DLA CLIFFE DEKKER HOFMEYR

TAX ALERT

21 September 2012

IN THIS ISSUE

BANK SECRECY – THE DIFFERENCE BETWEEN THEORY AND REALITY

Bank secrecy (or the lack thereof?) has recently been in the news all over the world.

Global changes relating to bank secrecy will accelerate and could especially impact the High Net Worth Individual (HNWI) constituency. South Africans in that category should take note.

Unfortunately the theoretical (read statutory) foundation of banking secrecy and how things pan out in real life are often very different. HNWI's on both sides of the Atlantic can attest to that.

The South African legal position regarding bank secrecy was analysed in a case where a SA big-four bank took on Noseweek magazine in *FirstRand Bank Ltd v Chaucer Publications (Pty) Ltd 2008(2) SA 592 (CPD)*. Traverso DJP pointed out that a banker's contractual obligation to preserve the confidentiality of its client's banking affairs had long been recognised in English law (*Tournier v National Provincial & Union Bank of England [1924] 1 KB 461*). It was a qualified legal right arising *ex contractu*. Locally, a banker's duty of confidentiality had been recognised as early as 1914 (refer *Abrahams v Burns 1914 CPD 452*). Judge Traverso concluded: "It seems to me that for considerations of public policy the relationship between a bank and its client must be of a confidential nature. Equally – for considerations of public policy – this duty is subject to being overridden by a greater public interest". She also noted that, although the duty not to disclose rests with the bank, the privilege not to have the details of the dealings with the bank disclosed belonged to the client. It was therefore the client alone who could invoke this privilege and insist on the bank keeping its client's information confidential.

But often there is a disconnect between what the law says and what happens at the coal face.

The theft of confidential bank data and the on-selling of it to revenue authorities is big business these days. A 'gold mine' of data stolen from the LGT bank (owned by the Lichtenstein royal family) during 2008 found its way to the German tax authorities via a LGT employee. He received €4.2 million. The data was used, amongst other things, to convict the CEO of Deutsche Post of tax evasion. Germany's Constitutional Court expressly ruled that such stolen data could be used in further tax probes: "The constitution knows no rules saying that a legally flawed collection of evidence in any case bars the use of that evidence."

In February 2010, the German state of North Rhine-Westphalia bought stolen discs containing the names of approximately 1,500 German account holders with Swiss bank Credit Suisse. Despite criticism the UK Revenue and Customs authority immediately approached Berlin to purchase the stolen data in order to detect potential UK tax evaders with hidden Swiss accounts. The Dutch, Belgian and Austrian governments also showed strong buying interest. In October 2010, the man suspected of the Swiss data theft (and who allegedly got €2.5 million for it) was found dead in his Swiss prison cell – according to police it looked like suicide.

As recently as late August this year Swiss private bank Julius Baer confirmed that it had discovered a 'case of data misuse'. The bank said that a Zurich employee acted alone and had been

continued

arrested. The thief had been paid 'an undisclosed sum' by the German tax authorities.

The amounts paid by revenue authorities to bank data thieves in Europe are paltry compared to what the IRS has on offer in the USA. Under the IRS whistleblower regime, an informant could potentially collect up to 30% of the proceeds in instances where the amount in dispute exceeds $2 million. On 11 September 2012, it was announced that the IRS had paid $104 million (approximately R820 million) to Bradley Birkenfeld who earlier supplied the IRS with in-depth information on how Swiss bank UBS had helped US clients to evade tax. According to Birkenfeld's lawyers it could be the largest pay-out ever to a single whistleblower. The award by the IRS followed Birkenfeld's exceptional cooperation and took into account the extensive information he gave on the UBS tax-fraud scheme. Birkenfeld's offering to the IRS was used during 2009 to strong-arm UBS into a $780 million settlement with the IRS. (Incidentally, as a UBS private banker, Birkenfeld once smuggled diamonds into the USA by concealing them in toothpaste. This was the exceptional service UBS high-value customers received. He served three years jail for his role in the UBS tax fraud scheme but indicated that he will seek a presidential pardon.)

Data theft by bank employees and the buying of data by revenue authorities has seemingly become a fast-growing international sport. Bradley Birkenfeld has shown that the prize money could be staggering. So expect the sport to attract new-comers and to make banks internationally shiver in their collective boots.

The OECD published a report on 26 October 2011. Its title is "*The era of Bank Secrecy is Over*". The first sentence of the Report reads: "In April 2009, G20 Leaders took action to end the era of bank secrecy". The OECD must be smiling at the support its efforts at destroying bank secrecy have been getting from banking insiders who have access to sensitive client data.

Of course the banks are not doing themselves any favours: HSBC's large-scale money laundering on behalf of cocaine cartels was documented in a mid-July US Senate report. That will mean more pressure on banks everywhere. The chairman of the Senate Committee already said "Ultimately, the rest of us are forced to pay more on our tax bills to make up for those who shirk their taxpaying responsibilities".

It seems that bank data (however obtained) will increasingly inform and direct revenue authorities' compliance actions.

Locally, information provided by SA banks to SARS as "third-party data", features as an important cog in SARS's compliance plan. The SARS Annual Report says: "The use of third party data to verify self-assessments by taxpayers and to perform risk-profiling is a growing trend in international tax administration. Third party data has several uses, including the pre-population of tax returns, as inputs into a risk-profiling engine, and even at border posts to profile incoming and outgoing travellers. Sources of third party data range from financial institutions, employers, credit bureaus to other government agencies (eg the Department of Home Affairs)".

