23 November 2018

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RE: ANNEXURE C PROPOSALS FOR BUDGET 2019: TAX ADMINISTRATION

We have attached the Annexure C Proposals on behalf of the SAIT Tax Administration Technical Work Group. Tax Administration in South Africa has reached a critical point. The public fully understands the need for SARS to have the power to enforce, but there is a point where taxpayer fairness can no longer be ignored. Setting aside the various political events, there is a widespread perception that the Tax Administration Act is often unfair to taxpayers, especially smaller business and others without sufficient resources to properly defend themselves.

The Work Group has previously made various submissions in relation to problems with the Tax Administration Act, and the Work Group is of the view that these submissions have largely fallen on deaf ears. In this year's submissions, the Work Group reiterates submissions made previously, as well as identifying other areas within the Tax Administration Act that comprise obstacles in creating a tax culture of trust and compliance.

Yours sincerely,

Keith Engel
(on behalf of the Tax Administration Work Group)

Enclosures: Annexure C Proposals
SAIT representatives to be invited to National Treasury workshops

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ANNEXURE C SUBMISSIONS FOR 2019 BUDGET: TAX ADMINISTRATION

South African Institute of Tax Professionals

ANNEXURE C SUBMISSIONS FOR 2019 BUDGET – TAX ADMINISTRATION

1. KEEPING THE TAXPAYER INFORMED – LEGISLATION INADEQUATE TO COMPLY WITH ADMINISTRATIVE JUSTICE PROVISIONS

1.1 Problem

1.1.1 Section 42 of the Tax Administration Act 28 of 2011 (the "**TAA**") intends to keep a taxpayer informed when under audit. This includes the requirement to give the taxpayer a "letter of findings" and an opportunity to respond, before issuing an assessment.

1.1.2 The problem that has arisen in practice is that SARS has adopted the view that these provisions only apply to a "formal audit", and not to a "verification", an adjustment that SARS wishes to make as a result of a request for relevant material (this difference of operations is often not understood by taxpayers).

1.1.3 This approach by SARS undermines the intent of section 42 of the TAA, since SARS would then be able to avoid its obligations to keep a taxpayer informed, merely by changing the "label" of the relevant interaction with the taxpayer, again as taxpayers are often not aware of the distinction between verifications and audits.

1.1.4 It is important to note that section 42 was inserted into the TAA in order to comply with administrative justice provisions, and that the narrow application of section 42 arguably results in a breach of administrative justice requirements. In this respect, section 3 of the Promotion of Administrative Justice Act ("**PAJA**") applies to the decision to issue an additional assessment, because SARS is an administrative body, and because the issue of an additional assessment adversely affects the rights of a taxpayer. Section 3 of PAJA requires that an administrator (in this case SARS) must give the taxpayer adequate notice of *inter alia* the nature and purpose of the proposed administrative action (the issue of the additional assessment) and a reasonable opportunity to make representations.

1.1.5 In contrast to these administrative justice provisions, SARS is simply issuing additional assessments in "verification" matters. These would typically be the vast majority of interactions with individual taxpayers (personal tax "verifications"), and VAT refund "verifications". The problem with breach of taxpayer rights is accordingly widespread. This causes tremendous

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animosity, because taxpayers often do not understand the reasons for SARS' decision, which decisions are then made without "hearing the taxpayer's side of the story". The dispute process after assessment is far more expensive for taxpayers, with this expense having been caused by SARS' unlawful actions.

1.2 Recommendation

1.2.1 In order to preserve within the TAA the rights that are afforded in terms of administrative justice provisions, it is recommended that section 42 of the TAA should be amended such that it is compulsory for this section to be complied with, in relation not only to any "audits", but also any: <u>verifications,</u> or any other process the result of which is a potential assessment being raised.

1.2.2 In other words, the taxpayer should be entitled to receive a letter of findings setting out the potential adjustments of a material nature, and 21 business days within which to respond, before any additional assessment is issued by SARS, regardless of the form of the interactions between SARS and the taxpayer prior to this intended assessment.

1.2.3 SARS' rights in the case of jeopardy situations would remain unaffected by this change. Accordingly, the change would not prejudice the fiscus, but would promote compliance with administrative justice laws, as well as improving the relationship between SARS and taxpayers.

