Tax & Exchange Control

ALERT

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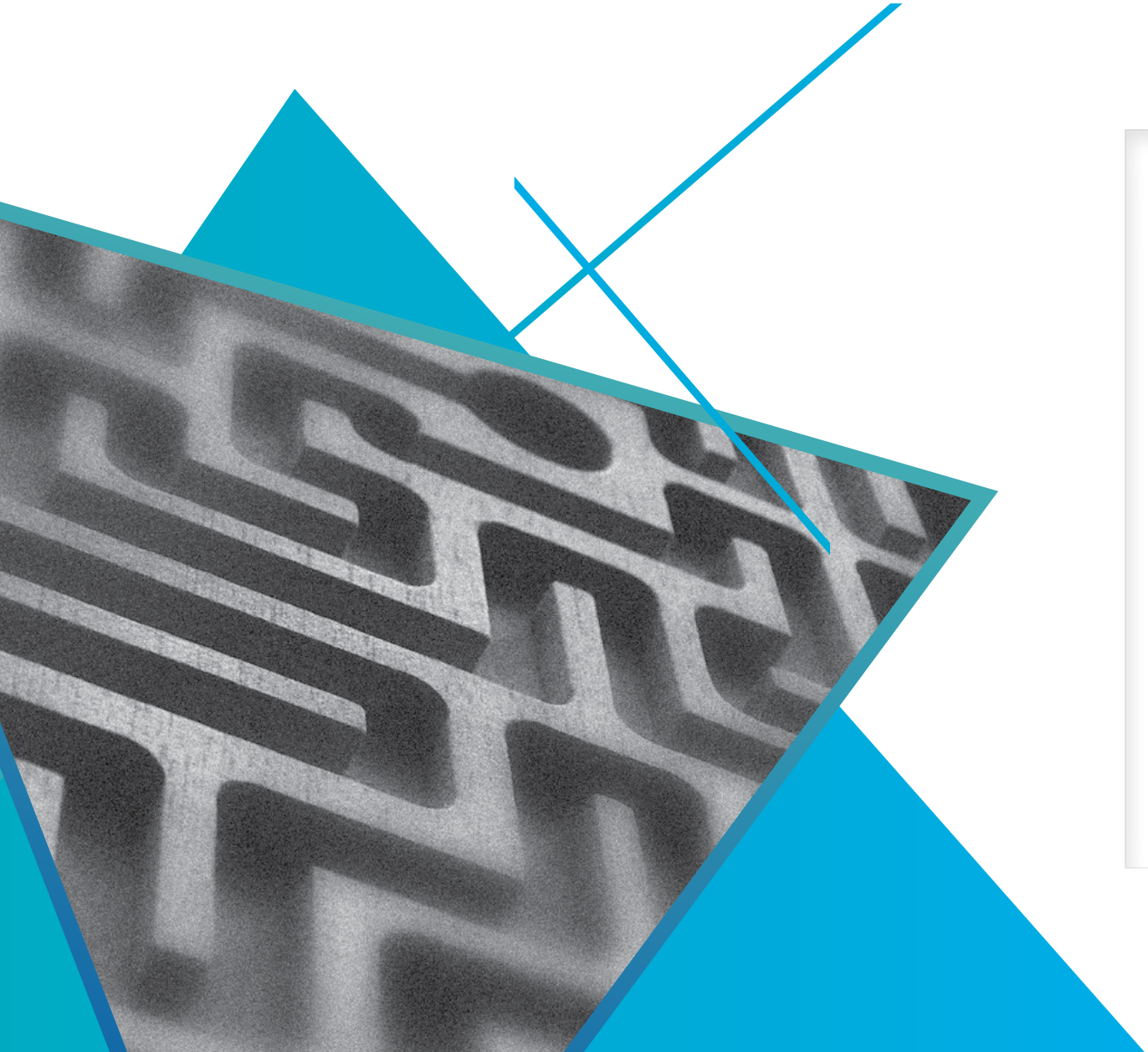
CLIFFE DEKKER HOFMEYR

INCORPORATING
KIETI LAW LLP, KENYA



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Tax exceptionalism in circumstance

Love it or hate it, tax exceptionalism (the idea that, due to its specialised nature, tax law operates within its own parameters) tends to arise when tax disputes cross the boundary between tax law and other areas of the legal landscape. The (now) not so recent amendment to section 105 of the Tax Administration Act 28 of 2011 (TAA) is an example of this as it tries to restrict tax disputes to specialised forums such as the Tax Court. In particular, the crossover between this section and administrative law is a circumstance where tax exceptionalism can become contentious, as it did again in the case of *Trustees of the CC Share Trust and Others v Commissioner, SARS* (38211/21) ZAGPPHC 597 (24 July 2023) (*CC Share Trust*).

