

# CONNECTING PEOPLE

FOR A BETTER FUTURE - NOW

# INDEX

- Marketing tips for difficult economic times
- Trust loan accounts in the spotlight
- Drought tests countries' adaptability
- Bonds, gold an attractive investment options with property shares remaining expensive
- New tax legislation will have a big influence on livestock and game farmers
- New B-BBEE Codes: Ask yourself these questions





## Marketing tips for difficult economic times

When a recession looms or when we face difficult economic times, the first area that usually faces the proverbial axe is the marketing budget. According to numerous marketing gurus, a downturn should not automatically mean a cut on the marketing spend. Rather develop an understanding of how the needs of your customers and stakeholders have changed and adapt your strategies to this new reality. Successful companies do not abandon their marketing strategies in a recession; they adapt them. It has even been found that brands that increase advertising during a downturn can improve market share and return on investment.

Here are five tips to consider when developing your marketing plan to face the current economic cycle:

### **1. Maintain your marketing spend**

There are many historic examples that brands that increase advertising during a recession, when competitors are cutting back, can improve their market share and return on investment at lower cost than during good economic times. Also, now is the time to negotiate for those special rates at advertising companies that are losing out on their other clients that are cutting budgets.

### **2. Research customers**

You need to understand how your customers are reacting to the new economic reality and how it impacts on their purchasing decision-making. During hardships, consumers tend to take more time searching for durable goods and negotiate harder at the point of sale. They are more willing to postpone purchases, trade down, or buy less. Take time to conduct some interviews and research your clients' changing needs.

### **3. Defend your market share (and maybe even gain some)**

Disappearing from your clients' view due to marketing cuts can give your competitors an ideal opportunity to gain extra market share from you. There is merit in the saying "Out of sight, out of mind", especially in an era when we are constantly bombarded with information. If you have to downsize your budget, try to maintain the frequency of your advertisements by shifting from 30-second to 15-second advertisements, or host events that are for 30 clients and not for 100, to name but a few options.

### **4. Support your suppliers**

You are not the only one feeling the economic pinch, your suppliers are also looking to secure contracts that will see them weather this storm. Now is the ideal time to strengthen your relationship, because no one wants to tie up working capital in excess inventories. Discuss options for early-buy allowances, extended financing, and generous return policies to motivate suppliers to stock your needs at a reduced cost.

### **5. Adjust pricing tactics**

Customers will now be looking for savings and might even be willing to test new brands that offer the same value at reduced fees. You do not have to cut your prices, but you can offer more temporary price promotions, reduce thresholds for quantity discounts and extend credit to long-standing customers.

Prepared by CORE Marketing and Public Relations  
For more information contact : +27 (0) 51 448 8188

## Trust loan accounts in the spotlight



Currently, the legislator is very concerned about the avoidance of Estate Duty and Donations Tax through the transfer or sale of assets to a trust by way of an interest-free loan account. Therefore, it issued draft amendments to the Income Tax Act (“Act”) by means of the new section 7C and 56 of the Act. According to the Explanatory Memorandum the purpose of this new Draft Section 7C is to combat the avoidance of Estate Duty and Donations Tax through the transfer or sale of assets to a trust by way of an interest-free loan account.

Currently, a person transferring assets to a trust has the following options, each giving rise to different tax outcomes:

- In the first instance, a person may donate the assets and trigger donations tax at 20 percent of the fair market value of the assets in the hands of the person.
- Secondly, a person may sell the assets to the trust on loan account at an arm’s length interest charge. If interest on the loan is market-related, the seller will be fully taxed on the interest portion of the loan repayments.
- Lastly, a person may sell the assets to the trust on loan account at an interest charge that is below arm’s length or charge no interest on the loan.

Currently, it is the use of the third option that the legislator is concerned about according to the Explanatory Memorandum.

Donations Tax will not be triggered on the asset when the asset is sold at market value to a trust in this manner because there is no gratuitous disposal as required for Donations Tax purposes. Coupled with the above, in some instances the seller reduces the loan capital which is supposed to be paid back to him/her by donating amounts to the trust to be set off against the loan to the trust using the current provisions of section 56(2)(b) which provides for the R100 000 annual exemption from Donations Tax. This further avoids Estate Duty through the tax-free reduction of the asset base of the seller achieved by such an annual donation to the trust.

Due to the fact that the loan is an interest-free loan or a loan with interest below market rates, meaning no interest is paid to the seller or interest paid is less than market rates, the seller will not be liable for income tax on the interest that is forgone or will not be liable for income tax on the interest that is below market rates. This results in a further reduction of the tax base.

