Tax Practice: On the Move – September 2021

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YOUR KEY TO THE TAX COMMUNITY
Introduction

• Discussion of the judgment delivered in Peri Formwork Scaffolding Engineering (Pty) Ltd v Commissioner for SARS (A67/2020).

• The case involves the imposition of percentage-based penalties.

• The case will be analysed with reference to the judgment in the Tax Court and the High Court.
Background

• Why is this case important?
Percentage-based penalties

• Distinguished from administrative non-compliance penalties (fixed amount) and understatement penalties (also percentage-based)

• Imposed by section 213 of the TAA:

213. Imposition of percentage based penalty
(1) If SARS is satisfied that an amount of tax was not paid as and when required under a tax Act, SARS must, in addition to any other ‘penalty’ or interest for which a person may be liable, impose a ‘penalty’ equal to the percentage of the amount of unpaid tax as prescribed in the tax Act.
(2) In the event of a change to the amount of tax in respect of which a ‘penalty’ was imposed under subsection (1), the ‘penalty’ must be adjusted accordingly with effect from the date of the imposition of the ‘penalty’.
Percentage-based penalties (cont.)

• Where an amount is not paid as required by a tax Act SARS must impose a percentage-based penalty.

• Section 213 must be read with the relevant provisions of other tax Acts, for example:
  • Section 35A(9)(b) of the ITA – 10% for late payment of WHT on sale of immovable property;
  • Par 6(1) of the 4th Sch – 10% for late payment of PAYE;
  • Par 14(6) of the 4th Sch – 10% for late payment of provisional tax;
  • Section 39(1) of the VAT Act – 10% for late payment of VAT; and
  • Section 4(1) of the Transfer Duty Act – 10% for late payment of transfer duty.
Remittance of percentage-based penalties

• Section 216 of the TAA:

216. Remittance of penalty for failure to register
If a ‘penalty’ is imposed on a person for a failure to register as and when required under this Act, SARS may remit the ‘penalty’ in whole or in part if—
(a) the failure to register was discovered because the person approached SARS voluntarily; and
(b) the person has filed all returns required under a tax Act.
Remittance of percentage-based penalties (cont.)

• Section 217 of the TAA:

217. Remittance of penalty for nominal or first incidence of non-compliance

(1) If a ‘penalty’ has been imposed in respect of—
   (a) a ‘first incidence’ of non-compliance; or
   (b) an incidence of non-compliance described in section 210 if the duration of the non-compliance is less than five business days,

SARS may, in respect of a ‘penalty’ imposed under section 210 or 212, remit the ‘penalty’, or a portion thereof if appropriate, up to an amount of R2 000 if SARS is satisfied that—
   (i) reasonable grounds for the non-compliance exist; and
   (ii) the non-compliance in issue has been remedied.

(2) In the case of a ‘penalty’ imposed under section 212, the R2 000 limit referred to in subsection (1) is changed to R100 000.
Remittance of percentage-based penalties (cont.)

• Definition of “first incidence”:

‘first incidence’ means an incidence of non-compliance by a person if no ‘penalty assessment’ under this Chapter was issued during the preceding 36 months, whether involving an incidence of non-compliance of the same or a different kind, and for purposes of this definition a ‘penalty assessment’ that was fully remitted under section 218 must be disregarded;

• What is “reasonable grounds”? 
Remittance of percentage-based penalties (cont.)

• Section 217(3):

(3) If a ‘penalty’ has been imposed under section 213, SARS may remit the ‘penalty’ or a portion thereof, if SARS is satisfied that—

(a) the ‘penalty’ has been imposed in respect of a ‘first incidence’ of non-compliance, or involved an amount of less than R2 000;
(b) reasonable grounds for the non-compliance exist; and
(c) the non-compliance in issue has been remedied.
Remittance of percentage-based penalties (cont.)

• Section 218:

218. Remittance of penalty in exceptional circumstances
(1) SARS must, upon receipt of a ‘remittance request’, remit the ‘penalty’ or if applicable a portion thereof, if SARS is satisfied that one or more of the circumstances referred to in subsection (2) rendered the person on whom the ‘penalty’ was imposed incapable of complying with the relevant obligation under the relevant tax Act.

• Section 218(2) limits the circumstances to – a natural or human-made disaster; a civil disturbance or disruption in services; a serious illness or accident; serious emotional or mental distress; serious financial hardship or the following acts committed by SARS – a capturing error, processing delay, provision of incorrect information, delay in providing information or failure to provide sufficient time for an adequate response to a request for information; or any other circumstance of analogous seriousness.
Facts of the case

• The taxpayer submitted its EMP501 on 18 December 2017 (for the period ending 31 December 2017), in terms of which R10,648,340.93 was due.

• The taxpayer submitted the instruction for payment of the tax to be made on 3 January 2018, but the payment could not be released due to insufficient funds in the account.

• Payment was made on Monday 8 January 2018, which was after the ostensible deadline of 6 January 2018.

• The reason advanced by the taxpayer for the delay was that it was waiting for its debtors to make payment and based on historic payments, it projected that the payments would cover its tax liability.

• The payments did not materialise, and the taxpayer had to request a R5 million overdraft from Nedbank to service the debt. The overdraft was approved on 5 January but there was still a shortfall of R138,261.58.
Facts of the case (cont.)

- The taxpayer anticipated that a further payment of R200,000 would be made on 5 January to cover the shortfall but the debtors only paid an amount of R132,338.19, leaving a shortfall of R5,923.39.

- This meant the payment could still not be released on 6 January and the taxpayer missed the ostensible deadline.

- The taxpayer had to request an additional R20,000 from one of its other entities to make up the shortfall for payment on the Monday morning, 8 January 2018.

