

SYNOPSIS

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In this issue



Tax amnesty extraordinarily generous! 2



The new social security tax . 3



Time limits - appeals against SARS determinations 5



Learnership allowance 6



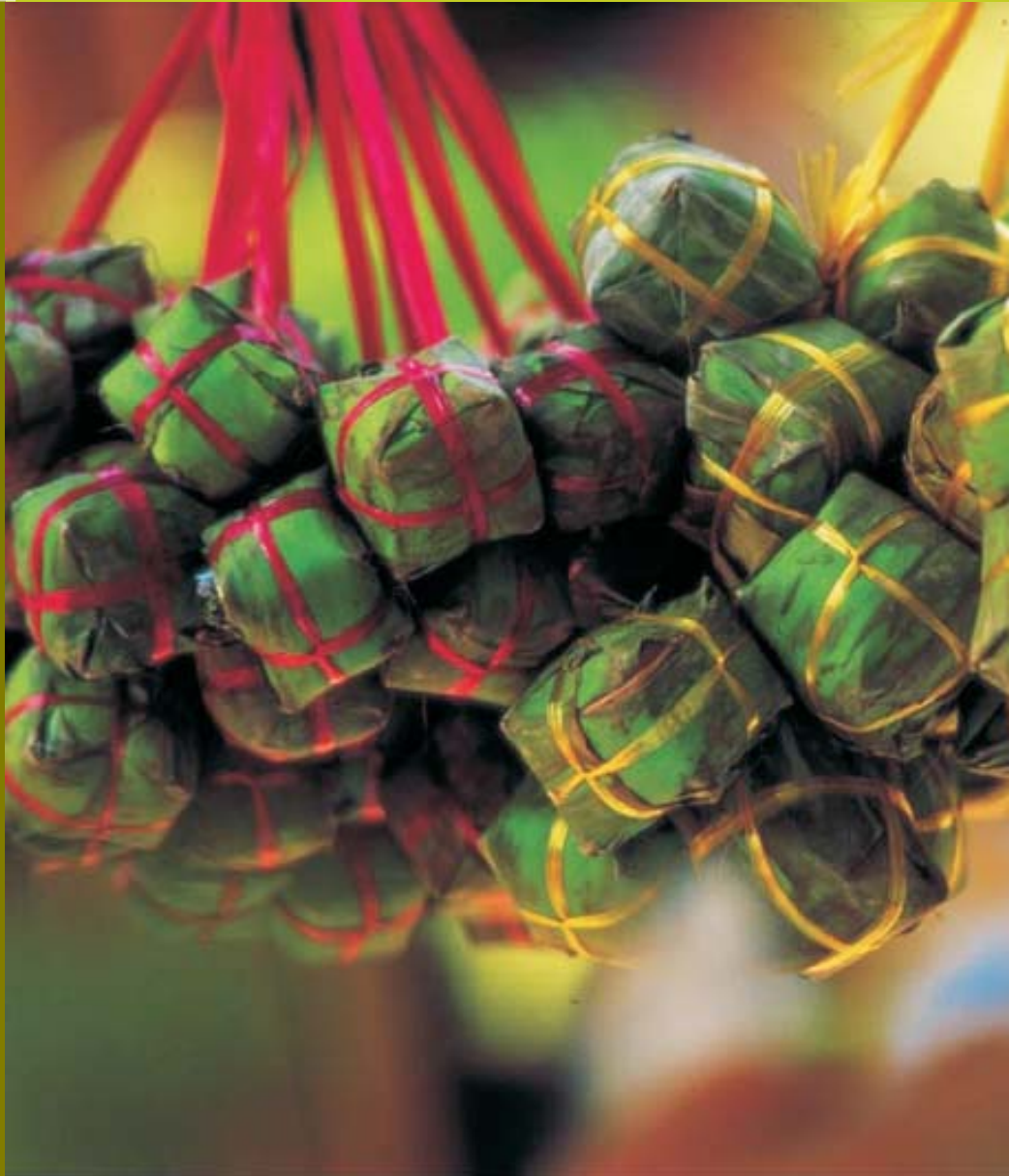
Formalised rulings under ATR system 7



Additional tax not a criminal penalty 8



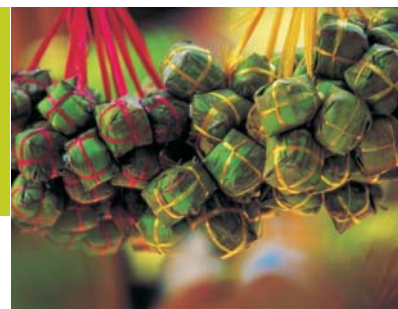
Draft regulations on writing-off of tax debts. 9



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Tax amnesty extraordinarily generous!