In order to limit taxpayers’ ability to transfer wealth without being subject to tax, draft legislation was prepared which proposes rules focusing on interest-free loans or loans with interest below market rates that are made directly or indirectly by a natural person, or by a company that is a connected person in relation to that person to a trust.

According to these rules, as stipulated in the Explanatory Memorandum, it is proposed that an amount equal to the difference between interest that would have arisen as determined in accordance with the official rate of interest (as determined in terms of the Seventh Schedule to the Act) and the applicable actual rate of the loan below market rates made to a trust will be regarded as an amount of income accrued or received by the seller. Such amount imputed as income in the hands of the seller will not qualify for the section 10(1)(i) exemption in respect of the interest.

Further, with regard to interest-free loans, as there is no actual payment of interest by the trust to the seller, no deduction may be claimed by the trust. On the other hand, with regard to loans with interest rates below market value, only the amount of interest below market rates that is actually paid by the trust to the seller can be claimed as a deduction if the requirements of the general deduction formula are met.

In addition, any reduction of the interest-free loans or to loans with interest below market rates to which these rules apply will not qualify for the section 56(2)(b) R100 000 annual exemption of Donations Tax.

However, if the proposed wording of section 7C of the Act is studied in detail we believe the actual implications of it to be much wider than the intention as stated by the legislator. From the wording in section 7C it appears that the deemed interest taxation provision will apply to any amount owed by any trust that is a natural person or a company which is a connected person to the trust.

Therefore firstly, section 7C will apply to any loan provided by such listed connected persons to a trust irrespective of the fact that, if the loan relates to an asset that was transferred or sold to the trust, the deeming interest taxation provision will apply. This appear to be much wider than the stated aim or intention as per the Explanatory Memorandum.

The following are examples of loans that will also be subject to the deeming interest provisions, where the loan was not utilised to finance the sale of an asset to a trust:

- Distributions to beneficiaries where the beneficiaries effectively loaned the distribution back to the trust – such loans were not necessarily utilised to fund the acquisition of an asset by the trust.
- Loans provided to a trust by connected persons to the trust to fund expenditure of the trust where the trust has a lack of available funds, for example where a trust established in terms of a will (for example for minor beneficiaries) owns assets transferred to the trust in terms of the will, but such a will trust do not have sufficient cash to pay its day to day expenditure – again these loans were not necessarily utilised to fund the acquisition of an asset by the trust.

Potentially an even more serious concern is that it only refers to “trusts” and does not distinguish between the different types of trusts. If the intended purpose of the amendment as stated in the Explanatory Memorandum was to be achieved, the targeted avoidance trusts can only be discretionary trusts as the “bewind”/vested trusts where the assets etc. in the trusts already vest in a beneficiary cannot be utilised to avoid Estate Duty. “Bewind”/vested trusts is a popular entity type in South Africa to conduct small to medium business, with the “owners” of the business each owning a percentage of this “bewind”/vested trust through unit certificates being allocated.

The impact of the proposed section 7C is that any start-up and other funding provided by the owners of the “bewind”/vested trust will be subject to the deeming interest provisions, even though no assets have been transferred/sold to the trust! This will also not be in line with other entity types utilised to conduct small and medium business, such as companies or close corporations, as the shareholders and the members of the companies and close corporations are allowed to provide interest-free loans to these entities without being penalised. Clearly a business trust should enjoy the same treatment.

Furthermore, the amount of normal tax attributable to the income which is included in the income received or accrued by the seller may be recoverable by the seller from the trust as the trust benefits from the low or no interest charge. If the seller does not recover this amount of tax from the trust within a period of three years after the end of the year of assessment in which the income was included in the income of the seller, the tax attributable to that income will be treated as a donation by the seller to the trust on the date on which the three year period ends, thus attracting Donations Tax.

This stipulation seems to be unclear and also not practical in our opinion. Firstly, it is not clear what is meant in terms of the legislation by “recovered”. Must the tax be paid by the trust (for example in cash) or can it be recovered but still owed by the trust to the connected person, for example on loan account? Secondly, if the legislation does imply that it must have been paid, due to a lack of funds it might be impossible for the trust to actually pay the amount to the trust, therefore resulting in Donations Tax without there being an intention to make such a donation.

These draft amendments to the Act raise serious concerns regarding the practical implications for trusts and loan accounts. There is little doubt that the issues identified in this article will be vigorously debated in the next few months.

