Standing Committee on Finance (SCOF): Report-Back Hearings

15 October 2015

Draft Taxation Laws Amendments Bill, 2015 and Draft Tax Administration Laws Amendment Bill, 2015

Draft Response Document from National Treasury and SARS, as presented to SCOF

(Final version of this document will be published by date of introduction of the Bills)

NATIONAL TREASURY

SARS

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1. BACKGROUND

1.1. PROCESS

The Draft Taxation Laws Amendment Bill (TLAB), 2015 and Draft Tax Administration Laws Amendment Bill (TALAB), 2015 were released for public comment on 22 July 2015. National Treasury and SARS briefed the Standing Committee on Finance (SCoF) on 4 August 2015. Public comments to the Committee were presented at a hearing that was held on 16 September 2015. The final report back to the Committee will be on 15 October 2015.

1.2. PUBLIC COMMENTS

The deadline for public comments to the Committee was 14 September 2015. National Treasury and SARS received responses from 52 organisations and individuals. There were 10 organisations who presented their responses orally during the public hearings hosted by the SCoF. Workshops with stakeholders to discuss and review their comments were held on 2 September 2015 for Business and International taxes, on 3 September 2015 for Personal Income Tax and Value-Added Tax and on 4 September 2015 for Tax Administration.

1.3. POLICY ISSUES AND RESPONSES

Provided below are the responses to the policy issues raised by the public comments received, both written and during the public hearings. These comments have been taken into account in the revised Bills. Comments that fall wholly outside the scope of the Bills have not been taken into account for purposes of this response document.

1.4 SUMMARY

- This response document includes a summary of the main written comments received on the 2015 Draft TLAB and the 2015 Draft TALAB as well as the issues raised during the public hearings held by the SCoF.

The main comments that arose during the Public Hearing and the other main issues in the 2015 Draft TLAB and the 2015 Draft TALAB are:

- Deleting the tax credit for withholding taxes imposed by other countries on services provided from South Africa;
- Measures to close a loophole that allows for the avoidance of estate duty;
- Tax relief for certain collateral transactions;
- Changes to the tax treatment of insurance companies (both short-term and long-term insurers) due to the Solvency Assessment and Management (SAM) regulatory initiative;

- Procedures when legal professional privilege is asserted;
- Reduced assessments;
- The period of limitations for issuance of assessments; and
- Liability of third party appointed to satisfy tax debts.

This response document also deals with Government's approach to the harmonisation in the tax treatment of contributions to retirement funds, to take account of consultations at NEDLAC.

The response document does not take into account proposals raised that were not part of the Budget proposals and the subsequent draft Bills. Should taxpayers and/or their advisors wish to raise issues that are not included in the draft Bills, they are welcome to write to the Minister of Finance through a separate process.

Draft Taxation Laws Amendment Bill

2. INCOME TAX: INDIVIDUALS, SAVINGS AND EMPLOYMENT

2.1. Retirement reforms

The Income Tax Act, 1962, was amended in 2013 through the Taxation Laws Amendment Act, 2013, to harmonise both the tax treatment of contributions and the requirement to purchase an annuity upon retirement for all retirement funds. The aim of the reforms is to deal with an alignment between tax principles and retirement reform objectives.

Key tax reform objective are:

- <u>improve vertical equity in income</u> by imposing a limit on the total allowable deduction to higher income taxpayers and reducing the scope for structuring of their tax affairs;
- <u>improve horizontal equity</u> by harmonising the same deduction across all retirement funds and hence allowing equal treatment for all retirement funds;
- improve transparency and data collection by deeming contributions by employers on behalf of members as a taxable fringe benefit;
- Improve simplicity by harmonising the tax treatment of contributions to retirement funds.

Key retirement reform objective;

- enhance post-retirement preservation through extending the requirement to purchase an annuity to all retirement funds. <u>The key principle to note is that the tax deduction is designed to encourage retirement savings and at the same time promote preservation and annuitisation, and hence the tax deduction should not be allowed where there is no annuitisation.</u>

The media statement issued by the Treasury on 22 July 2015 on the 2015 TLAB proposal noted that in addition to the TLAB amendments published, "...further amendments may be effected to the *de-minimis* threshold at which individuals would be required to purchase an annuity at retirement, to take into account consultations through NEDLAC. This will be in line with a request arising from hearings in the Standing Committee on Finance in 2014". This followed the proposal on page 153 in the 2015 Budget Review that noted that the effective date of the harmonization and annuitisation had been postponed by government "...to 1 March 2016 to enable further public communication and discussion with the affected parties".

Government has since the Budget continued to consult within NEDLAC and with affected stakeholders, and notes that despite its request to members (including the labour constituency or any trade union) to submit proposals for any amendments to the SCOF, no submissions have been received to delay or amend the implementation of the harmonisation and annuitisation reforms. However, though there are significant benefits for many low- and middle-income taxpayers, the NEDLAC process has not been concluded as the labour constituency has indicated that they will only engage on any retirement reform once government releases the social security reform paper. Their difference also relates to concerns on obligating annuitisation (and preservation) on provident funds, even though vested rights are protected under the 2013 and 2014 legislative amendments.

It should be noted that the legislation passed last year to delay the implementation of tax harmonisation in contributions from 2016 to 2017 was not supported by many taxpayers who were denied the opportunity to benefit from the higher tax deduction. Most retirement fund administrators had also proceeded with system changes, which had to be halted just prior to the initial implementation date. Further, from a tax reform perspective, it meant that the objective for greater equity between high- and low-income taxpayers had to be delayed, with the prospect that high income taxpayers would continue to enjoy relatively high tax deductions. The coming harmonisation measures will limit such deductions to 27.5% or R350 000, whichever is lower. It will also ensure that all tax contributions made by the employer are treated as a taxable fringe benefit, which will in future be taxed in the hands of the employee.

Government intends to proceed with the broader objective of tax reform to ensure more equity across income groups. As from 1 March 2016 the 27.5% or R350 000 tax deduction including taxing employer contributions in the hands of the employee will be implemented. Given the high inequality in income and wealth in South Africa, Government will continue to take steps to reduce the scope for tax structuring by high income taxpayers that undermines the progressivity of the tax system.

Government is also committed to implement retirement reforms encouraging the preservation and annuitisation of retirement funds. The Minister of Finance will be requesting an urgent meeting next week with the NEDLAC Labour constituency to discuss the implementation of retirement reforms related to the annuitisation of provident funds. The Minister intends to put forward two options:

(i) OPTION ONE: To continue with implementation of the annuitisation requirement (and recognising vested rights) for all provident funds on 1 March 2016, but a possible increase in applicable thresholds;

(ii) OPTION TWO: To slightly delay by one year the annuitisation requirement for provident funds to 1 March 2017. It should be noted that some members of provident funds will face paying higher taxes due to such delay, but government is willing to introduce a transitional measure to limit any adverse impact of the tax reform on members of provident funds by allowing for a limited deduction (from 10% to 15% for provident funds).

Government is also committed to releasing the social security reform paper later this year to ensure that these consultations on annuitisation and preservation can resume, thus facilitating the process of engaging with unions on broader retirement reform. Current legislation only deals with annuitisation, but not with preservation.

2.2. Closing a loophole to ensure consistent tax treatment of all retirement funds

(Main reference: section 1: definition of "pension fund")

Comment: The vested rights for paragraph (a) funds as defined under the definition of 'pension fund' in section 1 of the Income Tax Act are currently not protected as they are not included in the definition of 'provident fund' in section 1 of the Act.

