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TAX AND EXCHANGE CONTROL ALERT

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AMENDMENTS TO TAX FREE INVESTMENT REGULATIONS

With effect from 1 March 2015, the South African Government (Government) introduced tax free investments (TFI). In this regard, the Income Tax Act, No 58 of 1962 (Act) was amended to introduce a new s12T, in addition to the notice and regulations published in the Government Gazette on 25 February 2015.

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SECTION 104 OF THE TAX ADMINISTRATION ACT AND THE MEANING OF 'EXCEPTIONAL CIRCUMSTANCES' – A CAUTIONARY TALE

The court held that in order to satisfy the 'exceptional circumstances' requirement in s104(5)(a), the onus was on the taxpayer to prove that there were "...unusual facts... which have a causal connection to the delay which resulted".

The taxpayer, whose assessed liability runs into millions of rands, should have taken its tax responsibility more seriously by seeking tax advice from a firm of attorneys that specialise in such matters as soon as it received the assessments in December 2014.

In terms of s104 of the Tax Administration Act, No 28 of 2011 (Act), a taxpayer who is aggrieved by an assessment or decision of the South African Revenue Service (SARS), may object to the assessment or decision.

The Act states that the objection must be lodged within 30 business days from the date of the assessment. A senior SARS official may extend this period by no more than 21 business days, unless the official "...is satisfied that exceptional circumstances exist which gave rise to the delay in lodging the objection". In *ABC (Pty) Ltd v The Commissioner for the SA Revenue Service* (ITC Case Number: 0038/2015), the South Gauteng Tax Court had to consider the meaning of this provision.

Facts

After the taxpayer was audited by SARS in May 2014, assessments were raised against the taxpayer in December 2014 in respect of various taxes. The taxpayer had to lodge its objection by 2 March 2015, but only did so on 5 June 2015, meaning it was 65 business days late. SARS disallowed the objection in a letter dated 22 June 2015, as 'no exceptional reasons had been furnished'. The taxpayer appealed against SARS.

Judgment

The court held that in order to satisfy the 'exceptional circumstances' requirement in s104(5)(a), the onus was on the taxpayer to prove that there were "...unusual facts... which have a causal connection to the delay which resulted".

To support its contention that there were exceptional circumstances present, the taxpayer raised a number of arguments:

- First, the assessments and objections thereto involved complex issues of law. This argument was rejected as the nature of the complexities were never indicated.
- Second, the delay was due to the courts being closed over December 2014 and January 2015, during the court recess period. The court rejected this argument as the courts' closure had no impact on lodging the objection to SARS on time.
- Third, the taxpayer alleged that it was negotiating with SARS from December 2014 to March 2015. Except for a visit by the taxpayer's auditor to the SARS offices on 19 January 2015, there was no evidence that meetings had taken place between the taxpayer and SARS. This argument was consequently rejected.

SECTION 104 OF THE TAX ADMINISTRATION ACT AND THE MEANING OF 'EXCEPTIONAL CIRCUMSTANCES' – A CAUTIONARY TALE

CONTINUED

It appears that had the taxpayer acted sooner and more decisively in responding to the assessments, the court might have found in its favour despite the delay of 65 business days.

- Fourth, the taxpayer became dissatisfied with the abilities of its auditor and stopped using his services. The court rejected this argument and held that the taxpayer seemed to be dissatisfied with SARS' response as opposed to the competence of its auditor. This appeared to be the case, as a letter prepared by the auditor was very similar to an undated opinion of counsel, which formed part of the papers and was apparently acceptable to the taxpayer.
- Fifth, the taxpayer was only able to obtain new professional advice from a practitioner in Florida and received the name of his legal representative in April 2015, who then prepared an undated opinion for the taxpayer. As the taxpayer is based in Springs, on the West Rand, the court took judicial notice of the fact that there were a number of other attorneys' firms in the "...Witwatersrand region and up into Sandton...", that the taxpayer could have approached after receiving the assessments in December 2014.

The court concluded that none of these arguments proved the existence of unusual facts, which were causally connected to the delay. The taxpayer also raised a number of other arguments for the first time in court, which were all rejected as they had no merit and as they were not relevant to the 'exceptional circumstances' enquiry. With reference to SARS Interpretation Note 15 (IN15), which sets out SARS' interpretation of s104 of the Act, the court also rejected an argument that the taxpayer's objection enjoyed good prospects of success, as the argument was based on counsel's opinion that was not submitted to SARS prior to its decision to disallow the objection. The document contained nothing that showed that the taxpayer had a *prima facie* case and constituted no more than the 'mere say-so' of the taxpayer's counsel.

Comment

In its conclusion, the court indicated that it is sympathetic to an ignorant taxpayer who is confronted with an enormous amount of tax to be paid in terms of an assessment. However, it added that in this instance the taxpayer, whose assessed liability runs into millions of rands, should have taken its tax responsibility more seriously by seeking tax advice from a firm of attorneys that specialise in such matters as soon as it received the assessments in December 2014.

It appears that had the taxpayer acted sooner and more decisively in responding to the assessments, the court might have found in its favour despite the delay of 65 business days. IN15 lists the following events as examples of what may constitute 'exceptional circumstances' in terms of s104(5)(a):

- A natural or human-made disaster;
- A civil disturbance or disruption in services;
- A serious illness or accident; and
- Serious emotional or mental distress.

