INTERPRETATION NOTE: NO. 69

DATE: 12 February 2013

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
SECTION : SECTION 26 AND FIRST SCHEDULE
SUBJECT : GAME FARMING

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Preamble

In this Note unless the context indicates otherwise –

- **"CGT"** means capital gains tax, being the portion of normal tax attributable to the inclusion in taxable income of a taxable capital gain;
- **"First Schedule"** means the First Schedule to the Act;
- "**game"** means wild animals, birds or fish;
- **"paragraph"** means a paragraph of the First Schedule to the Act;
- **"section"** means a section of the Act; and
- any word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This Note –

- provides guidance on the application of selected sections of the Act and paragraphs of the First Schedule to persons carrying on game-farming operations, with its primary focus being the provisions applicable to livestock;
- is not intended to deal with farming in general; and
- replaces Practise Note No. 6 dated 30 July 1999.

2. Background

Section 26(1) stipulates that the taxable income of any person carrying on pastoral, agricultural or other farming operations shall, in so far as the income is derived from such operations, be determined in accordance with the Act but subject to the First Schedule. The First Schedule deals with the computation of taxable income derived from pastoral, agricultural or other farming operations.

The taxable income from farming operations is combined with the taxable income from other sources to arrive at the taxpayer's taxable income for the year of assessment.

The First Schedule applies regardless of whether a taxpayer derives an assessed loss or a taxable income from farming operations. The Schedule may further apply even after farming operations have been discontinued [section 26(2)].

Section 26 and the First Schedule are applicable to game farming since it comprises farming operations.

3. The law

Section 26

> **26. Determination of taxable income derived from farming.**—(1) The taxable income of any person carrying on pastoral, agricultural or other farming operations shall, in so far as it is derived from such operations, be determined in accordance with the provisions of this Act but subject to the provisions of the First Schedule.

(2) In the case of any person who has discontinued carrying on pastoral, agricultural or other farming operations and is still in possession of any livestock or produce, or has entered into a "sheep lease" or similar agreement relating to livestock or produce, which has been taken into account and in respect of which expenditure under the provisions of this Act or any previous Income Tax Act has been allowed in the determination of the taxable income derived by such person when such operations were carried on, the provisions of this Act, but subject to the provisions of paragraphs 1, 2, 3, 4, 5, 6, 7, 9, or 11 of the First Schedule, shall continue to be applicable to that person in respect of such livestock or produce, as the case may be, until the year of assessment during which he disposes of the last of such livestock or produce, notwithstanding the fact that such operations have been discontinued.

4. Application of the law

4.1 Farming operations

The First Schedule applies to any person who derives taxable income from carrying on pastoral, agricultural or other farming operations. Such a person can include an individual (whether farming alone or in partnership), a deceased estate, an insolvent estate, a company, a close corporation or a trust.

The expression "farming operations" is not defined in the Act and should be interpreted according to its ordinary meaning as applied to the subject matter with regard to which it is used.[1]

The question of whether a person is carrying on farming operations is one of fact[2] and must be decided considering all the facts of a particular case.

Farming and agriculture are defined in the *Merriam-Webster's dictionary*[3] as –

> "the science, art, or practice of cultivating the soil, producing crops, and raising livestock and in varying degrees the preparation and marketing of the resulting products".

However, every activity in the nature of farming will not constitute "farming operations". This was confirmed by Heher AJA in the Supreme Court of Appeal in *C: SARS v Smith* when he stated the following:[4]

> "In ordinary parlance the phrase 'carrying on farming operations' is capable of several meanings. In the context of s 26(1) it could mean simply 'a particular form or kind of activity' or it could bear a more commercial nuance, 'a business activity or enterprise'.
>
> "The Act is directed to the taxation of profit-making activities. There is no apparent reason why the legislature should have intended a taxpayer who farms as a hobby or who dabbles in farming for his own satisfaction to receive the benefits conferred by the First Schedule."

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[1] E A Kellaway *Principles of Legal Interpretation of Statutes, Contracts and Wills* (1995) Butterworth's Durban at 224.
[2] ITC 1319 (1980) 42 SATC 263 (EC) at 264, cited with approval in *CIR v D & N Promotions (Pty) Ltd* 1995 (2) SA 296 (A), 57 SATC 178 at 183.
[3] http://www.merriam-webster.com/dictionary/agriculture [Accessed 12 February 2013].
[4] 2002 (6) SA 621 (SCA), 65 SATC 6 at 9 and 10.

An example of the above principle can be found in ITC 1324[5] in which it was held that a grower who merely intended to sell crops surplus to his needs was not carrying on farming operations.

Thus, in order to fall within the First Schedule a farming operation needs to be a trade of the taxpayer and there must be an overall profit-making intention.

It is now settled law that the test for determining whether a taxpayer is carrying on farming operations is a subjective one, that is, one based on the taxpayer's intention. This was held to be the case in the *Smith case above* in which Heher JA stated that –[6]

> "a taxpayer who relies on s 26(1) is (over and above proof that he is engaged in an activity in the nature of farming) only required to show that he possesses at the relevant time a genuine intention to carry on farming operations profitably. All considerations which bear on that question including the prospect of making a profit will contribute to the answer, none of itself being decisive".

The court went on to cite ITC 1185 in which Miller J stated the following:[7]

> "It is no difficult matter to say that an important factor is: what was the taxpayer's intention when he bought the property? It is often very difficult, however, to discover what his true intention was. It is necessary to bear in mind in that regard that the *ipse dixit*[8] as to his intent and purpose should not lightly be regarded as decisive. It is the function of the court to determine on an objective review of all the relevant facts and circumstances, what the motive, purpose and intention of the taxpayer were . . . This is not to say that the court will give little or no weight to what the taxpayer says his intention was, as is sometimes contended in argument on behalf of the Secretary in cases of this nature. The taxpayer's evidence under oath and that of his witnesses, must necessarily be given full consideration and the credibility of the witnesses must be assessed as in any other case which comes before the court. But direct evidence of intent and purpose must be weighed and tested against the probabilities and the inferences normally to be drawn from the established facts."

In evaluating the genuineness of the taxpayer's intention the nature and extent of the enterprise will be relevant. The following examples of factors to be considered were provided by Erasmus J in ITC 1698:[9]

> "[T]he size and location of the property on which the operation is being conducted, the portion of that property being used for that purpose, capital expenditure, turnover, labour, the regularity and purposefulness of the activity, the time and effort spent thereon by the taxpayer in relation to his other gainful activities, if any, and the existence of a real prospect of profit (or lack thereof). The list is not exhaustive and the permutations of such activities are infinite. None of these considerations is necessarily in itself decisive."

Regard can also be had to the factors set out in section 20A(3) – see **4.8**.