2. DISPARITY BETWEEN TAXPAYERS' RIGHTS AND SARS' RIGHTS TO CORRECT ASSESSMENTS

2.1 Introduction

2.1.1 There is extreme disparity between SARS' entitlements to correct assessments (usually at least three years for income tax and five years for self-assessed taxes such as VAT), and a taxpayer's entitlements to have its assessments corrected, for example in the case of overpayment of taxes (or payment of tax in the incorrect period).

2.1.2 This issue is approached, in the detailed submissions below, in relation to the objection and appeal system, and the request for reduced assessment (section 93 of the TAA).

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2.2 *Objection and appeal*

2.2.1 Problem:

2.2.1.1 The taxpayer currently has only 30 business days in which to object to an assessment (to be extended to 60 days). A senior SARS official may under section 104(5) of the TAA extend the period by another 30 business days if reasonable grounds exist for the delay in lodging the objection. Beyond this limited period, the time for objection may be extended by up to three years but only if "exceptional circumstances" exist which gave rise to the delay. Naturally, "exceptional circumstances" would not exist in the vast majority of cases.

2.2.1.2 The policy question arises as to why the circumstances have to be "exceptional" for a taxpayer to "get their tax bill fixed" that is not to the detriment of SARS. In other words, why should taxpayers be compelled to overpay their taxes, simply because the relevant error was not found within 60 business days?

2.2.1.3 It is important to be aware of the fact that errors in a previous tax filing would typically only be identified during the course of a subsequent audit or tax filing. Typically, then, for income tax, any problematic prior submission would be identified at the earliest approximately one year later, during completion of the subsequent income tax return.

2.2.1.4 A similar issue arises when a taxpayer realizes that tax was paid in the incorrect tax period. In most instances, the taxpayer then owes the tax in the "correct" period, but is unable to obtain a refund in the period in which the tax was overpaid.

2.2.1.5 It appears unfair and unreasonable that SARS is still able to audit and assess a taxpayer as long as three or more years after the tax return submission, to correct underpayments of taxes, but that a taxpayer is not able to correct overpayments of taxes identified, even during the very next tax return filing process.

2.2.1.6 The objection process and timelines are therefore insufficient to address the real practical issues that taxpayers experience. Taxpayers easily experience the legislation, and SARS, as being there to "catch them out", or "make them overpay on a technicality". This type of disparity discourages tax compliance.

2.2.2 Recommendation:

2.2.2.1 The period within which an objection must be lodged should be extended, so that the period within which SARS can fix an incorrect assessment, and within which the taxpayer can fix an incorrect assessment so as not to be forced into overpayment, is more balanced and equal.

2.3 Reduced assessments under section 93 of the TAA

2.3.1 Problem:

2.3.1.1 Section 93 of the TAA was amended by the Tax Administration Laws Amendment Act, 2015, to provide that SARS may only issue a reduced assessment if SARS is satisfied that there is a (currently undefined) “readily apparent” undisputed error in the assessment.

2.3.1.2 In practice, it appears that taxpayers are severely negatively impacted by this amendment. What is “readily apparent” to one person may not be so to another. There is also no consistency from SARS in dealing with requests for reduced assessment and it would seem that SARS appears to interpret the words “readily apparent” to mean “effortlessly obvious” (which it is submitted is not the legal test).

2.3.1.3 The previous wording of the TAA stated that SARS may issue a reduced assessment if satisfied that an assessment contains an undisputed error by SARS or the taxpayer. The reduced assessment could be made within five years of the date of the original assessment in the case of VAT, which is a self-assessment tax, and within three years of the date of the original assessment in the case of income tax.

2.3.1.4 Since then, SARS and National Treasury accepted that the three-year period would be retained and that SARS would attempt to mitigate the risks presented by older requests for correction through its risk management systems. The insertion of the phrase “readily apparent” in addition to the requirement that the error be “undisputed” was purportedly to ensure that “substantive issues are properly challenged through the objection and appeal system”.

2.3.1.5 The SARS: Dispute Resolution Guide – Issue 1 (2014) is also by no means helpful as it effectively states that the taxpayer can apply for Section 93 reduced assessment, where typically two scenarios are present:

2.3.1.5.1 Mistake by taxpayer – here an example is given of a taxpayer forgetting to claim a retirement fund contribution in his tax return, and SARS suggests that the taxpayer makes use of the Request for Correction ("**RFC**") process; or

2.3.1.5.2 Mistake by SARS – here an example is given of a processing error of the double inclusion of an amount of income by SARS, which could be fixed by SARS voluntarily if SARS discovers this, alternatively that the taxpayer can follow the RFC process.