- SARS imposed a 10% penalty of R1,064,607.69 for the late payment.

- The Tax Court dismissed the taxpayer’s appeal after which it appealed to the Western Cape High Court.
The taxpayer raised a point *in limine* with regard to the computation of time periods, to show that the payment was in fact not late.

The 4th Sch states that an employer must “pay the amount so deducted or withheld to the commissioner within seven days after the end of the month during which the amount was deducted or withheld.”

The taxpayer argued that the time period should be calculated with reference to section 4 of the Interpretation Act where the first day is excluded and the last day is included unless it falls on a Sunday or public holiday.

This would mean that the payment was only due on 8 January and the payment was in fact made timeously.
The TC held that section 244(1) of the TAA clearly intended for the time period in this case not to be extended and payment was due on 5 January.

The HC came to the same conclusion but noted that section 244(1) does not prescribe the computation of time, it deals with when payment must be made if a deadline (calculated in terms of another provision) falls on a weekend or public holiday.

The HC held that the method prescribed under the Interpretation Act only applies if the relevant statute is silent on the method of computation. In this case the ITA is clear that it must be within 7 days, which means 7 January, being the Sunday.

In turn, section 244(1) then prescribes that payment must be made by the Friday, 5 January.
Reasonable grounds

• SARS describes it in IN15 as:

“the requirement of reasonable grounds will generally be met if the delay was caused as a result of circumstances beyond the taxpayer’s control.”

• What it means is the taxpayer’s non-compliance was caused by circumstances not of the taxpayer’s own making.

• What did the taxpayer do to anticipate and mitigate the circumstances in question?

• Distinguished from exceptional grounds which its extraordinary and something that could not be anticipated.
The judgment – reasonable grounds

• The taxpayer in this case argued that it experienced cash flow problems, which it did not anticipate in light of projections made by its bookkeeper. Arguably, the taxpayer took immediate steps to raise funds to meet the deadline.

• In the TC the court opined that the test is reasonable foreseeability or if the cause could have reasonably been avoided. TC held that bad debts are not a reasonable excuse as they are an inherent risk of business. TC also found that the bookkeeper was negligent.

• TC also referred to the now repealed paragraph 16(2C) of the 4th Sch to conclude that the rationale for this provision is that the amount due to SARS constitutes trustee funds and payment of the tax should have been given preference.

• The TC also found that no steps beyond updating the cash flow forecast were taken and it therefore failed to establish reasonable grounds for the late payment.
The judgment – reasonable grounds (cont.)

• The HC found that the bookkeeper’s reliance on payments from third parties was unreasonable.

• However, it found that the taxpayer did have reasonable grounds to have the penalty remitted –
  • First incidence of non-compliance
  • SARS did not consider the immediate steps taken by the taxpayer to rectify the situation
  • The fact that these steps had to be taken over a weekend, which resulted in the delay, constituted the third ground.
SARS heavy-handed in imposing the penalty?

• The legislative framework does not contain a graduated system of penalties depending on the nature of the defence.

• Section 213 states that a penalty must be imposed if SARS is satisfied payment was not made as required.

• Does this mean that SARS should have been satisfied before the penalty was imposed, and if so, what steps should have been taken by SARS in order to be satisfied?

• It is important to note that the penalty is imposed automatically.

• Taxpayer has the opportunity to follow objection and appeal process to dispute the penalty.

• Nevertheless, it could be argued that SARS did not properly consider the taxpayers submissions and unreasonably exercised its discretion.
The judgment – fiduciary relationship

• SARS argued that paragraph 2(1) of the 4th Sch establishes a fiduciary relationship between SARS and the taxpayer as employer.

• SARS argued that this is so because the employer is duty bound to deduct or withhold PAYE and to pay it to SARS within a stipulated period.

• Therefore, the employer owes the highest degree of care in collecting and paying over the tax to SARS.

• Generally, a fiduciary duty means the person is bound to exercise their rights and powers in good faith and for the benefit of another.

• The existence of the relationship depends on the case but it would mean that a person is in a position of trust where they act in the interest of another to the exclusion of their own.
The HC did not refer to the repealed paragraph 16 relied on in the TC.

The HC noted that paragraph 2 of the 4th Sch does create a relationship between SARS and taxpayers but questioned if this could be elevated as suggested by SARS.

SARS relied on the definition of “fiduciary” in a law dictionary as opposed that established by case law.

It is not clear from the HC judgment if this was a new argument raised by SARS or if it is an extension from the TC reasoning relating to a director’s duty to SARS in the repealed provision.

HC referred to the case of Grayston Technology Investment (Pty) Ltd and Another v S [2016] 4 All SA 908 (GJ) to find that the relationship was not akin to that of a fiduciary relationship.
The judgment – should the PAYE be ring-fenced?

- SARS argued that the taxpayer should have insulated to PAYE from the business income and from business risks.

- SARS submitted in the TC that the taxpayer had the onus to prove the PAYE had not been applied for the purposes other than payment of the amount to SARS.

- Can SARS expect the taxpayer to ring-fence the amounts at all times until it is paid over?
Did SARS apply its mind in this case?

• The principle of *audi alteram partem*.

• This principle forms part of our Constitution and is given effect to in PAJA, to ensure procedural fairness.

• It could be argued that SARS did not consider the circumstances properly, or the measures taken by the taxpayer to rectify the situation.
Should the system for percentage-based penalties be reconsidered?

- Ideally, penalties should serve to deter behaviour that abuses the tax system.

- In this case, it was the taxpayer’s first incidence of non-compliance. SARS should not go out of its way to make it difficult for taxpayers who endeavour to be compliant.
Closing comments