DEALING WITH SARS INCOME TAX AUDIT

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The Tax Faculty

Extract from 2021_2022 National Budget Speech delivered by Finance Minister Tito Mboweni

"We owe a lot of people a lot of money. … We must shore up our fiscal position in order to pay back the massive obligations we have incurred over the years."

"SARS has started to deepen its technology, data and machine learning capability. It is also expanding specialised audit and investigative skills in the tax and customs areas to renew its focus on the abuse of transfer pricing, tax base erosion and tax crime.

Course content

Given Government's focus on cash collections aimed at serving the ever-increasing debt burden of the country, one should expect a significant increase in SARS audits and investigations.

The Tax Practitioner and the Tax Executive has an obligation towards our clients and our employers to ensure that these audits can be dealt with effectively and efficiently whilst minimising the risk of revised assessments and by eliminating the risk of understatement penalties charged by SARS.

This course is designed for any person who is responsible for ITR 14 submissions and responding to SARS audits and requests for information. It will also be insightful for any Public Officer or Director responsible for overall Tax Governance of a Taxpayer. The course will consist of the following 4 sections:

Section 1: Since September 2018, 15 Income Tax Cases were heard in the Supreme Court of Appeal (SCA). Of the 15 cases, only 3 were found in favour of the Taxpayer. In Section 1, we will explore certain high-profile SCA and High Court cases and consider whether or not a different approach by the taxpayer in dealing with the SARS Request for information and the SARS audit could have avoided the cases being referred to the court in the first instance. Cases dealing with prepayments, stock valuations and Section 24C will be inter alia be discussed.

Course content (Continued)

Section 2: Under section 2, we will consider how a precautionary and anticipatory approach to ITR 14 preparation can avoid costly disputes with SARS and minimise the risks of understatement penalties. Under this section, we will discuss sound principles of tax risk management and tax governance that, if applied properly, can protect the taxpayer against most understatement penalties.

Section 3: Under section 3, we will deal with practical case studies where a strategy for dealing with SARS audits under different scenarios will be discussed in a practical and understandable manner. Participants will benefit from the practical experience built up over 30 years by the presenter in dealing with SARS audits. This is more than "knowing your rights". This section is about the subjective decisions to be made by the person dealing with SARS audits under a variety of scenarios.

Section 4: Under section 4, we will deal with the future of tax audits with specific reference to increased data analytical capabilities of SARS and reliance on 3rd party data submissions.

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This course complements the course to be presented by Bowmans on 13 May, 9 June and 15 June

- The Bowmans course provides guidance on the legal process to be followed once the taxpayer is in a dispute process.
- The aim of this course is the approach to be followed to avoid any disputes with SARS – i.e. a preventative approach

The Bowmans course content

Session 1: Dealing with Audits and Queries, before assessment

Requests for relevant material:

- What can SARS actually request?
- How does one cope with excessive information requests?
- What about legal privilege?

Unlocking Delayed Refunds

SARS extending prescription because of delayed responses

Dealing with "never-ending" audits

Rejected VDP applications

Unfavourable rulings

The Bowmans course content

Session 2: Dealing with Penalties, and "TAA opinions" to mitigate penalties

Percentage based penalties remittance – provisional tax underestimate penalties

Percentage based penalties remittance – "first incidence"

Percentage based penalties remittance – exceptional circumstances

Understatement penalties

"TAA" opinions to mitigate USP / provisional tax underestimate penalties

Brief segment on unfair customs & excise penalties

The Bowmans course content

Session 3: Dealing with Assessments

Suspension issues (application; section 9 requests)

Request for reasons

Objection

Disputes irt prescription

Invalid objection - process

SARS not complying with deadlines/Rule 56

Appeal

ADR meetings

Settlement

Section 1: Some High Profile Tax Cases

> Given the difficulties experienced by the courts and the incidence of appeals allowed, and then sometimes subsequently reversed, given the incidence of judicial commentary and complaint about the mind boggling complexity of the *Income Tax Act*, one finds it easy to conclude that the legislators do not understand the legislation which they enact.

The Honourable Francis Muldoon
Fibreco Pulp Inc. v. R., [1994] 2 CTC 114 (FC)

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The Purveyor case

The case deals with VAT but is important to gauge the approach of SARS towards a Taxpayer where the Taxpayer makes voluntary disclosures to SARS otherwise than through the formal VDP process

IN THE HIGH COURT OF SOUTH AFRICA

(GAUTENG DIVISION, PRETORIA)

CASE NO: 61689/2019

DELETE WHICHEVER IS NOT APPLICABLE

(1) REPORTABLE: YES/NO
(2) OF INTEREST TO OTHERS JUDGES: YES/NO
(3) REVISED

....

IN THE MATTER BETWEEN:

PURVEYORS SOUTH AFRICA MINE SERVICES (PTY) LTD Applicant

AND

THE COMMISSIONER FOR THE SOUTH AFRICAN

REVENUE SERVICE Respondent

The Purveyor case: The Facts

Purveyors had imported an aircraft into South Africa during 2015 which it then used to transport goods and personnel to other countries in Africa; Purveyors became liable for the payment of Import VAT to SARS in respect of the importation of the aircraft in 2015. Purveyors failed to pay Import Vat to SARS;

Respondent submitted that the **chronology of events demonstrates** that the relevant application did not constitute a “disclosure”, nor was it made voluntary:

- On 30 January 2017 Purveyors requested an appointment with SARS to discuss its liability to pay VAT in respect of the aircraft. In the e-mail, Purveyors explained to SARS the broad nature of the default it had committed.
- On the 1st of February 2017, SARS responded through an e-mail from Mr Duppie Du Preez ("Mr Du Preez") in which he indicated that the aircraft was subject to penalty implications. He also requested to see documentation in terms of Section 101 of the Customs and Excise Act 91 of 1964
- On 2 February 2017 Mr K Thakudi acknowledged receipt and indicated that he would revert as soon as possible with the requested information

The Purveyor case: The Facts

- On the 29th of March 2017 Mr Du Preez wrote to Purveyors in which he explained the reasons why VAT and penalties were payable. Mr Du Preez further indicated that Purveyors needed to appoint a clearing agent to assist it with an Import Permit in order to regularize its continued default;

- Purveyors responded on the same day (29 March 2017) in which it indicated that it understood from Mr Du Preez's e-mail and from their telephone discussion that VAT output and custom duties were applicable as well as fines and penalties;

- Mr Du Preez responded with an e-mail dated 30th March 2017 in which he sought to clear the misunderstanding. He indicated that there existed no waiver of potential penalties and further that if the tax to the Receiver is late the taxpayer would be liable for penalty and interest.

- On the 16th May 2017 Mr Du Preez wrote a further e-mail to Purveyors indicating that it had to address the matter as he had allowed Purveyors sufficient time to regularize its tax affairs. Purveyors responded and indicated that it was still awaiting a response from its Head Office.

- Subsequent thereto, Purveyors took no further steps until the 4th of April 2018 when it applied for voluntary disclosure relief. This was approximately a year after the last letter from Purveyors to SARS.

The Purveyor case: The Facts

It was applicant's contention that the crux of applicant's case was that as at the date of submission of its VDP application it had not been given notice by the respondent of the commencement of an audit or criminal investigation into the affairs of the applicant, which had not been concluded as contemplated by the provisions of s 226(2) of the TAA, and that the effect thereof was that this application was indeed "voluntary" as contemplated in s 227 (a) of the Act, despite the said prior knowledge on the part of the respondent.

The Purveyor case: The Facts

The further question was whether the VDP application was “voluntary”. The term is not defined but its ordinary meaning is “an act in accordance with the exercise of free will”. If there is an element of compulsion underpinning a particular act, it is no longer done voluntary. In the context of Part B of Chapter 16 of the TAA, a disclosure is not made voluntary where an application has been made after the taxpayer had been warned that it would be liable for penalties and interest owing from its mentioned default. It was submitted that the application was brought in fear of being penalised and with a view to avert the consequences referred to.

Lastly, it was contended on behalf of respondent that there had been no disclosure of information of which SARS had been unaware. This was not the case here. When applicant made the VDP application it was obviously aware that SARS knew of its default. It in fact disclosed nothing new the application was therefor not a valid one. There can be no disclosure to a person if the other already has knowledge thereof: certainly not in the present statutory context.

The Purveyor case: Lessons learned

Some questions….

- Why did the Taxpayer not seek formal tax advice from a reputable tax advisor who would have advised them that there is obviously a "default" when VAT was not paid on importation?
- Why did the Taxpayer approach SARS in such an informal manner when the TAA makes provision for a formal process that protects the Taxpayer's rights?
- Why did the Taxpayer take a year after the informal SARS enquiry before making a formal application in terms of the TAA? Why did SARS not initiate a formal audit once they became aware of the default?

It is important that Taxpayer's obtains reputable tax advice when they suspect that a "default" occurred

SARS is NOT a source for technical advice!

Time is of the essence

If Purveyor simply applied the formal VDP process once they became aware of the default and did not approach SARS for "advice" as if SARS is a "Tax Practitioner" the benefits under the VDP programme would CLEARLY have been available and this matter would never have served in front o the court

Note from the presenter…

The VDP process is your friend!

SARS is not your friend!

SARS is not your tax advisor!

Be careful on what basis you communicate with SARS.

> At some point, at some level, someone must look at the trees and see the forest…I am saying that a step back for a balanced look by a CRA official exercising a good dose of commercial common sense should not have resulted in relentless pursuit of a half-million dollar penalty. Yes, the Act stipulates taxpayers are to be penalized for remitting late, but do not bite the hand that feeds you when the hand tries so diligently to ensure you get every mouthful.
>
> The Honorable Campbell J. Miller
> *Home Depot of Canada Inc. v. R.*, 2009 TCC 281

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CASE NO: 24674 :DATE: 25 November 2020

REPUBLIC OF SOUTH AFRICA

IN THE TAX COURT OF SOUTH AFRICA
GAUTENG DIVISION, PRETORIA

CASE NO: 24674
DATE: 25 November 2020

(1) REPORTABLE: YES/**NO**
(2) OF INTEREST TO OTHER JUDGES: YES/**NO**
(3) REVISED.

25 November 2020
Date

SIGNATURE

Before the Honourable Justice P.M. Mabuse
Ms Anna Teichert, Commercial Member
Ms Natasha Singh, Accountant Member

In the matter between:

CBA (PTY) LTD APPELLANT

and

COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE RESPONDENT

Case deals with Understatement penalties charged by SARS when a Section 11(e) catch-up claim was made

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The facts

[1] This is an appeal by CBA (Pty) Ltd ("the taxpayer"), against the decision of the Commissioner for the South African Revenue Service (SARS) to impose under statement penalties ("usp") at the rate of 15% on the grounds of "no reasonable grounds for tax position taken". For purposes of convenience, the taxpayer will be referred to as the appellant.

[5] The taxpayer submitted to SARS an Income Tax Return for audit in 2017. This tax return was submitted in respect of the 2016 tax year. SARS completed the tax type for the said tax period 2016 and, based on the audit findings, made the following adjustment:

Summary and Explanation for the Proposed Adjustment

Tax Period:	2016
Provisions of Income Tax Act (ITA):	Section 11(*e*)
Brief Description of the Adjustment:	Wear and Tear
Adjustment Amount:	R17,564,368.00
Tax Amount:	R4,918,023.00

Appears to be a typo… rate should be 50%

The facts

[6] In the 2016 year of assessment tax return, the taxpayer had claimed "wear and tear" allowance of R54,305,235.00. Included in this allowance was an amount of R17,564,367.99 described by the taxpayer as "wear and tear catch-up" which was due to an error in the 2015 year's calculation of the "wear and tear' allowance. According to SARS the aforegoing description was according to emails sent to Ms Edith Mantloane by Ms LM on 16 April 2017. The taxpayer agreed with the proposed adjustment in its letter dated 30 June 2017 which was the taxpayer's response to SARS's Letter of the Audit Findings.

[8] The Commissioner contends that tax is an annual event and therefore expenses and/or allowance must be claimed in the year during which such expenses or assets are first incurred. The amount of the allowance must be determined on the basis of the period of use listed for the purpose of section 11(*e*) allowance issued by the Commissioner, or a shorter period of use approved by the Commissioner from the date the asset was brought into use. Therefore, the appellant may not in law, claim in the 2016 year of tax assessment, the "catch-up wear and tear" expenses that it was supposed to have claimed or that it incurred in the 2015 tax year of assessment. It was for that reason that the amount of "catch-up wear and tear' allowance of R17,564,368.00 was not allowed.

Appears to be a typo… rate should probably be 25%

The facts

[11] Relying on the law, SARS demonstrated how the understatement penalty was imposed. That was done as follows:

Description:	Tax amount
"Catch-up wear and tear":	R4,418 ,023.04
Applicable behaviour:	No reasonable grounds for tax position taken
Applicable conduct:	Standard
Usp percentage:	50%
USP Amount:	R2,459,011.00

[16] Then the taxpayer indicated that it was objecting against the penalties levied in terms of section 223 of the TAA. The taxpayer states that, because of the adjustment, the taxpayer had an original assessed loss of R37,635,914.00. After the adjustment, the assessed loss to be carried forward was R20,071,546.00. The taxpayer then contends that there had been no loss to the *fiscus* that resulted from the identified error.

USP is payable even though it only affects assessed losses and is timing in nature only

The facts

The appellant agrees with SARS's findings with regards to the over-claiming of the allowances. It contends that the over-claim of wear-and-tear resulted an error in the preparation of the financial and the registers.

Was this the right approach? Would the outcome have been different if SARS was challenged on this point?

NB – This case does not deal with the question whether or not catch-up claims are available. It deals with whether or SARS could levy USP

The Appellants Arguments

[17] The taxpayer objected to the understatement penalty imposed of R2,459,011.00 on the grounds that there is no understatement by the taxpayer in respect of the 2016 year of assessment under this ground of assessment. Under this ground of objection, the taxpayer contended that reading section 222 and section 221 together the understatement cannot be levied unless there is prejudice to SARS or *fiscus*. Harm would be caused to SARS if SARS consented to the erroneous refund and subsequently made payment of that refund to the taxpayer, in other words, to the appellant. In other words, if SARS would be out of pocket in the amount of incorrect sum. There is therefore no loss of the *fiscus*.

The Taxpayer argued that there was no "prejudice" to SARS due to the assessed loss

[18] SARS disallowed the objection and furnished written reasons for the disallowance. SARS pointed out that following the finalisation of an audit, when the catch up wear-and- tear allowance of R17,564,368.00 was disallowed (and the appellant agreed that this wear-and-tear should not have been claimed in the 2016 year of assessment), an understatement penalty of R2,459,011.52 was imposed. The understatement penalty was imposed because it was found that there was no bona fide inadvertent error; that there was an understatement and prejudice to SARS and *fiscus*. The applicable behaviour was determined to be "no reasonable grounds for the tax position taken" and the conduct was determined to be "standard". A penalty was determined at 50% of the tax of R17,564,368.00.

The law: Section 11(e)

11. General deductions allowed in determination of taxable income.—*For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived—*

*(e) save as provided in paragraph 12 (2) of the First Schedule, such sum **as the Commissioner may think just and reasonable** as representing the amount by which the value of any machinery, plant, implements, utensils and articles (other than machinery, plant, implements, utensils and articles in respect of which a deduction may be granted under section 12B, 12C, 12DA, 12E (1), 12U or 37B) owned by the taxpayer or acquired by the taxpayer as purchaser in terms of an agreement contemplated in paragraph (a) of the definition of "instalment credit agreement" in section 1 of the Value-Added Tax Act and used by the taxpayer for the purpose of his or her trade has been diminished by reason of wear and tear or depreciation during the year of assessment*

The law: Section 11(e) – IN 47

4.1.5 Use requirement

The allowance is deductible only to the extent that the qualifying asset is *used* by a taxpayer for purposes of his or her trade. The asset will be written off over its useful life.

(a) Qualifying assets for which write-off periods have been listed in the Annexure

The **Annexure** contains a schedule of write-off periods that are acceptable to the Commissioner for assets that are written off on the straight-line method. These write-off periods are acceptable for assets that are used for purposes of trade, including a trade of leasing, and apply to any asset brought into use on or after 24 March 2020. The assets listed in the **Annexure** are of general application and not intended for specific industries.

Annexure– Schedule of write-off periods acceptable to SARS

Asset	Proposed write-off period (in years)

IN 47 determines the "USEFUL LIFE" of the asset. If a catch-up claim is required in order to be in line with the useful life as determined by SARS, has there been truly non-compliance with SARS practice?

The law

The question is then whether or not whether there was any “understatement” for purposes of the understatement penalty regime. The term “understatement” is defined in section 221 as follows:

‘understatement’ *means any prejudice to SARS or the fiscus as a result of—*

(a) failure to submit a return required under a tax Act or by the Commissioner;

(b) an omission from a return;

(c) an incorrect statement in a return;

(d) if no return is required, the failure to pay the correct amount of ‘tax’;

(e) an ‘impermissible avoidance arrangement’.

The taxpayer clearly does not have the authority to determine the period over which a section 11(e) allowance may be claimed. This is the sole responsibility of SARS.

The ITR 14 therefore merely represent a request by the taxpayer for SARS to exercise their discretion in a particular manner. Nothing precludes SARS under a specific set of circumstances to allow a catch-up claim for section 11(e) claims.

Personal notes from the presenter…

The court case does not deal with 11(e) catch-up claims

The Taxpayer should not have conceded that it was not entitled to a catch-up claim. Given strong substantiation that an asset must be written off over its useful life, SARS may have been convinced to exercise their discretion favourably.

I suspect that the Taxpayer conceded on the disallowance of the catch-up claim since it was in a tax loss situation and the difference is temporary only. I still maintain that there was no prejudice to SARS. The fact that the taxpayer claimed allowances **over the expected life of the asset** but claims **less in the beginning years and more in the latter years** is to the advantage of SARS and not to the prejudice of SARS

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Personal notes from the presenter…

Be careful to concede too easily on the subject matter in dispute – even if it will only create a temporary adjustment

Be careful to make full disclosure in the ITR 14 for any discretionary allowances. This includes section 11(e) and Section 22 stock obsolescence. If the amounts are large, obtain a Binding Private Ruling. If relatively small, disclose separately under “other” with full description.

Personal notes from the presenter…

> Throughout his oral submissions before the Court, Mr. Sailsman kept referring to the fact that he would have expected a much better service on the part of the CRA, like the services financial institutions provide to their clients. These expectations were simply misplaced.
>
> The Honorable René LeBlanc
> *Sailsman v. R.*, 2014 FC 1033

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SARS is not the Taxpayer's friend…. This is an unfortunate reality created by SARS and not by the Taxpayer. One must anticipate a confrontational relationship with SARS. The 50% penalty charged by SARS for an issue where the allowance is subject to SARS discretion, the taxpayer was in an assessed loss, and the amounts will in any event qualify for deductions in future years, seems overly punitive and unfair.

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SARS vs Volkswagen SA

THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

JUDGMENT

Reportable

Case no: 1028/2017

In the matter between:

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **APPELLANT**

and

VOLKSWAGEN SOUTH AFRICA (PTY) LTD **RESPONDENT**

Case deals with the valuation of stock in terms of section 22 of the Income Tax Act

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Relevant Law

22. Amounts to be taken into account in respect of values of trading stocks.—

(1) The amount which shall, in the determination of the taxable income derived by any person during any year of assessment from carrying on any trade (other than farming), be taken into account in respect of the value of any trading stock held and not disposed of by him at the end of such year of assessment, shall be—

*(a) in the case of trading stock … the cost price to such person of such trading stock, less such amount **as the Commissioner may think just and reasonable** as representing the amount by which the value of such trading stock, not being any financial instrument, has been diminished by reason of damage, deterioration, change of fashion, decrease in the market value or for any other reason satisfactory to the Commissioner…* (Emphasis added)

The law requires **a net amount** to be included in taxable income namely:

- The cost of the trading stock.
- Less: an amount *"as the Commissioner may think just and reasonable as representing deterioration of stock value…"*
- It is therefore technically not a "deduction" that is claimed.

What was the case about?

- Volkswagen of South Africa (Pty) Ltd (Volkswagen), the respondent in this appeal, is the South African subsidiary of the well-known German motor manufacturer, Volkswagen AG. At the end of each tax year, Volkswagen holds as trading stock a number of unsold vehicles.
- In its returns for 2008, 2009 and 2010 tax years Volkswagen calculated the value of its trading stock at year end using its 'net realisable value' (NRV) in accordance with the provisions of International Accounting Standard 2 (IAS 2) and the IFRS-Accounting Handbook for the Volkswagen Group. This yielded an amount less than the cost price of the trading stock and it claimed a deduction from the cost price of the trading stock represented by the difference between that and NRV.
- The Commissioner for the South African Revenue Service … conducted a lengthy audit of Volkswagen's tax affairs covering a wide range of issues for the tax years 2008, 2009 and 2010. At the end of it the Commissioner rejected the contention that NRV represented the diminished value of the trading stock at the end of those years. The differences between cost price and NRV for the three years in dispute were respectively R72 002 161, R24 778 855 and R5 294 643.
- The refusal of an allowance in these amounts resulted in the issue of revised assessments levying additional tax for those three years. Volkswagen appealed against those assessments.