2.3.1.6 In other words, the SARS Guide indicates that taxpayers can request a reduced assessment where they have made an error, however no guidance is given concerning the "readily apparent" requirement.

2.3.1.7 The interpretation of section 93 has become much more complicated with the inclusion of the wording "readily apparent undisputed error" which now causes much confusion to taxpayers as well as SARS officials (as one internal governance committee does not necessarily regard "readily apparent" in a similar manner as another committee in a different region), which naturally causes discrimination between taxpayers.

2.3.2 <u>Recommendation:</u>

2.3.2.1 Section 93 of the TAA should be amended to afford greater clarity/guidance to taxpayers and SARS, to ensure proper utilisation of the section, as well as to ensure that the intention of the legislature is effectively practiced, as follows:

2.3.2.1.1 "readily apparent" should either be replaced or properly defined in the TAA; or

2.3.2.1.2 "readily apparent" should be deleted from section 93 of the TAA.

3. UNFAIR AND EXCESSIVE PERCENTAGE BASED PENALTIES

3.1 Introduction

3.1.1 Research conducted in various jurisdictions has confirmed that while higher penalties can increase taxpayers' compliance, imposing harsh penalties is only effective up to a certain point, whereafter increasing penalties actually triggers disengagement and resistance to the tax system.[1] Extreme or unfair penalties may backfire by creating a setting in which avoidance, evasion, bribery, and corruption, are more prevalent and the end result may be lower tax compliance and a general loss of trust in public institutions.[2] The majority of taxpayers rate fairness as one of the most important facets of the tax system,[3] and a high perception of fairness amongst taxpayers typically predicts increased levels of tax compliance, and vice versa.[4]

3.1.2 Section 209 of the TAA, which sets out the purpose of Chapter 15, the chapter dealing with administrative non-compliance penalties, states that the purpose is to ensure "*that an 'administrative non-compliance penalty' is imposed impartially, consistently, and proportionately to the seriousness and duration of the non-compliance.*" However, the percentage-based penalties that fall within this chapter, are standard percentages of the amount of tax payable in the relevant period, with no regard to "seriousness" or duration of non-compliance.

3.1.3 The imposition of a single percentage-based penalty regardless of the nature and/or seriousness of the prejudice occasioned by the behaviour also fails to take into account of mitigating circumstances which might apply.

3.1.4 For example, a common error for payment of VAT or PAYE is where the "normal" due date for payment falls over a weekend or on a public holiday, or where the employee responsible for payment falls ill and is absent from work. In these types of instances, the payment of the relevant tax one or two business days late, is a default of very short duration, and of low "seriousness". In this respect, the commercial benefit would be negligible or non-existent, and the taxpayer clearly does not intend to benefit from their conduct. However, the amount of the tax due in the relevant period could be very substantial, so that a 10% late payment penalty is harsh and

[1] Larissa-Margareta Bătrâncea, Ramona-Anca Nichita and Ioan Bătrâncea "Understanding the Determinants of Tax Compliance Behaviour as a prerequisite for increasing public levies"; The USV Annals of Economics and Public Administration Volume 12, Issue 1(15), 2012 201 at page 205 – 207; Ronald G. Cummings, Jorge Martinez-Vazquez, Michael McKee, Benno Torgler "Effects of Tax Morale on Tax Compliance: Experimental and Survey Evidence" Berkeley Program in Law and Economics, Working Paper Series at page 2 (Available at https://escholarship.org/uc/item/8sh2w9fp

[2] Supra note 1.

[3] Edward E. Marandu, Christian Mbekomize and Alex Ifezue "Determinants of Tax Compliance: A Review of Factors and Conceptualizations" Paper presented at the Proceedings of the First Middle East Conference on Global Business, Economics, Finance and Banking (ME14 DUBAI Conference) Dubai, 10-12 October 2014 ISBN: 978-1-941505-16-8 Paper ID_D4110 at page 12.