Response: Accepted. Provident funds under paragraph (a) of the definition of "pension fund" will be included under the definition of "provident fund" from 1 March 2016. Members of these funds will then be treated in the same way as members of provident funds by preserving their vested rights if they were to transfer to a pension fund or pension preservation fund after 1 March 2017.

Comment: The amended definitions of retirement funds cater for amounts credited before 1 March 2016 to form part of vested rights. The amendments do not cater for amounts credited after 1 March 2016.

Response: Not accepted. Credited amounts, other than returns, after 1 March 2017 are not intended to form a part of vested rights for transfers from a provident fund to a pension fund or pension preservation fund after 1 March 2017 as these amounts were not within the affected retirement fund at the time of the transfer.

Comment: All provident fund members' vested rights should be protected regardless of whether they move their benefits to other retirement funds. Those individuals who are 55 years and older should still be able to contribute to another retirement fund where the member is not required to purchase an annuity from those contributions even if they move retirement funds. At the least, members who are forced to move retirement funds, due to a merger of their employer for example, should not lose the option to make additional contributions for which they are not required to purchase an annuity upon retirement.

Response: Noted. The retirement reforms have been amended to allow provident fund members to continue to take a lump sum on retirement. The vested rights provisions have thus been adjusted to only apply for members of provident funds who wish to transfer their assets to a pension fund. Any future contributions will be afforded a greater tax deduction but the member would be required to purchase an annuity upon retirement from the retirement interest accumulated from those contributions.

Comment: Section 37D of the Pension Funds Act provides for a registered fund to make certain deductions from pension benefits. The amendment proposes that the vested rights be reduced by all the deductible contributions in terms of section 37D of the PFA, irrespective of whether they take place before or after 1 March 2016. This appears to prejudice individuals who will have a diminished vested right due to the section 37D deduction. The reduction in the vested right due to a deduction of pension benefits should only apply to contributions which took place prior to 1 March 2016 or the vested right should be reduced by the overall proportion of the vested right as part of the total retirement assets.

Response: Partially accepted. All deductions from retirement benefits in terms of section 37D of the PFA will be allowed as a reduction against vested rights for any transfers to a pension fund or pension preservation fund after 1 March 2017. However, in divorce cases the section 37D deduction will be eligible for a proportional measure, i.e. to proportionally reduce both the vested and non-vested rights to allow the vested right to be attributed in a fair manner between the two ex-spouses. The legislation will be amended to allow for the proportional treatment arising from divorce orders.

Comment: In the case of a member of a preservation or transferee fund who takes a withdrawal benefit in cash before 1 March 2016, there is no indication in the legislation on whether the withdrawal is deducted from the vested right or non-vested right portion or whether it is equally apportioned between the two parts. Where a member transfers to a preservation fund or other type of transferee fund after 1 March 2016, the transfer will consist of a portion which is a vested right portion; and a non-vested right portion (contributions and growth after 1 March 2016).

Response: Accepted. The legislation will be clarified to indicate that withdrawals from a preservation fund will be treated in the same manner as deductions from a provident fund after 1 March 2016. Withdrawals will be taken off the vested right portion before the non-vested right portion.

Comment: The reference to "policy of insurance" in section 10(1)(*gI*) of the Income Tax Act appears to imply that proceeds of all policies (including retirement fund-held death benefits) will benefit from tax free pay-out. This might bring retirement fund held income policies in line with employer held income protection policies.

Response: Noted. The legislation will be amended to clarify that this amendment was not intended to alter the tax treatment of benefit proceeds from retirement funds.

Comment: The removal of the approval by the Commissioner for SARS on paragraph (c) of the definition of "pension fund" creates confusion. Clarity is required in respect of paragraph (a) funds, whether they would need approval by the Commissioner for SARS from the proposed effective date.

> *Response*: Accepted. The approval by the Commissioner will be reinstated and the administrative and practical implications will be explored further.

2.3. Closing a loophole to avoid estate duty through excessive contributions to retirement funds

(Main reference: section 3 of the Estate Duty Act)

Comment: The amendment in respect of excess contributions to a retirement fund should be limited to death-bed excess contributions or contributions made 12 months before death. This would have a substantial impact on low and/or middle income earners whose intention is not to avoid tax.

> *Response:* Not accepted. The estate duty abatement of R3.5 million provides relief to lower and middle-income earners.

Comment: The insertion of paragraph (*bA*) of section 3(2) of the Estate Duty Act uses the wording "any contribution" which is open-ended. The provision should only become applicable where the excess contributions are above a specified percentage or rand amount. A percentage limitation could be relative to the contributions per taxpayer, and a rand amount used as a threshold could be adjusted regularly in line with inflation.

> *Response:* Not accepted. This proposal is against the underlying principle that contributions that did not qualify as a deduction or exemption should be a part of the dutiable value of the estate.

Comment: Member contributions made before 1 March 2015 should be excluded from this amendment, as per the recommendations put forward in the draft Estate Duty Report by the Davis Tax Committee. The amendments will be retrospective if contributions from previous years are included in the dutiable value of the estate. Taxpayers should not be adversely treated for arrangements that they made which were allowed by the legislation at the time.

> *Response:* Accepted. The proposal will be amended to only include contributions that were not eligible for a deduction or an exemption that were made on or after 1 March 2015.

Comment: Transfer values from "Associated Institutions Pension Funds" of which contributions did not receive a deduction for tax purposes should be excluded from dutiable estate.

> *Response:* Noted. The amendment to only include non-deductible contributions on or after 1 March 2015 should effectively address this issue.

Comment: Excess contributions are already "taken into account" through paragraph 2 of the Second Schedule to the Income Tax Act and the wording could be interpreted to mean that there would be no addition to the dutiable estate. It is better to simply make it clear that amounts not taxable according to the lump sum tax tables will be included in the dutiable estate.

> *Response:* Accepted. Amendments will be made to make the wording clearer.

2.4. Withdrawal from retirement funds by non-residents

(Main reference: paragraph (*b*)(x)(*dd)* of the proviso to the definition of "retirement annuity fund" in section 1)

Comment: The 2015 Draft TLAB amends the definition of "*retirement annuity fund:"* to allow for withdrawal from retirement funds by expatriates when these expatriates: cease to be tax resident; or when they leave South Africa at the end of the work visa; or when they leave South Africa and were not regarded as resident by the South African Reserve Bank for purposes of exchange control. The proposal requires the application of three different pieces of legislation and three different regulatory bodies (i.e. the South African Revenue Service, the South African Reserve Bank and the Department of Home Affairs) and would be overly burdensome to the taxpayer.

> *Response:* Misplaced. The criterion in the legislation does not need all three options to be satisfied. If one condition is met, that would be sufficient.

Comment: Consideration should be given to the monitoring of the departure of expatriates from South Africa subject to the expiration of their work visas and coming back to South Africa the next day on a retiree visa. The practical implementation is impossible as many expatriates leave before the end of their work visas. Do they have to submit proof renouncing their work visas?

> *Response:* Misplaced. The intention is not to require expatriate employees to renounce their work visas when they repatriate from South Africa before the expiration of their work assignments or work visas in South Africa.

Comment: SARS should require a good standing tax clearance certificate via SARS e-filing or permission to allow an IT88 deduction on retirement withdrawal upon departure.

> *Response*: Not accepted. The same procedure is required for emigration.

