 TC 538 Lord Clyde ascertained that a crucial question was whether the operations of the taxpayer is "*of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made*".

- Members create a profile with photos and a description of their home(s). Home swap participants agree on dates, terms and duration of the exchange. Points/rights are traded as an alternative to cash (LHS, 2016m).
- This manner of conduct simulates the procedures followed by a home owner in creating and maintaining a listing to facilitate a conventional rental operation.
- The nature of a profile established to participate in home swaps is thus analogous to that created for commercial rental. Subsequently, the ATO will not distinguish between the two when assessing the nature of the transaction.

## **b) Scale of operations**

Woellner *et al.* (2013:202) opines that greater reliance is placed on the extent of structure and organisation where operations are conducted on a smaller scale. Walsh J, in *Thomas v FC of T* [1972] 72 ATC 4094 however remarked that "*a man may carry on a business although he does so in a small way*". The court's finding in the *JR Walker case (supra)* substantiates this pronouncement. JR Walker's "business" consisted of a single goat and losses were incurred for an extended period of 14 years. This did however not preclude the venture's designation as a business.

- Participation (in home swap programmes) comprising of a single home and limited transactions will therefore not detract from a potential classification as a business.

### **c) Sustained, regular and frequent transactions**

Frequency of transactions generally sustains the notion of a business being operated (Woellner *et al.*, 2013:202). However, when evidence sufficiently assented, isolated transactions have been regarded as a business. In both the *Livingston case (supra)* and *FC of T v St Hubert's Island Pty Ltd (in liq)* [1978] 78 ATC 4104, 4118 the ATO considered a single transaction as adequate to regard the taxpayer's actions as a "business".

- Members of home swap programmes often participate in multiple swaps throughout an extended period (Millard, 2013; Schmalbruch, 2015). Sustained and regular home swaps further corroborate the business nature of these exchanges.
- The exception of participation that is limited to a single swap will however not defer the ATO's prerogative to consider such a transaction as a business.

### **d) Turning talent to account for profit**

This question is raised in the context of natural persons profiting from employment of a skill or talent and does therefore not apply to this study.

### **e) Profit motive**

Profit is generally the force compelling a business forward. Intent to generate profit is therefore considered a common characteristic of a business (Woellner *et al.*, 2013:205). The conventional connotation attached to profit ties it to a result measurable in monetary terms. Point and traditional swaps forego traditional currency; however, this does not preclude a non-cash home swap from being profitable to its participant. The Free Dictionary by Farlex (2016) defines profit as "*an advantageous gain or return*". *Glennan v FC of T* [1999] 99 ATC 4467, 4481 ascertained the presence of a profit motive if the taxpayer, at the time of embarking on a transaction, intends to realise a financial gain.

- Points/a right earned by a home swap participant translates into recompense attained for leveraging assets. A gain is consequently still realised, but its nature is in kind, as opposed to cash.
- The nature of non-cash home swaps often permits swapping experiences which would not have been within the financial reach of participants in the absence of a currency-liberated agreement (Trocky, 2016). Participants are making a profitable exchange by pledging their home/points in return for accommodation with a higher rental worth than their own. The inverse might however also be true. The homeowner of a villa in Tuscany will incur a notional “loss” when swapping with a rudimentary flat in Cape Town. In *Daff v FC of T* [1998] 98 ATC 2129, 2135, losses incurred over a period of 14 years did not disqualify a venture from being considered a business.
- A profit is consequently still realised, regardless of whether the proceeds are in cash or in kind.

Home swaps can therefore be considered a business when evaluated against the most crucial criteria established by wide-ranging Australian case law. This concept is further corroborated by paragraph 7 of IT 2668A. The “essential principle” when dealing with barter trade, in accordance with this ruling, is to establish whether a similar cash transaction would have been assessable or deductible. Rental income is deemed a common example of ordinary income (Woellner *et al.*, 2013:166). A rental agreement with non-cash compensation (of rights or points) will thus be equally assessable.