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[5] (1980) 42 SATC 288 (Z).
[6] Above at 65 SATC 13.
[7] (1972) 35 SATC 122 (N) at 123–4.
[8] According to the *Glossary of foreign terms* by J Silke and Justice MM Corbett which forms part of the South African Tax Cases Reports published by LexisNexis, Durban, the expression "*ipse dixit*" means " He himself said it; a bare assertion or statement without proof, resting on the authority of the person who made the assertion or statement".
[9] (2000) 63 SATC 161 (SEC) at 170.

It is not a requirement that a person has to own the land on which the farming operations are carried on but the person must have a right to the land and the yield from it. This principle was illustrated in ITC 1548[10] in which the court found that the shearing and harvesting activities undertaken by a farmer on behalf of others on their land was not farming and neither were the transport services the farmer provided – the farmer was performing a service for other farmers and did not have a right to those farmers' land or the yield from it.

The factors referred to above are not exhaustive and whether or not farming operations are being conducted will depend on all the facts and circumstances of each case.

The same test, used to determine whether a person is carrying on farming operations, applies to game farming.

Having regard to the above general principles, the activity of breeding and running game on a farm for the purpose of marketing the live animals, hunting the animals for a fee or slaughtering them for the meat, falls within the ambit of game farming.[11] A person who owns land and occasionally allows hunters to, for example, cull the game on the land, is unlikely to be regarded on such activities alone to carry on game-farming operations. The person would have to convince the Commissioner that game is being raised with a genuine profit intention before the activities would be regarded as carrying on farming operations. An occasional culling is, in isolation, unlikely to indicate and support a contention that there was a genuine intention to carry on farming activities profitably.

Raising livestock generally involves purchasing, breeding and selling or using the particular animals. The facts and circumstances of a particular case are critical because, for example, in some cases the regular purchasing of breeding stock will be required and in other cases regular purchasing will not be required. In addition, the degree of day-to-day hands on involvement of a game farmer in raising livestock is likely to vary depending on the particular species of game, however in all instances there would be a level of active involvement appropriate to the particular species and farming operation.

4.2 Game-farming income

4.2.1 Income derived from game farming

Section 26(1) only applies to income derived from the carrying on of pastoral, agricultural or other farming operations. The Supreme Court of Appeal in *CIR v D & N Promotions (Pty) Ltd*[12] considered the meaning of the term "derived from". The court quoted with approval the explanation of the meaning of this term from the court *a quo*[13] which held that –[14]

> "the income and the source from which it arises, namely the farming operations, which embraces numerous agricultural activities, must be directly connected. An indirect connection or remote one will not suffice".

[10] (1991) 55 SATC 26 (C).
[11] ITC 1698 (2000) 63 SATC 161 (SEC); ITC 1414 (1986) 48 SATC 174 (T).
[12] 1995 (2) SA 296 (A), 57 SATC 178.
[13] *CIR v D & N Promotions (Pty) Ltd* 1993 (3) SA 33 (N), 55 SATC 89.
[14] At 57 SATC 183.

Also in the court *a quo* Levinsohn J stated that –[15]

> "the legislature intended farmers to be placed in a privileged position as far as their entitlement to deduct capital expenditure from farming income and hence the concept of income derived from farming operations ought to be strictly construed, see *Ernst v Commissioner for Inland Revenue* 1954(1) SA 318(A) at 323C–D."

A taxpayer may earn income from distinct businesses, namely, farming operations and other operations – it is only the income which is directly connected to the farming operations which will fall under the ambit of section 26(1). For example, in ITC 1285[16] the court found that the prize money from racing horses, which the breeder had initially intended but had failed to sell, was not part of the taxpayer's stock farming and horse breeding business and did not therefore fall under section 26(1).

The same principle applies to game-farming operations. Some activities will generate income directly from the game-farming operations and will be regarded as game-farming income, while other activities and the income derived from them will not be regarded as such.

The following types of income are regarded as being derived directly from game-farming operations:

- Income from the sale of live game.
- Income from the slaughter and sale of game meat, carcasses and skins.
- Fees received from hunters to hunt the game.
- Income derived from supplying guides and trackers used in a hunting expedition.

See **4.2.2** for income not derived from game-farming operations.

4.2.2 Income not derived from game farming

The income earned from the following activities is not regarded as having the required direct connection to game-farming operations and accordingly will not be regarded as game-farming income:

- Accommodation and catering.
- Admission charges payable by persons spending holidays on the farm.

In determining whether or not game-viewing fees (for example, the fee paid to go on a game drive) constitutes income from game farming, it is necessary in the first instance to determine whether or not the particular taxpayer is conducting a farming operation. This will depend on the facts and circumstances of the particular case and will take into account whether the taxpayer has a genuine intention to make a profit from the raising of livestock and whether the objective review of all the facts supports that contention. For example, game viewing conducted in conjunction with other uses such as the hunting and sale of the game may be a part of a valid farming operation. However, when game viewing is incidental to activities which do not constitute farming activities, the income from game viewing will not constitute income from farming operations. For example, certain eco-tourism operations the purpose of which is tourism and accommodation and those elements are the revenue and profit

[15] At 55 SATC 97.
[16] ITC 1285 (1978) 41 SATC 73 (NC); *Rex v Porterville Ko-op Landbou Mpy Bpk* [1962] 1 All SA 278 (C).

generators, while the game viewing serves as an attraction and is an incidental revenue generator.

Income derived from activities which give rise to income from game farming and those which do not will have to be accounted for separately since the deductions provided for under the First Schedule can only be used to reduce the income derived from farming operations.

4.3 Livestock

4.3.1 Meaning and nature of livestock

Meaning of "livestock"

Various paragraphs of the First Schedule apply to livestock. The word "livestock" is not defined in the First Schedule or the main body of the Act. The word is described in the *New Shorter Oxford English Dictionary* as –[17]

> "animals kept or dealt in for use or profit".

The above meaning was confirmed in relation to the First Schedule in *R Koster & Son (Pty) Ltd and another v CIR* in which Nicholas JA stated the following:[18]

> "Paragraph 2 of the First Schedule refers to all livestock. This is a general term which comprises any animals kept or dealt in for use or profit."

Livestock thus includes animals held for breeding purposes (often referred to as fixed capital assets) and those held for resale (often referred to as floating capital assets).

The livestock must be used in the farming operations to fall within the ambit of the First Schedule.

Nature

The general rule in paragraph 2 is that all farmers, including companies carrying on farming operations, are required to include in their tax returns the value of their livestock held and not disposed of at the beginning and at the end of each year of assessment. The value of *livestock held and not disposed of at the end of the year of assessment* ("closing stock") is included in income and the value of *livestock held and not disposed of at the beginning of the year of assessment* ("opening stock") is allowed as a deduction from income[19] (see **4.3.2** for the determination of the values).