What was the case about?

- From a tax perspective, the higher the value attributed to closing stock at the end of a tax year, the lower will be the cost of sales for that year and the greater the taxable income of the taxpayer. Conversely, the lower the value attributed to closing stock, the higher the cost of sales and the lower the taxable income for that year**. If taxpayers had a free hand in determining the value of trading stock at year end it would open the way for them to obtain a timing advantage in regard to the payment of tax, by adjusting the value of closing stock downwards.** They could by adjusting these values manipulate their overall liability for tax in the light of their anticipations in regard to future rates of tax, future trading results, the need to incur significant expenses in the future and the like.
- The dispute in this case is whether the value of Volkswagen's trading stock had diminished entitling the Commissioner to make a just and reasonable allowance under the section. **In practical terms, an allowance permits the taxpayer to reflect the value of its trading stock at less than cost price in its tax return. Volkswagen contended that it should be entitled to do this on the basis of the NRV of its trading stock at each of the three year ends from 2008 to 2010. It said that NRV reflected that the value of the trading stock had diminished.**

This was the wrong argument by VWSA's counsel

What was the case about?

The parties formulated their dispute in a stated case in the following way:

'Whether the NRV of VWSA's trading stock, calculated in accordance with IAS 2 and taking account of the individual categories of costs referred to … above, may and should, where it is lower than the cost price of such trading stock as determined in accordance with section 22(3) of the Act, be accepted as representing the value of trading stock held and not disposed of at the end of the respective years of assessment for purposes of section 22(1)(a) of the Act.'

- The Special Court found in favour of VWSA. The special court stated that SARS failed to exercise its discretion as required by law.
- Since SARS did not exercise their discretion (they simply denied the total claim), the court can exercise its discretion in its stead.
- In exercising its discretion, the special court believed that IAS 2 is a fair and reasonable method of determining NRV

What was the concerns of the SCA

- The effect of the judgment was that where the valuation of trading stock at NRV at the close of a fiscal year reflected a value lower than cost price, the Commissioner was obliged to make an allowance for the diminution in value of the trading stock in accordance with s 22(1)(*a*) of the Act.
- As will be appreciated, this had potentially far-reaching consequences for the Commissioner extending beyond the present case.
- Under Generally Accepted Accounting Principles in South Africa (GAAP) trading stock at the end of a year must be valued at NRV. If the judgment of the Tax Court was correct then, wherever NRV was less than the cost price of trading stock, the Commissioner would be obliged to permit taxpayers to value trading stock at year end at the lower of cost price or NRV. The question is whether that was consistent with the provisions of s 22(1)(*a*).

I do not necessarily agree with this statement. The Special Court judgement simply stated that SARS failed to exercise their discretion and their failure to do so, forces the Court to do so in its stead

What was the finding of the SCA?

- The taxpayer is required to determine the value of its trading stock at a particular point in time, namely, the end of the tax year.
- As is generally the case in determining the taxpayer's taxable income that is an exercise of looking back at what happened during the tax year in question.
- An important aspect of the language in s 22(1)(*a*) is that the allowance that the Commissioner may think just and reasonable is 'an amount by which the value of the trading stock **has been diminished**'.
- **That language is couched in the past tense.**
- The section is accordingly not concerned with what may happen to the trading stock in the future, but with an enquiry as to whether a diminution in its value has occurred at the end of the tax year.
- All of the instances expressly referred to in the section, namely damage, deterioration, change of fashion and decrease in market value, relate to a diminution of value occurring prior to the taxpayer rendering its return as a result of events occurring prior to that date.

What was the finding of the SCA?

- Counsel for SARS submitted that it necessarily followed that there could only be a diminution of value arising from events that had already occurred before the end of the tax year.
- In other words, the events relied on as demonstrating a diminution in value of the trading stock must have occurred during the tax year, even though their impact might only be felt in the following year. The goods must already have been damaged or have deteriorated in condition.
- In the case of changes of fashion the change must already have been apparent by the end of the tax year.
- In the case of a decrease in market value, something must have occurred, such as the catastrophic decline in the price of wool in *Jacobsohn*'s case, to enable the taxpayer to say that the value of the trading stock was now less than its cost price.

What was the finding of the SCA?

- There is merit in this submission, although it does not entirely remove the element of futurity from the enquiry.
- A determination of the current value of goods that have not yet been sold, but will be sold in the future, necessarily involves a measure of prediction in regard to future events.
- In my view, the correct position is that the Commissioner may only grant a just and reasonable allowance in respect of a diminution in value of trading stock under s 22(1)(*a*), in two circumstances.
  - The first is where some event has occurred in the tax year in question causing the value of the trading stock to diminish.
  - The second is where it is known with reasonable certainty that an event will occur in the following tax year that will cause the value of the trading stock to diminish. An example might be knowledge that a glut had built up in the market for a perishable commodity, where that glut would ensure a marked, certain and unavoidable decline in the price of that commodity in the following year. Both scenarios are consistent with the basic proposition that the assessment of income tax relates to events that have already occurred rather than events that may occur in the future.

What was VWSA's submission?

- Volkswagen contended that there had been a reduction in the value of its trading stock 'for another reason'.
- It did not say that there had been a decrease in market value of its cars.
- Instead it contended that valuing trading stock at year end, in accordance with NRV and IAS 2, properly reflected a diminution in value of that trading stock and accordingly justified the reduction in value for which it contended.
- Whether that was so depends upon a consideration of IAS 2, the concept of NRV and its application to the facts of this case. That must then be measured against the provisions of s 22(1)(*a*) in accordance with the interpretation set out above.

What was VWSA's submission?

IAS 2 is the prescribed accounting treatment for inventories. These are defined to include all assets held for sale in the ordinary course of business. Net realisable value (NRV) is defined as the estimated selling price of inventory in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. It refers to:

'… the net amount that the entity expects to realise from the sale of the inventory in the ordinary course of business. Fair value reflects the amount for which the same inventory could be exchanged between knowledgeable and willing buyers and sellers in the marketplace. The former is an entity-specific value; the latter is not. Net realisable value for inventories may not equal fair value less costs to sell.'

The determination of NRV is firmly based on the entity's assessment of future market conditions. Clause 30 says that estimates of NRV are based on the most reliable evidence available at the time the estimates are made of the amount the inventories will realise.

Significantly, these estimates take into consideration matters such as fluctuations in price or cost relating to **events occurring after the end of the period for which the accounts are being prepared** 'to the extent that such events confirm conditions existing at the end of the period'. This does not mean that those conditions were anticipated or foreseen at the end of the relevant period. It means that if subsequent events make it clear that at the end of the period the inventory was worth less than cost it should be written down to NRV.

Where did it go wrong for VWSA?

Volkswagen's determination of NRV

Volkswagen classified the items forming part of its NRV calculations as 'Distribution and Selling Costs'.

- The distribution costs were its
  - rework/refurbishment costs,
  - outbound logistics,
  - marine insurance and
  - distribution fees.
- The selling costs were sales incentives, warranty costs, costs relating to the Audi Freeway Plan and the Volkswagen AutoMotion Plan and roadside assistance costs.
- Distribution costs were costs that were anticipated to be incurred between Volkswagen's headquarters in Uitenhage and the various dealerships through which its vehicles would be sold.
- Selling costs were costs that would be incurred once the vehicles were sold.

What was the finding of the SCA?

With the sole potential exception of some vehicles forming part of Volkswagen's stock in trade having suffered damage requiring refurbishment during the relevant year, **all of the items used by Volkswagen in its calculation of NRV were concerned with costs that would be incurred in the future in the sale and distribution of vehicles.**

Even the extent of any damage requiring refurbishment was anticipated to be minor.

The schedule attached to the stated case showed that a modest R525 per vehicle was allowed under this head.

There could be no question therefore of the value of trading stock being diminished below cost price as a result of damage to the vehicles constituting such stock.

This was a provision to cover minor scratches and dents.

No claim for refurbishment was made in respect of used vehicles, which is a further indication that this was a minor item.

Some of the deductions in this case appear to have had a disproportionate effect on the calculation of NRV. The illustrative schedule annexed to the stated case referred to eleven Audi vehicles of varying descriptions.

In respect of each one an amount of R29 906 was deducted from the wholesale selling price in respect of the Audi Freeway Plan.

What was the finding of the SCA?

With respect, I think that the learned judge in the Tax Court erred in failing to recognise that s 22(1)(*a*) is not concerned with contrasting cost price with a value determined by 'an appropriate method by which to determine the actual value of trading stock in the hands of the taxpayer at the end of the year of assessment'.

In looking for a sensible and businesslike manner of valuation of trading stock at year end he answered a question other than the one posed by the facts and formulated by the parties in the stated case.

That question was whether NRV should be used to determine the value of trading stock at year end for the purposes of claiming an allowance against cost price under s 22(1)(*a*).

Whether it was a sensible and businesslike manner of valuing trading stock from an accounting perspective was neither here nor there.

The concern was whether it accurately reflected the diminution in value of trading stock contemplated in the section.

Personal notes from the presenter…

It is important to note that the court only deals with the matter in front of it. In this case, the question was very simple, namely – would the application of IAS 2 automatically be in line with the requirements of Section 22. The answer is “no” since IAS 2 is concerned about future events and S22 is concerned about past events.

In so far as the approach on the Freeway Plan and Roadside Assist was concerned, I believe that VWSA approached SARS incorrectly. The argument was that it represents future costs that should be deductible. The True question is to compare “apples” with “apples” The vehicle in stock is an asset WITHOUT A MAINTENANCE PLAN. The sales price of the vehicle is the price WITH A MAINTENANCE PLAN. The question is what is the sales price of a vehicle without a maintenance plan in the open market will be. If this is less than the cost, then a S22 adjustment should be available

Personal notes from the presenter…

In so far as distribution costs are concerned, again the approach was incorrect. The market value for a car is the listed price in Sandton, Cape Town, Pretoria, Polokwane. The vehicle is currently in Uitenhage. The question should be:

"What is the sales price of the car of the customer must collect it in Uitenhage?"

It follows that I agree with the principles explained by the SCA. However, both the Special Court and the SCA did not address the true issue for consideration:

What is the market value of the car:

- In its current state
- In its current location (i.e. Uitenhage)
- Without any service plan or maintenance plan
- In so far as locally manufactured cars are concerned – without a warranty

The Tax Faculty

SARS vs Atlas Copco

THE SUPREME COURT OF APPEAL OF SOUTH AFRICA
JUDGMENT

Reportable

Case no: 834/2018

In the matter between:

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **APPELLANT**

and

ATLAS COPCO SOUTH AFRICA (PTY) LTD **RESPONDENT**

Case deals with the valuation of stock in terms of section 22 of the Income Tax Act

The Tax Faculty

Case is similar to VWSA – but deals with Spare Parts

- The taxpayer, Atlas Copco SA (Pty) Ltd, is a member of the Atlas Copco Group, with its parent company in Sweden.
- The main business of the taxpayer is to sell or lease – and thereafter service – machinery and equipment (including spare parts and consumables) that is imported mainly from Sweden, for use in the mining and related industries in South Africa.
- The taxpayer's parent company had conceived a policy known as the Finance Controlling and Accounting Manual (FAM) or The Way We Do Things (WAY), which was implemented and applied by all companies within the group.
- In terms of the policy, the taxpayer was to write down the value of its closing stock by 50%, if such closing stock had not sold in the preceding 12 months, and by 100% if it had not sold in 24 months.

Case is similar to VWSA – but deals with Spare Parts

- The taxpayer applied the policy by writing down its closing stock by the fixed percentages reflected in the policy.
- It included in its 2008 and 2009 tax returns the amounts it claimed the value of its trading stock had diminished by during those years of assessment.
- SARS, however, took the view that the write down of stock by the taxpayer did not comply with the provisions of s 22(1)*(a)* of the Act. SARS accordingly added back R30 191 000 for 2008 and R33 402 000 for 2009 and assessed the taxpayer to tax in respect of those amounts on the ground that 'there was no diminishing in value at year end for a deduction to be claimed as a result of damage, deterioration, change of fashion, decrease in the market value in respect of stock'.

The finding

- It is difficult to discern the basis on which the taxpayer contended for a diminution of the value of its trading stock.
- That is because its version migrated from an initial reliance on a deemed obsolescence to reliance on a group policy in accordance with IAS2.
- The taxpayer did not suggest that there has been a diminution by reason of ‘damage, deterioration, change of fashion [or] decrease in the market value’.
- It appears to be simply contending that because the items in question had remained on its shelves for a particular length of time, it was entitled to write down those items by fixed percentages by applying IAS2 to determine a new NRV and create provision for obsolescence.

This seems illogical. One can surely not accept SARS or the Court to simply accept, without scientific evidence that an adopted methodology is reasonable!

Surely at some point in time, there should be a scientific rationale, based on history and proper engineering analysis that the methodology is appropriate? Why was this research not placed into evidence?

The finding

In the light of the approach to NRV by this court in *CSARS v* Volkswagen, the evidence of Mr Towlson, who led the taxpayer's external audit team, was by and large irrelevant, because **the audit did little more than apply the taxpayer's group policy** and the NRV in accordance with IAS2.

Mr Chohan: *You don't test and nor were those your instructions, to test whether the stock that had been there for 12 months or 24 months should be written off at a lesser percentage or a higher percentage.*

Ms Towlson: *No, that wasn't part of our audit, that would have been looked at by the Group audit team . . .*

This is a failure of audit procedures. The audit team should have performed some procedures to satisfy themselves that the policy will have the result that IAS 2 is complied with. The local or global audit team should have performed audit procedures that the policy is reasonable

The SA Team should have on file evidence of the procedures performed by the German Audit Team and the RSA team should have ensured that this policy is deemed appropriate under RSA context.

It follows, despite the Tax Court's acceptance of Ms Towlson's evidence, that her evidence did little to advance the taxpayer's case. If anything, Ms Towlson's evidence serves to fortify the view that the taxpayer's employment of a fixed and rigid company policy was arbitrary and did not present the most reliable evidence available at the time in respect of any diminution in value.

The finding

Mr Smit: *Because if we look at, we have about 20000 items actively, any day in time, to go and to try and to do that specific verification item by item, with the relevant pricing confirmations, will be a gigantic and an impossible task to do.*

Mr Chohan: *So, the answer to my question is yes, Atlas did not take into account the price at which it had sold stock during that year? It relied on a method, in terms of which it had applied a 50% write-off, if it fell into a 12 month bucket, and a 100% write-off if it fell in a 24 months bucket?*

Moreover, although fleeting references were made to market value, as the following exchange between counsel for SARS and Mr Smit makes plain, no proper explanation or evidence was proffered, other than reliance on the group policy and the application of NRV.

The finding

It is apparent when the evidence relating to all six categories is considered, that the taxpayer's approach essentially boiled down to this: Because it held thousands of items of stock at year end, it was not feasible for it to individually value each item.

For that reason, it applied its policy with reference to item descriptions. This evidence was accepted by the Tax Court in support of the proposition that the legislature could not have intended that a trader assess each individual item of closing stock in circumstances were they hold thousands of items of trading stock.

But this was misplaced. SARS never contended that the taxpayer had to assess each individual item of stock. On the contrary, as SARS accepted, the practice of sampling in these situations is a well-recognised method of dealing with the challenges of high volume trading stock. But, that is not what the taxpayer did in this instance.

Personal notes from the presenter…

This case does not mean that SARS is not allowed to take into account the ageing of stock when determining the value of the stock that should be taken into account for purposes of S22. (NB – it is SARS that must exercise the discretion and not the taxpayer!!)

- In this case, the taxpayer did not advance any valid reasons why they believed that the value of stock has diminished due to ageing.
- In the absence of any recent scientific evidence, supported by sample testing and "sanity checks" SARS had no choice than to deny the request for reduction in value of stock.

- The case may potentially have had a different outcome if counsel relied less on a blind application of IAS 2 (that was in any event not even properly audited by the external auditors).
- Instead, counsels should have focused on schentific evidence, supported by statements from engineers (not accountants) why ageing is an important factor to determine the value of stock at any given point in time.

SARS vs Telkom

THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

JUDGMENT

Reportable

Case no: 239/19

In the matter between

TELKOM SA SOC LIMITED **APPELLANT**

and

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **RESPONDENT**

Deals with prepayments

The Tax Faculty

The facts

- Telkom made a ‘cash incentive bonus’ payment of R178 788 421 to Velociti in the 2012 year of assessment.
- The Commissioner allowed as a deduction only R42 256 879, by invoking s 23H(1) of the Act. The issue was whether the Commissioner was entitled to apply the section to limit the deduction in the year of accrual, with the result that the balance paid was spread out over a number of tax years.
- Telkom successfully appealed against this decision to the Tax Court and the Commissioner now cross-appeals against that finding and seeks to have the assessment confirmed.
- The facts which are common cause are as follows:

    (a) Telkom paid cash incentive bonuses to dealers on the connection of the initial subscriber contract in respect of a special tariff plan.

    (b) The amount of R178 788 421 related to connections that Velociti made to Telkom Mobile, which Telkom contends were cash incentive bonuses, for every subscription which Velociti made on behalf of Telkom Mobile.

    (c) Of the R178 788 421 claimed as a deduction by Telkom, the Commissioner added back R136 531 542 in terms of s 23H(1)*(b)*(ii) of the Act.

The facts

The Tax Court, in upholding the appeal, made the following findings:

(a) The benefit that was attached to the expenditure was the conclusion of the contract with the customer in question.

(b) Velociti rendered all the services which it was obliged to do in terms of the incentive letters and for which the payment of R178 788 421 was made.

The Commissioner, however, submitted that the key question was when and how the benefit, in respect of which the expenditure was incurred, was enjoyed.

This was because the pleaded dispute turned on, when and how Telkom enjoyed the benefit, received from the cash incentive bonus payment. The Commissioner pleaded that it was the subscription agreement with the client that was the source of the direct benefit to Telkom. The Commissioner also pleaded that the benefit to Telkom, flowed primarily and directly from the service contract, in terms of which the individual customer paid monthly subscription fees. The dealer was a mere facilitator, who brought about the source of the benefits, and the benefits ie the fees, were direct and central to Telkom's business. It was the agreement concluded between Telkom and the respective dealers which was the indirect source of the benefit.

The finding

The Commissioner therefore correctly submitted that the Tax Court erred, in disregarding the true benefit obtained by Telkom, in the form of the monthly subscriber payments over an anticipated 24 month period. Although the conclusion of the contract benefited Telkom, the enjoyment of that benefit was spread out over the period of the contract, so that the period to which the expenditure related could not be limited to the first year. The Commissioner also correctly submitted that the Tax Court erred in treating as relevant to the application of s 23H, the fact that Velociti had rendered all the services which it was obligated to do in terms of the agreement with Telkom, because this had no bearing upon the central question, being when and how Telkom would enjoy the benefit of the contract.

Personal notes from the presenter…

- There was nothing that Telkom could have done otherwise in avoiding this dispute.
- The thinking of Telkom, that was upheld in the Special Court was similar to the views cautiously held by most tax advisors, being a practical and realistic view.

- The case illustrates that the SCA seems to take a much more “legalistic” view of a case which may not always be “practical” or “commercial”.
- The Special Court did not truly consider the extremely wide wording of section 23H that includes “any other benefit”
- I believe that the SCA case is technically correct, but the section is practically flawed.
- Some questions remains open – e.g. the interaction between S11(d) and 23H

SARS vs Clicks Retailers

Deals with Section 24C

THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

JUDGMENT

Reportable
Case No: 58/2019

In the matter between:

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **APPELLANT**

and

CLICKS RETAILERS (PTY) LTD **RESPONDENT**

The Tax Faculty

The facts

- Clicks Retailers (Pty) Ltd, the respondent, owns and operates the well-known Clicks retail business at stores nationwide.
- Some years ago it instituted a Loyalty Programme in terms of which it awards points to members on presentation of a Clicks ClubCard when making purchases.
- The accounting and tax treatment of purchases made using a ClubCard and the benefits accruing to members as a result attracted the attention of the appellant, the Commissioner: South African Revenue Services (the Commissioner or SARS as may be appropriate).
- After conducting an audit the Commissioner disallowed Clicks' claim to an allowance in terms of s 24C(2) of the Income Tax Act 58 of 1962 (the Act).
- An appeal to the Tax Court, Cape Town (Nuku J) succeeded. The appeal by the Commissioner is with his leave.