Comment: In a case where emigrants for tax purposes fail to pay the tax liability arising from the Capital Gains Tax (CGT) exit charge because they do not have funds immediately available to pay the exit charge tax liability, the current process makes it impossible for tax emigrants to access the retirement annuity to pay the

CGT exit charge liability. By the time they realise there is a tax liability due, they would have already taken out their benefits from preservation funds.

Response: Noted. The intention is to allow tax emigrants to take out their retirement fund benefits as a lump sum upon departure. In such cases, taxpayers are required to be in good standing with the tax authorities where they would have already been required to settle any tax liability in order to access their retirement benefit pay-out upon departure.

2.5. Removing anomalies for income and disposals to and from deceased estate

(Main reference: New section 9HA, sections 22(8)(b), 25 and paragraphs 40, 41, 67 of the Eighth Schedule)

Comment: If the spouse is non-resident for tax purposes in South Africa, the roll-over relief should be provided for assets contemplated in paragraph 2(1)(b) of the Eighth Schedule to the Act (i.e. immovable property situated in the Republic).

Response: Not accepted. The primary purpose of this amendment is to align and remove anomalies and difficulties regarding the application and the interpretation of the law of the provisions dealing with capital gains tax and section 25 of the Act. The roll-over relief from the deceased estate in respect of immovable property situated in South Africa to a non-tax resident spouse is thus beyond the scope of the proposed changes. Hence, the current amendment in respect of roll-over rules does not extend to non-resident spouses. The deferral of imposing capital gains tax in the deceased estate for later imposition in the hands of a foreign tax resident national is a policy matter not forming part of the current changes.

Comment: From the wording in the new section 9HA of the Act, it appears that the taxpayers have a choice between paragraph 2(b)(i) and paragraph 2(b)(ii). Legislation should be made clear that paragraph 2(b)(i) applies when the asset was trading stock and that paragraph 2(b)(ii) applies if the asset was held as a capital asset.

Response: Accepted. Changes will be made in the legislation to make it clearer that paragraph 2(b)(i) of section 9HA applies when the asset was held as trading stock and paragraph 2(b)(ii) of section 9HA applies when the asset was held as a capital asset.

Comment: Foreign beneficiaries will not be able to claim a tax credit in their country of tax residence on the amount of tax paid by the estate if the tax is paid within the deceased estate. A special provision should be added for non-residents.

Response: Not accepted. Income received or accrued to the deceased estate will be taxed in the hands of the deceased estate, except where roll-over relief provisions apply in respect of transfers from the deceased estate to any heir or legatee. On the basis that the tax is borne by the deceased estate itself which is a separate taxpayer and not the heir or legatee, no foreign tax credit can be claimed by the non-resident beneficiary as taxes are charged and payable by the deceased estate. This is in line with the basic principles of taxation underlying the Act, where each taxpayer is subjected to taxation on receipts and accruals received or accrued in the hands of the said person, the same treatment applies to the tax reliefs such person is rightfully entitled.

Comment: The current system is more fair and equitable as the income that flows to the heir or legatee would still be subject to the natural person rebate in terms of section 6 of the Act, in the hands of the heir or legatee which would not be possible in the deceased estate.

Response: Partially Accepted. The legislation will allow for the deceased estate to be treated as a "natural person" for tax purposes (as defined in section 1 of the Act). Some of the exemptions applicable to a "natural person" will apply to the deceased estate.

Comment: It is more administratively burdensome to tax the income in the estate rather than the heir or legatee. Recommendation is that instead of aligning the income with the capital gains rules, that the legislation be amended to allow for the capital gains to be aligned with the current income "flow-through principle".

Response: Not accepted. The "flow-through principle" has not been taken away. The roll-over rules still apply in respect of transfers from the deceased estate to any heir or legatee subject to meeting applicable requirements.

Comment: To ensure that the fiscus is not prejudiced in that the heir or legatee might not be registered for income tax; recommendation is put forward to introduce stricter legislation to ensure that the executor or an estate reports the distributions, income and capital, that was made to the heir or legatee which would be a process similar to that of an employee with regards to IRP5 type information.

Response: Noted. We are open to suggestions that would assist in strengthening the compliance obligations and provide for transparency in the tax matters of the deceased estate from dealings between executors and the heirs or legatees during the winding up process of the estate.

Comment: It is recommended that the current provisions of section 25(2) of the Act dealing with tax treatment of income of beneficiaries and estates of deceased persons be retained. The repeal of the current provisions of section 25(2) of the Act allowing certain deductions and allowances utilised by the deceased estate or the heirs or legatees, means that the estate must rely on the normal deduction and allowance provisions in sections 11 and 12 of the Act.

Response: Not accepted. As clarified in the Explanatory Memorandum on the 2015 Draft Taxation Laws Amendment Bill, the presence of the current provisions in section 25 of the Act, in effect, allows for an heir or legatee to claim a deduction in terms of section 25(2) of the Act in respect of expenses not incurred by him or her. This goes against the basic principle underlying the Act, which requires a person to have actually borne the expense in order to be able to claim a deduction in respect of that expense. As a result, the deceased estate will be entitled to claim the expenses actually incurred in accordance with the applicable provisions of the Act.

2.6. Clarification of the interrelationship between taxation of share incentive trusts, time of disposal and attribution of capital gains to trust beneficiaries

(Main reference: Paragraphs 11(2)(*j*), 13(1)(*a*), 64C and 80(1) & (2A) of the Eighth Schedule)

Comment: The 2015 Draft TLAB proposed changes to clarify the interaction between the taxation of share incentive trusts and the time of disposal as well as attribution of capital gains to beneficiaries of a share incentive trust (employees) as contemplated in the Eighth Schedule. The clarification sought by the amendments is to defer the recognition of the capital gain in the trust when an employee share trust disposes of shares to an employee, until the equity instrument is unrestricted and vests in the employee's hands for purposes of section 8C. As a result, three amendments were made in the Eighth schedule in this regard. The first amendment was the deletion of paragraph 11(2)(j) of the Eighth schedule. Taxpayers submit that the deletion of paragraph 11(2)(j) of the Eighth schedule is problematic and it should be withdrawn as such deletion would result in the triggering of two taxing events, i.e., firstly, CGT on the disposal of a restricted equity instrument and a potential section 8C again later at the vesting of the equity instrument.

Response: <u>Not accepted.</u> The repeal of paragraph 11(2)(*j*) of the Eighth schedule will remain as this paragraph was misused as some taxpayers interpreted the provisions of this paragraph to mean that there is no disposal at all, whereas the provision of this paragraph meant that disposal should be deferred and triggered when an equity instrument becomes unrestricted and vests for purposes of section 8C. The issue regarding the double taxation will be addressed and consequential amendments will be proposed by inserting new paragraphs 64C and 80(2A).

Comment: The second amendment in this regard is the insertion of a new paragraph 13(1)(*a*)(iiB), which deals with the time of disposal of the equity instrument from a trust to a beneficiary of a trust (employee). Taxpayers request clarification regarding the intention of the insertion of new paragraph 13(1)(*a*)(iiB) as paragraph 13 merely regulates the time of disposal and not the disposal event itself. In addition, the proposed amendments in paragraph 13(1)(*a*)(iiB) uses the word "granting". This use of the word "granting" is confusing in the context of the Eighth schedule.

Response: <u>Noted.</u> The use of the word "granting" purely means the happening of an event where the beneficiary (employee) is given the right (option) to purchase the shares in the entity.