Section 21A’s mandate, as previously discussed, is predominantly subject to the existence of a non-cash business benefit, of which a prerequisite is the presence of a “*business relationship*”. Neither “business” nor “relationship” is defined by Australian tax legislation. A positive affirmation of the existence of “business” has been established in the preceding paragraphs. Consequently, substantiation of a “relationship” will confirm compliance with the first condition of section 21A.

The term “relationship” is left undefined by both the ITAA 36 and the ITAA 97. The Free Dictionary by Farlex (2016) however defines it as “*a particular type of connection existing between people related to or having dealings with each other*”. The term “relationship” in the context of “business” is therefore interpreted to mean the affiliation resulting from commercial dealings in which taxpayers are participants. A “business relationship” will

therefore come into existence when home swap participants negotiate the specifications relating to an explicit swap.

As the concept of “business relationship” has been elucidated, compliance to a “non-cash business benefit” is established. The ATO’s intent with “Provide” and “Services” will be determined next.

IT 2668A defines “Provide” as:

*“(b) in relation to services – includes allow, confer, give, grant or perform.”*

*“Services” “includes any benefit, right (including a right in relation to, and an interest in, real or personal property), privilege or facility and, without limiting the generality of the foregoing, includes a right, benefit, privilege, service or facility that is, or is to be, provided under*

*(a) an arrangement for or in relation to:*

*(i) the performance of work (including work of a professional nature), whether with or without the provision of property;*

*(ii) the provision of, or of the use of facilities for, entertainment, recreation or instruction; or*

*(iii) the conferring of rights, benefits or privileges for which remuneration is payable in the form of a royalty, tribute, levy or similar exaction;”*

The right conferred (by a host to a guest) warrants such a guest to utilise the property of the host for a predetermined period. Consequently, the host provides a service in the context of a non-cash business relationship. A non-cash home swap therefore complies with the first condition required by Section 21A.

#### **5.4.2.2 The benefit must constitute income originating from carrying on a business with the intent to generate assessable income**

The extent to which the ATO will consider the non-cash benefit (arising from a successful swap) as a derivative from carrying on a business has been established in 5.4.2.1. The concept of assessable income, as per section 995 of the ITAA 97, is given the meaning assigned to it by sections 6.5, 6.10, 6.15, 17.10 and 17.30 of this act. These sections encompass ordinary income, statutory income and regulations about tax on capital gains

(which does not apply to this study). The notion of ordinary income extends to include non-cash benefits (Woellner *et al.*, 2013:115).

Categorisation of the non-cash benefit as assessable income is further substantiated by the condition set out in paragraph 12 of IT 2668A. This section requires a commodity obtained in a barter trade to be either in *“the form of money’s worth or in a form which can be employed in the acquisition of some other right or commodity”*. A home swap endows the member with points or a right, which constitutes a currency exchangeable for accommodation. The second requirement stipulated by section 21A is therefore sufficiently met.

#### **5.4.2.3 The assessable value of non-cash business benefits must exceed A\$300 in a specific tax year**

An investigation of rental values on Love Home Swap’s website, pertaining to Australian homes, indicates a daily accommodation fee ranging from A\$85–A\$1 390 (LHS, 2016n). An accommodation fee less than A\$100 is generally for a studio apartment or for a home that is less desirably located. The average home’s accommodation fee per night is A\$254 (LHS, 2016n). The probability of participation in a point or traditional swap of which the value exceeds A\$300 in a tax year is therefore highly likely. Even though improbable, a non-cash swap of which the annual value is less than A\$300 is possible. Such a swap will not prompt section 21A, due to its failure to comply with the annual assessable value.

#### **5.4.2.4 The cost derived as a result of the benefit must not qualify as a non-deductible entertainment expenditure**

Non-deductible entertainment expenditure is governed by sections 32.5, 32.10 and 32.15 of ITAA 97.

Section 32.10 of ITAA 97 defines entertainment as:

- (a) entertainment by way of food, drink or \*recreation\*; or*
- (b) accommodation or travel to do with providing entertainment by way of food, drink or \*recreation\**

Point or traditional swaps specifically offer the distinct option to travel in a manner that differs from traditional hotels and bed and breakfast establishments. A home exchange does not offer food or entertainment and only comprises the property – consequently there is no food, drink or recreational component present. The fourth criterion stipulated by section 21A is therefore not applicable to home swaps.

