DLA CLIFFE DEKKER HOFMEYR

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TAX ALERT

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CRACKDOWN ON HNWI'S: WHAT COMES NEXT?

By now the theme is well-known: revenue authorities everywhere are looking to bolster government coffers; the wealthy are firmly in their sights.

It's no different locally. Could recent overseas developments therefore be indicative of where SARS might be heading with its recent crackdown on High Net Worth Individuals (HNWI's)?

As we know: "*All roads lead to Rome.*" Italy is reported to have one of the world's highest rates of tax evasion. The bond market has put Italy at the centre of the Euro zone debt crisis. Desperate times call for desperate measures: the comparison of taxpayers' declared incomes with third party data is old hat. New are the sniffer dogs at border posts detecting Italians trying to smuggle out savings in their luggage. Cash transactions have been capped at €1,000 to counteract the undervaluing of goods and services. A 2011 Saatchi & Saatchi ad campaign painted tax evaders as parasites living at the expense of others, so eroding the social fabric. The revenue agency says the ad campaign was "*...to increase tax compliance by changing the mentality.*" The tax collection agency Equitalia in Rome received two letter bombs last December. The first blew off part of the finger of its director general. An Italian anarchist group claimed responsibility. Scary stuff. Prime Minister Monti seethed that it was a "criminal act" against Italian institutions. He remains determined to find the €120 billion that tax evasion is costing his treasury annually.

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In South Africa, the Exchange Control (Excon) regime has for many years restricted capital flight. Treasury and the SA Reserve Bank have liberalised Excon extensively over the recent past. R5 million per annum can now effectively be invested off-shore, turning Excon into a non-event for most South Africans — therefore no dogs needed at OR Tambo Interntaional Airport sniffing suitcases (at least not for bank notes). SARS' ads, which borrow richly from a brandy manufacturer's "Eish" campaign, might not be Saatchi stuff, but what the heck? The local cash economy — now that's a different kettle of fish...

Next-door to Italy the Greek government have recently started "naming and shaming" tax evaders. A change in privacy laws was required, but after lengthy debates it's happened. Four thousand names of taxpayers owing €15 billion are there for all to see (and despise) – so sorry that not much of those billions is collectable. The chart topper is someone who owes €952 million and who has already been sentenced to 504 years in prison. A November 2011 EU report puts the unpaid taxes in Greece at €60 billion, ie approximately 25% of that country's economy.

Locally, section 4 of the Income Tax Act 58 of 1962 (the Act) provides for the preservation of secrecy in relation to a person's tax affairs (with certain exceptions). However, since 1998, the lesser known section 75A of the Act specifically empowers SARS to publish for general information certain personal particulars of individuals convicted of prescribed tax offences. So far SARS has used this power sparingly, but that could change. Nothing stops SARS following the Greek example.

As one commentator points out: "*Exploiting the social norming on tax compliance is clearly desirable from a government perspective. The social norms must be activated, or brought to mind before they can influence behaviour. The South African government has attempted to achieve this by stigmatising tax evasion through 'naming and shaming' of high-profile individuals.*"

On the other side of the Atlantic, the IRS reopened its voluntary disclosure program for off-shore accounts (off-shore VDP), on 9 January this year. Thirty-three thousand disclosures have been made and $4,4 billion collected under the previous two programs. The well-publicised criminal prosecutions of UBS and HSBC clients helped, of course. The revival of the IRS' off-shore VDP is part of the drive to eliminate tax evasion the world over. The reopened off-shore VDP will run indefinitely but the penalty has been increased to 27.5% (25% previously) of bank balances at a set point. The IRS says that penalties might increase further and the programme could be terminated at will.

South Africa's last Tax and Excon Voluntary Disclosure programs ran from November 2009 to 31 October 2010. Not much detail has emanated from the SARB or SARS regarding uptake and the amounts to be collected – the jury is still out.

The current Tax Administration Bill (TAB) provides in Chapter 16, Part B, sections 225 - 233 for a permanent voluntary disclosure mechanism. The TAB's disclosure dispensation by and large follows the model of the statutory Tax VDP which terminated last year. Taxpayers that have missed that boat would be able to come clean under the Tax Administration Act (TAA), once signed into law. However, expect the penalty and/or interest relief to be less generous. [Promulgation can probably be expected during the first quarter of 2012 with the TAA taking effect towards the middle of the year.]

SARS in its "*Strategic Plan 2010/11 - 2012/13*" mentions "voluntary compliance" and "enforced compliance" – fancy words for the old carrot and stick approach. In the HNWI space it will probably be no different: wealthy taxpayers will first be "Saatchi-ed" ie they will be urged through moral suasion "to do the right thing", to come clean and to comply fully of their own accord (simultaneously parting with some money). In parallel expect there to be some harsher measures potentially taking its toll on wealth, health and reputation.

SARS has already indicated that 9 300 HNWI's are under scrutiny (ie annual earnings in excess of R7 million, alternatively assets of more than R75 million).

Where appropriate, a serious look by exposed HNWI's at the TAA's VDP regime, once operative, might be worthwhile. At least any disclosure under that process occurs within the bounds of statutorily defined parameters.

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