[4] Larissa-Margareta Bătrâncea, Ramona-Anca Nichita and Ioan Bătrâncea "Understanding the Determinants of Tax Compliance Behaviour as a prerequisite for increasing public levies" The USV Annals of Economics and Public Administration Volume 12, Issue 1(15), 2012 201; Edward E. Marandu, Christian Mbekomize and Alex Ifezue "Determinants of Tax Compliance: A Review of Factors and Conceptualizations" Paper presented at the Proceedings of the First Middle East Conference on Global Business, Economics, Finance and Banking (ME14 DUBAI Conference) Dubai, 10-12 October 2014 ISBN: 978-1-941505-16-8 Paper ID_D4110 at page 12; L M Tan "Taxpayers Perceptions of the Fairness of the Tax System – A Preliminary Study" (1998) 4 New Zealand Journal of Taxation Law and Policy 59 at page 60; Ken Devos "An Investigation Into Australian Personal Tax Evaders – Their Attitudes towards Compliance and the Penalties for Non-Compliance" Revenue Law Journal 2009 Vol 19 Issue 1 Article 2 at pages 7 and 35; G Richardson "The Impact of Tax Fairness Dimensions on Tax Compliance Behaviour in an Asian Jurisdiction: the Case of Hong Kong" (Winter) (2006) International Tax Journal at page 29;

disproportionate. It should be mentioned that prior to the promulgation of the TAA, SARS was much more amenable to consider remissions of penalty based on the particular circumstances of the matter.

3.1.5 The penalty remittance provisions in Chapter 15 of the TAA are extremely restrictive. In relation to percentage based penalties, there is essentially only a "first instance" (within a 36 month period, across all tax types) remittance, and remittance for "exceptional circumstances".

3.1.6 Taxpayers who are largely compliant, experience percentage based penalties as excessive and unfair. This drives down tax compliance.

3.2 First incidence remittance: ADR or other settlements should not comprise non-compliance

3.2.1 Problem:

3.2.1.1 The "first incidence" remittance criteria apply to a "first incidence", being an incidence of non-compliance where no penalty assessment has been issued during the preceding 36 months.

3.2.1.2 A problem arises in practice, where SARS and the taxpayer enter into a settlement, either during ADR or in terms of the statutory settlement provisions. In this instance, the matter is typically very complex, with sufficient levels of uncertainty that the parties decide to agree on a commercial resolution, ordinarily with neither party accepting the other party's interpretation. However, the actual assessments issued by SARS may or may not still reflect a penalty. In this type of situation, it does not appear fair and reasonable to treat the relevant matter as "non-compliance", where the taxpayer did not concede on the merits, and where the matter was complex.

3.2.2 Recommendation:

3.2.2.1 The definition of "first incidence" in section 208 of the TAA should be amended, to include wording along the following lines: "*and for the purposes of this definition a 'penalty assessment' that was subject to a subsequent settlement in terms of the Alternative Dispute Resolution provisions or Part of this Act, must be disregarded".* It should be considered that in years prior to the promulgation of the TAA that the criteria of "reasonable circumstances" were considered as test.

3.3 Bona fide inadvertent error remittance required

3.3.1 Problem:

3.3.1.1 As set out above, percentage based penalties are not proportionate to the seriousness or duration of non-compliance, which is the purpose of the relevant Chapter, and are perceived by taxpayers to be excessive and unfair.

3.3.1.2 The SARS Guide to Understatement Penalties (Issue 2) states, in relation to "understatement penalties": "*A taxpayer who acts in good faith, without the intention to deceive, will escape a penalty, not because the trigger is necessarily a bona fide inadvertent error, but because the regime is designed not to punish such behaviour.*"[5] (own emphasis)

3.3.1.3 There does not appear to be any reason why similar principles should not apply to percentage-based penalties.

3.3.2 Recommendation:

3.3.2.1 The "*bona fide* inadvertent error" exclusion which exists in respect of understatement penalties, be adapted to apply as a remittance criterion for percentage-based penalties. Alternatively, a similar remittance provision, based on lack of intention and particular circumstances of a case, should be enacted.

3.4 Nominal non-compliance remittance required

3.4.1 Problem:

3.4.1.1 As set out above, percentage based penalties are not proportionate to the seriousness or duration of non-compliance, which is the purpose of the relevant Chapter, and are perceived by taxpayers to be excessive and unfair.

3.4.1.2 In respect of fixed amount penalties, section 217 of the TAA provides for potential remittance for "nominal" non-compliance, being the duration of the non-compliance is less than five business days.