### **Conclusion: Classification of benefits in kind as assessable income**

The compliance of home swaps (for rights/points) with the conditions stipulated by section 21A has been ascertained. Compliance with this section ensnares business benefits in kind, which cannot be encashed, in the assessable income net. *Cross v London & Provincial Trust Ltd* [1932] All ER 428, 430 (Greene MR) established the principle which diverts classification of an amount as ordinary income if it cannot be encashed. Section 21A however supersedes this principle. Consequently, the valuation of the non-cash business benefit is assigned to section 21. The time at which a tax burden is incurred and the appraisal of the benefit are considered next.

#### **5.4.3 Timing of taxation**

There is no disparity in the timing principles between non-cash and cash benefits (Woellner *et al.*, 2013:659). A distinction is drawn between compensation in points and a right:

A point swap is conducted in a manner similar to a rental agreement. Collection of the points precedes accommodation of the guest (refer 3.4.1.3). Repudiation by the host will compel a refund of the points to LHS (LHS, 2015c). The non-cash benefit will therefore only become ordinary income once the host has “earned” the accommodation fee by fulfilling the obligation to provide lodging (Woellner *et al.*, 2013:667). The accrual basis will therefore be applied for point swaps (*Arthur Murray (N.S.W.) Pty. Ltd v FC of T* [1965] 114 CLR 314; *Case B47* [1970] 70 ATC 237).

A traditional swap, constituting an exchange of rights, is facilitated in one of two ways: the Australian resident can either be the first to host the guest or he/she can initiate the traditional swap by consuming the reciprocal right. The accrual basis will apply regardless of the order in which the right is expended. In the event of the Australian resident being the first to consume the right, receipt of the benefit transpires (analogous to a host collecting

rental income/points). The obligation to offer accommodation however remains invariable. The act of lodging the guest, should it precede the Australian resident's consumption of the right, constitutes the "earning" of ordinary income; consequently, assessable income will be augmented on the accrual basis. The valuation of such a non-cash benefit is discussed next.

#### 5.4.4 Valuation

Section 21 assigns the "money value" to a benefit in kind in order to calculate assessable income. IT 2668's paragraph 14 expands on the valuation by including "*the arm's length value of that consideration*" as an alternative. Paragraph 15 of IT 2668 further stipulates the ATO's stance as "*the cash price which the taxpayer would normally have charged a stranger for the services or for the sale of the goods or property*". This denotes the value for inclusion in ordinary income to be the market value at which the right/points can be traded in an arm's length transaction.

Valuation is contingent on the time at which the ATO classifies the benefit as ordinary income. Australian tax legislation favours the taxpayer by deferring the tax burden until accrual has transpired (*Case B47 (supra)*; *Arthur Murray (supra)*). Both point and traditional swaps only enter the realm of ordinary income once the guest has resided in the host's home. An exchange of points and rights will be considered independently.

As traditional swaps are established on the basis of a mutual exchange, the rental value of the home (to which a right has been obtained), is assessable when the benefit vests (*Case B47 (supra)*). The valuation of point swaps is slightly more convoluted. Expended points can be valued based on the rental rate of the property to which accommodation was acquired. Vacant points for which the host has relieved the obligation of accommodation sufficiently adheres to the requisites of ordinary income. Valuation is however arduous as it cannot be associated with a specific home.

Paragraph 15 of IT 2668 addresses the taxation of credit units of which the exchange is facilitated via a business-oriented countertrade organisation. Sections 3 and 4 of IT 2668 explicate a countertrade organisation as barter trade "*controlled by member only organisations where credit units have become the medium of exchange*". Points, traded for accommodation, resemble credit units of which the adequacy as a currency is limited to LHS

affiliates. A further distinction is drawn between community-based and business-oriented countertrade organisations in terms of IT 2668 (Australia, 1992):

- Membership of the latter generally consists of businesses that are operated profitably.
- The countertrade organisation will retain detailed digital records of transactions to ensure tax compliance.