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Tax exceptionalism in circumstance

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Background

In the *CC Share Trust* case, the taxpayers had entered into a transaction for the sale of assets which was challenged by the South African Revenue Service (SARS) under the general anti-avoidance rules (GAAR). This entailed SARS issuing the taxpayers a notice in terms of section 80J of the Income Tax Act 58 of 1962 (ITA) inviting the taxpayers to give reasons why the GAAR should not be applied to the impugned transaction.

However, this section 80J notice did not come before SARS had already indicated its intention to audit the taxpayers under section 42(1) of the TAA. In terms thereof, SARS requested information from the taxpayers in order to conduct its audit, which information the taxpayers supplied.

At no time did SARS explicitly indicate that it had completed its audit of the taxpayers, but following the later section 80J notice, SARS issued the taxpayers a letter indicating that it intended to apply the GAAR to the impugned transaction and reassess the taxpayers accordingly. An exchange between SARS and the taxpayers ensued, during which SARS requested, and was provided with, various further pieces of information pertaining to the transaction in question.

Finally, this was followed by a further letter in which SARS set out why it rejected the taxpayers' argument against the application of the GAAR. In this letter, SARS set out the adjustments it had made to the taxpayers' incomes and levied understatement penalties on the taxpayers.

The taxpayers took exception to the process SARS had followed and made a request to SARS under section 9 of the TAA to withdraw its assessment as neither the first letter nor the second letter received from SARS was the finalisation of audit letter required by section 42(2) of the TAA. Therefore, the taxpayers argued, SARS had followed a procedurally flawed process in reassessing them for tax.

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SARS rejected this request, and this led the taxpayers to approach the High Court under the provisions of the Promotion of Administrative Justice Act 3 of 2000 (PAJA). Arguing that section 42(2) of the TAA was not followed, the taxpayers argued this was reviewable under PAJA as they had been denied the opportunity to receive, consider and respond to an audit outcome letter.

The legal framework and arguments

Section 42(1) of the TAA provides that:

> *"A SARS official involved in or responsible for an audit under this Chapter must, in the form and manner as may be prescribed by the Commissioner by public notice, provide the taxpayer with a notice of commencement of an audit and, thereafter, a report indicating the stage of completion of the audit."*

The first notice sent to the taxpayers was in terms of this section and notified them of the audit SARS intended to conduct.

Section 42(2)(b) of the TAA then provides that:

> *"Upon conclusion of the audit … and where the audit identified potential adjustments of a material nature, SARS must within 21 business days … provide the taxpayer with a document containing the outcomes of the audit, including the grounds for the proposed assessment …"*

The taxpayers argued that this section meant that once SARS had initiated an audit with the section 42(1) notice, it was obligated to then issue a section 42(2) notice setting out the audit findings. Following the section 42(1) notice, however, SARS then sent a notice in terms of section 80J of the ITA in order to challenge the impugned transaction in terms of the GAAR.

Section 80J of the ITA provides, *inter alia*, that:

> *"(1) The Commissioner must … give [a] party notice that he or she believes that the provisions of this part may apply in respect of an arrangement and must set out in the notice his or her reasons therefor.*
>
> *(2) A party who receives notice in terms of subsection (1) may, within 60 days … submit reasons to the Commissioner why the provisions of this part should not be applied.*
>
> *(3) The Commissioner must within 180 days of the receipt of the reasons or the expiry of the period contemplated in subsection (2):*
>
> *(a) request additional information in order to determine whether or not this part applies in respect of an arrangement;*

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(b) give notice to the party that the notice in terms of subsection (1) has been withdrawn; or

(c) determine the liability of that party for tax in terms of this part."

SARS then argued that its first letter to the taxpayers (which was in reply to the taxpayers' reasons provided under section 80J(2) of the ITA), although not explicitly stating it, was also a finalisation of audit letter as contemplated in section 42(2) of the TAA.

Although complying with the provisions of section 42(2) of the TAA, the taxpayers argued that it was impossible for the first letter from SARS to have been the finalisation of audit letter as it had still submitted documents to SARS following the receipt of this letter. Therefore, SARS had not been in a position to finalise the audit. As the second letter did not comply with the provisions of section 42(2), the taxpayers brought the review application in terms of PAJA.