Comment: The third amendment relates to the inclusion of certain words in paragraph 80 of the Eighth Schedule. Ordinarily, paragraph 80 has the effect that any capital gain arising on the vesting by a trust of an asset of a beneficiary would be attributed to and taxed in the hands of the beneficiary rather than the trust. Taxpayers are of the view that the effect of the amendment in paragraph 80(1) is that any gain will remain taxable in the trust and will not be attributed to the employee beneficiary. However, where an employee becomes entitled to a cash amount instead of shares, the employee will have a section 8C gain (on the basis that the beneficial interest in the trust is a section 8C equity instrument). Where the trust then disposes of shares and vests the profit in the hands of the employee, the capital gain will be attributed to the employee in terms of paragraph 80(2).

Response: Partially accepted. In order to address these concerns, further amendments have been made in the Act by inserting new paragraphs 64C and 80(2A).

2.7. Refinements to the Employment Tax Incentive

(Main reference: the definition of "monthly remuneration" in section 1 of the Employment Tax Incentive Act)

Comment: The employee remains employed while on unpaid leave and unpaid leave hours will not reduce employed (or contractual) hours. Thus, unpaid leave hours should reduce employed hours for the "monthly remuneration" definition and should not reduce employed hours for the section 4 of the ETI, the "wage qualifying test" in the current legislation. Employers do not capture actual hours of unpaid leave and the number of instances where unpaid leave is taken is minimal. The administrative costs of implementing this amendment for payroll companies and employers for only a few cases will be substantial and may not be justified in trying to align marginal cases.

Response: Accepted. Further adjustments to the employment tax incentive will be made after the incentive is reviewed and evaluated before the end of 2016.

2.8. Deleting "as the Commissioner may allow" for exemption of expenses incurred when moving residence

(Main reference: Section 10(1)(*nB*)(ii))

Comment: The removal of the Commissioner for SARS' discretion creates uncertainty as to how this exemption will apply in future. In practice, the Commissioner allows an amount equal to one month's salary to be tax-free to the employee for expenses without having to submit proof of expenditure. Recommendation is that, if the Commissioner's approval is removed, then this practice should be included in the legislation.

Response: Noted. The discretion of the Commissioner for SARS will be reinstated.

2.9. Deleting the definition of “remuneration” as it is no longer required

(Main reference: Paragraph 9(1) of the Seventh Schedule to the Act)

Comment: The definition of “remuneration proxy” specifically excludes travel allowances, company car benefit and the value of the accommodation fringe benefit. These amounts were previously included in the definition of “remuneration”.

Response: Partially accepted. For the purpose of determining the “remuneration proxy” in respect of the accommodation fringe benefit, the definition of “remuneration proxy” will specifically exclude the value of the accommodation fringe benefit. Travel allowances and the value of the company car fringe benefit will be included.

3. INCOME TAX: BUSINESS (GENERAL)

3.1. Debt-financed acquisitions of controlling share interests

(Main reference: section 24O)

Comment: The 2015 Draft TLAB amendments to section 24O relating to indirect acquisitions of operating companies that lead to unintended interest deductions are recognised. However, the requirement to re-determine the tax deductibility of interest incurred in respect of debt used to fund transactions that have already been concluded is onerous. Ideally the amendments should only apply to future acquisition transactions.

Response: Not accepted. The 2015 changes seek to align the current special interest deduction to the underlying policy objectives that seek to solely accommodate debt-push-down acquisitions that would have enjoyed tax-deferred treatment under section 45. No new policy position has been taken. Failure to apply the 2015 changes to transactions that have been concluded but where debt remains outstanding will lead to abuse of these special interest deduction rules through the creation of unintended interest deductions, which may also lead to base erosion and profit shifting. To ensure that interest deductions are only claimed in respect of structures intended, the 2015 changes will apply to any interest incurred on or after 1 January 2016 in respect of debt used to acquire a controlling share interest.

Comment: The requirement that the acquirer must re-determine the allowed special interest deduction (following the initial acquisition of a controlling share interest) when a subsequent reorganisation involving the group of companies of any operating company takes place is too wide and onerous. It is proposed that a time limit should be placed on the re-determination requirement in respect of subsequent reorganisation.

Response: Not accepted. There is no policy rationale to subject the subsequent re-determination requirement to a time limitation. Taxpayers seek to deduct interest incurred on a debt for the period that such debt remains outstanding.

During such period taxpayers must determine whether they are in fact eligible for such a deduction in accordance with the provisions of the Income Tax Act.

Comment: There should be a safe harbour in respect of the look-through approach of determining a qualifying interest on the indirect acquisition of controlling interests in operating companies. Negligibly low value non-productive interests should not deny an acquirer a full deduction on the interest incurred to acquire largely productive operations.

Response: Accepted. To accommodate *bona fide* and non-erosive indirect acquisitions of largely productive operations, where at least 90 per cent of the value of the equity shares of a company being acquired is derived from an equity share held by that company in an operating company, 100 per cent of the interest expense will be allowed on debt use to acquire the equity share of such a company.

Comment: The definition of an "operating company" is overly inclusive. It leads to a full interest deduction being allowed in schemes where minimal levels of operating income producing assets are placed into an otherwise non-income producing target company solely for the section 24O special interest deduction. The look-through approach being adopted in respect of indirect acquisitions does not deal with these types of schemes.

Response: Accepted. The special interest deduction under section 24O was introduced to mirror the tax treatment under section 11(*a*) had the acquiring company directly acquired all the underlying assets of a target company. A pragmatic approach was taken to allow a 100 per cent deduction on the indirect acquisition of productive business assets through a share acquisition on the basis that the target company's sole or main purpose would be to carry on a business which generates income and the acquirer would have largely qualified for a section 11(*a*) deduction on the direct acquisition of the business assets of the target company.

However, as a result of avoidance schemes that some taxpayers enter into, this position will be legislatively clarified. An operating company's receipts and accruals in a year of assessment will now be required to consist of at least 80 per cent income generated from carrying on business continuously through the sale of goods or the rendering of services.

3.2. Debtors allowances on instalment sale agreements

(Main reference: sections 42(3)(*c*), 44(3)(*c*) and 45(3)(*b*))

Comment: Though this amendment is welcomed, there is concern that it may result in the perception that debtor's allowances on instalments agreement could previously not be claimed by a transferee under the re-organisation rules.

Response: Noted. It is noted that the debtor's allowances granted in terms of section 24 relate to trade debts. For purposes of the re-organisation rules, such debts are considered allowance assets in respect of which allowances may be enjoyed by the transferee. This amendment is purely meant to clarify this position.

Comment: The proposed amendments still contain references to an obligation contemplated under section 24C for purposes of the roll-over of allowances in respect of contracts giving rise to future obligations. In addition, the amendments must be extended to section 47 in respect of roll-over liquidation transactions.

Response: Accepted. The references to an "obligation" resulting from contracts giving rise to future obligations by taxpayers will be removed and more generic references to "contracts" will be made. In addition, the changes will be extended to section 47 dealing with liquidation transactions.

3.3. Addressing the problem of return of capital after a taxpayer has held a share for three years

(Main reference: section (9C))

Comment: The proposed inclusion of the wording "held for a period of at least three years" in the section 9C(2) has rendered various limitations and exclusions in the definition of "qualifying share" to be irrelevant. It could be interpreted that equity shares held for a period of at least three years will be capital irrespective of whether it relates to exclusionary items as currently listed in the definition of "qualifying share" e.g. shares in a share block company. As an additional matter there is no link any more between 'qualifying share' and the charging provision of section 9C(2).

Response: Accepted. To ensure clarity the definition of 'qualifying share' will be removed and all relevant subsections be reworded to more clearly reflect the policy intent that (a) any amount received or accrued (including return of capital) and (b) that any expenses incurred on any equity share after the period of three years , will be capital in nature.