Once an animal is classified as livestock any consideration received or accrued on its disposal must be included in the farmer's gross income regardless of whether the animal was acquired as fixed capital or floating capital. This was confirmed in *R Koster & Son (Pty) Ltd & another v CIR*[20] in which the court cited with approval the following passage from *Farmer v COT*[21] in which this principle was upheld in relation to equivalent provisions of the Southern Rhodesia Income Tax Act:

> "The main provision of this section is that every farmer is bound to include in the return rendered by him for income tax purposes, i.e., for the determination of his

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[17] Lesley Brown 4 ed (1993) Oxford University Press Inc., New York, United States of America in vol 1.
[18] 1985 (2) SA 831 (A), 47 SATC 23 at 32.
[19] Paragraph 3(1).
[20] Above, 47 SATC 23 at 33.
[21] 1944 SR 80, 13 SATC 158 at 159.

> taxable income, the values of all livestock and produce held by him and not disposed of at the beginning and end of each year of assessment. The section has a wide embrace, both as to the farmer affected and the class of livestock. It makes no distinction between ranching stock and dairy, sheep, pig or other livestock, and it treats livestock in the same category as produce; in other words, it abolishes the importance or necessity of inquiring into the purpose with which the farmer has acquired his livestock or what his scheme or method of profit making is, and treats all the farmer's livestock and produce as his floating capital. In respect of these two commodities the farmer is treated, willy nilly, as an ordinary trader for income tax purposes. Dependent upon the difference in the value of his livestock at the commencement and the close of each year, there is either an accrual or a loss of his floating capital; if the former this forms part of his income, if the latter the loss is deducted from his income. His sales during each year of his livestock of whatever category, whether of part or the whole of his herd, form part of his income and his losses, whether mortality or other losses, are deducted from his income. This basis of computation for income tax purposes has been imposed compulsorily upon the farmer by legislation, and the Commissioner of Taxes and the Courts are no longer concerned to inquire whether in a particular farming business the farming livestock can be treated as fixed capital, because it must now be treated as part of the stock in trade of his farming business."

The trade of farming is specifically excluded from the opening and closing stock provisions in section 22.[22] The opening and closing stock provisions in paragraph 3 only deal with livestock and not consumable stores. Accordingly, a farmer's consumable stores, which include items such as fuel, spare parts, fertilizer and packing materials, do not need to be brought into account in opening stock or closing stock.[23]

Application to game farming

A game farmer (see **4.1**) is generally involved in the activity of breeding and running game on a farm for the purpose of marketing the live animals, hunting the animals for a fee or slaughtering the animals for meat. The game which is part of the farming operations clearly falls within the definition of livestock discussed above and is accordingly considered to be livestock for purposes of the First Schedule.[24]

Animals which are not part of the farming operations, that is, animals which the farmer is not raising with the intention of exploiting commercially, will not fall within the scope of the First Schedule. For example, a game farmer may have hyenas, foxes or rodents on the farm which are not part of the farming operation and therefore do not fall within the provisions of the First Schedule.

Under paragraph 2 a game farmer must include in the return of income the value of all livestock "held and not disposed of" at the beginning and end of each year of assessment. In the context of the First Schedule SARS interprets "held" as referring

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[22] Amounts to be taken into account in respect of values of trading stock.

[23] Section 22(8) still applies to consumable stores of farmers, but does not apply to livestock and produce which are covered by paragraph 11.

[24] Before 1 March 1999 SARS did not treat game as livestock for purposes of all the paragraphs of the First Schedule – see Income Tax Practice Manual [A:F14] read with Practice Note No. 6 of 1999 and Practice Note No. 27 of 1994 (withdrawn).

to ownership.[25] The expression would therefore mean livestock owned by the taxpayer which has not been disposed of.

The question of ownership is particularly relevant to wild game because under the common law wild game are regarded as *res nullius*, that is, things owned by nobody but which can be owned. Ownership is established by taking control of the animal with the intention of being the owner. Typically in the game farming context this is achieved by erecting fences around the farm. The common law position has been modified by the Game Theft Act No. 105 of 1991. This Act ensures that a farmer remains the owner of game that escapes from the farm. "Game" is defined in the Game Theft Act as follows:

> **"game"** means all game kept or held for commercial or hunting purposes, and includes the meat, skin, carcass or any portion of the carcass of that game.

Section 2 of the Game Theft Act No. 105 of 1991 reads as follows:

> **2. Ownership of game.—**
>
> (1) Notwithstanding the provisions of any other law or the common law—
>
> (*a*) a person who keeps or holds game or on behalf of whom game is kept or held on land that is sufficiently enclosed as contemplated in subsection (2), or who keeps game in a pen or kraal or in or on a vehicle, shall not lose ownership of that game if the game escapes from such enclosed land or from such pen, kraal or vehicle;
>
> (*b*) the ownership of game shall not vest in any person who, contrary to the provisions of any law or on the land of another person without the consent of the owner or lawful occupier of that land, hunts, catches or takes possession of game, but it remains vested in the owner referred to in paragraph (*a*) or vests in the owner of the land on which it has been so hunted, caught or taken into possession, as the case may be.
>
> (2) (*a*) For the purposes of subsection (1)(*a*) land shall be deemed to be sufficiently enclosed if, according to a certificate of the Premier of the province in which the land is situated, or his assignee, it is sufficiently enclosed to confine to that land the species of game mentioned in the certificate.
>
> (*b*) A certificate referred to in paragraph (*a*) shall be valid for a period of three years.

For the reasons discussed above, all game livestock is dealt with on revenue account as if it were floating capital.

4.3.2 Opening and closing stock

As noted above the value of closing stock is included in income and the value of opening stock is allowed as a deduction from income. The value of the livestock to be included in opening stock and closing stock is determined according to paragraphs 4 (opening stock) and 5 (closing stock).

[25] Various writers support this interpretation see - D Clegg and R Stretch *Income Tax in South Africa* LexisNexis, Durban in 19.3; D Meyerowitz *Meyerowitz on Income Tax* 2007–2008 The Taxpayer CC, Cape Town in 20.24; A P de Koker *Silke on South African Income Tax* LexisNexis, Durban in § 15.10.

Paragraph 5(1) stipulates that the value to be placed on the livestock for purposes of the First Schedule shall be the standard value applicable to that livestock. The standard value of any class of livestock of a farmer is generally either –

- the standard value of that class of livestock fixed by regulation under the Act, or
- another standard value adopted by the farmer (or company or the executor of the estate) when a particular class of livestock is adopted for the first time and such value is within 20% of the standard values fixed in the regulations or which, in certain circumstances, has been approved by the Commissioner.