The small business tax amnesty, provided for in the Small Business Tax Amnesty and Amendment of Taxation Laws Act no 9 of 2006, is extraordinarily generous. Any non-compliant taxpayer ought to seize the opportunity to regularise his tax affairs for the bargain price of the modest levy laid down in section 6 of the Act.

Section 13 of the Act provides that the Minister can, by regulation, prescribe the circumstances in which the Commissioner can waive, in whole or in part, any additional tax, penalty or interest payable by a person who satisfies the requirements for amnesty as set out in section 2 of the Act, but to whom the tax amnesty relief will not apply as a result of the provisions of section 10(b) or (c) of the Act. These two sub-sections state that the tax amnesty does not apply to any tax, levy, contribution, interest, penalty or additional tax to the extent that it –

- is or becomes payable in consequence of any information which was furnished to the Commissioner by the applicant or his representative in any return, declaration or otherwise before the submission of the amnesty application; (in other words, where the taxpayer – no doubt unaware of the forthcoming amnesty – had confessed his transgressions to SARS before applying for amnesty);
- is payable by the applicant in terms of an assessment issued by the Commissioner before the submission of the application; (in other words, amnesty is not available in respect of tax, additional tax, interest and penalties due in terms of an assessment issued by SARS before the taxpayer made his amnesty application).

The draft regulations, issued by SARS on 24 January 2007 for comment by no later than 9 February 2007, allow the Commissioner, in effect, to extend the amnesty albeit via the different mechanism of the waiver of tax, to an applicant who did not qualify for amnesty because of the operation of either of the bulleted points above.

Indeed, the draft regulations say that the Commissioner “must” approve the application for waiver if the applicant meets the stipulated requirements.

However, as the draft regulations make clear, the waiver is possible only in relation to additional tax, penalties and interest, and not to the principal amount of tax.

Paragraph 7 of the draft regulations further narrows the scope of a potential waiver by providing that the Commissioner is not permitted to effect a waiver if, before the application for the waiver –

- the sheriff of the High Court has attached the assets of the applicant in execution of a warrant of execution obtained by SARS in respect of a business tax debt;
- sequestration or liquidation proceedings have been instituted against the applicant; or
- the Commissioner has given notice to the taxpayer of an audit or investigation into a failure to comply with tax legislation, unless that notice is withdrawn or the audit or investigation has been concluded.

Another limitation on the scope of the waiver is that the Commissioner cannot waive a “business debt” (which is defined as the additional tax, interest and penalty) to the extent that it exceeds R1 million.

The regulations are still in draft form and may well undergo further amendment. In terms of section 13(3) of the Act the regulations must be submitted to parliament for scrutiny at least 30 days before they are published, and that scrutiny could give rise to further amendments.



The new social security tax

Retirement savings are to be compulsory

In his State of the Nation address on 9 February 2007, President Mbeki said that – “the contributory earnings-related pillar of our social security system is missing or unreliable for large numbers of working people. The principle guiding this approach is that, over and above social assistance provided through the government budget, we need to explore the introduction of an earnings-related contributory social security system”.

The particulars of the proposed scheme are contained in a confidential concept document, thus far made available only to Cabinet. Further details may be made public in the Budget review.

Press reports suggest that what is envisaged is a new system in which retirement saving will become compulsory and “all working South Africans will have to pay about 15% of their income into a new government-subsidised pension fund or to an approved private fund”.

The new scheme, say reports, will provide basic health care and a pension of about 40% of the contributor’s

last pay cheque. Those who want a higher pension than this will have to take out additional cover privately, but without any tax breaks.

Cabinet agreement on the three pillars of the new scheme

The new plan is still to be discussed with business and labour, but there is reported to be agreement within Cabinet on the three pillars of the new scheme, namely –

1 current state pensions and grants, currently paid to about 11 million people, will continue;

2 the new social security tax will finance basic retirement savings as well as death, disability, and unemployment benefits; and

3 a wage subsidy will be introduced for new entrants to the job market and for low-income earners.

Universal pension benefits

Under the new plan, all women over 60 and men over 65 will be paid a state pension of R850 per month. Those who had contributed to retirement funding during their working life will be paid an additional pension that will be partly dependent on how the invested funds have performed.

