TAX

IN THIS ISSUE

BIG BROTHER IS WATCHING YOU!

Even George Orwell, with his prophetic satirical insight, would have been confounded by the level of domestic and global surveillance that characterises our lives today. Not that all of it is as malignantly ubiquitous and pervasive as the notoriously illegal "Stellar Wind" programme conducted by the United States (US) National Security Agency (NSA) under the guise of cybersecurity. Indeed, given the objectives of the Organisation for Economic Development and Cooperation (OECD) Base Erosion and Profit Shifting (BEPS) Action Plan - to combat international tax avoidance by multinational enterprises (MNEs) and to secure government revenues - surveillance in the form of the inter-jurisdictional exchange of information and administrative assistance for tax collection purposes is not only justifiable but indispensable. Nonetheless, it behoves taxpayers to be alert to the rapidly expanding web of tax surveillance in which they operate.

In October 2014 the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum), the world's largest tax organisation comprising 125 member jurisdictions, held its 7th meeting in Berlin, Germany. South Africa was amongst the 101 jurisdictions represented at the meeting, at which the Global Forum members resolved to take "tax transparency to a new level." This resolve was evidenced by *inter alia*:

- the majority of Global Forum members committing to implement the new standard on the Automatic Exchange of Information (AEOI) by 2017; and
- the pledge of support to developing countries through facilitating their participation in AEOI and the launch of the Africa Initiative.

As an aside, it bears mention that Mr Kosie Louw, Chief Legal and Policy Officer of the Legal and Policy Division of the South African Revenue Service (SARS), who was appointed as the Chair of the Global Forum for the period commencing January 2013 to December 2014, was re-elected for a further two year term at the meeting held in October 2014.

Also in October 2014, the Forum on Tax Administration (FTA), the preeminent international body concerned with tax administration, comprising heads of tax administrations from the OECD, G20 and large emerging economies, met in Dublin, Ireland and agreed that increased co-operation would be necessary to implement the results of the BEPS project and AEOI. Among other items on the agenda, the FTA concurred on the need to invest resources on the implementation of the new standard on AEOI.

By way of background, in September 2013, G20 leaders endorsed the OECD proposal for a global model for AEOI and tasked the OECD, working in conjunction with G20 countries, to develop a new standard for AEOI to combat tax evasion and ensure tax compliance.

The new global standard on AEOI, which purports to reduce the possibility of tax evasion by enabling governments to recover tax revenue from evasive taxpayers, and bolster international efforts to enhance transparency, cooperation and accountability amongst financial institutions and tax administrations, while simultaneously minimising costs to governments and business - was approved by the OECD Council in July 2014. The new standard is strikingly similar to the model that many jurisdictions will employ to implement the US Foreign Account Taxpayer Compliance Act (FATCA).

AEOI requires jurisdictions to annually obtain non-resident financial account information from their financial institutions (ie deposit-taking banks, custodial institutions, and certain investment entities and insurance companies) and automatically exchange that information with the tax authorities in the account holders" (individuals and entities, including trusts and foundations) jurisdictions of residence. The AEOI sets out the financial account information (including account balances, interest, dividends, and sale and redemption proceeds from financial assets) to be exchanged, the financial institutions required to report, the different types of accounts and taxpayers covered, together with prescribed common due diligence procedures (drawn from international anti-money laundering standards) to be followed by financial institutions.

Further it is anticipated that the new standard on AEOI will precipitate ancillary benefits by encouraging taxpayers to voluntarily disclose information regarding formerly concealed assets.

As information is increasingly disclosed through AEOI, the importance of the existing standard of Exchange of Information on Request (EOIOR) will increase commensurately. EOIOR involves the inter-jurisdictional

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request by one competent authority for information from another competent authority; typically information relating to an examination of or investigation into a taxpayer's tax liability for a specified period.

The AEOI and EOIOR standards are intended to operate in conjunction with one another to improve the efficacy of tax administrations' endeavours to counter international tax evasion. The Global Forum has been tasked with monitoring the global implementation of the new standard on AEOI and assisting developing countries to benefit from it, consensus being that its implementation will stimulate the establishment of a global level playing field and ensure that jurisdictions transact on even ground.

At the Global Forum's 7th meeting, EOIOR was also advanced by the decision to incorporate into its Terms of Reference, the 2012 Update to Article 26 (Exchange of Information) of the OECD Model Tax Convention on Income and on Capital (Model Tax Convention) and its Commentary.

Briefly, Article 26 of the Model Tax Convention provides for the exchange of information by the competent authorities of Contracting States "*foreseeably relevant* for carrying out the provisions of (the Model Tax) Convention or to the administration or enforcement of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention." The EOI is not restricted by Articles 1 (Persons Covered) and Article 2 (Taxes Covered).

The Commentary provides that the standard of "foreseeable relevance" is intended to provide for EOIOR in tax matters to the broadest conceivable extent, while simultaneously clarifying that Contracting States are precluded from conducting "fishing expeditions," by requesting information unlikely to be relevant to the tax affairs of a particular taxpayer, or submitting speculative requests that have no apparent causal link to an open investigation or inquiry. The standard requires that at the time the request is submitted, a reasonable possibility exists that the requested information will be relevant. It is immaterial whether the information is actually proved to be relevant upon provision. As such a request may not be denied in circumstances where a definitive assessment as to the relevance of the information to an investigation can only be made pursuant to the receipt of such information. Contracting States are encouraged to consult in situations where the content of the request, the circumstances precipitating the request, and/or the foreseeable relevance of the requested information are opaque to the State subject to the request. However once the State submitting the request has provided an explanation as to the foreseeable relevance of the information requested, the State subject to the request may not deny the request or withhold the requested information because it believes that the requested information is irrelevant to the investigation process.