The facts

- In order to become entitled to points under the loyalty programme a customer must purchase goods and present his or her ClubCard at the checkout point in respect of that transaction.
- Every R5.00 spent earns one loyalty point. In order to qualify for vouchers customers must accumulate at least 100 club card points by a qualification date.
- At the end of each reward cycle, Clicks issues vouchers to all ClubCard members who have earned 100 or more points during the cycle.
- Every 100 points earned by a customer will entitle that customer to a voucher to the value of R10.00 that can be used in payment or part payment for his or her future purchase.
- Vouchers may be redeemed by the customer when he or she makes a subsequent purchase and presents his or her club card and voucher at the checkout point.
- The voucher cannot be redeemed for cash.
- In practice the vouchers will in almost all instances be used in part payment of a basket of goods, so that the customer acquires those goods at a discounted price.

The Dispute

- During the 2009 financial year, Clicks claimed an allowance of R44 275 965 to be deducted from its gross income based on s 24C of the Income Tax Act.
- The allowance was calculated on the basis of the cost of sales to Clicks, in honouring vouchers that Clicks expected members to redeem in the following tax year.
- The Commissioner disallowed the claim to the allowance and Clicks objected to the disallowance.
- On 29 April 2015 it lodged an appeal against the disallowance of its objection against the assessment for the 2009 tax year.
- The Tax Court upheld the appeal and directed the Commissioner to partially allow Clicks' claim in terms of s 24C and revise the allowance.

The Dispute

- In *CSARS v Big G Restaurants (Pty) Ltd* [2018] ZASCA 179, 2019 (3) SA 90 (SCA) this court held that in order to qualify for the allowance the income received and the future expense to be incurred, must arise from the same contract. It said that s 24C had two basic requirements:
  - First, there must be income received or accrued in terms of a contract and
  - Second, the Commissioner must be satisfied that such amount, i.e. the income received from the contract, will be used wholly or partially to finance future expenditure that a taxpayer will incur in performing its obligations under that same contract.

  The section therefore envisages income, future expenditure and a single contract that links the two.

  This court expressly rejected the notion that the section applies where the different contracts are 'inextricably linked.' The legislature did not use the term 'scheme' or 'transaction'. The operative concept was 'contract.'

SARS contention

The Commissioner submitted that the deduction was correctly disallowed, for the following reasons;

(a) The contract of purchase and sale, whereby a customer purchased merchandise at a Clicks store, in terms of which income was received, was separate from the ClubCard contract;

(b) The ClubCard contract itself did not give rise to any income in the hands of Clicks, because it was issued free of charge and there were no hidden charges to members;

(c) The obligation of Clicks to award the member points, based on qualifying sales and to issue vouchers, when the specified number of points had been earned, arose under the ClubCard contract;

(d) Clicks was likely to incur future expenditure, when a member redeemed a voucher and Clicks supplied the member with goods equal to the value of the voucher, at no cost to the member. This obligation would arise under the ClubCard contract, which was a different contract from the contract of purchase and sale, under which the income was received.

The finding – in favour of SARS

There is no doubt that the income-earning contracts in this case are the initial sale contracts. The ClubCard contract is not a source of income and Clicks no longer contends that it is. Yet, as the main judgment says, the initial sale contracts on their own do not result in Clicks incurring any obligation to the customer. Absent a ClubCard contract and the presentation of a ClubCard at the point of sale, the sale agreements are complete when the customer leaves the store having paid for the goods. Clicks has no further obligation to fulfil under the sale contract. If the customer has concluded a ClubCard contract and presents the card at the point of sale, Clicks incurs an obligation under the ClubCard contract to award them points. Even then it does not incur any expenditure, because it is only if the customer accrues 100 points during a qualification period that they get anything at all. If the customer changes allegiance and shops at one of Clicks' competitors, or changes address and now resides in an area not served by Clicks, their accumulated points will not be used and after a year any vouchers issued will lapse.

The finding – in favour of SARS

It is appropriate at this point to say something about the concept of expenditure in relation to Clicks' claim to the allowance.

- The 'expenditure' on which Clicks relied was nothing more than its conventional purchases of stock in the ordinary course of its business.
- It does not purchase any item of stock specifically for the purpose of satisfying its obligations under the loyalty programme. Instead it acquires stock for the purpose of its ordinary trading activities.
- When customers purchase items and present a rewards voucher in payment for the goods, the value of the voucher is deducted from the overall price and the customer pays the balance.
- In other words the goods are sold at a discount represented by the amount of the voucher.
- No expense item is shown in the taxpayer's accounts.
- Its purchases of stock are accounted for in the usual way by adding purchases to stock on hand at the beginning of the tax year and deducting the stock on hand at the close of the year. In simplified terms that is the primary cost of sales.
- The discount is reflected in the fact that sales are less than they would otherwise be by the amount of the discount. But that is no different from the effects of a pensioners' discount on one day of every week, a stock clearance sale or the recently popular 'Black Friday' sale.

Personal notes from the presenter…

- Clients are often irritated when a tax advisor plays “devil’s advocate” – however, this is an important part of the responsibilities of the tax practitioner – i.e. to anticipate a potential challenge by SARS.
- At the outset, one should have anticipated 2 difficulties with the Section 24C claim on a loyalty programme:
  - The “one contract” requirement; and
  - Whether one can argue that by only earning less of a profit in future years, would meet the “expenditure” requirement.

- This is again an example where a ruling made by the Special Court is overturned by the Appeal Court.
- This seems to become more common and is reducing the credibility of the Special Court.

The Tax Faculty

Section 1: Some learning points

- SARS is much more litigious than ever before. Given an 80% success rate in the SCA, their confidence in an outcome in their favour is significant.
- The impact of case law is often misconstrued. It is in fact very narrow and limited to the specific topic under the specific scenario subject to review.
- The grounds for objection is extremely important. The outcome of the VWSA and Atlas CopCo cases may have been totally different if different grounds of objection were submitted.
- Full disclosures for any discretionary claim is extremely important. This will protect the taxpayer against understatement penalties.
- The strategy on how a dispute will be addressed is critically important. In ITC 24674, the taxpayer conceded too easily on the catch up wear and tear claim. This impeded the objection on the understatement penalty
- Understatement penalties are applicable even if in an assessed loss situation.
- Plan to go to court, hope that it will never happen!!

The Tax Faculty

Section 2:

Under section 2, we will consider how a precautionary and anticipatory approach to ITR 14 preparation can avoid costly disputes with SARS and minimise the risks of understatement penalties. Under this section, we will discuss sound principles of tax risk management and tax governance that, if applied properly, can protect the taxpayer against most understatement penalties.

Personal notes from the presenter…

- Dealing with SARS Requests for Information and SARS Audits does not start when a RFI is received or when notification of an audit is received.
- Dealing with SARS audits starts with
  - Establishing a business appropriate “Tax Strategy”
  - Incorporating a bespoke “Tax Risk Management” process ensuring that the tax consequences of every transaction is correctly accounted throughout the tax lifecycle.

The Tax Faculty

Characteristics of Tax Strategy

Tax strategy summary

UK Finance Act 2016

HTTPS://WWW.LEGISLATION.GOV.UK/UKPGA/2016/24/SCHEDULE/19

PART 2 PUBLICATION OF TAX STRATEGIES

Qualifying UK groups: duty to publish a group tax strategy

16(1) This paragraph applies in relation to a UK group which is a qualifying group in any financial year ("the current financial year").

(2) The head of the group must ensure that a group tax strategy for the group, containing the information required by paragraph 17, is prepared and published on behalf of the group in accordance with this paragraph.

(3) The group tax strategy—

(a) must be published before the end of the current financial year, and

(b) if the group was a qualifying group in the previous financial year, must not be published more than 15 months after the day on which its previous group tax strategy was published.

UK Finance Act 2016

HTTPS://WWW.LEGISLATION.GOV.UK/UKPGA/2016/24/SCHEDULE/19

Content of group tax strategy

17(1) A group tax strategy required to be published on behalf of a UK group by paragraph 16 must set out—

(a) the approach of the group to risk management and governance arrangements in relation to UK taxation,

(b) the attitude of the group towards tax planning (so far as affecting UK taxation),

(c) the level of risk in relation to UK taxation that the group is prepared to accept, and

(d) the approach of the group towards its dealings with HMRC.

The Tax Faculty

Tax Strategy for the Owner Managed Business

Benefits of having tax strategy for the SMME?

- Tax management is often neglected when a new business is started.
- It becomes increasingly important as the business grows and becomes more profitable.
- The benefits of an embedded tax strategy is most notable when:
  - The company is subject to an external Due Diligence (sell total business, attract strategic investor, listing)
  - There is a dispute with SARS and one needs to avoid understatement penalties.
- At a minimum the strategy should include:
  - Who is ultimately responsible for all tax affairs
  - Strategy regarding consulting with Tax Advisors
  - Tax Status Reporting

Example of Tax Strategy for the Owner Managed Business

- [Taxpayer Name] philosophy in dealing with taxes:
  - To comply with all the tax laws affecting the business.
  - To ensure that all tax returns are completed and payments made within the time limits provided by law.
  - To ensure that it can produce clean “Tax Clearance Certificates” at any point in time.
  - Will not process any non-business or private related expenditures via the company. Any transactions (including employment contracts) with related parties will be at arms length.
  - Will conduct tax planning prudently and with the benefit of reputable external tax advice. Any tax planning must be underpinned by the commercial substance of transactions.
  - Seek Tax Certainty by ensuring that the tax consequences of transactions are considered before finalising any material transaction.

Example of Tax Strategy for the Owner Managed Business

- [Taxpayer Name] strategy with regards to Tax Advisory services are as follows:
  - [Taxpayer Name] will seek professional and reputable tax advice with regards to all "out of ordinary" transactions. These include but are not limited to the following:
    - All transactions affecting the shareholding in the company.
    - All transactions with shareholders and directors.
    - Mergers, acquisitions, major disposals and major acquisitions.
  - [Taxpayer Name] will engage with a reputable Tax Advisor to perform a Tax Health Check every 3rd year. [Taxpayer Name] will make use of the Voluntary Disclosure Programme to rectify potential underpayments of tax and will make use of Section 93 of the Tax Administration Act to rectify potential overpayments of tax.
  - [Taxpayer Name] will engage with a reputable Tax Advisor to assist in all material Tax Audits and Requests for Information initiated by SARS.

Example of Tax Strategy for the Owner Managed Business

- The [Managing Director/Financial Director/Financial Manager] is ultimately responsible for the tax management of [Taxpayer Name].
- The Financial Accountant will submit a tax status report to the person responsible for the tax management of the company on a monthly/quarterly/six-monthly basis. This report will include at the minimum:
  - Status report on Income Tax, VAT, PAYE and other tax compliance submissions.
  - Details of any outstanding disputes with SARS including Requests for Information, Tax Audits, IT 14SD's, VDP's and Section 93 requests for reduced assessments.
  - Action taken to address any issues raised by the external auditors/external reviewers in their management letters.
  - Status report on health check performed by external tax advisor.

Tax Risk Management

The Tax Strategy sets the high-level principles and philosophy of the group with regards to the approach to tax risks.

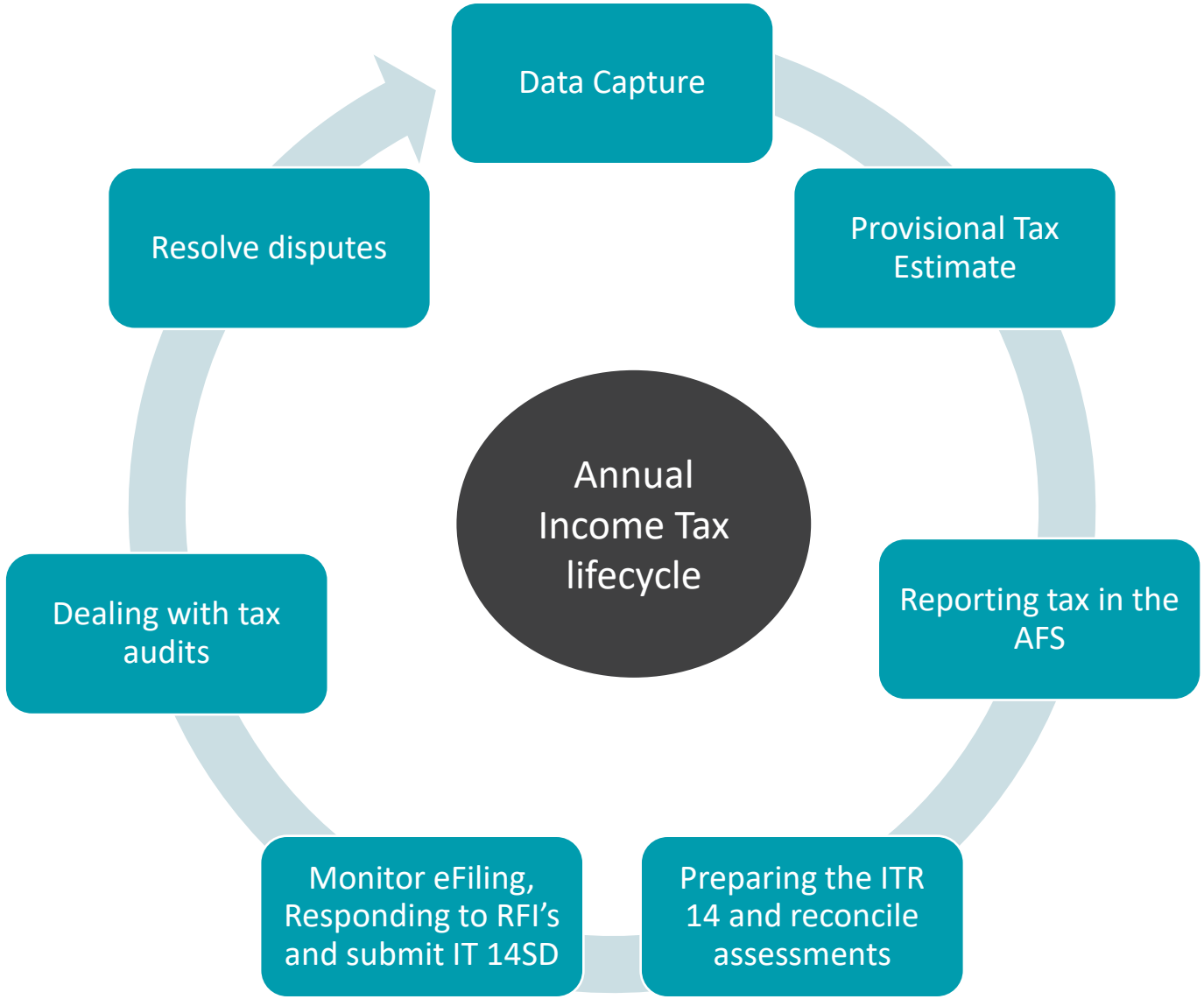
Tax risk management is the collection of activities, policies and procedures adopted by the company in order to implement the Tax Strategy.

Tax Risk Management bridges the gap between the tax strategy and the day-to-day activities of the taxpayer.

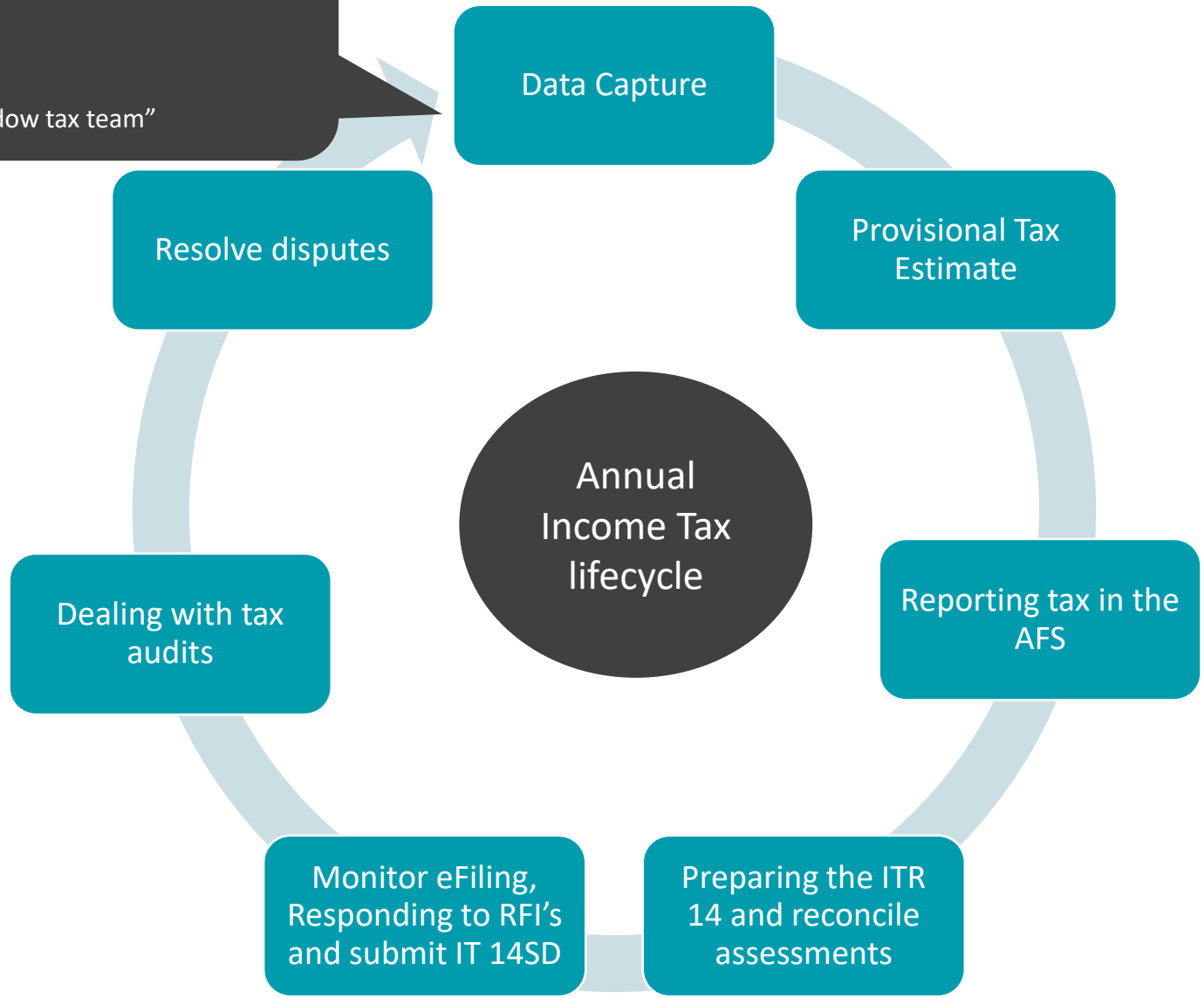
The Tax Faculty

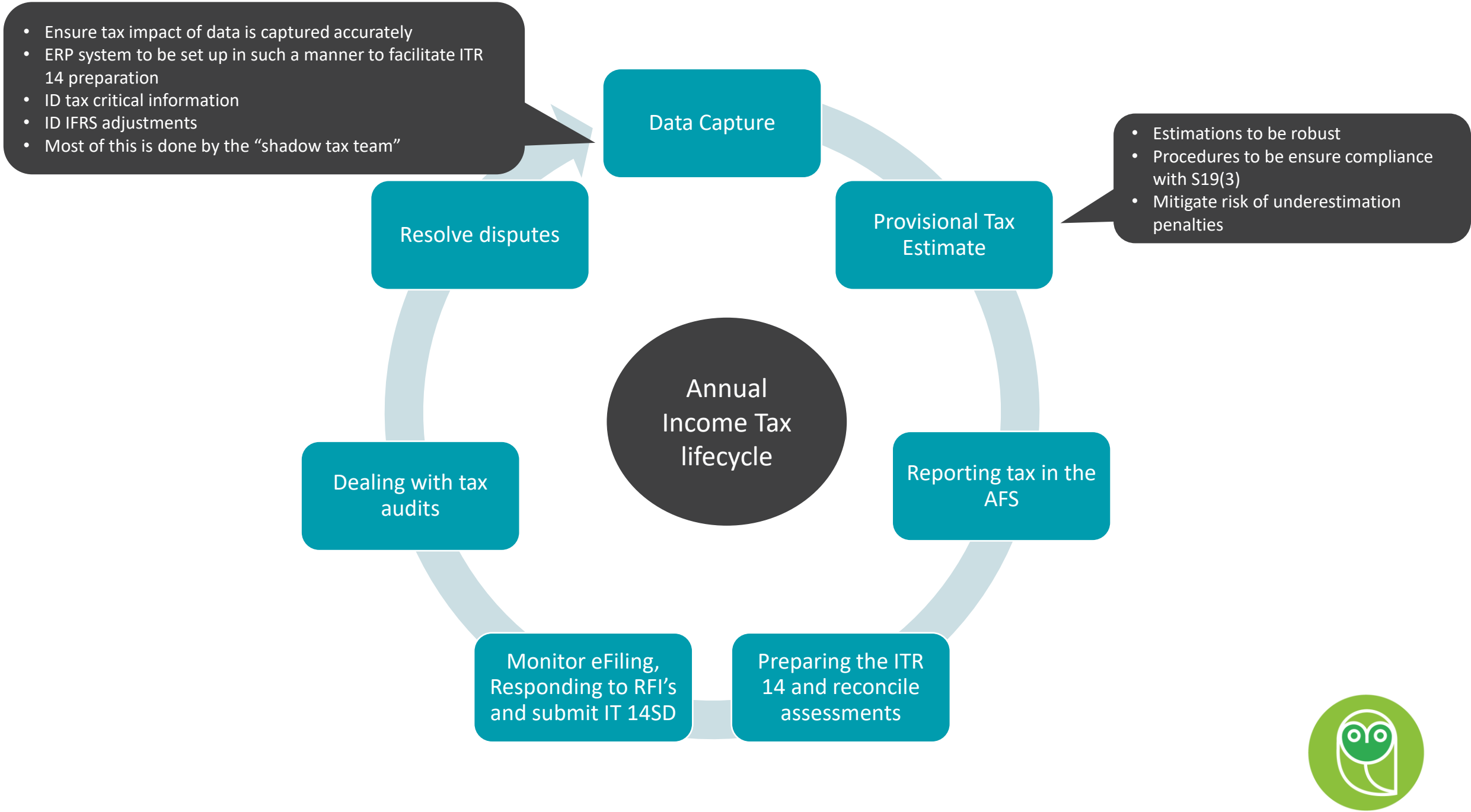
The Tax Faculty

Tax Risk Management: Tax/Finance Department specific considerations


Annual Income Tax lifecycle
Data Capture
Provisional Tax Estimate
Reporting tax in the AFS
Preparing the ITR 14 and reconcile assessments
Monitor eFiling, Responding to RFI's and submit IT 14SD
Dealing with tax audits
Resolve disputes