However, section 7(2) of PAJA provides that, unless there are *"exceptional circumstances"* present, a court cannot hear a review in terms of PAJA until all internal remedies have been exhausted.

This is bolstered by section 105 of the TAA which now provides that: *"A taxpayer may only dispute an assessment or 'decision' as described in section 104 in proceedings under this chapter, unless a High Court otherwise directs."*

This meant that in order to circumvent the processes prescribed in section 104 of the TAA (objection and appeal to the Tax Court) and rely on PAJA, the taxpayers would require permission from the High Court.

Decision

Reading section 105 of the TAA together with section 7(2) of PAJA, the court in *CC Share Trust* found that the nub of the enquiry for both was whether exceptional circumstances existed. In coming to this conclusion, the court relied on the recent case of *Commissioner, SARS v Rappa Resources (Pty) Ltd* [2023] JDR 0861 (SCA) (*Rappa*) where the Supreme Court of Appeal held that a taxpayer must dispute an assessment using the objection and appeal processes unless the High Court indicates otherwise, the High Court only being permitted to do this where exceptional circumstances exist.

Therefore, the court in *CC Share Trust* concluded that the taxpayers would only be able to approach it directly on review in terms of PAJA where exceptional circumstances existed for this. Turning to what constitutes exceptional circumstances, the court examined the legal development of this concept, particularly as it has been set out in previous tax cases.

In short, prior to *Rappa* the Tax Court had held in *Commissioner, SARS v FP (Pty) Ltd* 84 SATC 321 that an error by SARS relating to section 42 of the TAA would constitute exceptional circumstances as it directly related to a taxpayer's

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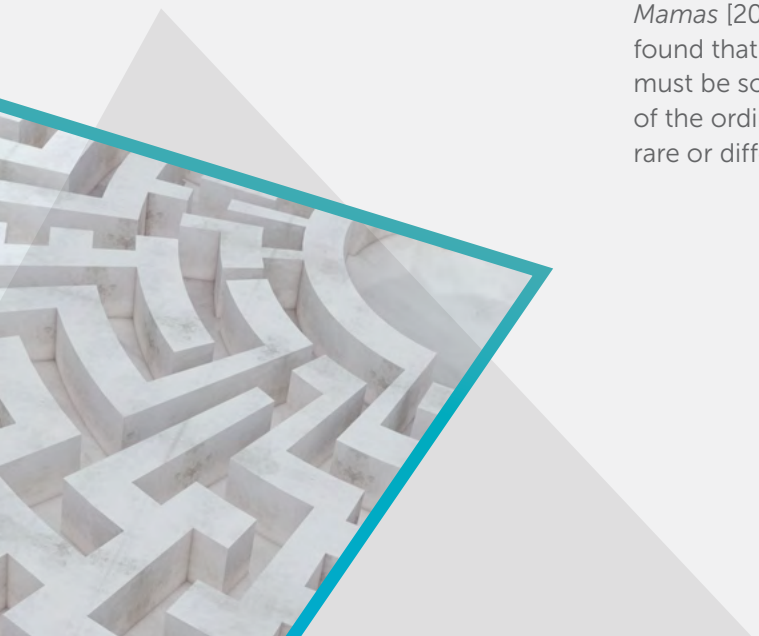
rights under the South African Constitution. Further, the High Court in *ABSA Bank v Commissioner, SARS* [2021] (3) SA 513 (GP) had stated that a dispute that turns wholly on a point of law constitutes an exceptional circumstance.

Following *Rappa*, however, the position has been clarified that the Tax Court wields broad powers which include the power to determine the legality of an assessment on review. On this basis, the court in *CC Share Trust* found that no longer is a point of law adequate to constitute exceptional circumstances. Rather, and as pointed out in *MV Ais Mama Seatrans Maritime v Owners, MV Ais Mamas* [2002] (6) SA 150 (C), the court found that exceptional circumstances must be something which is out of the ordinary, uncommon, rare or different.



As the taxpayers in *CC Share Trust* had argued the applicability of review under PAJA on a purely legal point, the court decided not to permit this review. Rather, the taxpayers were directed to challenge SARS' decisions in terms of the objection and appeal processes set out in the TAA.

To review or not to review

To turn a phrase on its head, the court in *CC Share Trust* took with one hand while giving with the other. In a clear and well-structured decision, the court summarised the history of using administrative review in terms of PAJA in tax disputes, and then set out the parameters in which a taxpayer can review a decision by SARS.

