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TAX & EXCHANGE CONTROL **ALERT**

IN THIS **ISSUE**

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In the recent judgment of *Peri Framework Scaffolding Engineering (Pty) Ltd v CSARS* (A67/2020) (23 August 2021), the High Court of South Africa considered an appeal brought by the taxpayer (the appellant) which pertained to a non-compliance penalty imposed by the South African Revenue Service (SARS) for the appellant's late payment of its employees' tax obligation.

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Redefining *"reasonable grounds"* for the remittance of non-compliance penalties

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Facts

Pursuant to the submission by the appellant of its Employer Reconciliation Declaration on 18 December 2017 (which was only due on 31 December 2017), the appellant became liable to pay employees' tax in the amount of R10,648,340.93 to SARS. In terms of Paragraph 2(1) of the Fourth Schedule to the Income Tax Act 58 of 1962 (Fourth Schedule), the appellant was liable to make payment of its employees' tax obligation within seven days after the end of the month during which the employees' tax was withheld by the appellant.

On the date of submission of the return, the appellant also submitted an instruction to its bank to make payment of the amount owing to SARS on 3 January 2018. However, the payment could not be released on 3 January 2018 due to there being insufficient funds in the relevant bank account.

As a consequence, the appellant sought (and obtained) an overdraft from its bank on 5 January 2018. The overdraft, in addition to a payment that was expected to be received from a debtor on 5 January 2018, would have been sufficient to ensure that the appellant made full, timeous payment to SARS of its employees' tax obligations. However, the payment ultimately received from the debtor was insufficient to cover the full tax debt and the appellant therefore approached a connected entity for additional funds to make up the shortfall.

The tax debt was paid by the appellant on 8 January 2018.

In terms of Paragraph 6(1) of the Fourth Schedule, SARS imposed a 10% penalty on the employees' tax amount that was due on the basis that the employees' tax was not paid to SARS within the period prescribed by Paragraph 2(1). SARS also imposed interest in respect of the late payment of the employees' tax.

Judgment

The dispute between the parties was first heard by the Tax Court, which ruled in favour of SARS. The appellant then appealed the decision in the High Court. The appellant contended that:

1) the calculation of the time period in which payment of its employees' tax obligation was due ought not to have been determined having regard to section 244(1) of the Tax Administration Act 28 of 2011 (TAA), but should have been determined on the basis of the statutory rules of interpretation as prescribed in section 4 of the Interpretation Act 33 of 1957 (IA); alternatively,

2) even if it was found that the appellant had been late in making payment of the employees' tax, it had demonstrated reasonable grounds for the late payment as envisioned in section 217 of the TAA (dealing with the remittance of penalties for nominal or first incidence of non-compliance), such that the penalty ought to have been remitted by SARS.

Redefining *"reasonable grounds"* for the remittance of non-compliance penalties*...continued*

Section 244 of the TAA provides that if any date specified in a tax Act for payment, submission or any other action falls on a Saturday, Sunday or public holiday, the action must be done not later than the last business day before the Saturday, Sunday or public holiday.

First ground of appeal: Computation of time periods

Section 244 of the TAA provides that if any date specified in a tax Act for payment, submission or any other action (or if the last day of a period within which such payment, submission or other action must be made) falls on a Saturday, Sunday or public holiday, the action must be done not later than the last business day before the Saturday, Sunday or public holiday.

The appellant argued that this section pertains only to deadlines and that it plays no role in the determination of the time period prescribed in Paragraph 2(1) of the Fourth Schedule. To this end, it contended that the following interpretation, as set out in sections 1 and 4 of the IA, should be applied by the court:

- the days in a prescribed period must be counted exclusive of the first and inclusive of the last day of the period; and
- to the extent that the last day of the period falls on a Sunday or a public holiday, that last day must be excluded from the reckoning and the next Monday or ordinary day counted as the last day.