Paragraph 4(1) provides that the value of the opening stock will be –

- the value of the closing stock at the end of the preceding year;
- the market value of livestock acquired during the current year of assessment otherwise than by purchase, natural increase or in the ordinary course of the farming operations carried on, for example, by donation or inheritance;[26] and
- the market value of livestock which was previously held, but not as part of the farming operations, becomes part of the farming operations.[27]

Note: Any opening stock still on hand at the end of the year of assessment must be included in the closing stock at its standard value and not market value.

The regulations do not fix a standard value for game livestock. For the purpose of standard values the Commissioner accepts that game livestock may be allocated a standard value of nil.[28]

4.3.3 The cost of acquiring game

The cost price of game livestock acquired by a person carrying on farming operations may be claimed as a deduction under section 11(*a*).

4.3.4 Limitation under paragraph 8 of the First Schedule

Paragraph 8 reads as follows:

> 8. (1) Where any farmer has during any year of assessment incurred expenditure in respect of the acquisition of livestock, the deduction which may be allowed to him under section 11(*a*) of this Act in respect of the cost price of such livestock shall be limited to an amount which, together with the value of livestock held and not disposed of by him at the beginning of such year, does not exceed the income received by or accrued to him from farming during such year and the value of livestock held and not disposed of by him at the end of such year.
>
> (2) Any amount which has been disallowed under the provisions of subparagraph (1) shall be carried forward and be deemed to be expenditure incurred by the farmer in respect of the acquisition of livestock during the succeeding year of assessment.
>
> (3) The provisions of this paragraph shall not apply—
>
> (*a*) in any case where it is shown by the farmer that livestock the cost of which falls to be dealt with under such provisions is no longer held and not disposed of by him; and

[26] Paragraphs 4(1)(*a*)(ii) and 4(1)(*b*)(ii).
[27] Paragraphs 4(1)(*a*)(ii) and 4(1)(*b*)(ii).
[28] Paragraph 6(1)(*b*)(ii), (*c*)(ii) or (*d*)(ii) read with paragraph 6(3).

> (*b*) to so much of any expenditure (including any amount which has been carried forward under the provisions of subparagraph (2)) which falls to be disallowed under subparagraph (1) as, together with the value of livestock held and not disposed of by him at the beginning of the year of assessment, exceeds such amount as is shown by him to be market value of all livestock held and not disposed of by him at the end of such year.

Paragraph 8 provides that the deduction of expenditure incurred during the year of assessment for the acquisition of livestock, which may be allowed under section 11(*a*) for the cost price thereof, is ring-fenced. The deduction available is limited to the sum of the income received and accrued from farming operations plus the value of the livestock held and not disposed of by the farmer at the end of the year of assessment less the value of livestock held and not disposed of by the farmer at the beginning of the year of assessment. Any amount not allowed as a deduction will be carried forward to the succeeding year of assessment and will be deemed to be expenditure incurred in that year (and hence subject to potential limitation in the succeeding year depending on the facts).

This potential limitation only applies to the deduction which may be allowed under section 11(*a*). Although opening stock forms part of the limitation calculation under paragraph 8, the opening stock deduction[29] is not itself subject to the paragraph 8 limitation.

See **4.3.2** for a discussion on the determination of the opening and closing stock values to be taken into account for game livestock – the values will often be nil.

The potential limitation is assessed on the totality of all the farmer's livestock regardless of its nature. For example, if a taxpayer conducted sheep farming and game farming, a single limitation calculation taking into account both the sheep and game livestock would be performed.

A taxpayer that can demonstrate that the cost of acquisition of a particular animal, which is no longer held and not disposed of at the end of the year of assessment, is included in the amount to be carried forward under paragraph 8 (for example, the animal purchased has been hunted and killed) may exclude the cost of that particular animal from the carried-forward amount and immediately claim it as a deduction. It is considered unlikely that this will apply frequently, if at all, in the context of game farming because it is often impracticable to accurately count and track particular livestock.

In addition, a farmer will be entitled to an immediate deduction if the opening stock value of livestock plus the amount to be carried forward under paragraph 8 exceeds the market value of all livestock held and not disposed of at the end of the year of assessment. The amount of the deduction is equal to the amount of the excess and the onus rests on the taxpayer to substantiate the amount claimed. The amount to be carried forward under paragraph 8 must also be reduced by the excess.

[29] Provided for under paragraph 3 and 4 – in the context of game farming this will often be Rnil but it could include, for example, a market value deduction for inherited game livestock.

Example 1 – Application of paragraph 8 limitation to game farmers

Facts:

Farmer A, who is carrying on game-farming operations, submits the following information with his tax return at the end of the year of assessment:

	R
Farming income	50 000
Standard value of livestock at the end of the year of assessment:	
Game	Nil
Other livestock	300
Value of produce at the end of the year of assessment	2 000
Standard value of livestock at the beginning of the year of assessment:	
Game	Nil
Other livestock	279
Value of produce at the beginning of the year of assessment	Nil
Purchases of game livestock this year	300 000

Result:

Determination of taxable income of the farmer:

		R
Farming income		50 000
Closing stock		
Livestock at standard value:		
Game	Nil	
Other	300	
Value of produce	2 000	2 300
		52 300
Less:		
Opening stock:		
Livestock at standard value		
Game	Nil	
Other	279	
Produce	Nil	(279)
		52 021
Less:		
Allowable deduction – purchase of livestock [section 11(*a*) limited by paragraph 8 – see below]		(50 021)
Taxable income from the carrying on of farming operations		2 000

Limitation on the cost of acquisition of livestock (paragraph 8):

Income received and accrued from farming operations	50 000
Value of livestock held and not disposed of at the end of the year	300
Value of livestock held and not disposed of at the beginning of the year	(279)
Maximum deduction permissible	50 021
Expenditure deductible under section 11(*a*) on the acquisition of game livestock	300 000
Less: Deductible amount current year	(50 021)
Amount of deduction carried forward to the following year	249 979

Example 2 – Application of paragraph 8 limitation to game farmers – cost of livestock exceeds its market value

Facts:

The facts are the same as Example 1 except that Farmer A is able to show that the fair market value of all the livestock at year-end is R220 000.

Result:

Determination of taxable income of the farmer:

Farming income		50 000
Standard value of livestock at the end of the year:		
Game	Nil	
Other	300	
Value of produce at the end of the year of assessment	2 000	2 300
		52 300
Less:		
Standard value of livestock at the beginning of the year:		
Game	Nil	
Other	279	
Produce	Nil	(279)
Subtotal		52 021
Less:		
Allowable deduction – purchase of livestock [section 11(*a*) and paragraph 8]		(50 021)
Allowable deduction – excess above market value		(30 258)
Assessed loss from the carrying on of farming operations		(28 258)

Determination of the limitation on the acquisition of livestock:

Income received and accrued from farming operations	50 000
Value of the livestock held and not disposed of at the end of the year	300
Value of livestock held and not disposed of at the beginning of the year	(279)
Subtotal	50 021

Expenditure deductible under section 11(*a*) on the acquisition of game livestock	300 000
Less: Deductible amount current year	(50 021)
Additional amount under paragraph 8(3)(*b*) (see below)	(30 258)
Amount of deduction carried forward to the following year	219 721

Determination of the additional amount to be allowed under paragraph 8(3)(*b*):

	R
Expenditure disallowed (Example 1)	249 979
Value of opening stock	279
	250 258
Less: Market value	(220 000)
Additional amount allowable	**30 258**

4.4 Expenditure and allowances

Expenditure and losses incurred for purposes of trade, that do not qualify as a deduction under the First Schedule, may be claimed under other provisions of the Act provided they meet the requirements of the particular provision.