- Ensure tax impact of data is captured accurately
- ERP system to be set up in such a manner to facilitate ITR 14 preparation
- ID tax critical information
- ID IFRS adjustments
- Most of this is done by the “shadow tax team”

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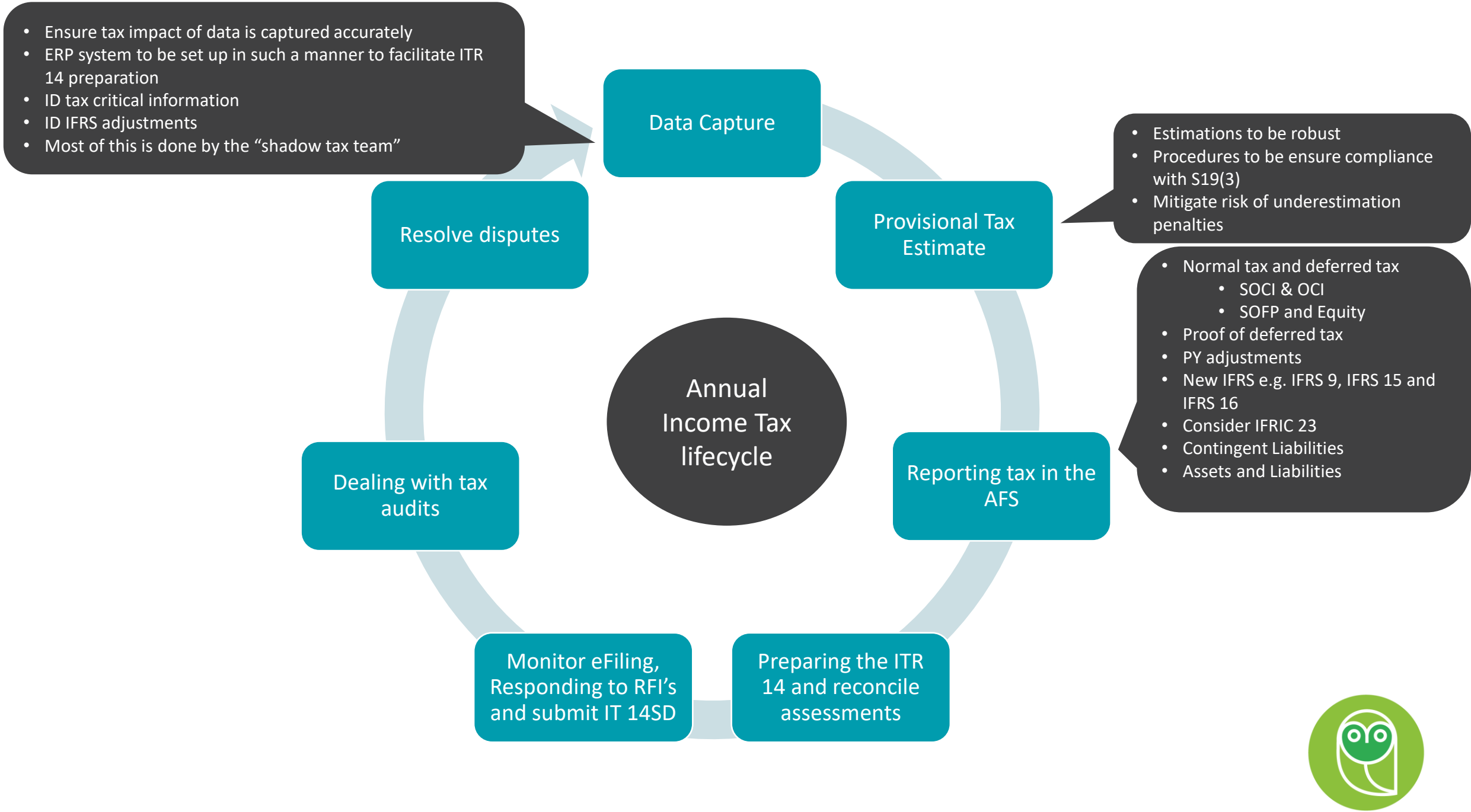
Data Capture
Provisional Tax Estimate
Estimations to be robust
Procedures to be ensure compliance with S19(3)
Mitigate risk of underestimation penalties
Reporting tax in the AFS
Preparing the ITR 14 and reconcile assessments
Monitor eFiling, Responding to RFI’s and submit IT 14SD
Dealing with tax audits
Resolve disputes
Annual Income Tax lifecycle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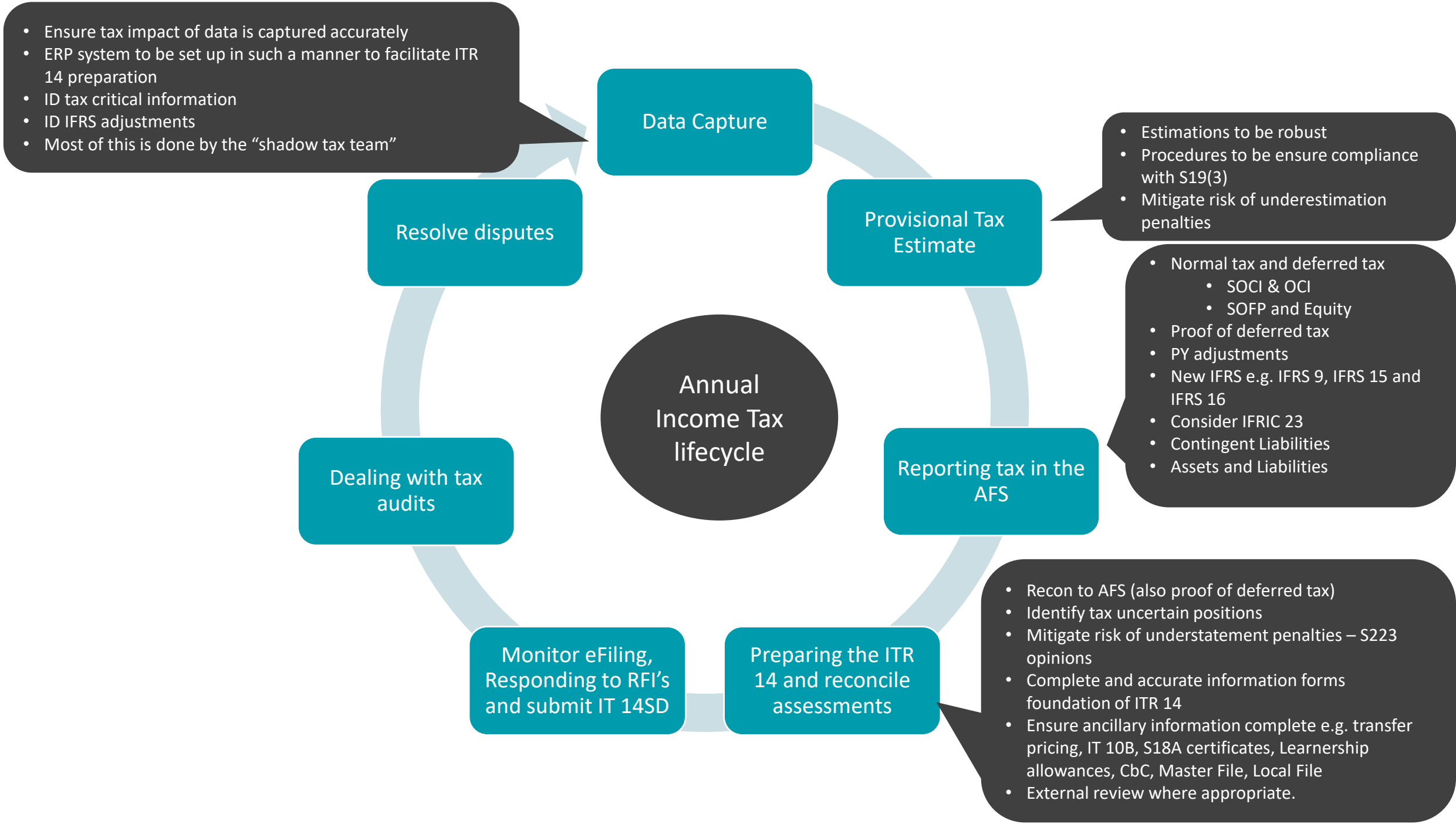
Data Capture
Provisional Tax Estimate
Estimations to be robust
Procedures to be ensure compliance with S19(3)
Mitigate risk of underestimation penalties
Reporting tax in the AFS
Normal tax and deferred tax
SOCI & OCI
SOFP and Equity
Proof of deferred tax
PY adjustments
New IFRS e.g. IFRS 9, IFRS 15 and IFRS 16
Consider IFRIC 23
Contingent Liabilities
Assets and Liabilities
Preparing the ITR 14 and reconcile assessments
Monitor eFiling, Responding to RFI’s and submit IT 14SD
Dealing with tax audits
Resolve disputes
Annual Income Tax lifecycle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Procedures to be ensure compliance with S19(3)
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SOFP and Equity
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PY adjustments
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Consider IFRIC 23
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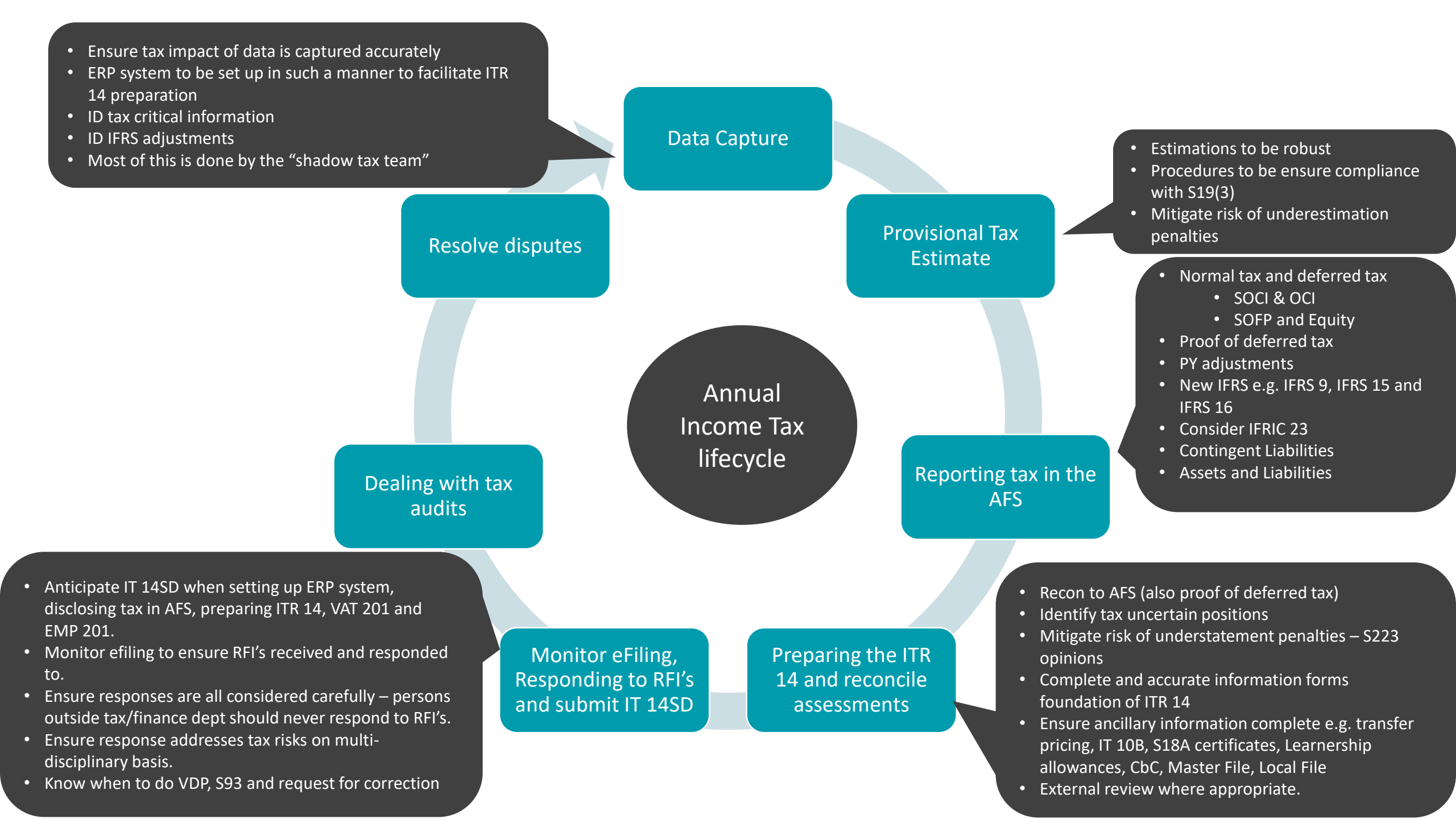
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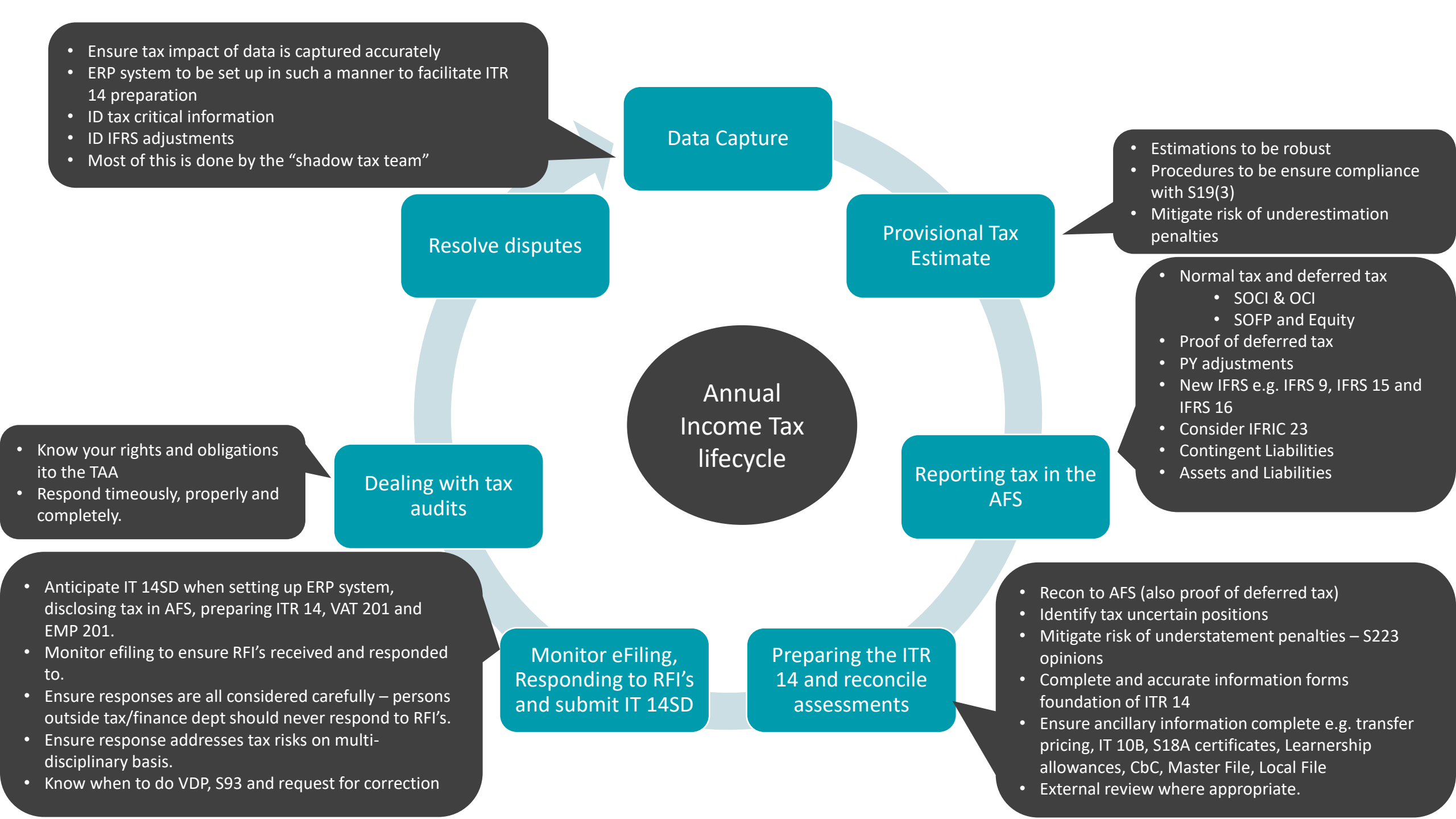
Monitor efiling to ensure RFI's received and responded to.
Ensure responses are all considered carefully – persons outside tax/finance dept should never respond to RFI's.
Ensure response addresses tax risks on multi-disciplinary basis.
Know when to do VDP, S93 and request for correction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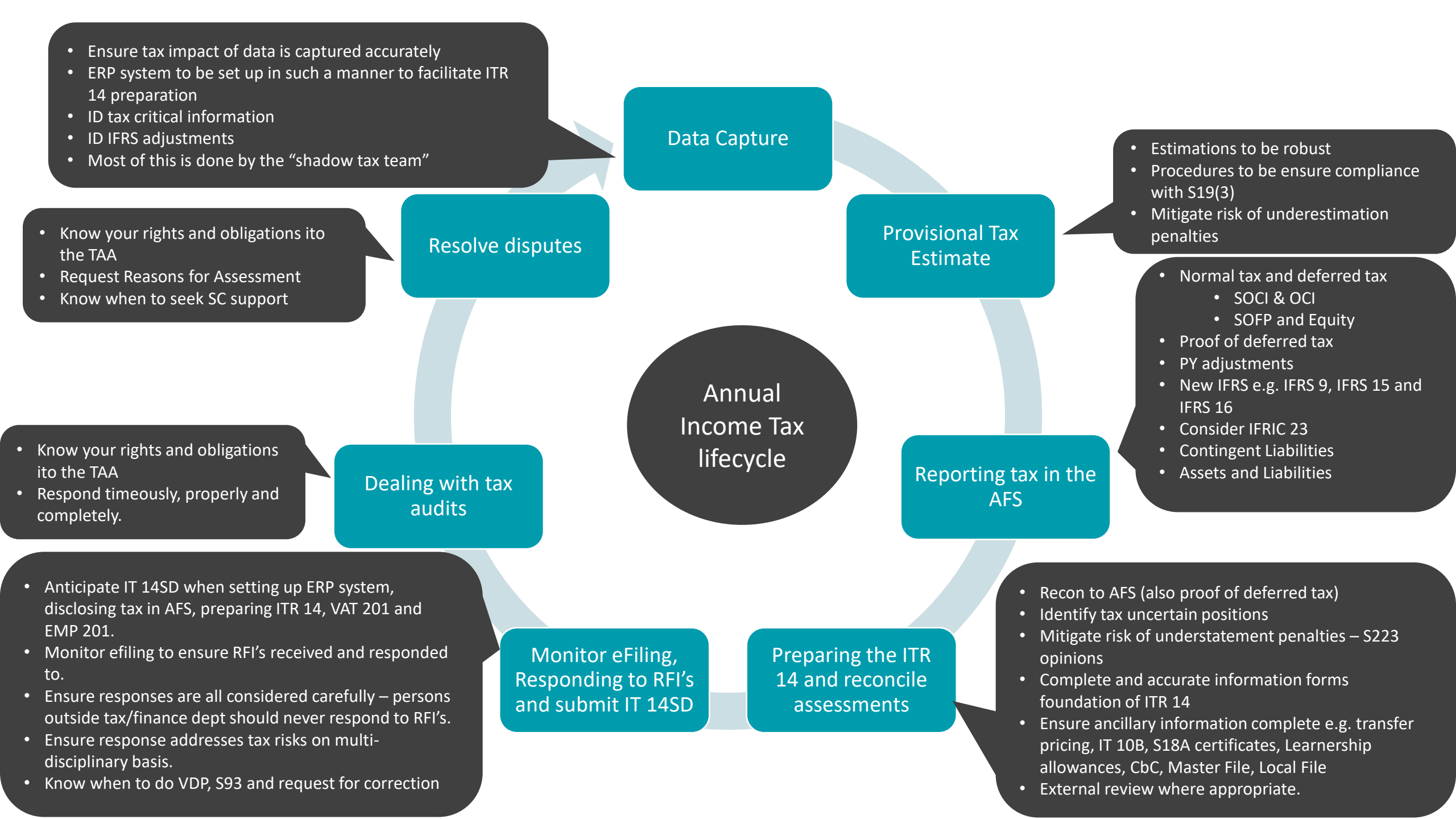
Know when to do VDP, S93 and request for correction
Dealing with tax audits
Know your rights and obligations ito the TAA
Respond timeously, properly and completely.
Resolve disputes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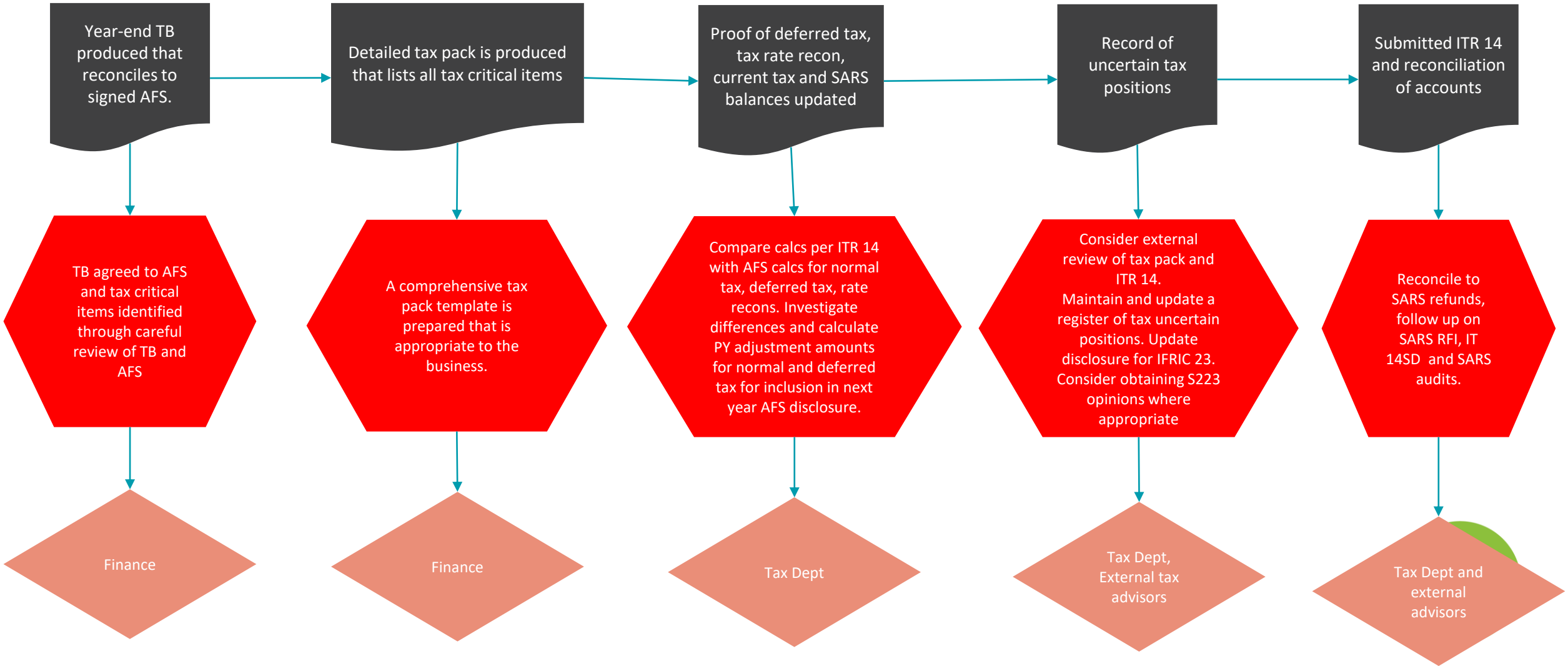
Ensure response addresses tax risks on multi-disciplinary basis.
Know when to do VDP, S93 and request for correction
Know your rights and obligations ito the TAA
Respond timeously, properly and completely.
Know your rights and obligations ito the TAA
Request Reasons for Assessment
Know when to seek SC support