The tax-deductibility of contributions

If a recommendation contained in a confidential concept document drafted for the cabinet is accepted, the current tax relief for pension fund contributions will be partly or entirely withdrawn and medical-aid contributions will be loaded in order to fund post-retirement medical aid insurance.

Obligatory or elective contributions

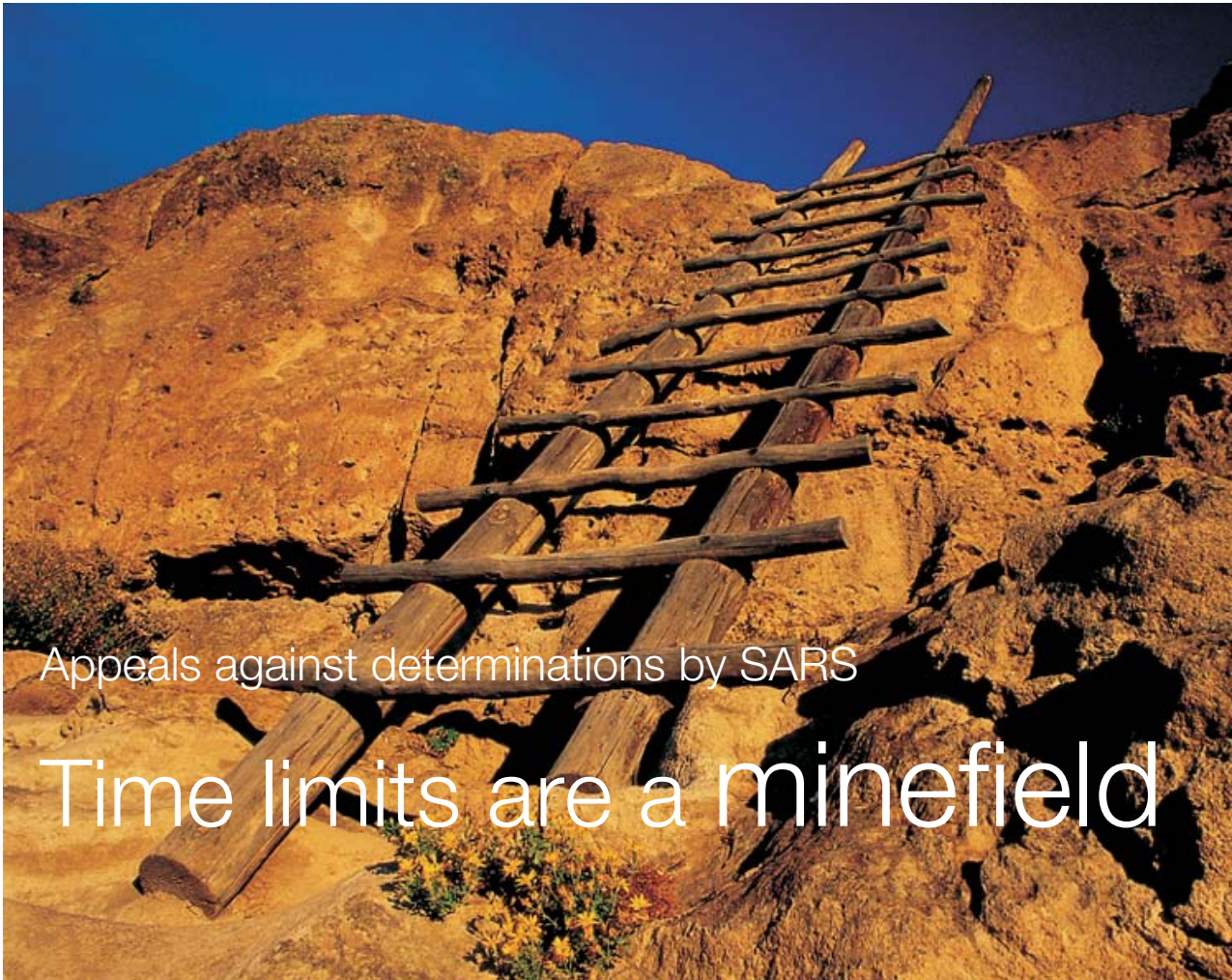
Initial press reports suggest that contributions to the government pension fund will not be obligatory, but that private funds will have to satisfy stringent requirements in order to qualify for registration as “approved investment agents”.

It seems doubtful whether an open election of this kind will be workable, since affluent workers would, if given the choice, prefer to pay into a private fund in which their contributions will not be used to subsidise benefits for other contributors. Press reports have said that government officials concede that, “There will be an element of cross-subsidy from the affluent to the poor”.