Section 11(a) and section 23(g)

In determining a person's taxable income derived from carrying on any trade, the general deduction formula in section 11(*a*) requires that the expenditure and losses must be actually incurred in the production of income and must not be of a capital nature. In addition, expenditure and losses must be claimed during the year of assessment in which they are actually incurred.

Section 23(*g*) prohibits the deduction of moneys not expended for the purposes of trade.

Amounts generally deductible under section 11(*a*) by a game farmer include, for example, –

- normal running expenses of the farming operation (for example, expenditure on ammunition, electricity, feed, fuel, livestock, wages & salaries, and veterinary fees);
- cost of butchers, trackers and professional hunters;
- advertising and promotion costs; and
- travelling costs (both local and overseas).

This list is not exhaustive and the facts of each case will dictate which items of expenditure qualify as a deduction under section 11(*a*).

Capital allowances

Capital expenditure, which does not qualify as a deduction under paragraph 12 (see **4.5**), may qualify for a deduction under one of the other capital allowance provisions in the Act. Depending on the nature of the particular asset and the context in which it is used, the provisions which are likely to be of relevance in the context of game farming are section 12B, 12C or 11(*e*) and in respect of buildings, section 13*bis*, 13*quin* or 13*sept.*

The different capital allowance provisions are not discussed in detail in this Note. However given its particular relevance to farming operations, section 12B is briefly discussed below.

Section 12B provides for the deduction of a special depreciation allowance on machinery, implements, utensils or articles (other than livestock) which are –

- owned by the taxpayer or acquired under an instalment credit agreement;
- brought into use for the first time by that taxpayer; and
- used in the carrying on of farming operations.

The deduction under section 12B is –

- 50% of the cost to the taxpayer in the year of assessment during which the asset is brought into use;
- 30% of the cost to the taxpayer in the second year; and
- 20% of the cost to the taxpayer in the third year.

Equipment used by game farmers that would generally qualify for the special allowance under section 12B includes, for example, vehicles, firearms, meat saws and two-way radios. This list does not limit the qualifying assets and each asset must be considered on its own merits.

The following assets are specifically excluded from section 12B:

- Any motor vehicle the sole or primary function of which is the conveyance of persons.
- Any caravan.
- Any aircraft other than an aircraft used solely or mainly for the purpose of crop-spraying.
- Any office furniture or equipment.

An asset that does not qualify under section 12B may still qualify for an allowance under another provision of the Act. For example, if a game farmer also runs a game lodge business, the capital assets used in that business (such as beds, furniture, refrigerators and stoves) would not be considered to be used for farming operations and would not qualify for an allowance under section 12B. An allowance under section 12B would also not be available for certain assets used in the farming operations (such as aircraft used for the counting of game and office equipment) as those assets are specifically excluded. The taxpayer may, however, qualify for a depreciation allowance under section 12C in some instances and in other instances under section 11(*e*).[30]

The deductions allowed under sections 11(*e*), 12B and 12C are included in the income of the taxpayer if subsequently recovered or recouped under section 8(4)(*a*). These deductions must also be taken into account when determining whether any

[30] See Interpretation Note No. 47 (Issue 3) "Wear-and-Tear or Depreciation Allowance" (2 November 2012).

deduction under section 11(*o*) is available on the alienation, destruction or loss of a depreciable asset.[31]

4.5 Capital development expenditure

Section 11(*a*) prohibits the deduction of expenditure of a capital nature. The First Schedule, however, provides an exception to this general rule for persons who carry on farming operations and have incurred expenditure of a capital nature as listed in paragraph 12. Paragraph 12 also applies to persons carrying on game-farming operations.

Amounts qualifying as a deduction under paragraph 12 include amongst others expenditure incurred for –

- the eradication of noxious plants and alien invasive vegetation;
- the prevention of soil erosion;
- dipping tanks;
- dams, irrigation schemes, boreholes and pumping plants;
- fences;
- erection of or extensions, additions or improvements (other than repairs) to buildings used in connection with farming operations, other than those used for domestic purposes;
- the building of roads and bridges used in connection with farming operations; and
- the carrying of electric power from the main transmission lines to the farm apparatus or under an agreement with the Electricity Supply Commission under which the farmer has undertaken to bear a portion of the cost incurred by the Commission in connection with the supply of electric power consumed by the farmer wholly or mainly for farming purposes.

The expression "in connection with" (see 6th and 7th bullet above) was considered by the Tax Court in ITC 885.[32] After an analysis of a number of cases dealing with the subject, the court concluded as follows:[33]

> "It seems to me that it is possible to extract from these judgments a number of guiding rules. One must give to the phrase "a wide and comprehensive meaning" but not as wide and comprehensive as to embrace a remote and indirect connection. There must be something in the nature of a direct connection and this must be subservient and ancillary to the particular business under consideration."

The direct connection to game-farming operations is important. Expenditure incurred on facilities like slaughter rooms, meat rooms, cooling rooms, biltong rooms, skin rooms and trophy rooms will generally have the required connection in order to qualify for deduction under paragraph 12.

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[31] See Interpretation Note No. 60 "Loss on Disposal of Depreciable Assets" (10 January 2011).
[32] (1959) 23 SATC 336 (C).
[33] At 338.

In contrast, expenditure incurred on facilities used to accommodate visitors and hunters will not have the required connection and will not qualify for a deduction by a game farmer under paragraph 12. Similarly, the cost of buildings erected in connection with a canning or other industry run in conjunction with the farming operations will not be deductible under paragraph 12.

Expenditure on the construction of roads and bridges will also only qualify as a deduction for a person carrying on game-farming operations if they are used in connection with the farming operations.

The deduction available for capital development expenditure (excluding expenditure incurred on the eradication of noxious plants and alien invasive vegetation or the prevention of soil erosion) is ring-fenced. The deduction available in a particular year of assessment is limited to taxable income from farming before claiming the deduction.[34]

The excess is carried forward and is deemed to have been incurred in the following year of assessment.[35]

Under paragraph 20A of the Eighth Schedule a farmer who ceases to carry on farming operations and who subsequently disposes of the immovable property on which they were carried on, can, subject to the limitations specified in that paragraph, elect to treat any un-deducted balance of capital development expenditure as expenditure incurred and paid in respect of the immovable property. In this way the un-deducted balance of capital development expenditure may form part of the base cost of the farm property for CGT purposes.