End-to-end process – ITR 14 process



Phased approach to ITR 14 preparation

Phased approach to ITR 14 preparation

Phase	Description
1: Understanding client's business and industry.	• Anticipate Tax adjustments. • Anticipate accounting approach followed in AFS • Identify areas where Tax Rulings were issued. • Advise client to consult Tax Practitioner BEFORE major transactions are concluded – Tax Rulings vs Tax Opinions.
2: Information gathering.	• Requesting and collecting required information timeously and in an appropriate format expedites the ITR 14 process. • It is strongly advised that a comprehensive well laid out tax pack be developed that contains detailed information of all tax critical items. These include but are not limited to the following: Detailed TB with explanations, Detailed tax asset register, legal fees, consulting fees, section 24C, Section 6quat etc.
3: Critical and objective analysis of information.	• Analysing and interpretation of information. • Draft preparation of Tax computation. • Prepare draft tax computation and compare to that used in AFS. (Normal and Deferred Tax) • Identification of tax critical items, tax uncertain positions and tax aggressive positions. • If applicable, prepare register of Tax Uncertain Positions for IFRIC 23. • DO NOT file return if the above has not been satisfactorily addressed!!
4: Tax computation and supporting WP	• Preparing supporting working papers • Completion of draft ITR14. • Anticipate SARS audit and the request for an IT 14SD.

Phased approach to ITR 14 preparation

Phase	Description
5: Tax opinions and tax rulings	• Consider section 223 opinions for any Tax Positions Taken. • "More likely than not" obtained before ITR 14 is "due". • SARS may not levy understatement penalties. • Note: Ensure person who issued the opinion is suitably qualified and that the assumptions aligns with the reality. Often, the opinion is subject to inaccurate assumptions. Critically review opinion – do not simply accept opinion!
6: Formal communication	• Issue formal report to taxpayer client. • If Tax Practitioner is part of the external auditing firm, communicate to external auditor. • Obtain formal sign-off from taxpayer who understands tax positions.
7: eFiling	• Submissions of ITR 14 and comparing with ITA 34 assessments. • Ongoing monitor of statement of account and emails for queries, disputes. • Ongoing check of Tax Clearance position.
8: Tax Disputes and Tax Audit	If applicable – manage tax disputes including requests for refunds under section 190 of the Tax Administration Act.

Personal notes from the presenter…

- If the taxpayer follows the above process, it is highly unlikely that SARS will raise a query on a topic that has not been anticipated by the Taxpayer.
- If the above process has been followed, it will be impossible for SARS to raise a 25% understatement penalty being “Reasonable care not taken in preparing the return”.

Understatement penalty

1	2	3	4	5	6
Item	*Behaviour*	*Standard case*	*If obstructive, or if it is a 'repeat case'*	*Voluntary disclosure after notification of audit or criminal investigation*	*Voluntary disclosure before notification of audit or criminal investigation*
(i)	'Substantial understatement'	10%	20%	5%	0%
(ii)	Reasonable care not taken in completing return	25%	50%	15%	0%
(iii)	No reasonable grounds for 'tax position' taken	50%	75%	25%	0%
(iv)	'Impermissible avoidance arrangement'	75%	100%	35%	0%
(v)	Gross negligence	100%	125%	50%	5%
(vi)	Intentional tax evasion	150%	200%	75%	10%

Where S223 opinions are obtained from independent tax practitioner, protection is obtained against this penalty.

If the ITR 14 process is followed, SARS will have extreme difficulty to prove that "reasonable care was not taken in preparing the ITR 14"

The process is designed to identify uncertain tax positions and where appropriate obtain external tax advice.

Understatement penalty

1	2	3	4	5	6
Item	*Behaviour*	*Standard case*	*If obstructive, or if it is a 'repeat case'*	*Voluntary disclosure after notification of audit or criminal investigation*	*Voluntary disclosure before notification of audit or criminal investigation*
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(v)	Gross negligence	100%	125%	50%	5%
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ORDINARY NEGLIGENCE

Negligence would include the failure to take reasonable care in completing returns or the lack of reasonable grounds for the assumption of a particular tax position.

(Guide to understatement Penalties (Issue 2))

Note: Impermissible avoidance arrangements falls short of "gross negligence" but will arguably also be "negligence".

Transnet Limited t/a Portnet v Owners of the N B Stella Tingas and Another 2003(2) SA 473 SCA

- *"It follows I think that to qualify as gross negligent the conduct in question, … must involve a departure from the standard of the reasonable person to such an extent that it may properly be categorised as extreme.*
- *It must demonstrate where this is found to be conscious risk-taking, a complete obtuseness of mind or where there is no conscious risk taking a total failure to take care. If something less were required the distinction between ordinary and gross negligence would lose its validity."*

The Tax Administration Act S222(1)

Understatement penalty.—(1) In the event of an 'understatement' by a taxpayer, the taxpayer must pay, in addition to the 'tax' payable for the relevant tax period, the understatement penalty determined under subsection (2) unless the 'understatement' results from a *bona fide* inadvertent error.

The Tax Administration Act S223(3)

(3) SARS must remit a 'penalty' imposed for a '**substantial understatement**' if SARS is satisfied that the taxpayer—

(a) made full disclosure of the arrangement, as defined in section 34, that gave rise to the prejudice to SARS or the fiscus by no later than the date that the relevant return was due; and

(b) was in possession of an opinion by an independent registered tax practitioner that—

(i) was issued by no later than the date that the relevant return was due;

(ii) was based upon full disclosure of the specific facts and circumstances of the arrangement and, in the case of any opinion regarding the applicability of the substance over form doctrine or the anti-avoidance provisions of a tax Act, this requirement cannot be met unless the taxpayer is able to demonstrate that all of the steps in or parts of the arrangement were fully disclosed to the tax practitioner, whether or not the taxpayer was a direct party to the steps or parts in question; and

(iii) confirmed that the taxpayer's position **is more likely than not to be upheld if the matter proceeds to court.**

'substantial understatement' means a case where the prejudice to SARS or the fiscus exceeds the greater of five per cent of the amount of 'tax' properly chargeable or refundable under a tax Act for the relevant tax period, or R1 000 000;

Commonly found misconceptions

Commonly found misconceptions

Erroneous statement	Reason
I can rely on the tax computation prepared by the client for AFS purposes and audited by the external auditor.	• The objective of the audit is to ensure that the AFS are “reasonably” stated. • The audit is completed with “materiality” in mind. • The auditor is concerned with the net effect between current and deferred tax. • The audit is often completed immediately after year-end and incomplete information is available. • ITR 14 requires complete and accurate disclosure of current tax only. Materiality is not relevant. • The auditor relies on the work done by the Tax Practitioner in preparing an audit opinion (especially with regards to prior year tax computations) – The Tax Practitioner cannot rely on the auditor – since this is outside the scope of the audit.

Commonly found misconceptions

Erroneous statement	Reason
Make full disclosure and SARS can decide whether to accept or not.	• The ITR 14 is effectively a “self-assessment system” • The Tax Practitioner must have the ability to identify any tax position and evaluate whether or not it will be defendable if queried by SARS. • The rationale behind understatement penalties is that the taxpayer and tax practitioner will make concerted effort and take due care when completing the ITR 14.

Commonly found misconceptions

Erroneous statement	Reason
Tax compliance is simply an administrative function to be completed by inexperienced staff	The person completing the tax return must have the following specialist skills: • Strong accounting skills – the gap between IFRS and Tax Accounting is increasingly becoming larger. E.g. Straight lining of leases, Share Based Payments, Business Combinations etc. • Strong broad-based tax skills – Each Tax Return effectively requires a mini "Tax Due Diligence" to be prepared in order to identify tax critical items. • Solid understanding of Dividend Tax, Interest WTH Tax, PAYE and VAT principles. The interaction between various taxes is extremely relevant. IT14SD's are becoming the rule instead of the exception. E.g. Transactions between connected parties may hold VAT and PAYE implications. Loans to shareholders and group companies may give rise to Dividend Tax concerns.

Commonly found misconceptions

Erroneous statement	Reason
The Tax Practitioner will not be held liable if the Tax Return is incomplete or inaccurate.	• Where SARS levies a penalty on the grounds that "*Reasonable care not taken in completing return*" then the client may potentially hold the Tax Practitioner Liable for interest and penalties – subject to engagement letter limitations. This may lead to reputational damage to the individual, his/her employer and SAIT. • Section 241(2) of TAA: "*A senior SARS official may lodge a complaint with a 'recognised controlling body' if a registered tax practitioner has, in the opinion of the official without exercising due diligence prepared or assisted in the preparation, approval or submission of any return, affidavit or other document relating to matters affecting the application of a tax Act;*

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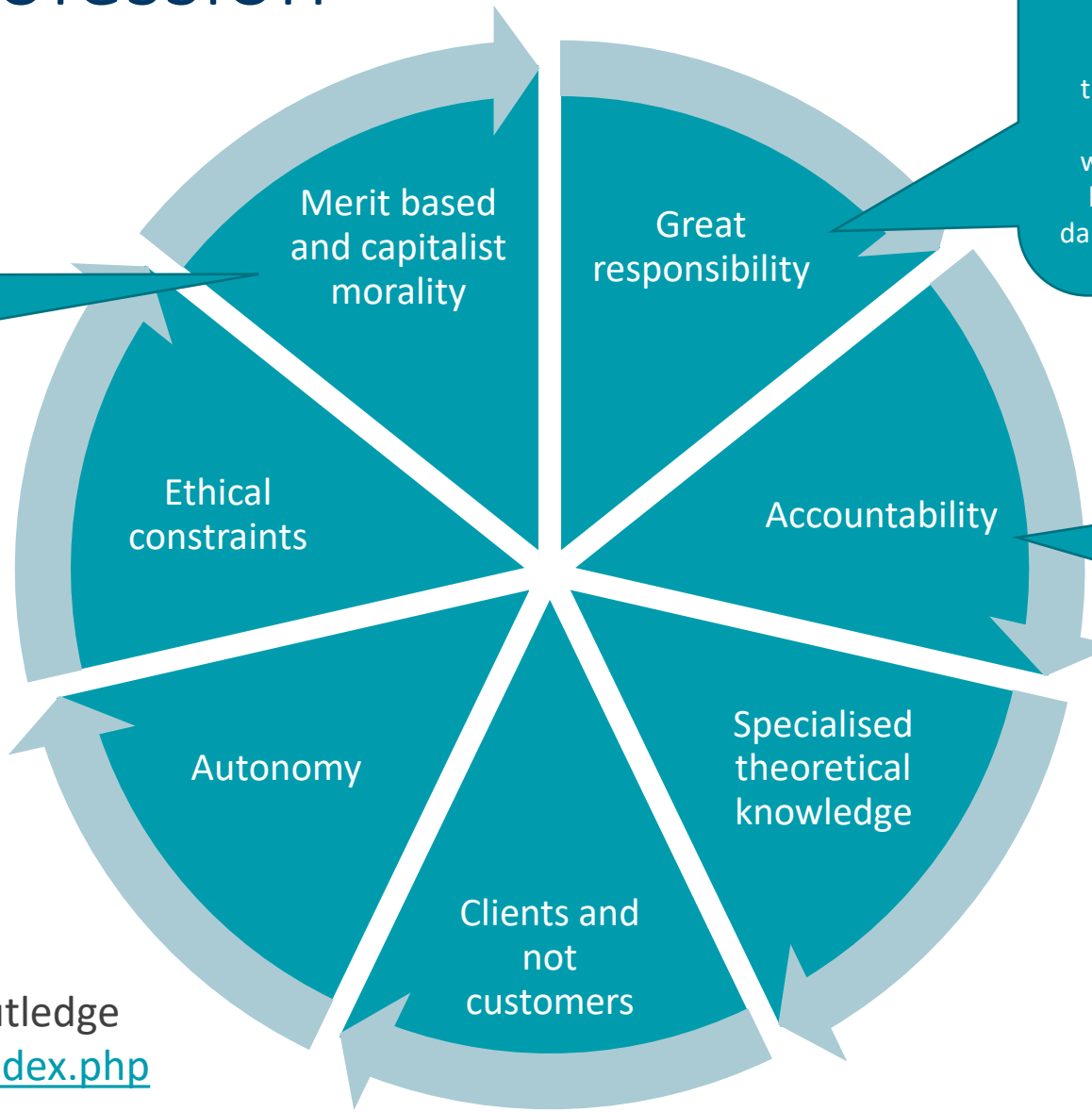
Section 3:

Under section 3, we will deal with practical case studies where a strategy for dealing with SARS audits under different scenarios will be discussed in a practical and understandable manner. Participants will benefit from the practical experience built up over 30 years by the presenter in dealing with SARS audits. This is more than “knowing your rights”. This section is about the subjective decisions to be made by the person dealing with SARS audits under a variety of scenarios.

Attributes of a profession



A professional is one who must attract clients and profits due to the merits of his work.

Professionals deal in matters of vital importance to their clients and are therefore entrusted with grave responsibilities and obligations. Given these inherent obligations, professional work typically involves circumstances where carelessness, inadequate skill, or breach of ethics would be significantly damaging to the client and/or his fortunes.

Professionals hold themselves ultimately accountable for the quality of their work with the client.

"Design Professionalism" by Andy Rutledge
http://designprofessionalism.com/index.php

The Tax Faculty

Introductory comments:

Responding to a

- SARS Request for Information or
- SARS letter of audit findings

Introductory comments

The objective when responding to a SARS letter of audit findings or a request for information is different from a situation where one needs to issue an opinion.

When communicating with SARS, please consider the following:

- Respond comprehensively and truthfully to the questions and/or findings of SARS.
- Avoid providing information outside the scope of the questions/findings.
- Acknowledge situations where there was indeed a contravention of the law. Use the opportunity to provide reasons for this in order to minimise the risk of understatement penalties.
- Ensure that the document is self-standing.
- Confirm the contents of any potential communication with SARS with the client before sending it to SARS.
- Take note of the fact that your submissions will be regarded as evidence for or against the Taxpayer should this matter go to ADR or a court of law. As such, take extreme care in the responses to ensure that you represent the client appropriately.
- If you believe that the topic is sufficiently contentious so that it will escalate to a court of law, advise the client that Senior Counsel should be consulted before making submissions. Since Senior Counsel will need to represent the Taxpayer in a court of law, it would be advisable to obtain such guidance as early as possible.

Layout

Assume that the SARS official knows nothing of the client's business and/or industry. Extra care should be taken to explain the background to the client's business and to provide context to transactions concluded.

The layout of the document must be:

- Logical
- Have appropriate headings
- At the minimum cover the following:
  - Background information to the Taxpayer. What industry, what business etc.
  - The facts as specifically confirmed by the client.
  - Details of SARS query/request for information.
  - The law
    - The required sections
    - Appropriate case law
    - Appropriate guidance by SARS
  - Application of the law to the facts

Language

It is critically important to use clear and concise language when communicating with SARS. SARS will interpret ambiguous statements to favour SARS and not the taxpayer.