3.4.1.3 There does not appear to be any reason why similar principles should not apply to percentage-based penalties.

[5] SARS Guide to Understatement Penalties (Issue 2) at page 16.

3.4.2 Recommendation:

3.4.2.1 Section 217 of the TAA should be amended, to provide for full remittance of percentage based penalties where the duration of non-compliance is less than five business days. This would address the scenarios discussed above, where errors as a result of public holidays or brief illness give rise to late payment, remedied within a very short timeframe.

3.5 Remittance based on seriousness

3.5.1 Problem:

3.5.1.1 As set out above, percentage based penalties are not proportionate to the seriousness or duration of non-compliance, which is the purpose of the relevant Chapter, and are perceived by taxpayers to be excessive and unfair.

3.5.2 Recommendation:

3.5.2.1 National Treasury should introduce further remittance criteria, based on "seriousness", as referred to in section 209 of the TAA, including with regard to the potential prejudice or loss suffered by SARS and the fiscus. For example, a taxpayer paying his VAT "late", because he has received incorrect advice that indicates that he is entitled to an input tax deduction, is quite clearly of lesser "seriousness" than a taxpayer who decides not to submit any VAT returns or make any payments for many months for no legitimate reason whatsoever.

4. UNFAIR AND EXCESSIVE INTEREST

4.1 VAT interest provisions not aligned to the TAA

4.1.1 Problem:

4.1.1.1 Section 45 of the VAT Act contains various detailed provisions relating to interest on VAT refunds. These provisions are restrictive, and deny the taxpayer interest in various circumstances, whereas similar provisions do not apply in relation to other tax types.

4.1.1.2 There is legislation intended to align the VAT interest provisions to the TAA, however these have not yet come into effect.

4.1.2 Recommendation

4.1.2.1 Section 45 of the VAT Act should be amended to be aligned to the TAA.

4.2 Additional interest remittance provisions should be inserted

4.2.1 Problem:

4.2.1.1 As set out above, higher penalties can trigger disengagement and resistance to the tax system, and perceived unfairness likewise drives down tax compliance.

4.2.1.2 There are certain areas in which interest imposition is considered by taxpayers to be unfair and excessive. This is primarily where the interest imposed is substantially higher than the actual loss to SARS or the fiscus. Typical examples of this would include: where VAT was not correctly accounted for between two group companies (so one company underpaid, while the other overpaid or underclaimed, so that the fiscus is neutral); or where customs VAT was underpaid, however this was immediately recoverable as input tax and so the net loss to the fiscus would only have been for a few days.

4.2.2 Recommendation:

4.2.2.1 An interest remittance provision should be inserted into the TAA, to apply to all relevant tax types, in terms of which SARS is authorised to remit, in whole or in part, interest imposed, to the extent that, having regard to both output tax and input tax, the failure to make payment of tax within the relevant period did not result in financial loss to the fiscus.

5. PROBLEMS WITH THE UNDERSTATEMENT PENALTY REGIME: *BONA FIDE* INADVERTENT ERROR

5.1 Problem:

5.1.1 In relation to the imposition of understatement penalties, section 222 of the TAA contains an exclusion for an understatement that results from a "*bona fide inadvertent error*", which was introduced in the 2013 legislative cycle. This term is not defined in the legislation.

5.1.2 The Draft Memorandum on the Objects of the Tax Administration Laws Amendment Bill, 2013 contained explanations of what was intended with this exclusion. However, the final version of the Memorandum on the Objects of the Tax Administration Laws Amendment Bill, 2013 did not contain these explanations, and stated: *"Due to the broad range of possible errors, the proposal to define the term "bona fide inadvertent error" has the potential to inadvertently exclude deserving cases and include undeserving cases. SARS will, however, develop guidance in this regard for the use of taxpayers and SARS officials."*

5.1.3 SARS finally issued a guide in 2018. However, this guide is highly problematic, in that it contradicts existing case law precedent, as well as contradicting both versions of the 2013 Memorandum, concluding that only an extremely narrow category of errors could qualify for this exclusion: *"From the foregoing, it seems likely that the only errors that may fall within the bona fide inadvertent class are typographical mistakes – but only properly involuntary ones…",* after which SARS indicates that if there is any level of moral blameworthiness from "reasonable care not taken" upwards, this is not involuntary.[6] If this were indeed the intention of the legislation, and of the Finance Minister when announcing the *bona fide* inadvertent error exclusion, it would have been easy to simply specify that the *bona fide* inadvertent error exclusion only applies to penalties for "substantial understatement" that are as a result of accidental typographical mistakes. In the circumstances, SARS' guide is creating uncertainty and disputes.