As discussed in 5.4.2.1, a merchant in accommodation, whether collecting recompense in cash or otherwise, will be considered to operate a business with the intention of doing so profitably. LHS and HE keep detailed records of each transaction – further serving to confirm that LHS and HE will qualify as business-oriented countertrade organisations (hereafter referred to as “BCO”).

IT 2668, paragraph 15, offers a potential solution to appraise vacant points at the end of the tax year. Credit units, if the BCO has ascribed a rate of conversion to establish the Australian dollar equivalent, can be valued according to such specified regulations. The converted value is to equate the market value, as a prerequisite to this method. LHS does however not ascribe a value to points. Points, as discussed in 4.3.1, are affected by various factors. Assigning a predetermined value to a fixed number of points might result in an inaccurate appraisal of a taxpayer’s ordinary income. Australian tax legislation does however not provide a distinct solution to valuing a vacant point balance at the end of a tax year. Subsequently, this warrant reverting to the default method of appraisal: a valuation reflecting the fair market value.

### **Conclusion: Timing and Valuation**

By virtue of its compliance with section 21A, the non-cash benefit derived from a point or traditional swap constitutes ordinary income. The nature of the point/right swap defers its assessment until the Australian resident has accommodated the guest. The SARS, on the other hand, levies normal tax at receipt, if it precedes accrual. The inference of the gross income definition therefore translates into a harsher tax regime implemented by the Receiver.

Valuation of the benefit in kind is determined by assessing the market-related rental value of the home for which the right/points are pledged. This school of thought parallels the

method of appraisal followed by the Receiver. Explicit guidance on the assessment of unspent points is deficient in both South African and Australian tax legislation.

The nature of non-cash benefits has been deliberated in the context of Australian legislation and case law. The most significant findings are condensed in the conclusion to Chapter 5.

## **5.5 Conclusion**

Home swaps, whether compensated in a traditional currency or via a non-cash benefit, will constitute ordinary income subject to tax. Non-cash benefits must comply with four conditions to sanction their submission to section 21A. Adherence to these requirements places the points/right in the domain of ordinary income. The compliance of the benefit in kind to the aforementioned section subjects it to section 21 and IT 2668A, which, in turn, govern valuation. The SARS and ATO are therefore in unison with regard to the income nature of the benefits arising from a home swap.

Valuation, in both the Republic and Australia, is established with reference to the market value for which the points/right can be traded. Neither country's tax authorities offer distinct guidance on the appraisal of points which cannot be connected to a specific home. Differences however arise with regard to the time at which a tax burden is incurred. The ATO only imposes taxation once the resident has satisfied the conditions of the agreement. The accrual basis is consequently followed. The SARS can levy normal tax in the absence of accrual, as receipt is sufficient.

The tax treatment applied by the Commissioner is therefore congruent to the practices implemented by Australian tax authorities. The only deviation relates to the time at which tax is levied. However, by including section 21A, the ATO does remove ambiguity obscuring the taxation of intangible benefits which cannot be encashed. The author proposes that the SARS, following the guidance offered by section 21A, augments the ITA with an explicit section offering distinct direction on the treatment of non-cash benefits. As discussed in 1.1, Muli (2014:1) found that a lack of simplicity often results in inadvertent non-compliance to tax legislation, further supporting the proposal to include more definitive guidance. In Chapter 6 the findings in the current and previous chapters are evaluated and a conclusive inference and supplementary recommendations are presented.

## CHAPTER 6: CONCLUSION

### 6.1 Introduction

The core focus pursued in this study pertained to the resolution of the following:

Assessing the normal tax implications for a South African resident, in possession of property within the Republic of South Africa, upon receipt or accrual of the benefit of a successful home swap.