- Avoid using long sentences.
- Avoid long paragraphs
  - Make use of bullets or sub numbering
- Ensure that the headings and sub paragraphs are suitably numbered.
- Use “professional” language.
  - Avoid words such as “think”, “like”.
  - Avoid complex terms.
  - Preferably use “everyday language” but avoid “slang”.
- The language must be free of ambiguity.
- If you make use of abbreviations, then it should
  - Be defined the 1st time that it is used
  - Be consistently used thereafter

  E.g. The Annual Financial Statements (“AFS”), or Big Fish (Pty) Ltd (“Big Fish”) or the Income Tax Act No 58 of 1962 (“The Income Tax Act”)

The facts

- Reproduce the SARS questions in point form.
- Contextualise these questions with accurate facts in a logical and understandable way.
- When responding to SARS audit findings, evaluate whether the potential dispute is a question of law or a question of fact.
- Avoid assumptions. Only communicate verifiable facts.
- If the facts are dependant on the verbal submissions of a taxpayer (e.g. the "intention" of a taxpayer, then explore of there are any surrounding evidence that will support the *ipse dixit* of the taxpayer.

Responses and the law

Responses to audit findings/requests for information

- Be specific to the question in your response.
- If the SARS finding is ambiguous, first obtain clarity before responding.

The law

The law will generally have sub-headings e.g.:

- The Income Tax Act
- Relevant Case Law
- SARS Guides and Binding Rulings
- There is no prescribed format how to respond to SARS, but the general "rule of thumb" is to put yourself in the position of the SARS official when reading through your response and assuming that that SARS would use any opportunity to deny a tax deduction or include an amount in gross income.

The Tax Faculty

Phased approach when dealing with SARS RFI

Phased approach when dealing with SARS RFI

Phase 1: Logistics and planning

Step 1: What is the scope of the RFI?
Is it limited to Income Tax or does it include other taxes? Confirm that it is an RFI and not a formal notification of an audit. Do you have the appropriate skills to deal with the full scope of the RFI?

Step 2: Is the timeline realistic and is the information available?
Should one request extension for the submission of the responses? Factors such as changes in ERP systems, business acquisitions etc may impact the availability of information.

Step 3: In what format must the information be provided to SARS?
Generally a narrative in a report combined with supporting schedules in pdf or excel.

Step 4: Does the taxpayer have sufficient resources to obtain the information.
Can it be obtained manually? Should ERP extraction and data analytics be used?

Step 5: Obtain Power of Attorney from client if necessary.

Phased approach when dealing with SARS RFI

Phase 2: Communication with SARS

Step 1: Depending on the outcome of Phase 1, contact SARS and request extension where appropriate.

Step 2: If the scope of the RFI is too wide for electronic submission, consider communicating this fact to SARS. Potential amendment of scope of RFI is possible.

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Phased approach when dealing with SARS RFI

Phase 3: Information gathering

Step 1: High level discussion on each question.

Meet with client and discuss each question in detail. Even though the scope of the RFI may be Income Tax focused, evaluate the scope of each question as to whether or not it may lead to a non-Income Tax risk. E.g. A question regarding transactions with connected party transactions may lead to transfer pricing risks and/or denial of income tax deductions for unproductive expenditure.

Step 2: Obtain information from client and review carefully.

Identify potential contraventions of the law on a multi-disciplinary basis. This may include risks and opportunities.

Step 3: Discuss potential risks and opportunities with the client as well as the appropriate treatment thereof.

Distinguish between, clear contraventions of the law and Tax Uncertain positions

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Phased approach when dealing with SARS RFI

Phase 4: Prepare response to SARS

Step 1: Perform proper planning around the lay-out of the response and the flow of information. An "information dump" may lead to future questions and/or assessments.

Step 2: Prepare the response and clarify any uncertainties in supporting information.
Take specific care where large volumes of data is provided to SARS based on narratives provided by junior data capture staff.

Step 3: Consider how disclosure will be made of law contraventions. Full disclosure in responding to an RFI is compulsory.

Phased approach when dealing with SARS RFI

Phase 5: Obtain client approval regarding the proposed response to SARS

Step 1: Ensure that the client is fully aware of all tax uncertain positions, contraventions of the law as well as potential consequences.

Step 2: Obtain and retain sign off for your records.

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Phased approach when dealing with SARS RFI

Phase 6: Submit response to SARS

Step 1: Make sure that the submission is made in an appropriate format and that the SARS RFI is included in the submission pack.

Step 2: Obtain confirmation of receipt from SARS.

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Phased approach when dealing with SARS RFI

Phase 7: Await further responses from SARS

Step 1: SARS may

- issue further requests for information or
- may issue an assessment or
- May notify the taxpayer of the commencement of an audit

Step 2: For further requests for information, follow the previous process again.
For an assessment – consider the merits and object where necessary
For notification of an audit, await further instructions from SARS.

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The Tax Faculty

Introductory comments:

Lodging an objection

Introductory comments

The objective when submitting an objection to an assessment is different from a situation where one needs to issue an opinion or when one responds to a RFI.

When preparing the objection, please consider the following:

- The objection is prepared from the perspective of the taxpayer. ***It does not represent your personal opinion***. The wording in the objection must reflect this. (NOTE: Even if you disagree with the position of the taxpayer, you can still prepare the objection with grounds and reasons that supports the taxpayer's viewpoint.) It is strongly advisable to inform the taxpayer whether you believe that his chances for success is weak, moderate or strong. You should also advise him/her of the process going forward should SARS deny the objection.
- Respond comprehensively and truthfully to the **specific issue** under dispute.
- Do not address anything outside the scope of the additional assessment.
- Ensure that the document is self-standing. It forms the foundation of the dispute resolution process. The taxpayer is prohibited to add any further grounds of objection if this matter were to proceed to court.

Introductory comments

- Assume that this matter will proceed to court of law and prepare it in such a manner that you will be satisfied that it can be scrutinised in a court of law and become public knowledge.
- Confirm the contents of the objection with the client before sending it to SARS.
- NB – address every single item on the assessment separately. E.g:
  - The additional income
  - Understatement penalty
  - The Section 89quat(2) interest.
- If the candidate fails to object separately to this, then one will be precluded to do so at a later stage.
- If you believe that the topic is sufficiently contentious so that it will escalate to a court of law, advise the client that Senior Counsel should be consulted before making submissions. Since Senior Counsel will need to represent the Taxpayer in a court of law, it would be advisable to obtain such guidance as early as possible.

Layout

Assume that the SARS committee that will consider the merits of the objection knows nothing of the client's business and/or industry. This assumption becomes increasingly important as the case may proceed through the dispute resolution process. Extra care should be taken to explain the background to the client's business and to provide context to transactions concluded.

- The layout of the document must be:
- Logical
- Have appropriate headings
- At the minimum cover the following:
  - Background information to the Taxpayer. What industry, what business etc.
  - The facts as specifically confirmed by the client.
  - Details of the specific item under dispute.
  - The law
    - The required sections
    - Appropriate case law
    - Appropriate guidance by SARS
  - Application of the law to the facts

Language

In the context of an “objection” the language is critically important.

- The manner in which the argument is submitted must be convincing, eloquent and professional.
- Great care must be taken with the language so that it presents the argument of the taxpayer in a convincing, elegant and eloquent manner.
- This is important as it will positively influence the SARS committee as to the bona fides of the taxpayer and that the taxpayer has reasonable grounds supporting any tax positions taken.
- It is critically important to use clear and concise language when preparing the objection. SARS will interpret ambiguous statements to favour SARS and not the taxpayer.
- A court of law will furthermore highlight ambiguous language and since the onus to prove that an amount is not taxable rests on the taxpayer, will interpret ambiguous language to the detriment of the taxpayer.

Language

The following should be considered:

- Avoid using long sentences.
- Avoid long paragraphs
  - Make use of bullets or sub numbering
- Ensure that the headings and sub paragraphs are suitably numbered.
- Use “professional” language.
  - Avoid words such as “think”, “like”.
  - Avoid complex terms.
  - Preferably use “everyday language” but avoid “slang”.
- The language must be free of ambiguity.
- If you make use of abbreviations, then it should
  - Be defined the 1st time that it is used
  - Be consistently used thereafter
- E.g. The Annual Financial Statements (“AFS”), or Bad Karma Luxury Lodge (Pty) Ltd (“Bad Karma”) or the Income Tax Act No 58 of 1962 (“The Income Tax Act”)

The facts

- Reproduce the “reasons of assessment” by SARS in point form.
- Contextualise these questions with accurate facts in a logical and understandable way.
- When preparing an objection, evaluate whether the dispute is a question of law or a question of fact.
- Avoid assumptions. Only communicate verifiable facts.
- If the facts are dependant on the verbal submissions of a taxpayer (e.g. the “intention” of a taxpayer, then explore of there are any surrounding evidence that will support the *ipse dixit* of the taxpayer.

The law

The law will generally have sub-headings e.g.:

- The Income Tax Act
- Relevant Case Law
- SARS Guides and Binding Rulings

There is no prescribed format how to submit the objection to SARS, but the general “rule of thumb” is to put yourself in the position of the SARS official or the judge of a tax court when reading through your response and assuming that that SARS would use any opportunity to deny a tax deduction or include an amount in gross income.

The Tax Faculty

SOME EXAMPLES

The Tax Faculty

Example 1 – Head Office Costs

Example 1: RFI

CLIENT (Pty) Ltd

Income Statement	2020	2019
Gross income	237 500 000	12 500 000
Dividends Received	20 000 000	10 000 000
Profit on sale of 100% equity held in foreign company	200 000 000	
Foreign exchange gain (proceeds on sale of investment held in f	15 000 000	
Admin fees: Group Companies	2 500 000	2 500 000
Expenses	-30 000 000	-2 000 000
Remuneration paid	-30 000 000	-2 000 000
Net income before tax	207 500 000	10 500 000

Tax Computation	2020	2019
Net Income before tax	207 500 000	10 500 000
Less: Exempt dividends received	-20 000 000	-10 000 000
Less: Capital profit on sale of investment	-200 000 000	0
Taxable income for the year	-12 500 000	500 000

SARS RFI

Kindly explain why remuneration (R30 000 000) should be allowed as a deduction for Income Tax, and explain how was it incurred in the production of interest, foreign exchange differences, and 'administration and management fees received'.

Background

- The company is the ultimate holding company in the group. The group consists of approximately 30 subsidiaries of which approximately 5 are foreign.
- The salaries of the directors are recovered from group companies with a margin via an admin fee.
- In the 2020 tax year, the taxpayer disposed of its 100% interest in a foreign entity and made a capital profit of R200m. This profit is exempt from CGT ito par 64B of the 8th Schedule.
- The amount received on the sale is held in a foreign bank account and the unrealised forex gain of R15m was taxed ito S24J
- R28m of the R30m fees was paid as a bonus to one shareholder who played a key role in historically managing the foreign company and was to a large extent responsible for the success of this company.
- The amount of R28m was subjected to PAYE and included in the Taxable Income of the Director.

Relevant Case Law: MTN vs SARS

Event	Audit fee	KPMG consulting fee
MTN ITR 14	Claimed 100% of the fee	Claimed 100% of the fee
SARS assessment	Apportioned the audit fee based on turnover and allowed between 2% and 6% of the fee depending on the year of assessment.	Denied 100% of the fee
Special Court	Believed that a 50/50 apportionment is appropriate	Agreed with SARS that no amount is deductible being capital in nature
South Gauteng High Court	Allowed 94% of audit fees to be deducted.	Allowed 100% tax deduction for KPMG fee.
Supreme Court of Appeal	Believed that only 10% of the audit fee is deductible in terms of section 11(a).	No amount of the KPMG fee is to be deducted.

NB – This part of the appeal failed due to evidentiary issues

There was, it must be added, no explanation from Holdings for its failure to call as witnesses persons at Holdings or KPMG with personal knowledge of the implementation and workings of the Hyperion system. ***Accordingly, given the inadequacy of the evidence adduced by Holdings, it was well-nigh impossible to determine whether the KPMG fee fell legitimately to be deducted by Holdings.*** *It follows that the Commissioner cannot be faulted for having disallowed that fee in its entirety. In the result the contrary conclusion reached by the full court to that of the Tax Court that the deduction of the KPMG fee must be allowed in full, falls to be set aside.*

Extracts from MTN Case

The MTN case is an important reference guide as to the most likely approach that SARS will follow in a potential revised assessment.

[10] It is well settled that 'generally, in order to determine in a particular case whether moneys outlaid by the taxpayer constitute "expenditure incurred in the production of the income", important, sometimes overriding, factors are the purpose of the expenditure and what the expenditure actually effects' (per Corbett JA in Commissioner for Inland Revenue v Standard Bank of SA Ltd 1985 (4) SA 485 (A) at 498F-G). And, in this ***connection the court has to assess the closeness of the connection between the expenditure and the income earning operations*** *(Nemojim at 947G-H).*

[12] ***Where - as here - expenditure is laid out for a dual or mixed purpose the courts in South Africa and in other countries, have, in principle, approved of an apportionment of such expenditure*** *(Secretary for Inland Revenue v Guardian Assurance Holdings (SA) Ltd 1976 (4) SA 522 at 533E-H). Thus in Nemojim, Corbett JA stated:*

'As pointed out in the Rand Selections case supra at 131E-G, the Income Tax Act makes no provision for apportionment. Nevertheless, apart from the Rand Selections case, it is a device which has previously been resorted to where expenditure in a globular sum has been incurred by a taxpayer for two purposes, one of which qualifies for deduction and one of which does not . . . It is a practical solution to what otherwise could be an intractable problem and in a situation where the only other answers, viz disallowance of the whole amount of expenditure or allowance of the whole thereof, would produce inequity or anomaly one way or the other. ***In making such an apportionment the Court considers what would be fair and reasonable in all the circumstances of the case.'***

Extracts from MTN Case

[15] ***Apportionment is essentially a question of fact depending upon the particular circumstances of each case*** *(Local Investment Co v Commissioner of Taxes (SR) 22 SATC 4). As Beadle J put it in Local Investment Co (at II):*

'It does not seem possible to me to lay down any general rules as to how the apportionment should be made, other than saying that the apportionment must be fair and reasonable, having regard to all the circumstances of the case*. For example, in one case an apportionment based on the proportion which the different types of income bear to the total income might be proper, as was done in the Rand Selections Corporation's case, supra. In another case, however, such an apportionment might be grossly unfair; for example, in the case where the bulk of the expenditure was clearly devoted exclusively to operations intended to earn income, but which unfortunately in fact earned very little income, with the result that in the particular year of assessment the company earned very little "income", but from operations which incurred little expense earned relatively large non-taxable amounts. In such a case to apportion the bulk of the expenses to the non-taxable amounts would be unfair. In another case a fair method of apportionment might be to take the proportion which the capital invested in the operations earning the non-taxable amount bears to the total capital invested, as was done in I.T.C. No 832 of 1956, supra.'*

(Emphasis added)

Personal notes from the presenter…

- This dispute should have been anticipated when the tax return was prepared. If it was, then as section 223 opinion should be available to support the tax position taken. If it was not anticipated, then it casts a doubt about the tax risk management processes adopted by the taxpayer.
- It is very likely that SARS will deny the tax deduction of R28m on the grounds that it was incurred to earn the tax exempt capital gain of R200m. If the sale was subject to CGT (which it is not) then it could potentially qualify as “selling expenses”.

- It is too late to make use of the VDP programme since a disclosure under the VDP would not be “voluntary”
- One may concede that a portion of the salary is not deductible. The deductible portion could be apportioned based om the capital gain plus forex gain.
- SARS is likely to levy either a 25% or 50% penalty. SARS is obligated to levy the highest percentage per the table

Personal notes from the presenter…

- This is the worst possible outcome….
  - The shareholder is taxed on the receipt of R28m
  - The company does not receive a tax deduction.
- Depending on the circumstances, one may potentially have argued that the amount paid is in fact a “dividend” as defined and not a salary. The dividend would not be tax deductible, but would only attract 20% tax in the hands of the shareholder.
- Please note special definition of a dividend in the ITA

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Example 2 – Salary Sacrifice and Lockdown payments

The facts

Good Heart (Pty) Ltd is a subsidiary in a large group of companies. During the lockdown period in 2020, Good Heart (Pty) Ltd's executives took a cut in salary of 33.3%.

The proviso is that the saving in executive salaries must be applied to pay ex gratia payments to employees in the group forced to take unpaid leave due to the fact that they cannot work during the lockdown period.

The saving in executive salaries for the December 2020 tax year was R400 000. These amounts were applied by the company to make payments to employees employed by other group companies and not for employees employed by Good Heart itself.

SARS issued a letter of assessment where the deduction of R400k is denied stating that the amounts were not paid in the production of Good Heart's income but in the production of a 3rd party's income.

Tax considerations

Even thought the query deals with Income Tax, enquire in whose name was PAYE calculated. In this regard, take note of the following:

"gross income", in relation to any year or period of assessment, means—

(i) in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or

(ii) …

during such year or period of assessment, excluding receipts or accruals of a capital nature, but including, without in any way limiting the scope of this definition, such amounts (whether of a capital nature or not) so received or accrued as are described hereunder, namely—

(*c*) any amount, including any voluntary award, received or accrued in respect of services rendered or to be rendered or any amount (other than an amount referred to in section 8 (1), 8B or 8C) received or accrued in respect of any employment or the holding of any office: Provided that—

(i) …

(ii) **any amount received by or accrued to or for the benefit of any person in respect of services rendered or to be rendered by any other person shall for the purposes of this definition be deemed to have been received by or to have accrued to the said other person**

Tax considerations

- It is my view that the Executive still worked and that the R400k was paid in compensation of the executives employment.
- The payment is not an ex gratia payment, but a contractual payment for which the underlying quid pro quo is that the executive will provide employment services.
- It follows that a tax deduction in terms of section 11(a) is available

HOWEVER…..

- Due to par (c) of the gross income definition, the originating cause of the payments made to the employees of other group companies, is the services rendered by the executive, this payment is deemed to be income of the executive and not the recipient employee.
- There is a significant risk that PAYE should have been calculated at the rates applicable to the executive and not the recipient employee and the company may be faced with an increased PAYE obligation.
- One will need to analyse the “salary sacrifice” arrangement and consider the risk from a multi-disciplinary perspective.

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Example 3 – Pre-Trade Income

Facts

- Your client is a company formed with the specific purpose of building a shopping centre and thereafter leasing the various shops to tenants and managing the communal property.
- During the Feb 2018 tax year, the taxpayer incurred pre-trade expenditure of R5million that was correctly added back in the tax computation in terms of section 11A.
- The taxpayer commenced trade in the 2019 tax year and calculated a R7million assessed loss after claiming the S11A deduction (R5million) in full.
- SARS issued a letter of audit findings stating its intention to issue a revised assessment whereby the assessed loss will be reduced to R2million.
- Whilst there is no additional income tax (assessed loss is simply reduced), SARS intend raising an understatement penalty of R5m x 28% x 10% = R140 000.

Facts (Continue)

SARS quotes IN 51 in providing reasons for assessment as follows:
Under section 11A pre-trade expenses which would have qualified under sections 11 (excluding section 11(x)), 11B, 11D and 24J but for the trade requirement in those provisions, are deductible in the year of assessment in which trade commences, subject to certain requirements, irrespective of when they were incurred, but subject to section 23H.[1]

However, under section 11A(2) the section 11A(1) deduction may only be set off against the taxable income[33] *from the particular trade. If the pre-trade expenses exceed that taxable income, the excess may not be set off against the income from any other trade notwithstanding section 20(1)(b). Section 20(1)(b) permits a taxpayer to set off an assessed loss incurred in one trade against any income from another trade derived during the same year of assessment.*

Any pre-trade expenses not allowed because of insufficient taxable income from the particular trade must be carried forward for set off against any future taxable income from that trade *(see* ***4.6.3****).*

Thus pre-trade expenses cannot create an assessed loss in respect of the trade to which they relate. Nor can they increase an assessed loss from that trade.

Process to follow when evaluating a SARS letter of audit finding

Step 1: Consider the facts on which the letter of audit finding is issued. Are the facts in line with the facts provided to SARS. Are the facts accurate?

In this case, the facts are not in dispute. SARS and the taxpayer are in agreement that the section 11A is applicable to the value of R5million.

Process to follow when evaluating a SARS letter of audit finding

Step 2: Consider the legislation quoted by SARS. The letter of audit findings will contain the relevant legislation that SARS believes applies.

In this case, there is a potential dispute over the law that should be further investigated.

Review of the law

Section 11A(2) in point form reads as follows:

- *So much of the expenditure and losses contemplated in subsection (1)*
- *as exceeds the income derived during the year of assessment from **carrying on that trade** after deduction of any amounts allowable in that year of assessment in terms of any other provision of this Act,*
- *shall not be set off against any income of that person which is derived **otherwise than from carrying on that trade**, notwithstanding section 20 (1) (b)*

Application of the law

Section 11A(2) prohibits a tax loss arising from a section 11A(1) deduction from the particular trade to which it relates to be offset against any income arising ***any other trade.***

Since the taxpayer only conducts one trade (namely the construction of a shopping centre with the purpose of leasing it to tenants) it is strongly arguable that section 11A(2) is not applicable at all.