On this basis, the appellant argued that in calculating the seven-day period provided for in Paragraph 2(1) of the Fourth Schedule, 31 December was to be excluded from the calculation, and it would therefore start on 1 January 2018 and end on Sunday 7 January 2018. However, as the last day was a Sunday, that day should be excluded from the seven-day period and Monday 8 January 2018 should be taken as the last day of the period. As payment was made on 8 January 2018, the appellant contended that it had complied with its obligations and no penalty should have been imposed.

The High Court disagreed with the appellant's contentions pertaining to the calculation of the seven-day period prescribed in the Fourth Schedule and the calculation method to be employed. It held that section 244(1) of the TAA does, in fact, deal with the calculation of days specified in a tax Act for payment, submission or any other action under the act and it clearly states that if the last day of a period in which the taxpayer is meant to make payment falls on a Saturday, Sunday or public holiday, such payment should be done no later than the last business day before that Saturday, Sunday or public holiday. The court found that the intention of the legislature as set out in section 244 of the TAA was clear and prescriptive, as a result of which sections 1 and 4 of the IA would not find application in this instance.

To this end, the court concluded that the seven-day period provided for in the Fourth Schedule ought to be calculated in days, inclusive of weekends and public holidays, and that in the event of a payment due date falling on such days, the payment should be made on the last day before the weekend or public holiday. As such, the payment by the appellant of its employees' tax obligation, which was made on 8 January 2018, was not made in compliance with the time periods prescribed in the Fourth Schedule and this ground of appeal failed.

Redefining *"reasonable grounds"* for the remittance of non-compliance penalties*...continued*

SARS argued that the appellant could not contend that *"reasonable grounds exist"* in circumstances where it treated the employees' tax amounts deducted or withheld as its own and subjected such funds to the whims of the business.

Second ground of appeal: Reasonable grounds shown for late non-compliance

In its judgment, the Tax Court found that the 10% penalty that had been imposed by SARS should not be remitted as the appellant had failed to show that reasonable grounds existed for making the late payment of the employees' tax to SARS.

Section 213 of the TAA states that if SARS is satisfied that an amount of tax was not paid as and when required under a tax Act, SARS must, in addition to any other *"penalty"* or interest for which a person may be liable, impose a *"penalty"* equal to the percentage of the amount of unpaid tax as prescribed in the tax Act.

Section 217 (3) of the TAA provides that SARS may remit a penalty imposed in terms of section 213 if SARS is satisfied that:

- the penalty has been imposed in respect of a *"first incidence"* of non-compliance;
- reasonable grounds for the non-compliance exist; and
- the non-compliance in issue has been remedied.

On this basis, a penalty in terms of section 213 may be remitted in circumstances where the penalty has been imposed in respect of a *"first incidence"* of non-compliance (i.e. where no other fixed amount or percentage based administrative penalty has been imposed during the preceding 36 months) or where exceptional circumstances exist, which rendered the taxpayer incapable of complying with the relevant obligation under the relevant tax Act.

The appellant contended that it had never before been non-compliant with any of its tax related obligations (and in particular it had never been late with paying its payroll taxes) and that it had taken immediate steps to remedy its non-compliance such that payment of the employees' tax obligation was made as soon as possible. As such, the appellant argued that the 10% penalty should be remitted.

SARS, however, argued that the explanation provided by the appellant for the late payment of the employees' tax did not constitute *"reasonable grounds"* as required in section 217 of the TAA and that the appellant was therefore not entitled to any relief.

In particular, it argued that Paragraph 2(1) of the Fourth Schedule establishes a fiduciary relationship between SARS and an employer as the employees' tax amounts that are deducted and withheld by an employer are collected on behalf of and for the benefit of SARS. It contended that the appellant had failed to act in a manner consistent with the requisite degree of care in its approach to collecting and paying over the amounts due to SARS, because the appellant failed to insulate the employees' tax amounts collected from its employees from the business income. SARS argued that the appellant could not contend that *"reasonable grounds exist"* in circumstances where it treated the employees' tax amounts deducted or withheld as its own and subjected such funds to the whims of the business. Such conduct, it argued, was unreasonable and unacceptable.

