TAX

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RELATIONSHIP BETWEEN A VAT VENDOR AND SARS

The Supreme Court of Appeal (SCA) recently handed down judgment in the matter of *Director of Public Prosecutions, Western Cape v Parker* (103/14) [2014] ZASCA 223 (12 December 2014).

In this matter a close corporation, being a registered vendor for purposes of Value-added Tax (VAT), together with its sole representative, Mr Parker, were charged in the regional court on several counts.

The charges included:

- breaching s28(1)(a) of the VAT Act No 89 of 1991(VAT Act) by failing to submit certain VAT returns; and
- common law theft for failing to pay certain amounts of VAT to the South African Revenue Service (SARS).

The close corporation and Mr Parker pleaded guilty and were convicted and sentenced.

Mr Parker was sentenced to a fine in respect of breaching s28(1)(a) of the VAT Act, and was sentenced to five years' imprisonment in respect of the common law theft conviction.

Mr Parker appealed to the Western Cape High Court in respect of his sentence of imprisonment. However, after certain questions were raised by the High Court as to whether Mr Parker should have been charged with common law theft in the first instance, Mr Parker also appealed against his conviction. The close corporation did not appeal.

The High Court held that Mr Parker did not commit common law theft because the money belonged to the vendor and not to SARS, and set the conviction (and sentence) aside.

The State subsequently approached the SCA on a point of law. The SCA was tasked with answering the following question: "Whether a VAT vendor who has misappropriated an amount of VAT which it has collected on behalf of SARS can be charged with the common law crime of theft?"

The State argued that:

- A vendor acts as an agent for SARS;
- A vendor effectively holds VAT in trust for SARS;
- If the vendor uses such VAT for another purpose, the vendor is guilty of theft, irrespective of whether the vendor is the owner of the money; and
- Only if the vendor is not obliged to keep the VAT in a separate account, and it has sufficient liquid fund available to cover the VAT, would it not be theft to use the VAT amount for other purposes.

The SCA disagreed with SARS:

"I do not believe, however, that s7(1) of the [VAT] Act either expressly or impliedly creates a relationship of trust. On the contrary, it is clear to me that the relationship created by the [VAT] Act is one of a debtor and his creditor."

The SCA further described the relationship between a VAT vendor and SARS as follows:

"It is clear that the [VAT] Act is a scheme with its own directives, processes and penalties. The relationship it creates between SARS and the registered vendor is *sui generis* – one with its own peculiar nature. <u>The [VAT] Act does not confer on the vendor the status of a trustee or an agent of SARS.</u> If it did, the vendor would either have to keep separate books of account or alternatively, would have to be sufficiently liquid at any given time in order to cover the outstanding VAT. The [VAT] Act makes no provision for this situation nor does it seek to compel a vendor to keep separate books of account in respect of VAT."

It became clear during the hearing that the reason for the State having charged Mr Parker with theft, and for approaching the SCA to rule on the matter, was that it sought to procure more severe penalties where transgressions involving VAT are concerned. The penalties contemplated in the VAT Act were too lenient. The SCA was not in favour of extending the crime of common law theft to apply to the failure to pay VAT, and suggested that the appropriate solution for the State would be to approach the legislature and amend the VAT Act.

Accordingly, the State's appeal failed. The State was also ordered to pay the costs of Mr Parker in opposing the appeal.

The judgment is a welcome clarification of the position that a VAT vendor holds in relation to SARS. It is clear that a VAT

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vendor does not 'collect' VAT 'on behalf of' SARS from the recipients of goods or services, but that VAT (at least in terms of section 7(1)(a) of the VAT Act) is a tax imposed on the VAT vendor itself, which the VAT vendor is obliged to pay as debtor to SARS.

This analysis is however not necessarily applicable to, for example, the relationship between an employer and SARS in respect of employees tax. It is submitted that in such circumstances, an employer may very well be regarded as an agent for SARS, holding amounts deducted from the remuneration of employees in trust for SARS. Where such amounts are misappropriated, a charge of common law theft could very well succeed.

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EXPIRY OF STC CREDITS ON 31 MARCH 2015

Dividends tax was introduced into the South African tax regime on 1 April 2012 and effectively replaced secondary tax on companies (STC). STC was levied on dividends distributed by companies at the flat rate of 10%. In terms of the dividends tax regime, a 15% tax is levied on the amount of any dividend paid by a company. The company is liable to withhold the amount of the tax in respect of cash dividends and pay it over to the South African Revenue Service (SARS).

Any STC credits which companies calculated as at 31 March 2012 (ie the day before dividends tax came into effect) could be carried over into the newly introduced dividends tax regime. These STC credits could be used by the company for a period of three years from 31 March 2012 to reduce any dividends tax paid by a company, to the extent that the dividend does not exceed the STC credit of the company and the company has, by the date of payment of the dividend, notified the recipient of the amount by which the dividend reduces the STC credit of the company.

In terms of s64J of the Income Tax Act No 58 of 1962 (Act), the STC credit of a company (company A) as at 31 March 2012 could be calculated as the sum of the amount by which the dividends accrued to company A during the dividend cycle ending on 31 March 2012 exceeded the dividends declared during that cycle by company A. This STC credit could be increased by any dividends accrued to company A on or after 1 April 2012 and in respect of which company A received a notification from the company paying the dividend (company B) of the amount by which the dividend paid reduced the STC credit of company B and the notification was received by no later than the date on which the dividend was paid. This effectively resulted in a transfer of a STC credit between company A and company B, ie the company paying the dividend and the company in favour of which the dividend accrued.

The STC credit calculated by a company in accordance with the aforementioned formula would then be reduced by any dividends declared and paid by that company after 1 April 2012 until such time that the company's STC credit is used up. The reason for this treatment of STC credits is to prevent double taxation of the excess net accrued dividends of a company that have already been subject to STC.

The STC credit used by the company must be apportioned between all shareholders receiving a dividend from the company by taking into account the ratio between the total reduction in the STC credit and the total dividend paid to all shareholders. This ensures that any particular shareholder does not unduly benefit from a company's STC credit by setting off a disproportionate share of the company's entire STC credit against its liability for dividends tax with the effect of prejudicing the company's other shareholders.

In terms of s64J(7) of the Act, in the event that a company neglects to withhold dividends tax from a dividend paid to a person as a result of an inaccurate notification by the company, the company itself will be liable for the amount of dividends tax.

Section 64J(5) of the Act clearly states that the STC credit of a company on or after the third anniversary of the effective date, being 1 April 2012, is nil. Accordingly, companies should be aware that the expiry date for the use of any unused STC credits is 31 March 2015, after which date the dividends tax regime will be of full force and effect and companies will no longer be able to set off STC credits against dividends in order to reduce the dividends tax liability arising from dividends paid to shareholders. It is therefore recommended that companies with STC credits pay any outstanding dividends to shareholders before 31 March 2015 in order to take advantage of any STC credits before the expiry thereof.

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