Process to follow when evaluating a SARS letter of audit finding

Step 3: Consider the financial impact of the dispute

In this case, SARS is of the view that the unclaimed Section 11A deduction may be carried forward to future years to be offset against future income from that trade.

From an economic perspective, it is irrelevant whether an unclaimed section 11A is carried forward to future years or if an increased assessed loss is carried forward to future years. Both will have the same impact.

The issue for consideration is however the understatement penalty of 10% that has been raised (R140 000).

The aim of the letter of response to the SARS letter of audit findings is therefore primarily to obtain a waiver of the understatement penalty.

Process to follow when evaluating a SARS letter of audit finding

Step 4: Formulate the approach to the response

It is advised that the response is two-pronged:

1. Dispute with regards to the technical application of section 11A(2). Focus must be on fact that the taxpayer only conducts one trade and as such there is no *"income of that person which is derived otherwise than from carrying on that trade"*
2. Dispute the levy of understatement penalty on following grounds:
    1. SARS has failed to meet the burden of proof requirement;
    2. There is no "**understatement**" as defined in S221 of the TAA since there is no "**prejudice**" to SARS. Whether or not an amount is carried forward as an assessed loss or is carried forward as an unclaimed S11A amount creates the same economic effect for SARS and for the taxpayer in this particular set of circumstances since the taxpayer only carries on one trade.
    3. The taxpayer maintains that the SARS interpretation of the law in IN 51 is incorrect and it holds no standing in law.

In the conclusion, you may state that the taxpayer is prepared to accept the SARS interpretation of the law, but only if the understatement penalty is waived.

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Process to follow when evaluating a SARS letter of audit finding

Step 5: Communicate with taxpayer

Obtain formal sign-off from taxpayer before any responses are sent to SARS. The taxpayer should be aware of the strategy and the risks and the chances of success.

In this case, the chances of success is high on technical grounds, but since a position is taken that is contrary to one that is published in a formal Interpretation Note, it may be time consuming to resolve. It would probably be referred to Head Office. If the strategy is to obtain a waiver of the understatement penalty and not necessarily obtain a revised assessed loss, then the matter should be resolved sooner.

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Example 4 – Donations

The facts

“Donations” made by franchise holder

Your client is a franchise holder in the fast food industry.

As part of the agreement with the franchisees, the franchise holder is obligated to use 2.5% of the total franchise fees received for community development initiatives.

Your client duly transferred the amount over to a Public Benefit Organization (PBO) that issues a section 18A certificate to your client.

The amount is claimed as an income tax deduction in the ITR 14 but SARS issues a letter of audit findings stating its intention to deny the tax deduction on the grounds that your client is in an assessed loss situation and a section 18A deduction is limited to 10% of taxable income.

Analysis of the letter of audit findings

Step 1: Consider if the dispute is a question of law, or a question of fact

SARS argues that the amount constitutes a “donation” and is therefore made with gratuitous intent.

The true facts is that the franchise holder is not transferring the monies to the PBO out of gratuitous intent, but due to the fact that it is obligated to transfer 2.5% of gross franchise revenue to a PBO in terms of its contract with the franchisee.

It follows that the dispute has its origins in a “factual” dispute over the “intent” with which the donation is made.

Evidence: Facts

Step 2: Obtain evidence supporting the factual situation

The following evidence will support the contention that the payment was not made with gratuitous intent:

- Extracts from the contract with the franchisee
- The disclosure in the ITR 14
- The disclosure in the AFS

Evidence: The law

Step 3: Obtain evidence supporting the legal contention

In essence, the client argues that the amount paid to the PBO qualifies as a tax deduction in terms of s11(a) as opposed to S18A on the grounds that the amount is actually paid (and incurred) in the course of producing taxable franchise fees not of a capital nature.

Evidence: The law

Step 3: Obtain evidence supporting the legal contention

BPR 282 may be of assistance in formulating a legal response:

The applicant is a company that owns and operates a wind farm that generates electricity. In terms of the agreement entered into with the government of the Republic to supply electricity to the national grid and the electricity generation licence issued by the regulator, it must commit funds equal to a specified percentage of its annual revenue to SED and ED expenditure.

Pursuant to its SED and ED obligations, the Applicant established a trust that will specifically undertake the projects or provide funding to other organisations registered as public benefit organisations as contemplated in section 30(3) which will undertake them. The applicant proposes to contribute amounts to the trust on a quarterly basis based on the specified percentage of its revenue earned in the previous year of assessment.

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Evidence: The law

BPR 282 (Continued)

The ruling made in connection with the proposed transaction is as follows:

a) *The contributions to be made by the applicant to the trust in respect of the SED and ED commitments will be deductible under section 11(a) read with section 23(g). The total amount incurred in each year of assessment will be equal to the specified percentage of the applicant's revenue, as defined in the agreement, earned by the applicant in that year of assessment.*

b) *The expenditure incurred by the applicant in respect of the SED and ED commitments will not be a donation as defined in section 55(1) nor a deemed donation, as contemplated in section 58.*

Preparation of response to letter of audit findings

Step 4: Prepare response

The focus of the response to the SARS letter of audit findings is to provide evidence to SARS that the payment to the PBO was not made with gratuitous intent but out of the obligations arising from the contracts with the franchisees.

Once SARS can be convinced regarding this factual situation then the application of the law should be simple given the rulings in BPR 282 as well as BCR 002.
In BCR 002 it is ruled that *"Expenditure incurred in respect of the CSI programmes for purposes of earning BEE scorecard points will be deductible under section 11(a) read with section 23(g)."*

Preparation of response to letter of audit findings

Step 5: Obtain client approval for response, submit and await response

The chances of a successful resolution of this dispute is excellent.

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Example 5 – Management Fees

The facts

“Management fee”

Your client is a large group of companies. The management fee paid to a particular group company increased from R1million in 2018 to R11 million in 2019.

SARS issues a RFI requesting reasons why the management fee increased by such a large amount.

Phased approach

Step 1: Obtain clarity regarding the facts

Upon discussion with the client, it was established that a management fee of R10million was not supported by any services provided by the group company.

The payment was simply made in order to enable a connected party group company to fund an acquisition of shares from minority shareholders.

Phased approach

Step 2: Ask probing questions

Did the recipient company declare the receipt as income?
In this case the recipient included the amount as gross income and paid tax thereon.

Did the recipient company pay output VAT on the payment and did the taxpayer claim VAT on the management fee?
In this case VAT was paid and claimed.

Was there any contravention of another law?
In this case a potential contravention of the companies act occurred since financial assistance was provided in order to acquire shares in other group companies from outside shareholders.

Would there be dividend tax consequences?
N/A since all companies were resident

Phased approach

Step 2: Summarise potential contraventions of the law

The position may be summarized as follows:

- The taxpayer to whom the RFI was issued, incorrectly claimed an income tax deduction of management fees to a connected resident company. This is a clear contravention of the law. Since a specific RFI was issued, it is SARS view that VDP relief is not available.
- This taxpayer incorrectly claimed VAT on this amount since no taxable supply was made. Since a specific RFI was issued, it is SARS view that VDP relief is not available.
- The taxpayer receiving the "admin fee" incorrectly declared tax on this management fee since it is a capital receipt. S93 relief may potentially be available.
- The taxpayer receiving the "admin fee" incorrectly paid VAT on this admin fee since no supply was made. A credit note can be issued.
- The potential contravention of the Companies Act should be referred to legal counsel for a detailed opinion.

Phased approach

Step 3: Strategy for the response

- The response strategy is to make full disclosure to SARS of the fact that the payment of R10m was not in fact a management fee but was a capital distribution by the company to a connected party and SARS should issue a revised assessment. The response also states that VAT was overclaimed.
- Simultaneously, a request for a reduced assessment should be made in the hands of the recipient company whereby a reduction in taxable income of R10m is requested on the grounds that the income is capital in nature. The application is made ito S93 of the TAA.
- The response to the RFI elaborates on reasons why no understatement penalty should be levied by SARS – mainly, since holistically seen, there was no prejudice to SARS. The chances of success on this holistic approach remains slim however.

Phased approach

Step 4: Await SARS response

- SARS issued additional income tax assessments and levied 25% understatement taxes.
- An objection was lodged against the understatement tax, requesting a reduction to 10%.

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Example 6 – DD Report

Request for relevant information

- Your client operates a series of fast food restaurants in Gauteng. Your clients wishes to attract investors with the aim of expanding its footprint into the Western Cape. Your client instructs an external firm to perform a vendor due diligence.
- The vendor due diligence is completed and the Due Diligence report was provided to your client's management.
- To date, no strategic investor could be found and the proposed expansions have not occurred.
- In the ITR 14 submitted to SARS, the full cost of the vendor due diligence have been added back for both VAT and Income Tax purposes.
- SARS issues a Request for Information whereby the full vendor due diligence report is requested.
- Your client approaches you for advice as to whether or not the information must be provided to SARS.

The Tax Admin Act

"relevant material" means any information, document or thing that in the opinion of SARS is foreseeably relevant for the administration of a tax Act as referred to in section 3;

46. Request for relevant material.—
(1) SARS may, for the purposes of the administration of a tax Act in relation to a taxpayer, whether identified by name or otherwise objectively identifiable, require the taxpayer or another person to, within a reasonable period, submit relevant material (whether orally or in writing) that SARS requires.

Proposed Response

The definition of “relevant material” is very wide and is discretionary. If your client claimed either the VAT or the Income Tax on the DD costs, the contents and the scope of the work would probably be “relevant”. Unless covered by legal privilege, it is likely that the DD report should be provided to SARS.

It becomes more vague if the costs of the DD was not claimed for income tax or VAT. It appears that SARS is “phishing” for potential tax liabilities identified by the professionals conducting the DD.

It is advisable that SARS be contacted and requested to provide full reasons why the DD report is requested arguing that the DD report does not fall within the definition of “relevant material”.

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Example 7 – VAT on local travel

Request for Information

- Your client is a local firm of consulting engineers.
- SARS issues a RFI requesting detail of the VAT treatment of local travel and entertainment expenditures.
- The client informs SARS that it is prudent and do not claim any VAT on local travel and entertainment expenditures despite being entitled to an input tax deduction on:
  - Local flight costs
  - Local subsistence costs (accommodation and meals) of employees whilst away from their usual place of work and residence for at least one night.
- SARS issues an income tax assessment on the grounds that the section 11(a) deduction on these costs is overstated to the extent that it includes VAT.
- SARS levies a 25% understatement penalty on the ground that “reasonable care” was not taken in completing the return.
- Your client requires your advice in dealing with an objection.

The Law: Section 23C of the Income Tax Act

23C. Reduction of cost or market value of certain assets.—

(1) … where regard is to be had to … any expenditure incurred by him or her, and—

(a) the taxpayer is a vendor as defined in section 1 of the Value-Added Tax Act; and

*(b) the taxpayer is or was in any previous year of assessment **entitled** under section 16 (3) of the last-mentioned Act to a **deduction of input tax** as defined in section 1 of that Act,*

the amount of such input tax shall be excluded from the … the amount of such expenditure…

SARS is correct in law by denying an income tax deduction where the taxpayer was "***entitled***" to claim an input tax deduction even if they did not factually claimed the input tax.

Strategy is:

Accept the income tax assessment	Object to the understatement penalty on grounds that: • There was no **prejudice** to SARS – in fact there was a prejudice to the taxpayer • The error was bona fide and inadvertent that is proven by fact that the taxpayer was prudent in its VAT affairs to its own detriment • Argue what it means that "reasonable care" was not taken on completing the return given that the amounts are immaterial and in all other respects the return was completed properly.	Claim the claimable VAT if in 5 year period

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Example 8 – Pre-Trade

The facts

SugarCo. was formed in July 2016 with the sole purpose of acquiring land, constructing an office building thereon and to operate as a landlord by leasing the building to tenants.

SugarCo. acquired land in Ballito on 1 January 2017.

The cost of the land was R10million.

The purchase price of R10million was funded by a loan from the four resident shareholders of R2.5m per shareholder carrying 8% interest per annum. The interest incurred on this loan account may be summarised as follows:

Y/E 31 March 2017: R200 000

Y/E 31 March 2018: R800 000

Y/E 31 March 2019: R800 000

The loan account is not subordinated or subject to any special conditions.

The company has no other activities, i.e. its sole activity is the construction of this single office building for lease as office space to various tenants.

There were no activities in 2017 and 2018.

During 2019, the company paid an external services provider R100 000 to apply for the rezoning of the property.

The facts

The company has submitted the ITR14 tax returns for all the years up to 31 March 2019 and the company has been assessed with an assessed loss of R1.9million being the cumulative interest claimed in terms of section 24J of the Income Tax Act (R1.8million) as well as the cost of rezoning the land in 2019 (R100k).

Construction was originally delayed due to difficulties in obtaining rezoning permits.

The company officially started earthworks on 1 April 2019 – i.e. the 2020 tax year.

SARS issued a letter of audit finding stating that it will add back the R100k rezoning costs in the 2019 tax year and reduce the assessed loss from R1.9million to R1.8m.

A 50% understatement penalty is charged – R100k x 28% x 50% = R14 000

Considerations

The expenses is probably pre-trade expenses that should have been added back in terms of section 11A of the Income Tax Act.

Assuming full disclosure was made to SARS regarding the fact that trading has not yet commenced, the best strategy may be to:

- Accept the revised assessment as well as the USP
- Once the revised assessment has been issued and paid, apply for Voluntary Disclosure relief whereby the amount of R1.8m is denied and carried forward ito S11A

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Request for reasons: Template letter

Request for reasons: The law

Government Notice 550 as published in Government Gazette 37819

Definitions

"day" means a "business day" as defined in section 1 of the Act;

6. Reasons for assessment

(1) A taxpayer who is aggrieved by an assessment may, prior to lodging an objection, request SARS to provide the reasons for the assessment required to enable the taxpayer to formulate an objection in the form and manner referred to in rule 7.

(2) The request must-
   (a) be made in the prescribed form and manner;
   (b) specify an address at which the taxpayer will accept delivery of the reasons; and
   (c) be delivered to SARS within 30 days from the date of assessment.

(3) The period within which the reasons must be requested by the taxpayer may be extended by SARS for a period not exceeding 45 days if a SARS official is satisfied that reasonable grounds exist for the delay in complying with that period.

(4) Where a SARS official is satisfied that the reasons required to enable the taxpayer to formulate an objection have been provided, SARS must, within 30 days after delivery of the request, notify the taxpayer accordingly which notice must refer to the documents wherein the reasons were provided.

(5) Where in the opinion of a SARS official the reasons required to enable the taxpayer to formulate an objection have not been provided, SARS must provide the reasons within 45 days after delivery of the request for reasons.

(6) The period for providing the reasons may be extended by SARS if a SARS official is satisfied that more time is required by SARS to provide reasons due to exceptional circumstances, the complexity of the matter or the principle or the amount involved.

(7) An extension may not exceed 45 days and SARS must deliver a notice of the extension to the taxpayer before expiry of the 45 day period referred to in subrule (5).

Request for reasons: The law

Government Notice 550 as published in Government Gazette 37819

7. Objection against assessment

(1) A taxpayer who may object to an assessment under section 104 of the Act, must deliver a notice of objection within 30 days after-

(a) delivery of a notice under rule 6(4) or the reasons requested under rule 6; or

(b) where the taxpayer has not requested reasons, the date of assessment.

Extracts from SARS website

How should I request reasons?

There are two options:

- Electronic Request for Reasons for assessments: SARS has an electronic Request for Reasons process via eFiling and the SARS branches for Personal Income Tax (PIT), Company Income Tax (CIT), Value-Added Tax (VAT) and Pay-As-You-Earn (PAYE).
- Manual Request for Reasons for assessments or decision taken: A manual process for Request for Reasons or decision taken exists for all other taxes or decisions taken. The taxpayer must submit a letter detailing the request and adhere to the requirements mentioned above. The request must be submitted via post, submitted at a SARS branch or email it to SARS.

Request for reasons: Template letter

The South African Revenue Services

Taxpayer Name and Tax Reference Number

We refer to the notice of assessment issued to [**taxpayer name and tax reference**] dated [**date must be within 30 business days of date of assessment**] of which a copy is attached as Annexure A for your convenience. Please find attached as Annexure B a duly completed Power of Attorney from the taxpayer authorising us to act on its behalf in lodging an objection against this assessment.

We submit that the grounds provided in the assessment do not sufficiently enable us to understand the basis of the assessment and to formulate an objection against the said assessment. In terms of Rule 6 of Government Notice 550 as published in Government Gazette 37819, the taxpayer is entitled to, "*prior to lodging an objection, request SARS to provide the reasons for the assessment required to enable the taxpayer to formulate an objection in the form and manner referred to in rule 7.*"
We kindly request SARS to provide said reasons for the assessment within 45 days of the date of delivery of this letter.

Upon receipt of the required reasons for assessment we record our intention to deliver a notice of objection within 30 business days after the date of delivery of the reasons requested under rule 6. (Refer Rule 7 of Government Notice 550).

Please do not hesitate to contact the undersigned should you require any additional information.

Kind regards

Name of Tax Practitioner
Tax Practitioner Ref Number

The Tax Faculty

Lodging an objection: Rules and Template letters

Lodging an objection: The law

Government Notice 550 as published in Government Gazette 37819

7. Objection against assessment

(1) A taxpayer who may object to an assessment under section 104 of the Act, must deliver a notice of objection within 30 days after-
  (a) delivery of a notice under rule 6(4) or the reasons requested under rule 6; or
  (b) where the taxpayer has not requested reasons, the date of assessment.

(2) A taxpayer who lodges an objection to an assessment must-
  (a) complete the prescribed form in full;
  (b) specify the grounds of the objection in detail including-
    (i) the part or specific amount of the disputed assessment objected to;
    (ii) which of the grounds of assessment are disputed; and
    (iii) the documents required to substantiate the grounds of objection that the taxpayer has not previously delivered to SARS for purposes of the disputed assessment.

Lodging an objection: The law

Extract from the guide on the rules promulgated in terms of Section 103 of the Tax Administration Act issued by SARS

6.5. When will an objection be valid?

Under section 107(1) SARS must consider a valid objection in the manner and within the period prescribed under the TA Act and the rules. The requirements for a valid objection under rule 7(2) are as follows:

The objection must be made in the prescribed form (ADR1 / NOO) with the information requested in the form completed

The taxpayer must specify in detail the grounds upon which the objection is made, including—

- the part or specific amount of the disputed assessment objected to;
- which of the grounds of assessment are disputed;
- the documents required to substantiate the grounds of objection that the taxpayer has not previously delivered to SARS for purposes of the disputed assessment

Contrary to the old rules, a power of attorney is not required from a person who signs an objection on behalf of the taxpayer.

The Tax Faculty

Annexure F – Form NOO Look & Feel

SARS

Notice of **Objection**

Tax Number NTXNTC01 **NOO1**

Applicant Details - Individual INDIF01

Surname

First Two Names

ID No. Passport No. Passport Country (e.g. South Africa = ZAF)

Contact Email

Home Tel No.

Bus Tel No.

Cell No.

Applicant Details - Company / Close Corporation / Government / Foreign Entity COMIF01

Surname or Registered Name

Trading or Other Name

CK No. Bus Tel No. Fax No. Cell No.

Contact Email

Particulars of Representative (Person Dealing with Dispute on Behalf of Taxpayer) REPIF01

Surname Initials

ID No. Passport Country (e.g. South Africa = ZAF) Passport No. Cell No.

Tel No. Fax No. Tax Practitioner Registration No. **PR** -

Capacity: Public Officer ☐ Curator / Trustee / Liquidator / Executor / Administrator ☐ Partner ☐ Treasurer ☐ Accounting officer for Local / Public Authority / Accountant ☐ Sole Proprietor ☐ Tax Practitioner ☐ Legal Representative / Attorney ☐

Email

Are you signing on behalf of the taxpayer? Y ☐ N ☐ If yes, do you have a power of attorney from the taxpayer? Y ☐ N ☐ Is the taxpayer aware of and agree with the grounds of dispute? Y ☐ N ☐

Reason why taxpayer is unable to sign this dispute

Amounts Under Dispute - Income Tax Only

OTIIF01

Document number | Tax Year (CCYY)

Source Code	Amount reflected on Assessment - Rands only	Amount that should be Reflected - Rands only	Difference - Rands only
Provisional tax			
Additional tax/Understatement penalty			
Penalties			
Interest			

Reason and Ground for Dispute - Please write in black ink and enter one character per block

Supporting documents must be attached to this form

Number of pages attached

Reason(s) for Late Submission of NOA / NOO (if applicable)

Postal Address for Delivery of Notice (Correspondence)

Please ensure that you capture your postal address in the following sequence: Box / Bag Number, Suburb / District / City, Country Code, Postal Code Per Line of Delivery. Please follow the physical address format.