Secondary questions, of which satisfactory resolution was essential to achieve the primary research objective, were identified. The following ancillary questions were consequently addressed:

- Which are the most prominent home swap programmes available both in South Africa and internationally and what are their conditions and stipulations?
- Does the benefit received as part of a home swap agreement meet the requirements of the gross income definition in terms of the ITA or is it of a capital nature?
- When does this benefit accrue to the taxpayer?
- What is the value of the benefits obtained?
- Will it be beneficial to investigate the tax treatment for similar transactions of a country in which the tax legislation and practices are homogenous to those of South Africa?

A summary of the principal findings is subsequently discussed.

### 6.2 Home swap programmes and the conditions and stipulations governing them

LHS and HE, the two prevalent home swap programmes, were elected for further analysis of their terms and conditions. Four types of home swaps were identified and discussed: a traditional swap, a point swap, a hospitality exchange and a short-term rental agreement. Each swap type confers two rights:

- A right of use to a specific property (in exchange for a right to compensation); and
- Recompense contingent on the home swap type – encompassing a reciprocal right, points or money.

A non-cash home swap can therefore be equated to a short-term rental agreement facilitated through barter trade. Points/rights are exchanged, circumventing conventional currencies. Designation of these non-cash benefits as barter trade compelled an analysis of the pertinence of the gross income definition.

### **6.3 The nature of the benefits receivable from home swaps**

Chapter 2 commenced with an exploration of the gross income definition and the guidance offered by judicial precedents. Case law established the Commissioner's prerogative to regard a non-cash benefit as congruous with its cash equivalent. The most recent and controversial judgment of the *Brummeria case (supra)* assigned an exhaustive meaning to the word "amount". This ruling liberated the confines of the gross income definition to allow for the inclusion of intangible assets, regardless of their commercial viability. This judgment irrevocably altered the tax landscape. Arguments attempting to circumvent normal tax on non-cash benefits due to impediments on tradability were disabled by this ruling.

The expendable nature of the benefit furthermore substantiated its inherent nature as gross income. Recompense collectible from a home swap was therefore ascertained to constitute gross income, regardless of whether compensation is collected in cash or otherwise. Assessing the time at which the benefit transcends the perimeter of the Commissioner's tax net was considered in Chapter 3.

### **6.4 When does the benefit accrue to the taxpayer?**

The gross income definition, apposite case law, relevant legislation and the terms of the home swap programmes elected, were the foundations upon which the analysis in Chapter 3 was performed. Interplay between the ECTA, tax legislation and the specific conditions of each swap type were deliberated to offer a cohesive assessment that gives sufficient credence to each element in the timing equation.

The gross income definition renders the concurrent occurrence of accrual and receipt superfluous – either accrual or receipt is adequate for an amount to be included in gross income. As the current decrees of the ITA does not offer any reprieve for amounts considered accrued or received in this capacity, the resident will incur a normal tax liability. Case law's most significant contribution in amplifying this definition has been the

confinement of accrual to vested rights. Postponement of a receipt in the absence of an encumbered right will subsequently provoke normal tax.

The ECTA is considered for its jurisdiction over contracts concluded via an online platform. (Home swaps are concluded exclusively via online platforms facilitated by home swap programmes, which accentuates the relevance of the ECTA.) This law merely establishes legally enforceable rights; tax consequences are governed by whether accrual or receipt has transpired. The investigation of the time at which a normal tax burden comes into existence therefore reverts to the ITA, case law and the terms of LHS and HE.

The predominant variable in assessing the time of taxation is the swap type. A secondary aspect once the first variable has been ascertained is whether, in the event of a non-cash swap, the exchange will be simultaneous or non-simultaneous. Furthermore, cancellation clauses, contained within the terms, require deliberation in order to obtain a holistic comprehension of the normal tax consequences. (Cancellations are compelled by the terms per swap type. The occurrence of cancellations is however so sporadic that this matter does not merit a comprehensive discussion.) Each swap type was therefore considered independently to ascertain the ramifications on a resident's gross income. The principles for hospitality exchanges are homogenous to traditional swaps and are therefore congregated with traditional swaps.