The Minister of Social Welfare has been quoted as saying the scheme will be phased in over three years.

Detailed proposals are to be published for public comment in May.





Appeals against determinations by SARS

Time limits are a minefield

Time limits laid down in legislation for the taking of particular steps to contest tax liability are a minefield for taxpayers and their professional advisers. Where time limits are exceeded, the result may be that the case is decided on that technical point alone, and the merits of the case are never considered.

The time limits for lodging objections and appeals under the Income Tax Act are well-known, but those in other tax legislation are easily overlooked.

The decision in *Colgate Palmolive (Pty) Ltd v CSARS 2007 (1) SA 35 (N)* concerned the interpretation, in the context of the Customs and Excise Act 91 of 1964, of the requirement that an “appeal” against the classification, by SARS of imported goods be “prosecuted” within a period of one year from the date of the determination by SARS of the correct classification.

The classification at stake in this case had huge financial implications for the parties, as it determined whether the goods in question could be imported duty-free.

SARS made the determination in question on 28 April 2004. The taxpayer lodged an appeal against the determination in the Durban & Coast Local Division of the High Court on 22 April 2005, in other words, just within the statutory one-year period.

The taxpayer thereafter formally transferred the proceedings to the Natal Provincial Division of the High Court.

At the hearing of the appeal, SARS argued as a point *in limine* that the Durban & Coast Local Division did not have jurisdiction to hear the matter, and that the transfer to the Natal Provincial Division had taken place well after the one-year period within which to prosecute an appeal. Hence, so it was argued, the taxpayer’s right to pursue the appeal in the latter court had prescribed.

Time limits for the taking of steps to contest tax liability

The Natal Provincial Division held that the Durban & Coast Local Division did not have jurisdiction to hear the appeal, but that the proceedings instituted in that court were not, on that account, a complete nullity. The court went on to hold that, in any event, it had power under the Act to extend the one year period for the prosecution of an appeal where the interests of justice so require.

The court held that the interests of justice did indeed so require. In the present case, said the court, there

would be no prejudice to SARS if the period were to be extended, but there would be serious financial consequences for the taxpayer if it were not.

The court held that it was satisfied that the application for an extension of time to prosecute the appeal ought to succeed. That disposed of the point in limine advanced by SARS, with the result that the court was then free to consider the merits of the case.



Interpretation Note 20 (issue #2) Learnership allowance

The learnership allowance, provided for in section 12H of the Income Tax Act, is of great importance to employers and employees alike, and is a substantial tax incentive for job creation.

The statutory provisions, and in particular the compliance provisions for the employer, are complex. Interpretation Note 20, which explains the learnership allowance in plain language was first issued on 5 March 2004.

The reissue, in draft form, of the Interpretation Note in December 2006, is an update which takes account of amendments to section 12H, which were effected by section 22 of the Revenue Laws Amendment Act 31 of 2005 and section 25 of the Small Business Tax Amnesty and Amendment of Taxation Laws Act 9 of 2006.

As the re-issued draft Interpretation Note makes clear, the learnership allowance is available in addition to other deductions claimable by taxpayers in respect of expenditure incurred in the employment and training of employees.

Extended to 30 October 2011

The learnership allowance was due to expire in October 2006 but has now been extended to apply to learnership agreements entered into before 30 October 2011.

A deduction is allowed in the tax year in which the registered learnership agreement was entered into between a learner and an employee and also in the tax year in which it was completed by a learner. Where commencement and completion occur in the same year, an allowance is claimable in that year in respect of both events.

Workings of learnership allowance

The Interpretation Note explains, in plain language, the operation of the learnership allowance and gives useful worked examples by way of illustration. The note clearly explains to employers the requirements to be complied with in order to qualify for the allowance, the circumstances in which no allowance is available, and the circumstances in which a learnership allowance will be regarded as having been recouped.

An annexure to the Interpretation Note gives a flowchart to assist in determining whether an employer is eligible for an allowance in respect of a learnership agreement or contract of apprenticeship.

Formalised rulings under ATR system

The Advance Tax Ruling System (the ATR system), provided for in Part IA of Chapter III of the Income Tax Act, came into effect on 1 October 2006 in terms of a presidential proclamation under the Second Revenue Laws Amendment Act, 2005.

This brought into force the provisions regarding binding general rulings (section 76P), binding private rulings (section 76Q) and non-binding written opinions (section 76I), but not the provisions governing binding class rulings (section 76R).