Comment: When section 9C was introduced, the three-year safe harbour was excluded in respect of foreign shares because of the participation exemption under paragraph 64B of the Eighth Schedule of the Act. It is submitted that foreign-resident shares be included within the ambit of the section 9C.

Response: Not accepted. Comment is outside the scope of the 2015 Budget Review and subsequent proposed amendments to the Act. It still is the policy intent to limit the ambit of section 9C to local equity shares only.

Comment: The proposed amendments to section 9C(7) would still result in a problem as section 22(8) applies when trading stock ceases to be held as trading stock and not on disposal of the asset. The proposed amended section 9C(7) still indirectly refers to a disposal through the definition of "qualifying share". It is suggested that this subsection rather be cross-referenced to section 9C(2) than to the definition of "qualifying share".

Response: Partially accepted. It is proposed that the definition of 'qualifying share' be removed to negate any potential confusion on the policy intent.

Comment: The insertion of the definition of 'identical share' and the amendment to section 9C(6) appears to purposefully exclude shares obtained in a resultant company through an amalgamation transaction as envisaged in the Act from the ambit of section 9C. The intent of holding the shares would be the same on the resultant company shares as it would be for the amalgamated company.

Response: Misplaced. The amendment to subsection (6) was inserted in order to provide clarity on the policy intent of a first-in-first-out approach and not to change the policy. The determination of the three year period on resultant company shares will continue to be based on the current application of legislation i.e. section 44(6).

Comment: It is proposed that the application of section 9C should be extended to other instruments held by long-term insurers on behalf of or for the benefit of policyholders.

Response: Not accepted. Comment is outside the scope of the 2015 Budget Review and subsequent proposed amendments to the Act. It has always been the policy intent to limit the ambit of section 9C to local equity shares.

Comment: The effective date relating to amendment of section 9C(7) should be brought forward to 1 January 2015.

Response: Not accepted. The amendment is intended to clarify the intention only, the policy has not been amended.

Comment: The new definition of "disposal" creates confusion as the definition must include its ordinary meaning under the main portion of the Act (as well as the Eighthth Schedule). The goal is to treat a disposal under the main Act as a capital gain disposal under the Eighth Schedule. Therefore, the main Act should be the starting point for the definition of "disposal" instead of the Eighth Schedule.

Response: Not accepted. The disposal of a share is either revenue or capital in nature depending on the facts and circumstances. Section 9C deems a share to be capital in nature after three years but only upon disposal after such three year period and hence the definition of disposal in section 9C is linked to the Eighth Schedule definition.

3.4. Securities transfer tax and capital gains tax implications of collateral arrangements

(Main references: sections 1, 9(C)(4) and 22(4B) and (9) of the Act, paragraph 11(2)*(n)* of the Eighth Schedule and sections 1 and 8(1)*(u)* of the STT Act)

Comment: The 2015 Draft TLAB introduces the definition of "collateral arrangement" in section 1 of the STT Act and includes a requirement that the collateral arrangement was not entered into for the purposes of keeping a position open for a period of longer than 12 months. This requirement mimics the wording used in the definition of "lending arrangement". The limitation of a collateral arrangement to a period of 12 months or less without the ability to re-post collateral to the underlying obligation is unduly restrictive and would have the effect that it can only be applied in the context of short-term debt and would severely restrict the ability of banks to benefit from collateral arrangements on meeting new regulatory capital.

Response: Not accepted. The proposed amendment moves away from common law principles in regard to a change of beneficial ownership and as such has strict anti-avoidance measures to stop any abuse of the special dispensation. The 2015 Draft TLAB proposal is based on two options explored with taxpayers and the industry during discussions with National Treasury. The preferred option included the requirement that mimics the wording used in the definition of "securities lending arrangement".

Comment: The current proposed amendments limits the exemption on collateral arrangements to listed shares only to be transferred as collateral. Cash, bonds and equity shares are generally preferred as collateral and further more in that order of preference by industry. It is proposed that amendments take into account government / listed corporate bonds as allowable instruments on collateral arrangements.

Response: Not accepted. The 2015 Draft TLAB proposal is based on two options explored with taxpayers and the industry during discussions with National Treasury. The preferred options included the requirement that mimics the wording used in the definition of "securities lending arrangement". The extension of collateral arrangement to bonds lacks merit based on the fact that bonds are not subject to STT and will only be subject to CGT if and when it is traded in the secondary market at a gain. The value of bonds generally only increase when the market has low inflation or dis-inflationary expectations, which would see increased demand for fixed interest instruments like bonds. The vast majority of bonds in South Africa are held until maturity, meaning that there would be no capital gains, regardless of market conditions.

Comment: The definitions of "identical share" and "identical security" only caters for an amalgamation transaction as envisaged in the Act when there are possibly other corporate actions, outside of the control of a party to a securities lending / collateral arrangement, that could possibly result in an identical share / security being unable to be returned in terms of lending / collateral arrangements.

Response: Not accepted. Due to the impact of African Bank as an example of corporate actions outside of the control of parties to a collateral arrangement the extension of collateral arrangements to other corporate actions will be investigated and assessed in the long-term.

Comment: The definition of 'collateral arrangement' should clearly link the transfer of the listed share to a collateral arrangement as security to an underlying principal debt obligation.

Response: Accepted. Changes will be made to the draft legislation.

Comment: The proposed "collateral arrangement" definition in section 1 of the STT Act refers to the transfer of a "listed share". However, the STT Act does not contain a definition of "share" or "listed share", but rather it contains a definition of "security" and "listed security".

Response: Noted. In context of the use of "listed share" together with the proposed concept of "collateral arrangement" per the STT Act, it is clear through interpretation that "listed share" is sufficiently linked to the meaning assigned to it under paragraph *(a)* of the definition of "security" in the STT Act including a depository receipt.

Comment: It is proposed that the amendments to the exemptions in the STT Act also include "members" as a party to whom it could be certified that the change is in terms of a lending or collateral arrangement.

Response: Accepted. To help ease the administrative burden on security lending / collateral arrangements changes will be made in the legislation accordingly.

3.5. Removing potential anomalies arising from cancellation of contracts

(Main references: Paragraphs 3, 4, 11(2)(*o*) and 20(4) of the Eighth Schedule)

Comment: Paragraph 20(4) of the Eighth Schedule was deleted by section 130(1)*(b)* of Act 31 of 2013 with effect from years of assessment commencing on or after 1 April 2014. The proposed additions come into effect from years of assessment commencing on or after 1 January 2016. The reference to paragraph 20(4) of the Eighth Schedule therefore appears to be an error.

Response: Misplaced. The draft TLAB inserts a new paragraph 20(4) of the Eighth Schedule.

Comment: Any contract cancelled in a subsequent year already leads to a taxpayer being prejudiced in that there is a likely capital gain in the year of disposal and a deemed capital loss in the subsequent year when the contract is cancelled, which if there was no other capital gain in that subsequent year the capital loss would be carried forward until such time that a gain is realised. This unfairly benefits the state.

It is proposed that subsequent year cancellations be treated the same as same-year cancellations through reopening old assessments.

Response: Not accepted. As a fundamental principle any tax event needs to have a point of assessment at which any tax or duty leviable under the Act would become chargeable. As such the cancellation of contracts can result in different tax treatments depending on whether the cancellation happened in the same year or subsequent years. The proposed amendments still creates a neutral tax result over time. It is also SARS / National Treasury practice and an industry accepted standard to carry forward credits or losses and not carry back by reopening assessments for subsequent events.