5.2 Recommendation:

5.2.1 Legislative amendment is necessary, to provide clarity on the meaning of "*bona fide inadvertent error"*, and the intended scope of the exclusion from understatement penalties.

6. PROBLEMS WITH VOLUNTARY DISCLOSURE PROGRAMME (VDP) TAX PROVISIONS

6.1 Introduction

6.1.1 The VDP is set out in Part B of Chapter 16 of the TAA. The VDP serves an important policy objective, which is to bring more taxpayers, assets and income into the South African tax net. The VDP allows taxpayers to voluntarily regularise their tax affairs in relation to past non-compliance. It is important to note that the VDP is not a tax amnesty, in that there is no relief from the actual

[6] SARS Guide to Understatement Penalties (Issue 2), at page 17

underlying taxes. There is also no relief from interest payable on the relevant taxes. The only relief is in relation to certain penalties that could potentially otherwise apply.

6.1.2 In relation to VDP, the extra tax collections "walk through the door" to SARS, without any audit effort expended by SARS to identify past problems. However, there are various technical issues with the VDP tax provisions. This is highly problematic within the current context, since uncertainty or perceived inequity in relation to VDP has the result that taxpayers are disinclined to apply for VDP. Given these risks, taxpayers frequently rather adopt a "find me first" approach.

6.1.3 We note that VDP was discussed during the annexure C workshops held in 2017, at which time SARS arranged a subsequent meeting in January 2018 to discuss these issues. Whereas SARS expressed the view that the vast majority of taxpayer concerns could be resolved by means of an operational guide / standard operating procedure document, there has been no resolution of this matter to date.

6.2 Period of disclosure for VDP

6.2.1 Problem:

6.2.1.1 There is currently no limitation of period in relation to a disclosure in terms of the VDP.

6.2.1.2 In contrast, section 29 of the TAA requires that a taxpayer should ordinarily retain tax related records for a period of five years from the date of submission of the relevant tax return (or five years from the date of the end of the relevant tax period, where no return was required to be submitted). This period is extended in terms of section 32 of the TAA, where there is an audit, investigation, objection or appeal. Whereas the burden of proof in tax matters is ordinarily on taxpayers, the taxpayer is not obliged to retain documents past the record retention period, and accordingly ordinarily SARS cannot assess a taxpayer to tax in relation to these earlier periods (where tax records may have supported the taxpayer's tax submissions, but the taxpayer has lawfully no longer retained these records).

6.2.1.3 As a result of the record retention period, a taxpayer will often not have records relating to periods prior to the record retention period. In practice, in VDP situations, SARS has required that a taxpayer estimate its tax liability for these earlier periods, alternatively SARS has alleged that the failure to declare tax liabilities for earlier periods results in the disclosure not being "full and complete in all material respects" as envisaged in section 227(c) of the TAA. This is problematic in that ordinarily the record retention period would protect a taxpayer from tax liability in relation to these earlier periods, and the taxpayer does not have appropriate records to defend itself.

6.2.1.4 It should be noted that, in the first voluntary disclosure program (that ran from 2010 to 31 October 2011), there was a limitation of five years in relation to the period for disclosure.

6.2.1.5 There are also technical legal issues in relation to VDP extending back to multiple past periods. For example, the normal period of limitation for issuing assessments is 3 years from assessment for income tax matters and five years for VAT matters. For SARS to assess prior to these periods, exceptional circumstances such as fraud, misrepresentation or non-disclosure would need to be present. It would accordingly be the exception rather than the rule for SARS to be able to issue any tax assessments for these earlier periods. In the circumstances, it appears unfair and unreasonable to require taxpayers to disclose and pay taxes in relation to these earlier periods, or face rejection of their VDP application.

6.2.1.6 Given these perceived inequities or risks, taxpayers frequently decide not to make VDP disclosures regarding tax positions arguably incorrectly adopted in earlier periods, and rather simply "fix this going forward". This significantly negatively impacts the uptake of VDP.

6.2.2 <u>Recommendation:</u>

6.2.2.1 The period for disclosure of information and documentation relating to a VDP should be limited to the record retention period in section 29 read with 32 of the TAA.