Traditional swaps hinge on a mutually conferred right to occupy another member's home. In the event of a simultaneous exchange, receipt and accrual transpire concomitantly. A non-simultaneous swap however necessitates distinction between the order in which the resident exercises his/her right and discharges the condition impeding un-contingent entitlement. Receipt prevails if the resident exerts the right prior to accommodating the partner. Accrual will however transpire if the resident lodges the partner (and acquits the encumbering condition) before utilising the right.

The mechanisms of a point swap imitate rental income received in advance, with dissimilarity only arising with regard to the currency of recompense. Points are immediately credited to the host's account, but remain encumbered until the obligation of accommodation has been satisfied. Similar to a cash receipt, the absence of unconditional entitlement does not preclude the amount from the Commissioner's jurisdiction. Receipt transpires

immediately and gross income must be augmented with the value of the points when collected.

The time at which a normal tax obligation arises for rental agreements is dependent upon the duration of the stay. Recompense is transmitted (between 1 and 10 days) once the guest takes occupation of the rental property. Receipt is therefore likely to precede accrual in the event of a long-term rental. Collection of the accommodation fee might however supersede the expiration of a short-term rental. Accrual will transpire once the accommodation agreement has run its full term and the amount will be included in gross income. Whether accrual or receipt is the first to transpire is however only significant in the event of a rental agreement extending over more than one tax year. In Chapter 4 the valuation of the benefits at the time of their accrual or receipt was investigated.

## **6.5 Elements influencing the valuation of home swap benefits**

Chapter 4 investigated the elements that compel deliberation in assessing the amount subject to normal tax. Fundamental to appraising the value of traditional and point swap benefits is cognisance of an innate non-cash attribute, designating the relevant exchanges within the periphery of barter trade. Rental agreements are the exception to the rule and subsequently there are fewer impediments in appraising the value of such agreements. The treatment prescribed by the SARS for barter trade imitates the remedy administered for its cash counterpart: the market value of the rental fee of the house to which points/right entitles the resident is therefore of crucial importance when ascertaining the amount for inclusion in gross income. Components affecting the market value and which therefore necessitate consideration are the following:

- timing of accrual and/or receipt
- seasonality
- exchange rates (governed by section 25D and IN 63)
- impediments on tradability
- legislation offering tax reprieve (governed by section 6quat and DTAs)

An analysis of antecedent definitive case law dictates the valuation of non-cash recompense at the time of accrual. The nature of non-cash home swaps however necessitates a more moderate interpretation. In the event of receipt preceding accrual in consecutive tax years,

an ascetic application might contravene the gross income definition. Receipt is consequently an indicator that a normal tax burden should be acknowledged if its occurrence precedes accrual in successive tax years.

Traditional swaps will always be affiliated with a specific home for a distinct period, simplifying valuation. Unspent points at the end of a tax year however convolute the normal tax calculation. The inability to link these points to an exact home naturally complicates the valuation. A proposal by the author suggests a solution imitating principles of existing legislation: an estimated amount will be subject to normal tax and rectified in an ensuing tax year. When the amount received (in cash) or the benefit collected is valued in a foreign currency, further consideration is required.

Section 25D, aided by IN 63, governs the conversion of rental fees, whether in cash or kind. Leniency by the fiscus permits the resident to adopt either the average or the spot rate, conditional on consistency for a relevant tax year. This concession by the SARS is indicative of a disposition encouraging compliance, as opposed to an exacting one. There is currently no prevailing case law which indicates that a tax reprieve will be offered for unconventional recompense of which the tradability is reduced to members. Benefits in kind and cash rental will consequently provoke similar tax consequences. Deliberating the relevance of section 6quat and DTAs concludes the investigation to address the issues relating to valuation.

The contribution of these sections is however inconsequential due to the supposition that residents are exchanging property located within the Republic. The OECD's model tax convention is therefore rendered superfluous and non-conformance with the requisites of section 6quat disqualifies this section from further investigation. A resident will consequently be liable for normal tax on an amount equal to the rental value of the accommodation to which a right/points are obtained. This rental value will be computed at the earlier of accrual or receipt and must be cognisant of elements such as seasonality and exchange rates.