4. TAX: BUSINESS (FINANCIAL INSTITUTIONS AND PRODUCTS)

4.1. Amounts to be included in the income of a REIT: Deeming provisions in section 25BB(3)

(Main reference: Section 25BB)

Comment: In terms of section 25BB(3) any amount received or accrued by a REIT or a controlled company in respect of a financial instrument must be included in the income of that company. The meaning of the term "financial instrument" in this section is so wide that it can include the repayment of the capital amount advanced as a loan.

Response: Accepted. The provisions of section 25BB(3) were inserted to achieve neutrality in the tax treatment of amounts received or accrued in respect of financial instruments and the deductible on-distribution of those amounts by REITs and controlled companies. In the absence of the rule exempt dividends or partially taxed foreign dividends could have resulted in a full deduction when on-distributed.

4.2. Transitional tax issues resulting from the regulation of hedge funds

(Main references: sections 41, 42, 44 and 64D)

Comment: In consequence of the regulation of hedge funds, changes have been made in the 2015 Draft TLAB to provide tax relief to the hedge fund industry on transitioning to a new regulated hedge fund structure. As a result, amendments have been made in the definition of *"asset for share transaction"* in section 42 to allow the holder of interest in a hedge fund to dispose of its interest to a portfolio of a hedge fund collective investment scheme on a tax neutral basis. That said, the 2015 Draft TLAB does not contain a consequential amendment to include an equity share held by that person in a portfolio of a hedge fund collective investment scheme in the definition of the term "*qualifying interest"* in section 42. As a result, any disposal to a hedge fund will not qualify as an asset for share transaction. This appears to be an oversight. In order to correct this, it is proposed that the term "*qualifying interest"* in section 42 be amended to include an equity share held by that person in a portfolio of a hedge fund collective investment scheme.

> *Response:* <u>Accepted.</u> Paragraph (*b*) of the definition of the term "*qualifying interest*" in section 42 will be amended to include an equity share held by that person in a portfolio of a hedge fund collective investment scheme.

Comment: In order for the disposal to qualify as an "*asset for share transaction"* as defined in section 42, the persons disposing of the assets must have held the asset with the same intention (intention requirement). For example, section 42 requires the company acquiring the asset from the person disposing the asset to acquire such asset as trading stock, where the person holds it as trading stock, or as a capital asset, where the person holds it as a capital asset. Where the assets are held in a partnership and such partnership disposes of the assets, the partners effectively each disposes of his/her undivided interest in the partnership assets. To the extent that the partners did not hold their undivided interests in the asset with the same intention, the relief provided in terms of *"asset for share transaction"* in section 42 would not be available to the transfer of these assets on the basis that the assets are held collectively by partners and they have different intentions.

> *Response:* <u>Accepted</u>. The proviso to paragraph *(a)*(ii) of the definition of asset for share transaction in section 42(1) will be amended to provide that the capital/revenue intention test will not apply where assets are transferred to a portfolio of a hedge fund collective investment scheme. Section 42 could be used to unwind unregulated hedge funds even in the case of partnerships. The partner could dispose of its interest in the partnership to the portfolio of a hedge fund collective investment scheme in exchange for a participatory interest in the portfolio of a hedge fund collective investment scheme. When a partner disposes of its interest in an unregulated hedge fund, the partnership is dissolved.

Comment: The relief provided in terms of an *"asset for share transaction"* in section 42 contains a number of exclusions. As a result, an investor in a hedge fund that constitutes a partnership that is exempt from normal tax in terms of section 10(1), for example, a pension fund, cannot use the relief provided in terms of *"asset for share transaction"* in section 42.

> *Response:* <u>Not accepted</u>. A pension fund will not need the tax relief provided in terms of *"asset for share transaction"* in section 42 since it is already exempt from normal tax in terms of section 10(1)(*d*). It can exchange its interest in the partnership for a participatory interest in a portfolio of a hedge fund collective investment scheme without paying tax.

Comment: The relief provided in terms of an *"asset for share transaction"* in section 42 will not apply to any existing hedge fund that constitutes a trust since the trust is the owner of the assets and would transfer the assets to the newly regulated hedge fund CIS. However, the trust will not include the disposal in its taxable income or assessed loss as in terms of section 25B, such amount would be deemed to accrue to the beneficiaries.

> *Response*: Misplaced. The trust deed of the existing trust could be amended to comply with the requirements of the Collective Investments Scheme Control Act. No transfer of assets is necessary.

Comment: Currently, a portfolio of a collective investment scheme in securities constitutes a regulated intermediary for purposes of dividends tax in terms of section 64D. In terms of section 64G(2)(c) a company that declares and pays a dividend is not required to withhold dividends tax if it pays such a dividend to a regulated intermediary. The regulated intermediary has an obligation to withhold dividends tax in this regard. It is proposed that the withholding tax regime applicable to collective investment scheme in securities should be granted to portfolio of hedge funds collective investment schemes and that the definition of regulated intermediary in section 64D be expanded to include a portfolio of a hedge fund collective investment scheme.

> *Response:* Accepted. The definition of regulated intermediary in section 64D will be amended to include a portfolio of a hedge fund collective investment scheme.

4.3. Tax issues resulting from the introduction of the SAM basis for short term insurers

(Main reference: section 28)

Comment: As a result of the introduction by the FSB of the SAM framework and the Insurance Act, 2016, which will replace the current regulatory regime for the short term insurance industry, proposed amendments have been made in the 2015 Draft TLAB to cater for the tax treatment of the short term insurance industry. As SAM is not a suitable basis for tax purposes, the 2015 amendments propose changes to the tax system that is based on IFRS for short term insurers. As a result, in determining the taxable income derived by a short-term insurer, deductions under section 28(3) were amended in the 2015 Draft TLAB since they refer to deductions allowed under the current FSB regulatory regime, which also includes the cash-back bonus as determined by the FSB Board Notice. It is proposed that a cash-back bonus recognised as a liability under IFRS should be continued to be deducted under section 28(3).

> *Response*: Accepted. However, no amendment is required in this regard as the proposed amendments in section 28(3) will also cater for the cash-back bonus to be allowed as a deduction as an IFRS liability relating to premiums.

Comment: The Explanatory Memorandum to the 2015 Draft TLAB stated that the claim provisions will be the net amount after the short term insurer had reduced that amount with amounts it estimates to recover under reinsurance policies. However, no changes have been made in clause 49 of the 2015 Draft TLAB to provide for the reduction of the claims provision with reinsurance claims. .

Response: Accepted. Amendments will be proposed to the provisions of section 28 to cater for the reduction of the claim provisions with reinsurance claims.

Comment: Section 28 should be amended so that insurance contracts classified as investment contracts for IFRS purposes should be treated as insurance contracts for tax purposes. This is necessary to ensure consistent treatment in that premiums should be included in gross income, with deductions and allowances determined in accordance with the provisions of the Income Tax Act.

Response: Not accepted. For purposes of determining the taxable income of a short term insurer in terms of section 28, the current wording does not distinguish between "insurance contract' and "investment contract". It is submitted that there is a consistent treatment as short term insurers must include premiums received by or accrued to them in terms of section 28(2) and can claim deductions actually incurred under section 11(a) read with section 28(2).

Comment: It is proposed that section 28 should be amended so that all policies issued by a cell captive insurer are treated and taxed in accordance with the normal tax provisions applicable to short term insurers.