The development expenditure under paragraph 12(1) is not subject to recoupment under section 8(4)(*a*) because that section, with some exceptions, only applies to the deductions under sections 11 to 20. Paragraph 12(1B) and (1C) contain special recoupment provisions for paragraph 12 assets that become movable assets.

4.6 Housing for guests and employees

Expenditure incurred on residential facilities such as bedrooms, dining rooms, sitting rooms and kitchen facilities that are made available to safari guests and hunters, is not incurred directly in connection with farming operations and therefore does not qualify for deduction under the First Schedule (see **4.5**). Such buildings may qualify for an allowance under section 13bis if the taxpayer is carrying on the trade of "hotel keeper" as defined in section 1(1). In order to qualify as a hotel keeper the taxpayer would have to supply meals and sleeping accommodation.

Before 21 October 2008, the First Schedule provided for a person carrying on farming operations to deduct the expenditure incurred on the erection of dwellings for the person's farm employees. This deduction is no longer available under the First Schedule or under the main body of the Act. A deduction is, however, available under section 13*sept* for the sale of low-cost residential units on loan account to employees.

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[34] Technically the deduction is claimed and the excess above taxable income from farming is added back to taxable income.

[35] Paragraph 12(3).

4.7 Cessation of farming operations

Farming operations can be discontinued for various reasons such as voluntary cessation, death or sequestration of the taxpayer. The cessation of farming operations has tax implications for the taxpayer. The treatment of livestock under these circumstances is considered below.

4.7.1 Voluntary cessation of farming operations

A taxpayer who discontinues farming operations can decide to either dispose of all livestock or to retain all or some of the livestock. The proceeds received from the disposal of the livestock during that process (that is, the discontinuance of farming operations) will form part of the taxable income derived from the farming operations.

The position of a taxpayer who discontinues farming operations, but retains livestock or has entered into a "sheep lease" or similar agreement is governed by section 26(2). This section provides that certain provisions of the First Schedule will remain applicable until **all** such livestock retained has been disposed of.

Section 26(2) applies to livestock that has been taken into account and for which expenditure has previously been allowed as a deduction under the Act in the determination of the taxable income derived from farming operations. It therefore applies to game livestock of a farmer since the cost of the game would have been claimed under section 11(*a*) and the livestock would have been included in opening and closing stock albeit at a standard value of nil.

4.7.2 Death

The death of a game farmer has income tax and capital gains tax consequences for the deceased person, the deceased estate and the heirs or legatees. These consequences are briefly discussed below with reference to livestock.

(a) Income tax

Deceased person

The taxable income of a person upon death must be determined for the period from the beginning of the year of assessment to the date of death.

As discussed in **4.3.2** a person carrying on game-farming operations includes the value of game livestock held and not disposed of at the beginning and end of the year of assessment in opening and closing stock at a standard value of nil. The same principle applies to the final year of assessment of the deceased person with the result that game livestock will be reflected at a nil value in opening and closing stock in that year.

Deceased estate

An executor of a deceased estate must include the market value[36] of game livestock acquired from the deceased person in opening stock in the deceased estate's tax computation.[37] For the purposes of applying the limitation rule in paragraph 8 the market value of that opening stock must be taken into account (see **4.3.4**).

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[36] Determined at the date of death of the deceased.
[37] Paragraph 4(1)(*b*)(ii)(*aa*).

Any game livestock still on hand at the end of the deceased estate's first year of assessment will be included in closing stock at a standard value of nil, and the same applies to amounts to be included in opening and closing stock in subsequent years of assessment of the deceased estate.

On inclusions in the gross income of the estate and deductions claimable by the estate, see "Heirs and legatees" below.

Heirs or legatees

Any amount received by or accrued to the deceased estate from the disposal of game livestock must be included in the gross income of the deceased estate unless it is derived for the immediate or future benefit of an ascertained heir or legatee, in which case it must be included in the gross income of that heir or legatee [section 25(1)].

Deductions or allowances relating to game-farming operations conducted by the executor must be claimed by the deceased estate unless they relate to income which has been included in the income of an ascertained heir or legatee under section 25(1). In the latter event the deductions or allowances must be claimed by the heir or legatee [section 25(2)]. For example, an ascertained heir or legatee would claim the market value of game livestock acquired by the estate on the date of death.

The amount received by or accrued to an heir or legatee who disposes of game livestock acquired by inheritance will be of a capital nature provided that it was disposed of at the earliest opportunity and not made part of a farming operation (see *Capital gains tax* below).

By contrast, any amount received by or accrued to a farmer on disposal of inherited game livestock which has been incorporated into the farmer's farming operations must be included in the farmer's gross income. Under paragraph 4(1)(*a*)(ii)(*aa*) the farmer will be entitled to an opening stock deduction for the inherited livestock equal to its market value. Any inherited game livestock not disposed of in the year of assessment in which it was acquired will have a standard value of nil for closing stock purposes. However, for the purposes of applying the limitation rule in paragraph 8 the market value of the opening stock must be taken into account.

(b) Capital gains tax

For more information on the capital gains tax consequences of deceased estates, see chapter 16 of the *Comprehensive Guide to Capital Gains Tax* (Issue 4).

Deceased person

Under paragraph 40(1) of the Eighth Schedule a deceased person is deemed to dispose of that person's assets (with some exceptions) to the deceased estate for an amount received or accrued equal to their market value on the date of death.

One of the exceptions to this rule is assets bequeathed to the person's spouse. In that case the surviving spouse is subject to roll-over treatment under paragraph 67(2)(*a*) of the Eighth Schedule and steps into the shoes of the deceased person in relation to the asset. This means that the surviving spouse takes over from the deceased person, amongst other things, the date of acquisition, the date of incurral of expenditure and the amount of expenditure on the asset.

Game livestock held on the date of death is thus generally deemed to be disposed of by the deceased person for an amount received or accrued equal to its market value, except if the livestock is bequeathed to the person's spouse. This amount will comprise the proceeds for CGT purposes under paragraph 35 of the Eighth Schedule.[38]

In determining the base cost of game livestock, any expenditure incurred in acquiring it must be reduced by any portion which has been allowed as a deduction under section 11(*a*).[39] Thus the cost of any game livestock which has been fully allowed under section 11(*a*) will have a base cost of nil. However, to the extent that the cost has been limited under paragraph 8 it will have a base cost equal to the portion not allowed as a deduction under section 11(*a*).