6.3 VDP must not "result in a refund"

6.3.1 <u>Problem:</u>

6.3.1.1 One of the requirements for valid voluntary disclosure is that the disclosure must "*not result in a refund due by SARS*".

6.3.1.2 A tax position adopted erroneously or other error could affect multiple tax periods. This could potentially result in reductions of tax liability in certain periods, and increases in tax liability for other periods.

6.3.1.3 Because of the periodic nature of tax, it could then be argued that the default results in a refund in relation to a particular tax period, such that the VDP application is rejected (either as a whole, or as regards that period only).

6.3.1.4 In practice, SARS has been known to instruct taxpayers to apply for VDP only in relation to periods where the "default" results in increased tax liabilities, and to submit a request for correction or objection in relation to the periods where the "default" results in reduced tax liabilities.

6.3.1.5 However, as also set out in this submission, there are significant challenges associated with taxpayers attempting to have their tax assessments revised to correct overpaid taxes. There is accordingly a real risk to the taxpayer that they may be obliged to make payment of the underpaid taxes in one period, only to have the claim for overpaid taxes in another period rejected in the other period.

6.3.1.6 For example, assume that a taxpayer has identified an incorrect past tax position which, across five tax periods, results in a net tax liability of R13 million to SARS. The taxpayer would like to remedy this default by means of the VDP. However, amongst the five affected tax periods, there are "refunds" of R20 million and "payments" of R33 million. The taxpayer then faces the real risk that, in attempting to regularise a R13 million error, it may be compelled to pay R33 million (plus interest), with SARS potentially rejecting the corresponding "claim" of R20 million.

6.3.1.7 In these types of situations, taxpayers are strongly disincentivised to make any disclosure whatsoever to SARS, and the more common response is for taxpayers to decide to "let sleeping dogs lie".

6.3.1.8 A similar issue arises, in relation to errors between taxpayers who are related parties, if the group erroneously accounted for tax in the incorrect entity. For example, if one group company failed to charge VAT and issue tax invoices to another group company, there would have been an underpayment of VAT by one company in the group, and an under claim of VAT by another company. Another example would be if certain income was declared in the incorrect taxpayer's tax return, for income tax purposes. Although SARS is not "out of pocket", one taxpayer in the group has a substantial liability, with the other taxpayer not necessarily qualifying to have the corresponding adjustment made to their tax returns.

6.3.2 Recommendation:

6.3.2.1 Where the same issue results in an "understatement" in certain tax periods, and overpaid taxes in other tax periods, SARS should be authorised to accept the VDP application and process all relevant revised assessments so that only the net underpaid taxes are collected by SARS. In this respect, section 227(e) of the TAA should be amended to refer to not resulting in a refund on a net basis across all relevant affected tax periods.

6.3.2.2 Section 93 of the TAA (the section dealing with reduced assessments) should be amended to include "if necessary to give effect to a voluntary disclosure agreement under Part B of Chapter 16". (Although this amendment is arguably not a necessary change given section 232(1) of the TAA, this amendment would provide clarity to taxpayers.)

6.3.2.3 Similarly, where the same issue arises in an "understatement" for one taxpayer, and overpaid taxes (including underclaimed amounts) for a different taxpayer, SARS should be authorised to accept the VDP application, on the basis that both taxpayers' submissions will be corrected in an aligned manner.

6.4 No objection and appeal process for rejections of application for VDP

6.4.1 Problem:

6.4.1.1 The SARS VDP Unit may reject an application for VDP relief if it is of the view that the requirements in sections 226 and 227 of the TAA are not met.

6.4.1.2 Such decisions by the VDP Unit are not currently subject to objection or appeal under Chapter 9. A taxpayer who disagrees with such a decision must take the matter on judicial review. Because of the cost and delay involved in such a process, few taxpayers are willing or able to do so.

6.4.1.3 Many practitioners believe that certain decisions by the VDP Unit incorrectly narrow the qualification criteria for VDP. With the inability to access the normal objection and appeal process in relation to rejections of VDP applications, taxpayers are disinclined to "risk" a VDP application in various circumstances.

6.4.2 Recommendation:

6.4.2.1 Decisions concerning qualification for VDP relief in terms of Part B of Chapter 16 of the TAA should be subject to objection and appeal.

6.4.2.2 It is submitted that this amendment should apply retrospectively, so that applications incorrectly rejected in recent times can be reconsidered.