Response: Accepted. Amendments have been made to section 28(3) to cater for income derived by a short term insurer in respect of cell structures.

Comment: It is proposed that section 28 should be amended so that in determining the taxable income derived by any cell captive insurer from carrying on short term insurance via third party cell structures all amounts treated as reinsurance for IFRS must be disregarded.

Response: Accepted. The effect will be to tax the insurance activities of all cells in the cell structure.

Comment: The proposed amendments to delete subsections (7) to (11) of section 28 as those subsections refer to the statutory valuation method that will not apply in future. However, consequential amendments are required to ensure that the provisions of section 28 apply equally to controlled foreign companies (being a non-resident company conducting short term insurance business). It is proposed that section 9D (dealing with controlled foreign companies) should be amended so as to treat a controlled foreign company which conducts short term insurance business as a resident for purposes of section 28.

Response: Accepted. Amendments will be made to the provisions of section 9D(2A) to cater for this.

4.4. Tax issues resulting from the introduction of the SAM basis for long term insurers

(Main reference: section 29A)

Comment: As a result of the introduction by the FSB of the SAM framework and the Insurance Act of 2016, which will replace the current regulatory regime for long term insurance industry, proposed amendments have been made in the 2015 Draft TLAB to cater for the tax treatment of the long term insurance industry. As SAM is not a suitable basis for tax purposes, the 2015 amendments propose changes to the tax system that is based on IFRS for long term insurers. As a result, in the 2015 Draft TLAB, the *"adjusted IFRS value"* definition in respect of a policyholder fund in section 29A is proposed to be amended. The proposed *"adjusted IFRS value*" definition in respect of a policyholder fund does not address the treatment of (i) deferred acquisition cost, (ii) deferred revenue liability, (iii) reinsurance; and (iv) deferred tax even though some of these were addressed under the current FSB regulatory regime.

> *Response:* Partially accepted. Amendments have been proposed to the definition of *"adjusted IFRS value"* in section 29A to take into account amounts in respect of deferred tax liability and the amount recognised under policies of reinsurance in accordance with IFRS. Amounts in respect of deferred acquisition cost and deferred revenue liabilities should be accounted for under the other provisions of section 29A.

Comment: The 2015 Draft TLAB proposes amendments to the definition of "*adjusted IFRS value"* to use the amount of insurance liabilities as determined in accordance with IFRS as reported by the insurer to shareholders in their audited financial statements, and adjusts this value by applying the methodology used for statutory reporting to offset negative liabilities in 2014 and such methodology must be applied consistently for every year of assessment following that year of assessment. It is proposed that the requirement that the long term insurer be tied to the methodology it applied in respect of negative liabilities in its 2014 year be reconsidered as it creates difficulties for some long term insurers.

> *Response*: Accepted. In order to remove unintended anomalies as a result of this proposed amendment, amendments will be made in section 29A to calculate a specific amount to be phased in instead of requiring the application of the methodology applied in the past.

Comment: The proposed definition of *'value of liabilities'* in the 2015 Draft TLAB should not include expenditure not paid on the last day of the year of assessment since it will lead to a double deduction.

> *Response*: Noted. This is an operational aspect and does not require changes to the legislation. The tax returns will be updated to address this aspect.

Comment: It is proposed that the role of the FSB should continue in assisting with the determination of either the "*adjusted IFRS value"* or the *"value of liabilities"* for the purposes of section 29A to ensure that the methodology remains consistent with what was used prior to the 2015 Draft TLAB, especially in light of the fact that the "*adjusted IFRS* value" is an interim measurement for the *"value of liabilities"* until IFRS 4 Phase II becomes effective.

> *Response*: <u>Not accepted</u>. With the introduction of the SAM framework and the Insurance Act of 2016, the current FSB regulatory regime will no longer apply for tax purposes. Amounts reported according to IFRS will be used for calculating either the "*adjusted IFRS value"* or the *"value of liabilities"* for long term insurers.

Comment: Since the proposed changes to the tax treatment of long term insurers in the 2015 Draft TLAB are as a result of the introduction of the SAM framework and the Insurance Act of 2016, the proposed definitions of *"adjusted IFRS value"', "negative liabilities"* and *"value of liabilities*"' should come into operation when the Insurance Act 2016 is promulgated and should apply to years of assessment ending on or after that date.

> *Response:* <u>Accepted.</u> Changes have been made to the proposed amendments to section 29A to cater for the effective date.

4.5. Limitation of unwarranted relief from taxation in respect of foreign insurance by long term insurers

(Main reference: section 29A (11)(*g*)

Comment: In 2014, changes were made in section 29A(11)(*g*) of the Income Tax Act to limit the unwarranted relief from taxation in respect of foreign reinsurance. As a result, a proviso was added to section 29A(11)(*g*) to provide for the inclusion in gross income of reinsurance claims received by or accrued to an insurer in terms of reinsurance between the insurer and the non-resident with effect from 1 December 2014. The reference to reinsurance claims in the 2014 wording of section 29A(11)(*g*) created further loopholes and as a result changes were made in the 2015 Draft TLAB to replace the concept of "reinsurance" with "insurance". The proposed 2015 change affects some of the existing policies. It is therefore proposed that the effective date of 1 December 2014 which was inserted when the changes were made in the 2014 Draft TLAB be moved forward to 1 January 2016.

> *Response*: <u>Not accepted.</u> The main aim of the 2014 changes was to curb the unwarranted situation that gains under foreign reinsurance was not taxed. It has come to our attention that the 2014 changes created a further loophole as foreign insurance policies can also be used to achieve a tax benefit for policyholders compared to a direct investment in foreign assets. As a result, the proposed amendments in the 2015 Draft TLAB reflect the policy intention to tax claims under foreign insurance policies as income.

4.6. Refinement of taxation of risk insurance business of long term insurers

(Main reference: section 29A(13B))

Comment: In 2014, a fifth fund known as the risk policy fund (RPF) was introduced with effect from 1 January 2016. In the 2015 Draft TLAB, amendments were proposed to section 29A to allow for long term insurers to be granted a once off election to transfer all the existing risk policies to the new risk policy fund without triggering negative tax consequences. In order to limit increases in risk premiums and protect existing policyholder rights, it is proposed that long-term insurers identify homogenous books of existing risk business and have the option of transferring them to the new risk policy fund.

> *Response:* Accepted. The insurer may elect (once-off) that all policies or one or more classes of policies that share the same rights and obligations and that would have constituted risk policies on or after 1 January 2016 be eligible for transfer together with the associated liabilities and matching assets.

5. INCOME TAX: BUSINESS (INCENTIVES)

5.1. Accelerated capital allowances for manufacturing assets governed by supply agreements

(Main reference: New section 12CA)

*Commen*t: The way the section 12C(*bA*) (which accommodates an accelerated allowance where a taxpayer grants a components manufacturer the right of use of its plant without a rental being charged) is worded will give rise to substantial abuse and erosion of the tax base. Of great concern is that, although the business model for which the amendment is intended is well understood, the current version of the amendment could render section 23A, which governs the limitation of the 12C allowance in the cases or structures under which a manufacturing plant is provided to another person, for a rental charge.

> *Response*: Accepted. As one of the key sectors in the manufacturing sector, the manufacturers within the motor industry outsource parts of their manufacturing operations in order to secure the supply of components used in the assembly process of manufactured products. Along with these manufacturing operations, the plant necessary for the production of these components are acquired and made available by the manufacturer in the motor industry to the components supplier. Such an arrangement precludes both the manufacturer and the components manufacturer from benefitting from an accelerated capital allowance current available in respect of manufacturing assets.
>
> In order to ensure that the motor industry is not denied the intended incentive in the form of this accelerated capital allowance, a new section catering solely for this industry will be inserted to cover this business model.