Going forward revenue authorities will increase their attacks on bank secrecy. Banks will see ever-widening and invasive information requests.

The treasure troves of bank data have been prised open with help from bank employees eyeing lucrative whistleblower pay-outs. Legal precedent telling HNWI bank clients that bank secrecy is alive and well, and should be respected (also by revenue authorities), is unfortunately only part of the story.

Johan van der Walt

BINDING PRIVATE RULING 121: STC OR DIVIDENDS TAX?

During the transition phase from Secondary Tax on Companies (STC) to Dividends Tax at the beginning of April 2012 there had been some uncertainty as to whether particular dividends would be subject to STC or Dividends Tax with reference to the time of declaration or payment.

The uncertainty was partly caused by the co-existence of the STC provisions and the Dividends Tax provisions in the Income Tax Act, No 58 of 1962 (Act) and the perceived overlap of the application of some of these provisions, specifically with reference to terminology and timing.

However, s148 of the Taxation Laws Amendment Act, No 7 of 2012 made it quite clear that Dividends Tax would only apply in respect of dividends declared and paid on or after 1 April 2012.

The STC provisions would apply to dividends in respect of any other scenario, such as where a dividend was declared before 1 April 2012 but would only accrue or become payable thereafter.

In Binding Private Ruling 121, this particular question also arose. The applicant was a resident company, listed on the JSE, and the co-applicant was a non-resident company that had a secondary listing on the JSE. They both formed part of a global group. It is also understood that the shares of the applicant and co-applicant carried the same rights and that if a dividend was to be declared in respect of the applicant's shares, a matching dividend would be declared in respect of the co-applicant's shares.

The fact giving rise to the uncertainty in this ruling was that the board of directors of the applicant and the co-applicant had recommended, at the time of disclosure of the group's financial results (before 1 April 2012), that a dividend should be paid to the shareholders of the applicant and the co-applicant after 1 April 2012. This recommendation was subject to approval at the annual general meeting to be held after 1 April 2012.

continued

The question was whether such a recommendation fell within the ambit of 'declare' in s64B of the Act, and accordingly, whether there was a declaration of a dividend before 1 April 2012.

If there was such a 'declaration' before 1 April 2012, the STC provisions would have been applicable. It should be noted that the STC provisions generally only apply to residents. In other words, if the STC provisions were to apply, they would not apply to the co-applicant because it was a non-resident.

The term 'declared' in s64B(1) of the Act is defined as "in relation to any dividend (including a dividend in specie), means the approval of the payment of distribution thereof by the directors of the company or by some other person with comparable authority or, in the case of the liquidation of a company, by the liquidator thereof".

SARS ruled that the dividend would not constitute a dividend 'declared' before 1 April 2012 within the meaning of the definition of 'declared' in s64B(1) of the Act.

Accordingly, where the dividend would be declared and paid after 1 April 2012, it would be subject to dividends tax.

The ruling makes it clear that the entire dividend to be paid by the applicant would be subject to dividends tax because it was a resident company, and it fell within paragraph (a) of the definition of 'dividend' in s64D of the Act.

In respect of the co-applicant, only the dividend relating to the co-applicant's shares that are listed on the JSE would be subject to dividends tax because dividends paid by non-resident companies are only dividends to the extent they relate to locally listed shares. That is, they fall within paragraph (b) of the definition of 'dividend' in s64D of the Act.

Accordingly, it was ruled that the applicant and co-applicant would have to withhold dividends tax to the extent that exemptions or reductions in terms of tax treaties do not apply.

Heinrich Louw

DLA CLIFFE DEKKER HOFMEYR

CONTACT US

For more information about our Tax practice and services, please contact:

Emil Brincker
Director
National Practice Head
T +27 (0)11 562 1063
E emil.brincker@dlacdh.com

Alastair Morphet
Director
T +27 (0)11 562 1391
E alastair.morphet@dlacdh.com

Andrew Seaber
Senior Associate
T +27 (0)11 562 1768
E andrew.seaber@dlacdh.com

Ben Strauss
Director
T +27 (0)21 405 6063
E ben.strauss@dlacdh.co

Heinrich Louw
Associate
T +27 (0)11 562 1085
E heinrich.louw@dlacdh.com

Johan van der Walt
Director
T +27 (0)11 562 1177
E johan.vanderwalt@dlacdh.com

Tessmerica Moodley
Associate
T +27 (0)21 481 6397
E tessmerica.moodley@dlacdh.com

Ruaan van Eeden
Director
T +27 (0)11 562 1086
E ruaan.vaneeden@dlacdh.com

Carmen Moss-Holdstock
Associate
T + 27 (0)11 562 1614
E carmen.moss-holdstock@dlacdh.com

BBBEE STATUS: LEVEL THREE CONTRIBUTOR

JOHANNESBURG

1 Protea Place Sandton Johannesburg 2196, Private Bag X40 Benmore 2010 South Africa
Dx 154 Randburg and Dx 42 Johannesburg

T +27 (0)11 562 1000 **F** +27 (0)11 562 1111 **E** jhb@dlacdh.com

CAPE TOWN

11 Buitengracht Street Cape Town 8001, PO Box 695 Cape Town 8000 South Africa
Dx 5 Cape Town

T +27 (0)21 481 6300 **F** +27 (0)21 481 6388 **E** ctn@dlacdh.com

www.cliffedekkerhofmeyr.com