Esteemed direction is offered by the tax legislation and case law of developed countries of which the foundational tax principles are comparable to those of the Republic. Chapter 5 concludes the analytical investigation by examining the tax legislation and relevant case law of Australia.

## 6.6 Australian tax legislation and home swap programmes

Australia was elected due to its stature as a first world country which, like the Republic, was a former British colony. The tax system of this country also reveals many parallels to that of South Africa, distinguishing it as a valuable assessment aid when considering the practices implemented by the SARS.

The ATO offers explicit guidance in the identification and valuation of barter transactions which fall within the ambit of ordinary income. Three interdependent pieces of law govern the tax treatment of barter transactions:

- Section 21 of ITAA 36
- Section 21A of ITAA 36
- Taxation Ruling No. IT 2668A

Conformance to section 21A places a non-cash benefit in the dominion of ordinary income. The individual requirements of this section, in conjunction with substantiating case law, were examined to ascertain home swaps' compliance with the stipulations imposed by section 21A. Affirmative classification prompts section 21 and an assessable value can be determined. IT 2668A further elucidates the identification and assessment of non-cash transactions.

Section 21 assigns the monetary value to the non-cash benefit. IT 2668A augments section 21 by clarifying the term "money value" as an arm's length value at which the non-cash benefit can be traded. A distinction is however to be drawn between points and traditional swaps. Assessment of the ordinary income collectible from a traditional swap is by nature simpler and will constitute the market-related rental value of the pledged home. The valuation of unspent points is however not explicitly addressed by Australian tax legislation. Assessing a non-cash benefit of this nature therefore remains nebulous.

The ATO, in comparison with the practices followed by the Commissioner, prolongs the imposition of the tax burden until accrual. An Australian resident's entitlement to ordinary income only vests once the income has been earned by accommodating the guest. The tax regime followed by the ATO in this regard is therefore more lenient than its South African

counterpart. Accrual signifies the non-cash benefit's eligibility for inclusion in ordinary income and valuation becomes essential.

The tax treatment implemented by both the Commissioner and the ATO is congruent in its practice of assigning a market value to the non-cash benefit. Greater benevolence is however displayed by the ATO – the assessment of ordinary income is extended until the time of accrual. Both tax authorities are yet to find a practical solution to the assessment of unspent points. However, with the introduction of section 21, section 21A and IT 2668A, the ATO has made great strides in eradicating non-compliance due to the perplexity and ambiguity surrounding non-cash benefits. The author consequently proposes an implementation of sections that are congruent to those found in Australian tax legislation, in the ITA. Insightful research by Kudakwashe Muli (2014), suggesting that complexity of tax legislation results in inadvertent non-compliance, offers further incentive for inclusion of such sections in the ITA.

## **6.7 Conclusion**

The issue of home swaps, as contributor to the share economy, shows no sign of ceasing its relentless pursuit of continuous innovation and expansion. Transformation of traditional systems and practices follows in the wake of this revolution. The relevance of accurately addressing the fiscal and economic impact of home swaps is therefore of critical significance.

A comprehensive investigation of South African tax legislation and apposite case law eliminates any ambivalence regarding the subjectivity of non-cash benefits to normal tax. However, the time at and value upon which normal tax must be imposed are complex due to the nature of non-cash compensation. The novelty of home swaps and lack of case law bearing unique reference to these transactions further contributes to the uncertainty. Consequently, ill-informed taxpayers may inadvertently contravene the ITA due to the lack of explicit guidance. Figure 2 offers a simplified graphic representation to aid taxpayers in determining whether the benefits collected from a home swap constitutes gross income.

The author therefore proposes augmentation of the current ITA with additional sections and/or an explanatory memorandum to act as a custodian limiting future losses of tax revenue. The rapid expansion of technology continues to truncate conventional methods,

necessitating unfaltering commitment of governing bodies to refine and remodel existing legislation. The fiscus will have to be a pioneer in the progressive movement of the share economy in order to ensure the National Treasury is not left behind.