The court clarified that objection and appeal in terms of the TAA are the first port of call for a taxpayer. But in this, the Tax Court's powers extend to conducting a legality review of the decision brought before it in a preliminary hearing.

Further, in the event that a taxpayer is not successful following these preliminary proceedings, administrative review in terms of PAJA would potentially be a possibility. However, how the requirement to bring a review application within 180 days will be interpreted remains slightly unclear. In *Forge Packaging v Commissioner, SARS* (21634/2021) ZAWCHC 119 (13 June 2022), for example, the review application was declined as it was not brought within 180 days of the assessments being issued. What would also remain questionable, is the application of section 105 of the TAA to such subsequent proceedings. Unlike PAJA, this section does not impose a threshold of exhausting internal remedies, but rather, as set out in *Rappa*, imposes the higher threshold of exceptional circumstances.

Nicholas Carroll

OUR TEAM

For more information about our Tax & Exchange Control practice and services in South Africa and Kenya, please contact:

Emil Brincker
Practice Head & Director:
Tax & Exchange Control
T +27 (0)11 562 1063
E emil.brincker@cdhlegal.com

Sammy Ndolo
Managing Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E sammy.ndolo@cdhlegal.com

Mark Linington
Director:
Tax & Exchange Control
T +27 (0)11 562 1667
E mark.linington@cdhlegal.com

Gerhard Badenhorst
Director:
Tax & Exchange Control
T +27 (0)11 562 1870
E gerhard.badenhorst@cdhlegal.com

Jerome Brink
Director:
Tax & Exchange Control
T +27 (0)11 562 1484
E jerome.brink@cdhlegal.com

Petr Erasmus
Director:
Tax & Exchange Control
T +27 (0)11 562 1450
E petr.erasmus@cdhlegal.com

Dries Hoek
Director:
Tax & Exchange Control
T +27 (0)11 562 1425
E dries.hoek@cdhlegal.com

Alex Kanyi
Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E alex.kanyi@cdhlegal.com

Heinrich Louw
Director:
Tax & Exchange Control
T +27 (0)11 562 1187
E heinrich.louw@cdhlegal.com

Howmera Parak
Director:
Tax & Exchange Control
T +27 (0)11 562 1467
E howmera.parak@cdhlegal.com

Stephan Spamer
Director:
Tax & Exchange Control
T +27 (0)11 562 1294
E stephan.spamer@cdhlegal.com

Tersia van Schalkwyk
Tax Consultant:
Tax & Exchange Control
T +27 (0)21 481 6404
E tersia.vanschalkwyk@cdhlegal.com

Louis Botha
Senior Associate:
Tax & Exchange Control
T +27 (0)11 562 1408
E louis.botha@cdhlegal.com

Varusha Moodaley
Senior Associate:
Tax & Exchange Control
T +27 (0)21 481 6392
E varusha.moodaley@cdhlegal.com

Abednego Mutie
Senior Associate | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E abednego.mutie@cdhlegal.com

Nicholas Carroll
Associate:
Tax & Exchange Control
T +27 (0)21 481 6433
E nicholas.carroll@cdhlegal.com

Joan Kamau
Associate | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E joan.kamau@cdhlegal.com

Puleng Mothabeng
Associate:
Tax & Exchange Control
T +27 (0)11 562 1355
E puleng.mothabeng@cdhlegal.com

Esther Ooko
Associate Designate:
Tax & Exchange Control
T +27 (0) 11 562 1778
E esther.ooko@cdhlegal.com

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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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JOHANNESBURG
1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa.
Dx 154 Randburg and Dx 42 Johannesburg.
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E jhb@cdhlegal.com

CAPE TOWN
11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E ctn@cdhlegal.com

NAIROBI
Merchant Square, 3rd floor, Block D, Riverside Drive, Nairobi, Kenya. P.O. Box 22602-00505, Nairobi, Kenya.
T +254 731 086 649 | +254 204 409 918 | +254 710 560 114
E cdhkenya@cdhlegal.com

STELLENBOSCH
14 Louw Street, Stellenbosch Central, Stellenbosch, 7600.
T +27 (0)21 481 6400 E cdhstellenbosch@cdhlegal.com

CLIFFE DEKKER HOFMEYR | cliffedekkerhofmeyr.com

CLIFFE DEKKER HOFMEYR

INCORPORATING
KIETI LAW LLP, KENYA