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CONTINUED

The judgment should serve as a caution to taxpayers, to obtain legal advice as soon as possible, once they have received an assessment from SARS. Although the appointment of a tax practitioner does not absolve a taxpayer from its responsibilities under the Act, the speedy appointment of a tax practitioner will assist a taxpayer's cause, where it seeks to object to a SARS assessment and where more than 30 business days might be required to prepare such an objection.

IN15 goes on to state that the mere existence of one of these factors is not sufficient, but that the taxpayer needs to demonstrate that one of these factors were the reason for the delay. Although the court did not provide examples of what would constitute 'exceptional circumstances', the judgment seems to suggest that events less exceptional than the examples cited in IN15, could constitute 'exceptional circumstances'. However, the judgment is very clear that if the lateness in lodging the objection is due to the taxpayer's delay in obtaining proper legal advice, the 'exceptional circumstances' requirement will not have been met. The judgment should serve as a caution to taxpayers, to obtain legal advice as soon as possible, once they have received an assessment from SARS. Although the appointment of a tax practitioner does not absolve a taxpayer from its responsibilities under the Act, the speedy appointment of a tax practitioner will no doubt assist a taxpayer's cause, especially where it seeks to object to a SARS assessment and where more than 30 business days might be required to prepare such an objection.

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AMENDMENTS TO TAX FREE INVESTMENT REGULATIONS

Section 12T exempts certain taxpayers from paying normal tax on any amount received by, or accrued in respect of a TFI.

With effect from 1 March 2015, the South African Government (Government) introduced tax free investments (TFI). In this regard, the Income Tax Act, No 58 of 1962 (Act) was amended to introduce a new s12T, in addition to the notice and regulations published in the Government Gazette on 25 February 2015.

In the 2016 Budget, it was stated that TFIs were introduced to encourage individuals to save and not intended to serve as a vehicle to avoid estate duty.

Section 12T exempts certain taxpayers from paying normal tax on any amount received by, or accrued in respect of a TFI. Section 12T further states that, in determining the aggregate capital gain or capital loss of a person in respect of a year of assessment, any capital gain or capital loss in respect of the disposal of a TFI must be disregarded. Contributions to a TFI must be limited to cash, R30,000.00 in aggregate during any year of assessment and R500,000.00 in aggregate.

In the 2016 Budget, it was stated that TFIs were introduced to encourage individuals to save and not intended to serve as a vehicle to avoid estate duty. According to the Government, it has become aware that the current law allows individuals who protect their investment portfolio through a long-term insurer to nominate a beneficiary on the endowment policy. The transfer of the proceeds from the TFI asset to the beneficiary would circumvent estate duty. The Government therefore proposes to pass an amendment to the Act in order to prevent such circumvention of estate duty.

The 2016 Budget further stated that, currently, investors receiving dividends from TFIs must submit an exempt dividends tax return to the SARS following the receipt of every dividend payment. The dividends received from TFIs are exempt in terms of s64F(1)(o) of the Act. The Government proposes to remove the requirement to submit an exempt dividends tax return.

Lastly, the 2016 Budget proposed to postpone the implementation date to allow transfers of TFIs between service providers from 1 March 2016 to 1 November 2016 in order to allow more time for service providers to finalise the administrative processes required for such transfers. The date, 1 March 2016 was substituted by 1 November 2016 in terms of the regulations published in the Government Gazette, No 39765 on 1 March 2016. These regulations came into operation on 1 March 2016.

In the 2016 Budget, the Government proposed to introduce draft regulations to outline the transfer process, which have been released and will come into force on 1 November 2016. The draft regulations contain the basic requirements for a valid transfer that will not count against the annual and lifetime limits of a TFI mentioned above.

AMENDMENTS TO TAX FREE INVESTMENT REGULATIONS

CONTINUED

The transfer of the proceeds from the TFI asset to the beneficiary would circumvent estate duty. The Government therefore proposes to pass an amendment to the Act in order to prevent such circumvention of estate duty.

The draft regulations state that product providers will only be allowed to transfer TFIs directly to another product provider. According to the press release issued by National Treasury on 08 March 2016, investors may not accept transfer amounts into their own accounts outside of a tax free savings account as this will be considered to be a withdrawal. If the amount is subsequently reinvested into a tax free savings account it will have an impact on the annual and lifetime limits.

The draft regulations further state that a product provider must transfer an investor's TFI to another product provider within ten business days from being instructed to do so by the investor. However, a product provider is not obliged to transfer an amount in respect of a TFI of the same natural person, deceased estate or insolvent estate of the same natural person more than twice a year.

The transferring product provider must also provide the receiving product provider and the investor with a transfer certificate, which all parties must retain for a period of five years after the issue of the certificate. The draft regulations further state the minimum information which must be reflected on such a transfer certificate.

According to the press release, the reporting fields on the IT3(s) for TFIs have already been incorporated and will make it easier to transition into a regime that allows transfers.

The public has been invited to submit comments to the draft regulations to the National Treasury by, 8 April 2016.

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