6.5 "Notice" of an audit

6.5.1 Problem:

6.5.1.1 The SARS VDP Unit must ordinarily reject an application for VDP relief if "*the person seeking relief has been given notice of the commencement of an audit or criminal investigation…"*.

6.5.1.2 Practically, it appears that SARS' interpretation regarding what constitutes "notice" involves an element of subjectivity. As a result, taxpayers are disinclined to "risk" a VDP application in various circumstances.

6.5.2 Recommendation:

6.5.2.1 A potential solution would be for SARS to specifically indicate that the 'notice' (in whichever form it may be), is in fact a 'notice' for purposes of section 226(2) of the TAA, which then creates an objective determination and eliminates uncertainty for taxpayers.

6.6 "Voluntary" nature of VDP application

6.6.1 Problem:

6.6.1.1 One of the requirements for valid voluntary disclosure in terms of section 227 of the TAA is that the disclosure must "*be voluntary"*.

6.6.1.2 The classification of a disclosure as "voluntary" involves substantial subjectivity, which creates uncertainty and reduces the uptake of VDP. Practically, it appears that SARS' interpretation regarding what constitutes "voluntary" disclosure is such that VDP applications are quite broadly rejected. For example, SARS has been known to consider a VDP application as not being voluntary, if the taxpayer has received a request for relevant material in terms of section 46 of the TAA (even where there has been no audit notification, in other words there is no actual audit underway). Similarly, SARS has been known to consider a VDP application as not being voluntary, if it involves a period where a tax return is outstanding or even lately that an IT14SD has been issued and where the taxpayer has already been notified that the relevant tax return is outstanding.

6.6.1.3 As a result, taxpayers are disinclined to "risk" a VDP application in various circumstances.

6.6.2 <u>Recommendation:</u>

6.6.2.1 It is proposed that the requirement that the disclosure be voluntary either be deleted, or defined with reference to the lack of notification of audit, so that the only criterion in this respect is the lack of notification of audit (established as an objective standard as set out above). This creates an objective determination and eliminates uncertainty for taxpayers.

6.7 Potential denial of objection and appeal process for erroneous assessments in relation to VDP

6.7.1 <u>Problem:</u>

6.7.1.1 An assessment issued or determination made to give effect to a voluntary disclosure agreement is not subject to objection and appeal in terms of section 232(2) of the TAA.

6.7.1.2 In practice, clause 7 of SARS standard VDP agreement, reads as follows:

"***7 ASSESSMENT BY THE COMMISSIONER***

7.1 To give effect to this Agreement the Commissioner may issue an assessment or make a determination. Although great care is taken to ensure accuracy, it must be noted that any <u>amount payable</u> given to the Applicant by SARS for purposes of indicating the amount of tax payable <u>is merely an indicative amount</u> and is not an assessment of the Applicant's final liability.

7.2 Despite anything to the contrary which may have been issued by SARS during or after the assessment or determination, the assessment issued or determination made to give effect to this Agreement is not subject to objection or appeal (as per section 232 of the TA Act).
…" (emphasis added)

6.7.1.3 This wording implies that SARS may issue an assessment with a different amount, or potentially contrary to the principles submitted by the taxpayer during the VDP application, and the taxpayer may not object/appeal.

6.7.1.4 The actual legislation only prevents an objection and appeal process for assessments issued to give effect to the VDP agreement (and arguably not assessments that differ from the VDP agreement, since these would not give effect to the VDP agreement). However, the inclusion of the standard wording above in a VDP agreement would appear to either waive the taxpayer's rights, or create the situation where any assessment whatsoever could be said to "give effect" to the VDP agreement, since the VDP agreement purports to give SARS a discretion concerning the amounts to assess.

6.7.1.5 This leaves the taxpayer in the position where it may be left with no rights to object or appeal if SARS issues an assessment different to the submitted VDP information. This creates a situation of risk or uncertainty, and is a barrier to the uptake of the VDP.

6.7.2 Recommendation:

6.7.2.1 The proposal would be that section 232(2) of the TAA either be deleted, or at the very least be amended to allow for a taxpayer to object and appeal where the assessments issued or determination made differs from the substantive legal principles contained in the signed VDP agreement.

SAIT REPRESENTATIVES TO BE INVITED TO NATIONAL TREASURY WORKSHOPS

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