Redefining *"reasonable grounds"* for the remittance of non-compliance penalties*...continued*

The court disagreed with SARS' contentions regarding the establishment of a fiduciary relationship between SARS and employers and stated that:

> *"There have been various distinctions between the accountability of a trustee to his beneficiary and the accountability of a debtor to his unsecured creditor. Under a trust-type of relationship, the beneficiary is given an equitable proprietary interest in some specific trust property or at least the right to have specific trust property administered according to the terms of a trust or legislation, whereas an unsecured creditor only has a personal right against the debtor which is unrelated to any property in the hands of the debtor."*

On this basis, the court concluded that the relationship between SARS and employers who are obligated to withhold employees' tax could not properly be elevated to that of a fiduciary relationship which would preclude the appellant from applying the amounts so withheld in its business. To this end, the use of the amounts by the appellant in its business did not exclude the existence of reasonable grounds for the late payment.

A further argument advanced by the appellant in favour of the remittance of the penalty was that a penalty of 10% in the context of the appellant's non-compliance (being the next business day after the due date for the payment) was not proportionate to the seriousness or the duration of its non-compliance. In its counter argument, SARS contended that it was irrelevant whether the appellant was late by one day or by 20 days on the basis that, as long as the as the appellant had failed to pay the declared employees' tax amounts within the stipulated seven-day period, the imposition of the 10% penalty is triggered.

The court concurred with SARS and took the view that the imposition of varying degrees of penalties in relation to varying degrees of lateness would cause uncertainty and would likely expose SARS to a plethora of litigation pertaining to the evaluation of an appropriate penalty for the degree of lateness. On this basis, the court did not see fit to decrease the quantum of the penalty imposed on the appellant based on the degree of the appellant's non-compliance.

The court concurred with SARS and took the view that the imposition of varying degrees of penalties in relation to varying degrees of lateness would cause uncertainty and would likely expose SARS to a plethora of litigation pertaining to the evaluation of an appropriate penalty for the degree of lateness.

Redefining *"reasonable grounds"* for the remittance of non-compliance penalties*...continued*

SARS had failed to consider the manner in which the appellant, when it realised that it would be unable to comply with the payment instruction on 3 January 2018, attempted to rectify the deficiency.

However, it held that section 217(3) of the TAA makes provision for a "*mechanism to come to the assistance of an aggrieved first incidence non-complying tax payer*".

The court identified one factor that SARS had failed to consider and which, in its view, could establish reasonable grounds for the appellant's non-compliance. Specifically, SARS had failed to consider the manner in which the appellant, when it realised that it would be unable to comply with the payment instruction on 3 January 2018, attempted to rectify the deficiency.

Having regard to the steps taken by the appellant to ensure that payment was made, and the fact that payment was effected on the first business day after the payment due date (with the result that SARS suffered no prejudice), and further that there was no malintent on the part of the appellant, the court found that reasonable grounds existed for the penalty to be remitted. On this basis, the appellant's second ground of appeal was upheld and the 10% penalty was remitted.

Comment

While the relevant tax legislation provides various guidelines for SARS to exercise its discretionary powers (as they pertain to the remittance of penalties imposed on taxpayers under the tax Acts), these discretionary powers are broad and their application by SARS officials is very subjective.

A stringent approach to penalties is frequently adopted by SARS in practice (as was the case in this instance) and compliant taxpayers who encounter difficulties while trying to maintain their compliance status are often heavily penalised, despite their best efforts. To this end, this is a welcome judgment as it provides insights into what factors may be considered by SARS when ascertaining whether "*reasonable grounds*" exist for the purposes of remitting penalties.

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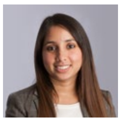

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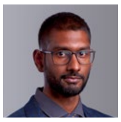

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