Similarly to the OECD Model Agreement on Exchange of Information on Tax Matters, a request for information does not amount to a fishing expedition merely because it fails to provide the name and/or address of the taxpayer under investigation. However in the absence of such information, the State submitting the request must include other information sufficient to identify the taxpayer. Further, although it may be more difficult to establish that a requesting State is not conducting a fishing expedition in relation to a group of taxpayers not individually identified, it may nevertheless meet the standard of "foreseeable relevance" by providing a detailed description of the group of taxpayers, together with the specific facts and circumstances precipitating the request, supplemented by an explanation of the applicable law such group of taxpayers are believed to have contravened or evaded.

Closer to home, alarm bells ought to be sounding for avid Tax Alert readers. In our Tax Alert edition dated 6 February 2015, we considered SARS' considerable power to request relevant material under s46 of the Tax Administration Act, No 28 of 2011 (TAA) and the extension of such power through the amended definition of "relevant material" provided for in the Tax Administration Laws Amendment Act, No 44 of 2014 (TALAA), which now means "any information, document or thing that in the opinion of SARS is foreseeably relevant for the administration of a tax Act …"

The Explanatory Memorandum to the TALAA provides that the standard for what is foreseeably relevant should have a low threshold. It states that it is sufficient that there is a reasonable possibility that the material is relevant for the purpose for which it is sought at the time the request is submitted. It is immaterial whether the information is actually proved to be relevant upon provision. As such a request may not be denied in circumstances where a definitive assessment as to the relevance of the material to an investigation can only be made pursuant to the receipt of such information.
The approach to adopt is to first produce the material and then allow for the subsequent determination as to relevance.

Déjà vu?

Let me leave you with these sobering facts:

- South Africa has exchange of information relationships with 119 jurisdictions through 78 Double Taxation Agreements (DTAs), 17 Tax Information Exchange Agreements (TIEAs) and 1 multilateral mechanism, Convention on Mutual Administrative Assistance in Tax Matters.
- Most recently, on 3 February 2015, South Africa gazetted the Protocol amending its DTA with India (signed 4 December 1996) in terms of which Article 25 (Exchange of Information) was deleted and replaced with a new Article 25 which broadens the scope thereof through the introduction of the OECD Model Tax Convention standard of "foreseeable relevance" and brings it into alignment with the 2012 updated version of Article 26 of the Model Tax Convention. The date of entry into force of the Protocol was 26 November 2014.

Lisa Brunton

TAX FREE INVESTMENTS ARE ALMOST HERE

From 1 March 2015, natural persons will be allowed to make contributions to so-called "tax free investments" in accordance with the newly introduced s12T of the Income Tax Act, No 58 of 1962 (Act).

The reasons for the introduction of "tax free investments," according to the Explanatory Memorandum on the Taxation Laws Amendment Act, No 43 of 2014, include that household savings have been declining in South Africa (SA) since the early 1980s, and that such savings continue to be low by international standards. According to the Explanatory Memorandum, the existing interest exemption has not been a very visible feature of the South African tax system, which limits its effectiveness as an incentive. In addition, the interest exemption is limited to interest-bearing instruments and does not contain product design features which could encourage households to save.

The legislature has therefore introduced the concept of "tax free investments." Section 12T of the Act allows for the contribution by natural persons of amounts up to R30,000 per annum into "tax free investments," further limited to cash and a lifetime contribution limit of R500,000. The amount of interest or dividends received or accrued to a person in respect of such investments will not be taken into account when determining whether that person has exceeded the contribution limits. Any transfer of an amount from one "tax free investment" to another must also be disregarded when determining whether the person contributed in excess of the contribution limits.

The penalty for exceeding the annual contribution limit of R30,000 in respect of a year of assessment is an amount of 40% of that excess, payable as normal tax by that taxpayer. Similarly, if a person contributes in excess of the R500,000 lifetime contribution limit in respect of "tax free investments," an amount equal to 40% of so much of that excess as has not previously been taken into account in terms of s12T of the Act will be deemed to be an amount of normal tax payable by the taxpayer in respect of the year of assessment in which the excess amount is contributed.

From the Explanatory Memorandum it appears that products for purposes of s12T of the Act may include exposure to money market instruments, equities and property investments. According to a draft notice released for public comment on 14 November 2014, the institutions that will be able to provide these products to taxpayers are:

- banks, as defined in the Banks Act, No 94 of 1990;
- long-term insurers, as defined in the Long-term Insurance Act, No 52 of 1998;
- managers, as defined in the Collective Investment Schemes Act, No 45 of 2002;
- the Government in the national sphere;
- an authorised user, as defined in s1 of the Financial Markets Act, No 19 of 2012; and
- an administrative financial service provider, as defined in board notice 79 of 2003 issued in terms of s15(1) of the Financial Advisory and Intermediary Services Act, No 37 of 2002.

The benefits of making use of this "tax free investment" opportunity, include that any amount received by or accrued to a natural person in respect of such investment will be exempt from normal tax, and any capital gain or capital loss made in respect of the disposal of a "tax free investment" must be disregarded when determining the aggregate capital gain or capital loss of a person for any year of assessment.

It appears from the draft regulations that have been released for public comment that a pre-existing financial instrument or policy owned by a taxpayer cannot be converted into a "tax free investment."

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