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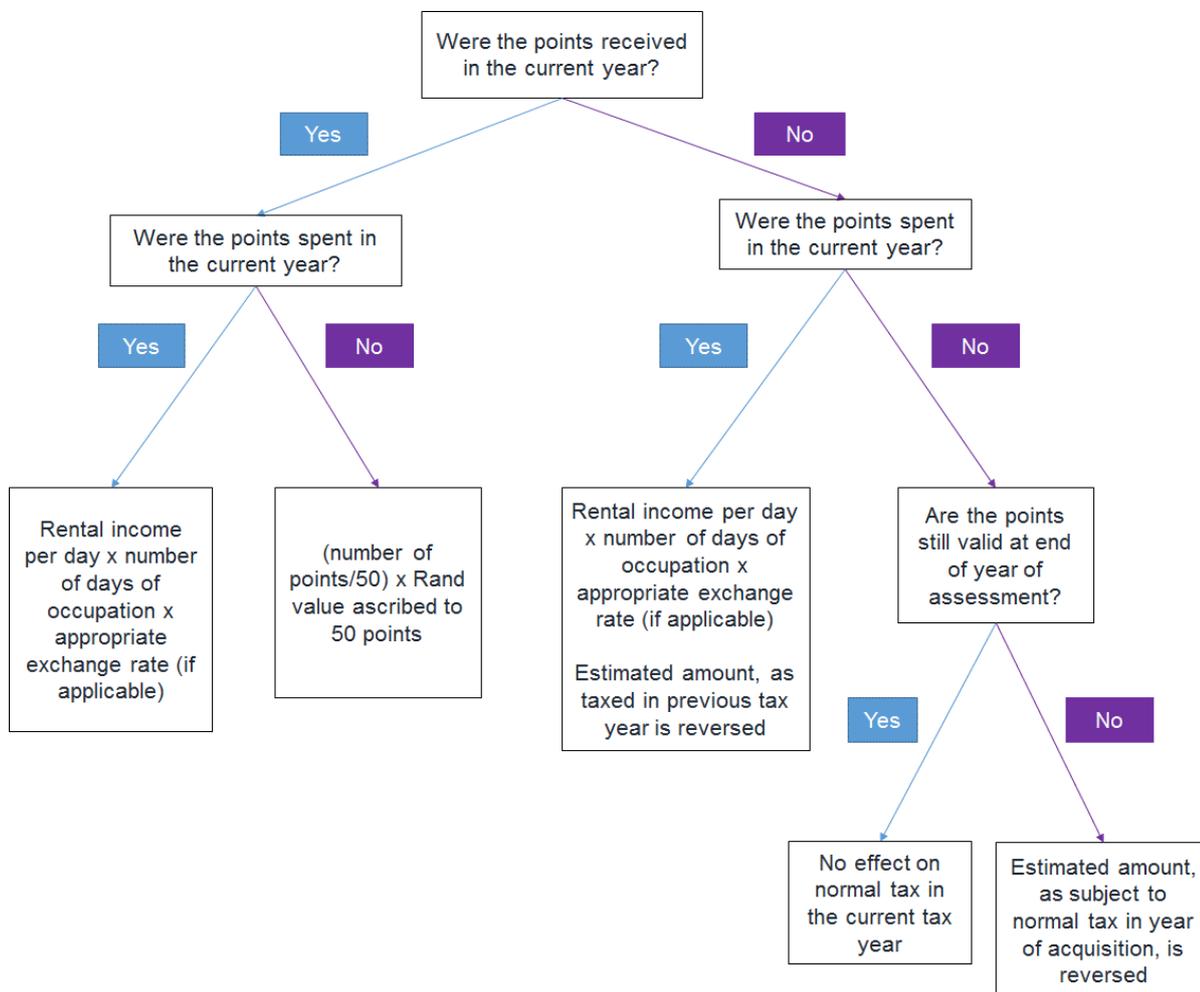
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## LIST OF FIGURES

**Figure 1: Determining the normal tax implication for points**



**Figure 2: Determining whether home swap benefits constitute gross income**