Prepared by CORE Tax.  
For more information contact : +27 (0) 51 448 8188



## Drought tests countries' adaptability

Objective measurement is a prerequisite for the application of policy, but too often final decision-making is steered by political goals. Food security is an aim, but for many countries with acute food shortages it remains an unobtainable dream unless humanitarian aid from outside the country brings relief. Household food security is the result and in 2015 chronic hunger's destructive consequences have resulted in a review of the Food and Agriculture Organisation's (FAO) goals pertaining to sustainable development.

Food and agriculture are comprehensively integrated into the 17 goals, which include poverty relief, the elimination of famine, improved food security and sustainable agriculture by 2030. Clear goals were also included in terms of the relationship between optimal use of resources and how this could improve food security, amongst others. In many instances these 17 goals are therefore safeguarded against political manipulation. A country's compliance could inform future aid as there is simply not enough capacity available to assist chronically dependent countries if these countries are not willing or able to get their own house in order.

The current drought is a good test of whether countries are prepared to adapt to the direct consequences but also to show how this will inform future policy. In South Africa there was an unnecessary delay in declaring the country drought-stricken. With eight of the nine provinces now declared drought-stricken areas, this has unlocked other aid. However, this has also resulted in questions regarding future policy that is becoming more important. The same goes for other countries in the region that are dependent on rain and favourable agricultural conditions in South Africa.

An authoritative and objective analysis of the food security status of 113 countries is published annually by Du Pont. This provides an interesting view on each country's historical achievements in three different categories, which indexes should consequently be extrapolated to account for the latest developments. The Du Pont Index analyses the three components of food security, namely affordability, availability, and quality and safety. These analyses are conducted at the hand of 28 unique indicators. The 2016 analysis shows some improvement since 2015 in Europe (+0.9), Central and South America (+0.8), North America (+0.7) and Asia and the Pacific Rim (+.06) as groups of countries. With 2.7 Indonesia has shown the biggest increase of the ten countries. Yemen's index has decreased by 4.2 and amongst the ten countries with the biggest decreases are Malawi (-0.6) and Botswana (-0.9). Each of these countries will probably experience further decreases in the next year, given the impact of the current drought.

In terms of South African (Namibia does not take part), the country is 47th out of 113 countries with an index of 62.9. In terms of provision, South Africa is 31st and in terms of affordability and safety 53rd. Strong points (with a score of 75 or more) include the presence of food protecting programmes, feeding standards, food safety, food losses and tariff protection regarding imports.

Important indicators that could hamper future improvement include the percentage of the population living below the subsistence minimum, as well as farmers' access to financing. The current high percentage of the number of unemployed and the impact that the drought is having on farmers' solvency will have a negative impact on future indexes.

Prepared by CORE Business Development.  
For more information contact : +27 (0) 51 448 8188



## Bonds, gold and attractive investment options with property shares remaining expensive

Britain's historic vote to exit the European Union (EU) has resulted in markets falling sharply. Shortly after the vote, global investors moved quickly out of risk assets to low risk assets and the JSE suffered an immediate loss - in June the JSE ALSI fell 3.1%. Company earnings have continued to come under pressure and earnings are down 20% over 12 months, resulting in a persistently expensive local market with a historical PE ratio in the order of 22 times. All three of the main indices fell as selling was across the full market. Gold and gold shares performed exceptionally well, gaining 23.7% as investors headed for safety. After May's large 10% depreciation of the Rand, it strengthened in June by 6.3% against the USD.

Global investors took their cue from the more dovish comments from US Federal Reserve chair, Janet Yellen. A much slower lift-off of US interest rates, off the back of what continues to be a low-growth economy, resulted in investors moving back into emerging markets. The MSCI EM index gained 4%, while the MSCI World Equity index declined by 1.12%. Emerging markets had been knocked back hard in 2015 and have therefore seen a relief rally year to date. In general equity market valuations are not cheap, with corporate earnings under pressure. Valuations continue to be underpinned by low interest rates as the global economy struggle to gain any traction.

Local listed property shares gained 1.1% for June after the 3% negative in May. This brings their annual return to just over 11%, and therefore one of the best performing asset classes over this period. Prices moved in sympathy with the strong moves in bonds in the month. Valuations across the full universe of property shares remain expensive with the historical yield on the sector at 5.8% (slightly cheaper than May) and a one-year forward yield of 6.3%. This remains expensive when compared to the yield on ten-year bonds of 9.3%. As with all market sectors there is large disparity in valuations between the various securities.

Over the last few months the Rand has been swinging wildly versus the major currencies. It gained ground in April, but then lost over 10% in May against the US dollar. From this very weak starting point, despite the Brexit vote towards the end of June, the Rand gained over 6% versus the US dollar. It also gained ground against the euro and sterling as the pound fell to a 30-year low against the USD. Despite some gains, when measured on a pure purchasing power parity basis, the Rand continues to be undervalued against a basket of currencies.