The base cost of game livestock acquired before 1 October 2001 may be determined using the time-apportionment, market value or 20% of proceeds method.[40]

Deceased estate

The deceased estate is deemed to acquire the assets from the deceased person for an amount of expenditure equal to their market value on the date of death (paragraph 40(1A)(*a*) of the Eighth Schedule).

Paragraph 40 of the Eighth Schedule envisages that an executor will deal with the assets of the estate either by –

- awarding an asset to an heir or legatee; or
- disposing of the asset to a third party.

An asset awarded by the executor to an heir or legatee is treated as having been disposed of for proceeds equal to its base cost.[41]

The deceased estate must determine a capital gain or loss for assets disposed of to a third party. The proceeds on disposal of an asset are reduced under paragraph 35(3)(*a*) of the Eighth Schedule by any amount included in gross income or which was taken into account in determining taxable income. Likewise, the base cost of an asset is reduced under paragraph 20(3)(*a*) by any amount which is or was allowable or is deemed to be allowed as a deduction in determining taxable income. Whether these proceeds and base cost reductions occur will depend on whether there is an ascertained heir or legatee.

If there is an ascertained heir or legatee any amount received by or accrued to the estate which would have been income in the hands of the deceased person is deemed to be income in the hands of the heir or legatee under section 25(1). In this situation the deceased estate will not reduce its proceeds under paragraph 35(3)(*a*) of the Eighth Schedule.

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[38] Since game livestock has a nil value for closing stock purposes under the First Schedule, the proceeds reduction rule in paragraph 35(3)(*a*) of the Eighth Schedule will not apply.
[39] Under paragraph 20(3)(*a*) of the Eighth Schedule.
[40] See *Comprehensive Guide to CGT* (Issue 4) in 16.1.2.3.
[41] Paragraph 40(2)(*a*).

If there is no ascertained heir or legatee, section 25(1) deems the amount to be income of the deceased estate, and in this event the amount received by or accrued to the deceased estate must be reduced under paragraph 35(3)(*a*) in arriving at its proceeds.

The same principle applies to deductions, that is, section 25(2) attributes them to an ascertained heir or legatee but leaves them in the deceased estate when there is no such heir or legatee. Thus, when the deductions remain in the deceased estate they will reduce base cost under paragraph 20(3)(*a*) of the Eighth Schedule but if they are attributed to an heir or legatee the deceased estate's base cost will not be reduced. An example of such a deduction is the opening stock of the deceased estate. In this regard the deceased estate is granted an opening stock deduction at market value for the game livestock acquired from the deceased person [paragraph 4(1)(*b*)(ii)(*aa*)]. As a result, its expenditure deemed to have been incurred under paragraph 40(1A)(*a*) of the Eighth Schedule will be reduced to nil by paragraph 20(3)(*a*) of the Eighth Schedule if there is no ascertained heir or legatee. The deceased estate will accordingly have a base cost of nil for the livestock in question. Conversely, if there is an ascertained heir or legatee there will be no such reduction because the deduction against income will have been attributed to the heir or legatee.

Heirs or legatees

Under paragraph 40(2)(*b*) of the Eighth Schedule an heir or legatee is deemed to have acquired inherited game livestock at a base cost equal to the deceased estate's base cost. This deemed cost is treated as expenditure actually incurred for the purposes of paragraph 20(1)(*a*) of the Eighth Schedule and may, depending on the circumstances (see below), be reduced under paragraph 20(3)(*a*) of the Eighth Schedule.

A disposal by an heir or legatee would, for example, be on capital account if the inherited game livestock was disposed of at the earliest opportunity and it is not made part of an existing farming operation.

As a rule, an heir or legatee who disposes of inherited livestock on capital account will have a base cost for that livestock equal to its market value on the date of death of the deceased person. The livestock acquired by the deceased estate by natural increase occurring after the date of the deceased's death would have a base cost to the estate of nil since the estate would not have incurred any expenditure for that livestock. An heir or legatee who inherits such "natural increase" livestock will also acquire it at a base cost of nil. The proceeds from a sale of livestock on capital account will as a rule be equal to the amount received or accrued.

By contrast, an heir or legatee who commences to use the game livestock in a farming operation or brings it into an existing farming operation will be on revenue account. In these circumstances the heir or legatee will acquire that livestock for revenue expenditure equal to its market value [paragraph 4(1)(*a*)(ii)(*aa*) read with section 25(2)]. The base cost of the livestock established under paragraph 40(2)(*b*) of the Eighth Schedule must therefore be reduced under paragraph 20(3)(*a*) of the Eighth Schedule by the paragraph 4(1)(*a*)(ii)(*aa*) deduction. An heir or legatee who

disposes of game livestock on revenue account will have proceeds of nil because the amount would be included in gross income.[42]

4.7.3 Insolvency or liquidation

Section 25C deems the estate of a natural person before sequestration and that person's insolvent estate to be one and the same person for the purpose of determining –

- any allowance, deduction or set off to which that insolvent estate may be entitled;
- any amount which is recovered or recouped by or otherwise required to be included in the income of that insolvent estate; and
- any taxable capital gain or assessed capital loss of that insolvent estate.

The person before sequestration must submit a return of income for the period commencing on the first day of the year of assessment and ending on the date before the date of sequestration.[43] Game livestock will have a standard value of nil for closing stock purposes at the end of that person's year of assessment in the normal way.

The insolvent estate must submit a return of income for its first year of assessment from the date of sequestration until the end of that year and for all subsequent years of assessment until the estate is wound up.

The insolvent estate will have an opening stock of game livestock of nil based on the "one and the same person" principle because the closing stock of the person before sequestration was nil. Any assessed loss of the person before the date of sequestration will be brought forward into the insolvent estate. Game livestock will continue to have a standard value of nil for closing stock purposes in the first year of assessment of the insolvent estate and for the purposes of determining future opening and closing stock. Any amount received by or accrued to the insolvent estate from the disposal of the livestock must be included in the gross income of the insolvent estate.

For CGT purposes there is no deemed disposal on date of sequestration as a result of the "one and the same person" principle in section 25C. Given that game livestock is floating capital there should be no CGT implications when game livestock is disposed of by the trustee of the insolvent estate.

A company that is being wound up or liquidated remains the same taxable entity until it is finally dissolved.[44] In practice a company must submit an interim return of income for the period from the beginning of the year of assessment up to the date immediately before the date of liquidation and another return from the date of liquidation until the end of the year of assessment. Game livestock will have a standard value of nil for opening or closing stock purposes. Any amounts derived by the company after date of liquidation must be included in its gross income.

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[42] The amount received by or accrued to the heir or legatee will be reduced by the portion included in gross income under paragraph 35(3)(*a*) of the Eighth Schedule.
[43] Paragraph (*b*)(i) of the proviso to section 66(13)(a).
[44] *Van Zyl NO v CIR* 1997 (1) SA 883 (C), 59 SATC 105.