Before the introduction of the ATR system, South Africa did not have a formal tax rulings system. Nonetheless, taxpayers often approached SARS for guidance or a view on the interpretation of provisions of tax

Taxpayers who received informal rulings prior to 1 October 2006 can now apply for them to be given the status of non-binding rulings under the ATR system.

legislation administered by SARS. In certain circumstances, SARS acceded to those requests. There was, however, no statutory basis for SARS's responses to these requests, and those responses were consequently not binding on SARS or on the applicant taxpayers.

In terms of Interpretation Note 37 of 24 January 2007, read together with Interpretation Note 36 of the same date, taxpayers who received such informal rulings prior to 1 October 2006 can now apply for them to be given the status of non-binding rulings under the ATR system.



Formalised rulings under ATR system

This will accord such rulings a formal status, though their substantive effect will remain unchanged, in that they will still be of a non-binding nature.

Request for confirmation of prior, informal non-binding private rulings

The procedure to be followed is the same as for binding private rulings (as set out in section 76E), save that no fees will be payable.

Taxpayers who have received written statements from SARS under the prior informal system may request that the Commissioner grant these prior written statements binding effect in terms of section 76I(4). The procedure to be followed in making such requests is set out in Interpretation Note 37. Where a non-binding private opinion was requested or issued after 1 October 2006 (in other words, after the new ATR system came into effect) no request for such non-binding opinions to be given binding status will, under any circumstances, be entertained.

Request for prior non-binding statement to be given binding effect

A taxpayer who requests, in terms of section 76I(4) that binding effect be given to a prior written statement must –

- complete form ATR1;
- attach all the required documentation; and
- submit the completed form and annexures to the Binding Private Rulings section of SARS.

All such requests must be submitted by e-mail or fax and must be marked “confirmation of prior written statement”.

The deadline for such requests is 30 June 2007, and no late requests will be considered.

Only written statements in respect of a “proposed transaction” will be considered. If the transaction has already occurred, no ruling can be obtained; unless the transaction will recur in the future.

In order for a binding ruling to be given, all the parties and all the relevant facts and circumstances and details of the particular transaction must be disclosed. Requests will not be granted where the prior written statement was originally granted on an anonymous basis or in respect of generic, hypothetical transactions or fact patterns unless such disclosure is now made.

Application fees and cost recovery fees

Interpretation Note 38 sets out the application and cost recovery fees chargeable for the issuing of binding private rulings. These fees are prescribed by the Commissioner.

The Interpretation Note sets out the scale of the application fee, namely R2 500 for small, medium and micro-enterprises (as defined in the Interpretation Note) and R10 000 for all other taxpayers.

The cost recovery fee has two components. The first is an hourly charge for the time spent by the tax specialists during the rulings process, which ranges from R400 to R500 and an estimated time of completion ranging from

20 to 60 hours or more for extraordinary cases. SMMEs are not charged for the first eight hours of time spent on their application.

Additional tax not a criminal penalty

In case 11641 (Johannesburg Tax Court; 4 December 2006, not yet reported) the taxpayer appealed against an assessment imposing liability for additional tax in terms of section 76(1)(a) of the Income Tax Act 58 of 1962. The grounds of the appeal were that it is unconstitutional for SARS to impose additional tax where the taxpayer has already paid an admission of guilt in terms of section 75(1)(a).

The additional tax had been imposed on the taxpayer for failure to submit income tax returns for the 1994 – 1998 years of assessment. He had been charged in the magistrate's court with a contravention of section 75(1)(a) and, after submitting the returns, he paid an admission of guilt fine of R300 for each year of assessment.

SARS thereupon imposed additional tax in terms of section 76(1)(a) for the late submission of the returns.

The Tax Court held that additional tax, payable in terms of s 76(1)(a) of the Income Tax Act 58 of 1962, is a penalty of an administrative nature which cannot be equated to a fine imposed by a criminal court. Hence, it was not a breach of the taxpayer's constitutional rights for him to be assessed to additional tax in terms of s 76(1)(a) after being convicted of an offence under section 75(1)(a); this did not amount to a second punishment for the same act, nor did it infringe the double jeopardy rule.



No challenge to the constitutionality of the legislation

In this case, the constitutionality of provisions of the Income Tax Act was not under challenge, but rather the manner in which SARS had applied those provisions.

Section 172(2)(a) of the Constitution provides that –

“The Supreme Court of Appeal, a High Court or a court of similar status may make an order concerning the constitutional validity of an Act of Parliament ...”