Postal Code

Declaration

PDAIF01

I declare that:
- The information furnished in and with this form is true and correct in every respect; and
- I have the necessary records to support all my declarations on this form when I will retain for inspection purposes for a period of five years.

Date (CCYYMMDD)

For enquiries go to www.sars.gov.za or call 0800 00 7277

Assessment Under Dispute

Assessment Type | Income Tax | Administrative Penalty

Lodging an objection: Template letter

The South African Revenue Services
By eFiling

Taxpayer Name and Tax Reference Number
We refer to the notice of assessment issued to [**taxpayer name and tax reference**] dated [**date must be within 30 business days of date of assessment or from the date that SARS provided reasons for the assessment i.t.o. Rule 6 of Public Note 550**] of which a copy is attached as Annexure A for your convenience.

We also refer to the Notice of Objection (NOO1) form duly completed on eFiling. The purpose of this letter is to provide the reasons and grounds for the objection and should be regarded as an integral part of the N001 form submitted on efiling.

Background facts

An additional assessment was issued by SARS on [**date**]. This additional assessment was issued subsequent to a formal audit conducted by SARS and is issued in terms of the letter of audit findings dated [**insert date**]. **[If SARS provided reasons for the assessment in terms of Rule 6 of Public Note 550, please refer to these reasons].**

The subject matter of the dispute is as follows:
[Provide the background to the dispute. E.g. the company is engaged in the construction industry and SARS disputes a S24C claim, or the company received income subject to the Consumer Protection Act that SARS regarded as taxable.]
[If there is a dispute in facts, use this opportunity to highlight the difference in facts as described in the SARS letter of audit findings or the SARS reason for assessment.]
[Top Tip: Be specific to the matter under dispute. Do not deviate to matters that are not being assessed by SARS. Make sure all information is True, Helpful and Relevant]

Lodging an objection: Template letter

Summary of items under dispute

[Summarise the specific items in the additional assessment that is being disputed. E.g. specifically state if the taxpayer accepts the revised normal tax assessment but only disputes the levy of understatement penalty.]

On behalf of the Taxpayer, with respect to the [XXX] year of assessment, we formally object against the following:

- The inclusion of an amount of Rx in the taxable income in terms of section [x] of the Income Tax Act.
- The inclusion of an amount of Rx as a Capital Gain in terms of par [x] of the 8th Schedule to the Act.
- The levy of an understatement penalty of Rx in terms of section 222 of the Tax Administration Act.
- The levy of interest on the underpayment of provisional tax of Rx in terms of section 89quat of the Income Tax Act.
- The levy of an underestimation penalty of Rx in terms of par 20 of the 4th Schedule to the Income Tax Act.

The law

[Provide the sections in the Act that applies to the matter under dispute. Also add any additional information that supports the legal contentions made by the taxpayer, e.g. case law, Advance Tax Rulings, Foreign Case law etc.]

Application of the law

[**Apply the law to the Taxpayers specific situation. Highlight areas in law or in facts where the taxpayer disputes any SARS contentions.**]

Lodging an objection: Template letter

Summary

In summary, we kindly request that SARS allows the following objections:

[Repeat the specific items on the tax assessment being objected to and summarise in a sentence the grounds on which the objections are based.]

[Top Tip: Once the objection letter is completed, reconsider if the grounds of objection are complete. One is precluded from adding further grounds of objections on appeal. Also ensure that the language used is clear and not subject to misinterpretation.]

Please do not hesitate to contact the undersigned should you require any additional information.

Kind regards

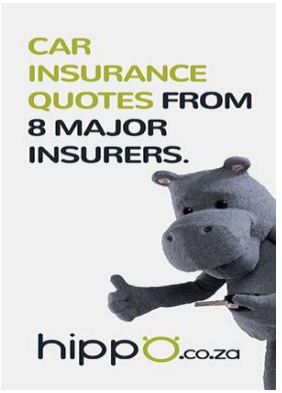
Name of Tax Practitioner
Tax Practitioner Ref Number

The Tax Faculty

Section 4:

Under section 4, we will deal with the future of tax audits with specific reference to increased data analytical capabilities of SARS and reliance on 3rd party data submissions.

Technology and impact on daily lives



kindle

travelstart

iTunes

LexisNexis

OnlineFitnessCoach.com

Uber

Uber Eats

property 24

NETFLIX

takealot.com

zapper™

The Tax Faculty

Technology even have an impact on religion

The Tax Faculty

Technology and Tax Compliance

SARS

e FILING

TaxJar®

The Tax Faculty

Reaction of role-players

- The Taxpayer
- SARS and Global Tax Authorities
- Tax Policy
- The accounting and Tax Advisory profession

The Taxpayer’s reaction to the digitisation of the economy

Move to shared service centres and decreased level of oversight by finance in transactions	• Move to automation of AFS, tax return preparation and tax return submissions. • Automation of accounting and tax treatment. More and more transactions are accounted for in its entirety without the finance departments having any oversight over the transaction. (e.g. Travelstart booking, iTunes, Amazon). SSC then simply prepare tax returns and file with tax authorities.
Small businesses are also operating globally – but lack access to tax expertise	• Physical location barriers are irrelevant • Tax legislation remains complex and the smaller business does not have access to expensive specialist advice
Increased uncertainty regarding global tax liabilities	• Transfer pricing is not applied consistently by tax authorities across the globe • Permanent Establishment tests and VAT presence tests have become outdated as they do not necessarily reflect economic presence. • Business evolved but tax legislation outdated.

The Tax Authority’s reaction to the digitisation of the economy

Align strategy to enable compliance with revised tax authority systems

Tax authority is tasked to "administer" the law. How can they do this in the digital economy where there is economic activity without physical presence?

Increased requirements for visibility (CbC Report, Master File, Local File)

Significant investment into technology

(Administration and visibility)

Investment in sophisticated data analytics to replace/enhance manual audits

Move away from "batch reporting" e.g. VAT and PAYE

Move away from "batch payments" and move towards real time payments and refunds.

Real-time transaction verification and compulsory transaction recording via tax authority systems

Increased collaboration amongst countries to address profit shifting

Companies and Intellectual Property Commission (CIPC)

http://www.cipc.co.za/index.php/xbrl-programme/

Driving Financial Compliance in the Digital Era

The Companies and Intellectual Property Commission (CIPC) embraces international best practices and the impact of the use of iXBRL when submitting Annual Financial Statements (AFS) online and in improving efficiencies. iXBRL will make it easier for Companies to report their financial information in an electronic format. CIPC **mandated** the digital reporting system for all qualifying entities from **1 July 2018.**

iXBRL is an Inline e*Xtensible Business Reporting Language* for electronic communication of business information providing major benefits in the preparation, analysis, communication of Annual Financial Statements.

Digital reporting in the format of iXBRL will assist companies with filing their Annual Financial Statements to egress from a PDF reporting format to a more structured format. This will ultimately reduce the burden of multiple submissions to different regulators.

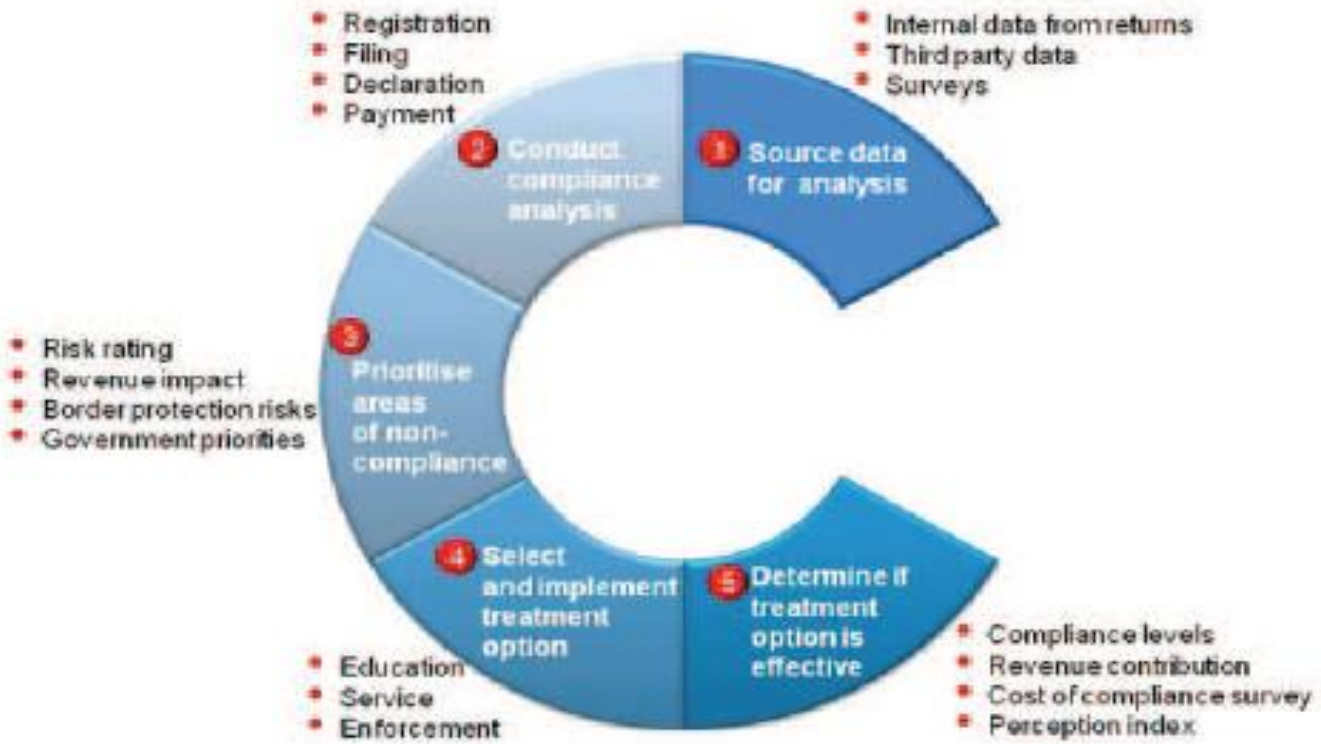
iXBRL Programme Objectives are:

- To reduce the administrative burden on businesses when they report financial information to government for regulatory compliance. Achieving this goal requires reducing duplication and inconsistency in business information reported to various government agencies - thus, a national (local taxonomy becomes a necessity; and
- To achieve regulatory compliance to accomplish the mission of the government agency. The CIPC's primary mission is to provide business and financial information to investors for better transparency and to reduce the administrative costs of reporting businesses.

Intention is to share information between SARS and CIPC. Discrepancies between AFS information in ITR 14 and CIPC AFS would lead to queries

COMPLIANCE PROGRAMME
2012/13 - 2016/17

OUR APPROACH IN DEVELOPING THE COMPLIANCE PROGRAMME



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Source
https://www.sars.gov.za/ClientSegments/Businesses/Mod3rdParty/Pages/Third-Party-Data-submission-at-a-glance.aspx

THIRD PARTY DATA SUBMISSION AT A GLANCE

The table below will give you an overview of the different third party data types:

Data	Who to submit	What to submit	How to submit	When to submit
IT3(b)	• Attorneys • Co-operative Banks • Banks (including Mutual Banks) • Estate agents • Long-term insurers • Postbank • State-owned companies that issue bonds, debentures or financial products • Organs of state (including the government in the national, provincial and local sphere) that issue bonds or similar financial products • Listed companies that issue bonds, debentures or similar financial products • Pension funds • Collective investment schemes etc.	Amounts that became due or payable or were paid or received in respect of, or by way of any investment, rental of immovable property, interest or royalty and Transactions that are recorded in an account maintained for another person i.e. transactional accounts like bank accounts	• eFiling, HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on IT3 (b), view the IT3 Data Submission External BRS.	Every six months: • **6 month submission:** March - 31 August (Submissions close by 31 October) • **Full year submission:** 1 March - 28/29 February (Submissions close by 31 May)

Investment income, interest, royalties, bank transactions.

IT3(c)	• Banks (including Mutual Banks) • Postbank • Financial Institutions • Co-operative Banks • Long-term insurers • Pension funds • Collective investment schemes • Organs of state (including the government in the national, provincial and local sphere) that issue bonds or similar financial products • Listed companies that issue bonds, debentures or financial products • State-owned companies that issue bonds, debentures or financial products etc.	Amounts paid in respect of the purchase and disposal of financial instruments.	• eFiling, HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on IT3 (c), view the IT3 Data Submission External BRS.	Every six months: • **6 month submission:**_ 1 March - 31 August (Submissions close by 31 October) • **Full year submission:** 1 March - 28/29 February (Submissions close by 31 May)
IT3(e)	• Co-operatives including any person who purchases livestock, produce, timber, ore, mineral or precious stones from a primary producer other than for retail purposes etc.	Monies paid in respect of a purchase, sale, or shipment of livestock, produce, timber, ore, mineral, precious stones, or by way of a bonus.	• eFiling, HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on IT3(e), view the IT3 data submission External BRS.	Submissions are done every six months: • **6 month submission:** 1 March - 31 August (Submissions close by 31 October) • **Full year submission:** 1 March - 28/29 February (Submissions close by 31 May)

Financial Instruments

Specific high risk trade.

IT3(s)	• Co-operative Banks • Banks (including Mutual Banks) • Long-term insurers • Collective investment scheme managers • Government (national sphere) etc.	General account demographics and financial values. In addition the Contributions, Transfers In, Transfers Out and Withdrawal according to the rules of the relevant BRS. Amounts received by or accrued to a natural person in respect of a tax free investment	• eFiling, HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on IT3 (s), view the IT3 data submission External BRS.	Every six months: • **6 month submission:** 1 March - 31 August (Submissions close by 31 October) • **Full year submission:** 1 March - 28/29 February (Submissions close by 31 May)
IT3(f) Insurance	• Long-term insurance companies etc.	All Retirement Annuity contributions made by the member, for the year of assessment.	• HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on IT3 (f), kindly view the Insurance Payments External BRS.	Every six months: • **6 month submission:** 1 March - 31 August (Submissions close by 31 October) • **Full year submission:** 1 March - 28/29 February (Submissions close by 31 May)
IT3(f) Medical	• Medical Schemes etc.	All medical contributions made by the member for the year of assessment. Included in the record should be: all expenses not covered by the medical aid, number of dependants	• HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on IT3 (f) view the Medical Scheme Contributions External BRS.	Every six months: • **6 month submission:** 1 March - 31 August (Submissions close by 31 October) • **Full year submission:** 1 March - 28/29 February (Submissions close by 31 May)

Contributions, Fund transfers and withdrawels

RAF

Medical aid contributions

Automatic Exchange of Information

AEOI (FATCA)	Reporting South African Financial Institutions as defined in the Inter-governmental Agreement e,g, the financial institutions (FI's) covered by the IGA means Custodial Institutions, Depository Institutions, Investment Entities and Specified Insurance Companies.	The financial information to be reported with respect to U.S. Reportable Accounts includes interest, dividends, and account balance, income from certain insurance products, sales proceeds from financial assets and other income generated with respect to assets held in the account or payments made with respect to the account. Reportable accounts include accounts held by individuals and entities (which includes trusts), and the IGA includes a requirement to look through passive entities to report on the relevant Controlling Persons.	• HTTPS or Connect Direct for data submission For more information on AEOI-FATCA, view the Automatic Exchange of Information External BRS.	Once a year: For the full year 1 March to 28/29 February – by 31 May.
AEOI (CRS)	For purposes of the CRS, Financial Institutions resident in SA (referred to as Reporting Financial Institutions or RFIs) that must apply the prescribed due diligence requirements to find reportable accounts and report the prescribed information, include any Financial Entity (whether a legal entity or legal arrangement such as a trust or partnership) that is a Custodial Institution, a Depository Institution, an Investment Entity, or a Specified Insurance Company. Certain Financial Institutions or financial accounts are specifically excluded under the CRS. The CRS Regulations give a generally description of exclude FIs or accounts and specific exclusions are listed in Annex 1 and Annex 2 to the regulations.	For the CRS, the information required for account reporting is described in Section I of the CRS Regulations.	• HTTPS or Connect Direct for data submission For more information on AEOI CRS, view the CRS Common Reporting Standard.	Once a year: For the full year 1 March to 28/29 February – by 31 May.

WTI (part of IT3(b)	Any person who pays an amount of interest to or for the benefit of a foreign person, to the extent that it is regarded as being from a source in South Africa,	Data as per the Withholding tax on interest return (WT002)	• eFiling, HTTPS or Connect Direct for data submission • eFiling to submit declaration For more information on WTI view the IT3 data submission External BRS.	Every six months: • **6 month submission:** 1 March – 31 August (Submissions close by 31 October) • **Full year submission:** 1 March – 28/29 February (Submissions close by 31 May) See the WTI page for first year submission rules
Dividends Tax	• South African tax resident companies; • Foreign companies whose shares are listed on the JSE; or • Regulated intermediaries (as defined in section 64D(1)) Insofar as they (other than a headquarter company) pay a "dividend" as defined in section 64D(1), which includes dividends and foreign dividends.	Dividends Tax is payable by the beneficial owner of the dividend, but is withheld from the dividend payment and paid to SARS by a withholding agent. The person liable for the tax, however, remains ultimately responsible to pay the tax should the withholding agent fail to or withhold the incorrect tax. An exception to this general principle is where a dividend consists of a distribution of an asset in specie, resulting in the liability for the tax falling on the company itself (such as with STC), which means that it may not withhold the tax from the dividend payment.	• eFiling (DTR01 form) • HTTPS, • Easy File or • Connect Direct For more information on DWT view the Administration of Dividends Tax BRS.	Submission done monthly if dividend declared.

Interest to foreign person

Dividends

Section 234(2)

(2) Any person who wilfully or negligently fails to—

(*d*) submit a return or document to SARS or issue a document to a person as required under a tax Act;

is guilty of an offence and is liable, upon conviction, to a fine or to imprisonment for a period not exceeding two years.

AUTOMATIC EXCHANGE OF INFORMATION (FATCA AND CRS)

https://www.sars.gov.za/ClientSegments/Businesses/Mod3rdParty/AEOI/Pages/default.aspx

What is Automatic Exchange of Information (AEOI)?

This information is required by law (US Foreign Account Tax Compliance Act (FATCA) and the OECD Common Reporting Standard (CRS)) to be collected by financial institutions around the world for reporting to tax authorities. Tax authorities will exchange this information to help make sure everyone pays the right amount of tax.

As part of the administration of the tax Acts as set out in the South African Tax Administration Act, SARS may provide administrative assistance to foreign governments under an international tax agreement, such as a Double Tax Agreement (DTA) or other multilateral or bilateral information exchange agreements between South Africa and foreign countries. In turn, these foreign countries may also provide similar administrative assistance. The three forms of information exchange between tax authorities are spontaneous exchange, exchange of information on request (EOIR) or automatic exchange of information (AEOI).

AEOI involves the systematic and periodic transmission of "bulk" taxpayer information by the source country to the residence country concerning various categories of income. In addition, information concerning the acquisition of significant assets may be used to evaluate the net worth of an individual, to see if the reported income reasonably supports the transaction. As a result, the tax authority of a taxpayer's country of residence can check its tax records to verify that taxpayers have accurately reported their foreign source income or assets. Thus AEOI has a deterrent effect on tax evasion and promotes voluntary compliance.

Greater transparency and AEOI between tax administrations is an important step forward in countering cross border tax evasion, aggressive tax avoidance and base erosion and profit shifting (BEPS) through, for example, transfer pricing arrangements. As a result AEOI has become a new international standard, in addition to EOIR.

Some personal views….

The accounting and tax profession is changing dramatically

Tax Return preparation is becoming increasingly automated. In the next 5 – 10 years, there will be no monthly VAT and PAYE returns filed. Tax will be paid per transaction as all transactions flow via the SARS system

Annual Financial Statements are increasingly antiquated and historical – the investor requires real time information and place less reliance on historical data. It will continue to play a role in Tax Reporting but the role will move to integrity of prior tax data provided (e.g. IT 14SD recons).

Regular automated reporting will become more relevant with the role of the auditor evolving to regular testing of the systems and controls producing that data. Potential competition from software providers that can provide automated assurance?

ITR 14's will become relevant only insofar as "audits" and Pillar 1 and Pillar 2 payments are concerned. Increased focus on provisional tax payments. With reliable technology with minimised human intervention, provisional taxes can be made monthly.

DISCLAIMER:

Nothing in this presentation should be construed as constituting tax advice or a tax opinion. An expert should be consulted for advice based on the facts and circumstances of each transaction/ case. Even though great care has been taken to ensure the accuracy of the answer, neither SAIT nor The Tax Faculty accept any responsibility for consequences of decisions taken based on this query and answer. It remains your own responsibility to consult the relevant primary resources when taking a decision.

The Tax Faculty