After both Fitch and S&P affirmed South Africa's local and foreign currency rating, bonds rallied, giving investors a total return on the ALBI of just over 4% for the month. Most of the performance came from the longer dated bonds as the yield curve shifted downward. From the disastrous December 2015 when yields blew out, bonds have been a wonderful asset class, giving investors a return of 11.2% for the six months. Foreigners bought R16 billion local bonds in the month. A question mark now hangs over the value. The yield on the R186 closed at around 8.8% from a previous 9.4% and at these levels is probably trading at fair value.

With the US monetary policy apparently remaining on the side-lines for now, with interest rates at the low end, investors took this as a cue to pile back into government bonds. The UK Brexit vote also sent investors into bonds, the result of which was yields falling back down to historical lows. The yield on the US ten-year bonds ended May at 1.84%, which appeared low, but flows took this down to 1.46%. At the beginning of July it traded at 1.38% and there are some commentators that are calling it down to 1%. The German ten-year bond traded into negative nominal yields for the first time ever. There is approximately \$12 trillion "invested" into negative yield bonds.

Prepared by CORE Financial Solutions.  
For more information contact : +27 (0) 51 448 8188



## New tax legislation will have a big influence on livestock and game farmers

Sufficient liquidity in an estate provides the key to a quick and efficient estate settlement. However, hidden costs are often the cause of insufficient liquidity in an estate, says Piet Swanepoel, Director of CORE Trusts & Estates.

When someone dies, all liabilities, costs and taxes in his estate have to be paid before the remainder of his assets may be distributed in accordance with his will. Usually people only think of the liabilities in the estate when quickly calculating whether there will be enough funds available in the estate.

The costs in an estate include, amongst others, executor fees, the Master of the High Court's fee, valuation and advertising costs, funeral costs as well as transfer costs relating to property.

Tax payable in an estate include mainly estate duty, capital gains tax and income tax. A lot has been written about estate duty and capital gains tax and therefore this article will not focus on these aspects.

Regarding income tax, a recent article 9HA, that not a lot of people are aware of yet, was added to the Income Tax Act. In short it entails that when someone dies after 1 March 2016 all his assets, including his stock, are deemed sold at market value. For a farmer his livestock and game are his stock.

The above-mentioned stipulation was already applicable to capital assets, including land, and capital gains tax is payable in this regard. Previously, capital gains tax was also payable on the difference between the market value and the standard value of the livestock in an estate. (The standard value of livestock is a very low tax value linked to livestock in terms of the Income Tax Act.) Game has a standard value of nil. From the point of view of capital gains tax the effective maximum tax rate is around 16.4% of the taxable profit (the difference between the base cost and the market value).

The impact of the new article 9HA of the Income Tax Act is that livestock and game will now be liable to income tax instead of capital gains tax. The maximum income tax rate could be as much as 41% of the value of the livestock and game. The increase in cost (in the form of tax) in the estate is around 24.6% of the value of the livestock and game in the estate. Should the value of the livestock and game in your estate be R1 million an amount of as much as R246 000 will be payable in additional income tax in the estate after 1 March 2016.

The above-mentioned problem should not be viewed in isolation. The best solution is to have a specialist conduct proper estate planning. Proper estate planning has several advantages. One of the advantages of estate planning is that the estate can be structured in order to benefit optimally from the structures in the Income Tax Act that provide a tax advantage. This does not only relate to death, but also to save tax during life and to bring about huge savings in terms of estate-related costs.

Proper estate planning include looking in detail at the feasibility of the will, the stipulations of trust deeds and whether these are in accordance with the latest legislation and court judgements, the cash flow in the estate, provision for the care of dependents and succession planning for businesses.

Prepared by CORE Trusts & Estates.  
For more information contact : +27 (0) 51 448 8188



## New B-BBEE Codes: Ask yourself these questions

In the last few months, we've had numerous encounters with worried clients who realised, often too late, that they were not geared for compliance to the New B-BBEE Codes. To avoid finding yourself in a similar position, ask yourself these questions:

### In which category will my business fall?

Categorisation in terms of B-BBEE is based mainly on two factors:

- 1) The annual total revenue, and
- 2) The percentage of black ownership of the business.