It has been held that that, although the Tax Court has certain features in common with the High Court, it is not a court of “similar status” to the High Court, and therefore does not have the power to make an order concerning the constitutional validity of an Act of Parliament. (See the case of VAT 304, decided in the Pretoria Tax Court and discussed in *Synopsis*, January 2006.)

Draft regulations on writing-off of tax debts



A clearly-defined process is laid down to extinguish irrecoverable tax debts

On 31 July 2006, draft regulations were issued in terms of section 91A of the Income Tax Act 58 of 1962, prescribing the circumstances under which SARS is empowered to write off or waive any tax, duty, charge, interest, penalty or other amount. See the discussion in Synopsis, August 2006.

On 24 January 2007, a second draft of those regulations was issued, for public comment by no later than 9 February 2006.

In this second draft, the fundamentals remain unchanged, but there have been numerous changes to terminology and other particulars.

The concept of a compromise has been introduced

Inter alia, the new draft introduces the concept of and the definition of a “compromise” between SARS and a debtor, and the definition section changes the definition of “write off”

from a “decision not to pursue recovery of a tax debt” (which implies that the tax debt remains in existence) to “to reverse a tax debt” which, in the case of a temporary write-off does not absolve the debtor from liability (see regulation 4(2)). A permanent write-off of the debt in terms of regulation 6 implies that the debt ceases to exist.

A temporary write off is essentially a unilateral moratorium on recovery proceedings, but the tax debt continues to incur interest (regulation 4(3)).

Overview

As with the first draft of the regulations, a clearly-defined process is laid down to extinguish irrecoverable tax debts and thereby clear SARS's books of worthless bad debts.

Although the regulations are intended to benefit the State, they will have an incidental benefit for taxpayers, in that they will be able to formally apply to SARS for the writing-off of a tax debt, and elicit a formal response.

Furthermore, the regulations formally give SARS the power to "temporarily write off an amount of tax debt", which is in essence a moratorium on any attempt to recover the debt.

Under the new draft regulations, a permanent write-off of a tax debt can be achieved by a compromise between SARS and the debtor; see regulation 6(1)(b). SARS is not bound by a compromise if the debtor did not make full disclosure, or supplied materially incorrect information, or if the debtor fails to comply with any provision of the agreement with SARS, or if the debtor is liquidated or sequestrated before fully complying with the agreement; see regulation 14.

A tax debt cannot be written off or compromised unless it would benefit the State

As before, the fundamental tenet of the regulations is that the writing-off or compromise of a tax debt will only occur if it would be for the benefit of the state (see regulation 2(2)), and not on account of any hardship suffered by the taxpayer (see regulation 12(g)). If payment of the due tax can be squeezed out of the taxpayer, even by sequestration or liquidation, then this must be done.

As before, the regulations apply only in respect of a tax debt which is not disputed by the debtor (regulation 3).

In determining whether a tax debt is uneconomical to pursue, the regulations now provide that one of the factors to be taken into account is the financial position of the debtor, including assets, liabilities, cash flow and future income streams; see regulation 5(2)(g).

Conditions for permanent writing-off of tax debt

SARS can permanently write off a tax debt if, inter alia, the Commissioner is satisfied that it is "irrecoverable at law" (regulation 6(1)(a)) which is defined as meaning that it cannot be recovered by a court judgment, or

that it is owed by a debtor who has been liquidated or sequestrated with no further dividend payable, or following a compromise or arrangement under section 311 of the Companies Act which has been sanctioned by the court (regulation 7(1)).

A tax debt is not "irrecoverable at law" if the debtor is a company or trust and the Commissioner has not first explored action against or recovery from the personal assets of any director, shareholder, trustee or manager (regulation 7(2)).

The definition of the circumstances in which the total cost of recovery of a tax debt will in all likelihood exceed the recoverable amount (which was previously set out in regulation 5(3)) has been dropped.

The regulation dealing with the circumstances in which it is not appropriate to write off a tax debt has been redrafted; see regulation 12.

A taxpayer can apply to SARS for a tax debt to be compromised, and the regulations prescribe the procedure for doing so (regulation 10). The regulations prescribe the factors to be taken into account by SARS in considering such an application (regulation 11) and define the circumstances in which it is not appropriate to compromise the debt (regulation 12).

If SARS does accede to an application to compromise a tax debt, the Commissioner and the taxpayer must sign an agreement to that effect, in which the Commissioner undertakes not to pursue recovery of the balance of the tax debt, and sets out any conditions to which the compromise is subject (regulation 13).