4.7.4 Cessation of farming owing to the sale of land to the state

Paragraph 20 provides for a concessionary rate of tax when a farmer's farming operations are wound up as a result of a sale of the farm land to the state and the farmer derives abnormal farming income. This could apply to, say, the expropriation of a game farm. Since this issue is not unique to game farmers it is not explored in further detail in this Note.

4.8 Ring-fencing of assessed losses [section 20A]

Section 20A was introduced with effect from 1 March 2004. It is a ring-fencing provision which limits the utilisation of an assessed loss from a tainted trade to the income from that trade. It only applies to natural persons (individuals).

Section 20A is discussed in detail in the *Guide on the Ring-fencing of Assessed Losses from Certain Trades Conducted by Individuals* (Issue 2) ("ring-fencing guide") which was issued on 8 October 2010 and is available from the SARS website. It is not the intention of this Note to deal comprehensively with section 20A since that task is taken care of by the above guide. Rather, an overview of the main issues which are likely to affect game farmers, many of whom are natural persons who conduct their operations on a small scale on a part-time basis, will be provided. Inevitably when losses arise from game-farming operations and the taxpayer is a natural person, the issue will arise whether or not the loss from carrying on that trade may be set-off against other taxable income.

Section 20A does not replace sections 11(*a*) and 23(*g*). Any expenditure which does not qualify under section 11(*a*) or which is denied as a deduction under section 23(*g*) will be permanently lost. By contrast, section 20A does not permanently deny a set-off of the affected assessed loss but merely ring-fences it by only permitting it to be set off against future taxable income from that trade.

Section 20A contains four steps which determine whether an assessed loss can be ring-fenced. These are as follows:

Step 1 [section 20A(2)] – The maximum marginal rate of tax pre-requisite

Under this step it is first necessary to adjust taxable income by adding back any assessed loss and balance of assessed loss carried forward from the previous year of assessment.

If the amount so determined falls within the highest tax bracket for individuals, the taxpayer will have met the first step in the potential ring-fencing process and must proceed to steps 2 to 4.

Conversely, if the adjusted taxable income is below the level at which the maximum marginal rate of tax becomes payable, the assessed loss may not be ring-fenced. There is then no need to proceed to steps 2 to 4.

Step 2 [section 20A(2)(a) and (b)] – The "three-out-of-five-years" pre-requisite or alternatively, the "listed suspect trade" pre-requisite

Step 2 is also a pre-requisite for the application of section 20A. It comprises two alternative tests – if either of these tests is passed section 20A will potentially apply, if neither of the tests is passed section 20A can be disregarded.

Under the "three-out-of-five-years" pre-requisite, a person who makes assessed losses from game farming in at least three out of five years will meet this requirement. The five year period includes the current and four previous years of assessment. This rule applies to persons carrying on game farming on a full-time basis (see below).

Under the "suspect trade" pre-requisite section 20A lists eight suspect trades. An assessed loss arising from any one of these trades will be subject to potential ring-fencing. Farming or animal breeding is listed as a suspect trade unless such activities (including activities of a similar nature) are carried out on a full-time basis.[45] It follows that game farming which is conducted on a part-time basis will be subject to potential ring-fencing. While full-time farming is not listed as a suspect trade, it could be subject to potential ring-fencing if losses are made in three out of five years of assessment (see the "three-out-of-five years" pre-requisite above).[46]

Step 3 [section 20A(3)] – The "facts and circumstances" test (the escape clause)

Step 3 is an escape clause. In other words, an assessed loss that qualified for potential ring-fencing under steps 1 and 2 can escape ring-fencing under step 3.

Under section 20A(3) the ring-fencing provisions will not apply to a trade that constitutes a business in respect of which there is a reasonable prospect of deriving taxable income (other than taxable capital gains) within a reasonable period. Special regard must be had to –

- the proportion of the gross income derived from the trade in the year of assessment in relation to the amount of the allowable deductions incurred in carrying on that trade during that year;
- the level of activities carried on by the person or the amount of expenses incurred by that person in respect of advertising, promoting or selling in carrying on that trade;
- whether the trade is carried on in a commercial manner, taking into account –
  - the number of full-time employees appointed for purposes of that trade (other than persons partly or wholly employed to provide services of a domestic or private nature);
  - the commercial setting of the premises where the trade is carried on;
  - the extent of the equipment used exclusively for purposes of carrying on the trade; and
  - the time that the person spends at the premises conducting the business;
- the number of years of assessment during which assessed losses were incurred in carrying on the trade in relation to the period from the date when that person commenced carrying on the trade and taking into account –
  - any unexpected events giving rise to any of those assessed losses; and
  - the nature of the business involved;
- the business plans of the person and any changes thereto to ensure that taxable income is derived in future from carrying on the trade; and

[45] Section 20A(2)(*b*)(vi). See the ring-fencing guide for more detail.
[46] Under section 20A(2)(*a*).

- the extent to which any asset attributable to the trade is used, or is available for use, by the person or any relative of that person for private use (recreational purposes or personal consumption).

For a detailed discussion on these special factors, see paragraph 7 of the ring-fencing guide.

Step 4 [section 20A(4)] – The "six-out-of-ten-years" requirement (the "catch all" provision)

Step 4 is a "catch all" provision that applies even if a taxpayer has escaped ring-fencing under step 3. However, it does not apply to farming operations. Thus even if a game farmer incurs losses in six out of the last ten years, ring-fencing can be prevented if the taxpayer can satisfy SARS that a business is being carried on with a reasonable prospect of deriving taxable income within a reasonable period.

5. Conclusion

The same principles used to determine whether a person carries on farming operations apply to game farmers. The test for this purpose is a subjective one, that is, one based on the taxpayer's intention.

Income from the sale of game, game meat, carcasses and skins and fees related to hunting constitute farming income. However, income from accommodation, catering and admission charges is not farming income. This will be relevant when applying the ring-fencing provisions of paragraph 8 to game livestock. Game viewing fees may or may not constitute farming income depending on the facts and circumstances of the particular case.

The rules governing the deduction of expenditure, including capital development expenditure, are similar to those which apply to normal farming operations.

A farmer is required to bring to account the value of game livestock in opening and closing stock. No standard values have been prescribed by regulation for game livestock, but the Commissioner accepts that game livestock may be allocated a standard value of nil. Game livestock which is acquired by donation or inheritance is included in opening stock in the year of acquisition at market value under paragraph 4.

The deduction under section 11(*a*) for the cost of livestock is ring-fenced under paragraph 8, while an assessed loss or balance of assessed loss from farming is subject to potential ring-fencing under section 20A.

A farmer who ceases to carry on game-farming operations must generally continue to deal with any game livestock under the First Schedule.

Special rules apply for income tax and CGT purposes upon the death or sequestration of a farmer.

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