The table below illustrates the three categories, as determined by the annual total revenue of the business, as well as the applicable compliance framework based on the percentage of black ownership of the business:

Total annual revenue	Category based on annual total revenue	Compliance framework based on % Black ownership		
		< 51% BO	> 51% BO	100% BO
< R 10m	Exempted Micro Enterprise	Sworn affidavit - level 4	Sworn affidavit - level 2	Sworn affidavit - level 1
R 10m - R 50 m	Qualifying Small Enterprise	B-BBEE verification certificate based on QSE scorecard	Sworn affidavit - level 2	Sworn affidavit - level 1
> R 50m	Generic Enterprise	B-BBEE verification certificate based on Generic scorecard	B-BBEE verification certificate based on Generic scorecard	B-BBEE verification certificate based on Generic scorecard

*\*\* Sector Codes may use different revenue thresholds*

According to the table above, you can determine if your business has to comply with the criteria of the scorecards. If not (for an EME or a >51% black-owned QSE), you can give a sigh of relief knowing that your business' B-BBEE compliance may be substantiated by merely completing a sworn affidavit, using the prescribed template issued by the Dti.

If your business is not exempt, you need to gain some understanding of the applicable scorecard indicators and targets. First you'll have to make sure that your business will be recognised as an Empowering Supplier.

### Will my business be recognised as an Empowering Supplier?

One of the new requirements in the New Codes is known as the "Empowering Supplier requirement". This requirement serves as a pre-requisite for B-BBEE compliance.

The first set of requirements determines that the business must be:

- 1) a B-BBEE compliant entity (thus level 1 – 8 contributor);
- 2) that is a good citizen South African entity; and
- 3) that complies with all regulatory requirements of the country.

Secondly, QSEs must adhere to at least one of the requirements below and in terms of Generics to at least three:

1)	25% of cost of sales (Excl. labour cost & depreciation) must be procured from South African producers or suppliers
2)	50% of new jobs created must be filled by Black people (and the number of Black employees since the prior measurement year, must be maintained)
3)	At least 25% transformation and / or beneficiation of raw materials must take place in South Africa (Incl. manufacturing, production, assembly and packaging)
4)	At least 12 days (within the measurement year) must be spent on skills transfer to Black owned EME's or QSE's to increase their operational or financial capacity
5)	At least 85% of labour costs should be paid to South African employees (only applicable to service industry entities)

Your B-BBEE certificate will be of no value to your clients if your business is not recognised as an Empowering Supplier, because of the fact that Preferential Procurement Points may only be earned on the scorecard for procurement from Empowering Suppliers.

Will my business meet the sub-minimum requirements in the priority elements?

In the New Codes priority elements have been introduced. Non-compliance with the sub-minimum requirements for the priority elements will result in a discount of one level on the B-BBEE scorecard result of your business.

Summarised in the table below is the sub-minimum requirements for each of the priority elements:

Category	Ownership	Skills Development	Enterprise & Supplier Development
QSEs:	40% of Net Value points 3.2 / 8 points ** Compulsory	40% of total weighting points (excl. bonus points) 10 / 25 points	40% of each of the 3 categories: Pref. Procurement: 8 / 20 points & Supplier Dev: 2 / 5 points & Enterprise Dev: 2 / 5 points
Generics:	40% of Net Value points 3.2 / 8 points	40% of total weighting points (excl. bonus points) 8 / 20 points	40% of each of the 3 categories: Pref. Procurement: 10 / 25 points & Supplier Dev: 4 / 10 points & Enterprise Dev: 2 / 5 points

**Will my business earn sufficient points on the scorecard to be compliant?**

It is important to note that, in addition to higher targets and more onerous requirements, the points to recognition level table in the New Codes has also been amended. Where previously an enterprise had to earn more than 30 points on the scorecard to qualify as a Level 8 contributor, an enterprise needs to earn more than 40 points on the New Codes scorecard to achieve the lowest level of compliance (Level 8). In order to achieve a Level 4 rating, an enterprise will now need to earn more than 80 points on the New Codes scorecard.

To that extent, if your business is going to achieve less than 40 points on the New Codes scorecard, you might want to reconsider entering into a verification process. If you can afford to be without a B-BBEE certificate for a while, your efforts may be better spent engaging the services of a B-BBEE consultant and improving your compliance in some areas before engaging in a verification process.

Do keep in mind, however, that most of the scorecard elements are measured based on compliance during your last financial year (thus retrospectively).

In order to avoid being caught off-guard or without sufficient time to make the required changes, contact the CORE BEE team. We have positioned ourselves to be able to offer either a consulting and advisory service or a verification service to our clients. For any B-BBEE-related assistance, please contact the CORE BEE team.

Prepared by CORE BEE  
For more information contact : +27 (0) 51 448 8188



the future - **now**



the **CORE**  
group

  
[www.thecoregroup.co.za](http://www.thecoregroup.co.za)