5.2. Extending the window period and introducing a compliance period for the industrial policy project tax incentive regime

(Main reference: section 12I)

Comment: The introduction of a compliance period will resolve the difficulty approved participants currently experience to meet all the milestones for assessment and reporting every year. However, the compliance period must be limited to 3 years or until the mandatory and points scoring criteria have been complied with. This will deal with the situation where the training compliance period is longer than 3 years and also cater for projects that are implemented in a phased approach over multiple years.

> *Response:* Not accepted. The compliance period for assets is already three years. Aligning the training allowance benefit period to the compliance period is aimed at reducing the 6 year reporting period, as well as reducing the fiscal risk of allowing projects to claim the training allowance before assets are brought into use.

Comment: The proposed amendment to extend the window period for section 12I to the end of 2017 is welcomed. However, with less than 20% left of the budget earmarked for this incentive, this proposed extension would be of limited impact if the budget is not increased to accommodate this extension.

> *Response:* Not accepted. The bulk of the R20 billion tax allowance will not be utilised by 2015 and an increase in the budget is not being considered due to fiscal constraints.

Comment: The wording in clause 20(1)(*f*) of the 2015 Draft TLAB is incorrect in that it refers to subparagraph (ii) whereas it should refer to the substitution of paragraph (a) of section 12I(12) of the Act

> *Response:* Accepted. Section 12I will be amended accordingly.

Comment: Subsection 5(b) should be similarly amended to refer to the compliance period.

> *Response:* Accepted. Amendments will be made to subsection 5(b) accordingly.

5.3. Further alignment of the tax treatment of government grants

(Main reference: Sections 10(1)(*zI*) and 12P)

Comment: The 2015 Draft TLAB moves the exemption for PPP grants from section 10(1)(zI) and includes them in the provisions of section 12P. The new provisions relating to PPP grants in section 12P refers to amounts received from Government. Government is an undefined term and it is not clear which spheres of Government is covered for the exemption of PPP grants.

Response: Accepted. To align section 12P provision with the PPP provisions under section 12N and 12NA, amendments will be made in section 12P so that amounts received by a taxpayer under a PPP arrangement are exempt to the extent that they are received from Government in the national, provincial and local sphere.

5.4. Depreciation allowance in respect of transmission lines or cables used for electronic communication outside South Africa

(Main reference: Subparagraph (B) of paragraph (*dd*) of the proviso to paragraph (*f*) of section 11)

Comment: The 2015 Draft TLAB proposes to reduce the write off period in respect of transmission lines or cables used for electronic communication outside South Africa from 20 years to 15 years. The proposed 15 year write off period for an indefeasible right of use (IRU) is still too long. IRUs are now frequently entered into for far shorter periods. The result is that many IRUs are disqualified from the allowance lease premiums on the grounds that they are for a shorter period. It is submitted that there is no need for a minimum term for an IRU. The provisions of section 11(*f*) will themselves result in the write off period being the term of the lease. The minimum period requirement for IRUs in section 11(*f*) should be deleted.

Response: Not accepted. When the 20 year write off period for IRUs was introduced in 2009, it was based on IRUs typically having a 20 year term. However, the proposed minimum write off period of 15 years in this case is still appropriate and in line with industry practice. There have been calls for the IRU write off period to be reduced further to 10 years and to add a scrapping allowance. At present, we do not consider this to be the appropriate treatment. An IRU can be thought of as a type of lease agreement, which provides the grantee with the right to use the capacity of the submarine cable without ownership. A scrapping allowance is generally considered in respect of property that is owned, which is not the case with the IRU.

5.5. Special Economic Zones (SEZ): Anti-profit shifting provision

(Main reference: section 12R)

Comment: To counter the potential shifting of profits from connected persons to benefit from the lower income tax rate available to companies operating within SEZ, the 2015 Draft TLAB proposes the introduction of an anti-avoidance measure. The concern around the potential profit shifting that taxpayers may engage in upon the commencement of the SEZ regime is well understood. However, the limitation of gross income generated from transactions with connected person is too restrictive as gross income includes exempt dividend income.

Response: Accepted. The anti-avoidance measure is intended to dissuade taxpayers from shifting taxable profits from connected persons in order to benefit from the 15 per cent tax rate envisaged under the SEZ regime. Exempt dividends were not meant to be subject to this limitation. As such, a company will be disqualified from the SEZ Income Tax incentives if more than 20 per cent of its deductible expenditure incurred or more than 20 per cent of its income arises from transactions with connected persons.

Comment: While the rationale for the proposed anti-avoidance is understood, the proposal would result in a doubling up of anti-avoidance measures where a qualifying company transact with a connected person that is not a resident. This is because these transactions are subject to transfer pricing which seeks to ensure an arm's length consideration between connected persons.

Response: Partially accepted. Amendments will be proposed so that the anti-avoidance measure in section 12R will only be applicable to transactions between connected persons that are resident or transactions with non-residents that are attributable to a permanent establishment of those non-residents in South Africa.

5.6. Depreciation allowances for renewable energy machinery

(Main reference: section 12B)

Comment: Instead of an absolute value which is currently proposed in the 2015 Draft TLAB, the approach should rather be one of an energy output range in order to give flexibility to companies wishing to invest in solar projects so that they make more informed decisions.

Response: Not accepted. The proposed absolute 1 MW value is based on the generation capacity of the machinery, plant, implement, utensil or article (essentially a more accurately determinable figure than output).

Comment: The trade requirement of section 12B(1)*(h)* will result in distortions as domestic installations will not qualify for the accelerated allowance as it requires the taxpayer to use the installation for purposes of trade.

Response: Not accepted. The proposed accelerated depreciation policy is intentionally aimed as a business tax incentive. An incentive for the installation of photovoltaic solar energy (PV rooftops) to households could be considered outside the tax system, similar to the previous subsidy for solar water geyser/ heaters at a later stage.

Comment: In light of the urgency of installing new capacity and addressing the electricity supply shortage, the proposed effective date of years of assessment commencing on or after 1 January 2016 seems unreasonable and should be accelerated to years of assessment ending on or after 1 January 2016.

Response: Not accepted. It is not prudent that the proposed amendments should apply retrospectively. Such a retrospective provision would provide an incentive where it is not necessary and will also have unforeseen financial implications for the fiscus.

Comment: In terms of section 12I (Industrial Policy Projects) only assets which qualify under sections 12C(1)*(a)*, 13 or 13*quat*, can qualify for the additional tax allowance as envisaged under this section. With the emphasis on promoting the use of renewable energy sources by the private sector it is suggested that assets qualifying under section 12B also be allowed to qualify under the section 12I allowance.

Response: Not accepted. The comment is outside the scope of the 2015 Budget Proposals and subsequent proposed amendments to the Act. It might also not be appropriate to provide additional benefits for the same investment.

5.7. Adjustment of energy savings tax incentive

(Main reference: section 12L)

Comment: A major drawback of the incentive is its limited scope. It applies only in the year of assessment in which energy efficiency savings are achieved. The incentive should be extended so as to apply to energy efficiency savings over a period of three to five years.

Response: Not accepted. The comment is outside the scope of the 2015 Budget Proposals and subsequent proposed amendments to the Act. It should be noted that the value of the incentive has been increased from 45 cents / kWh for verified energy efficiency savings to 95 c / kWh, quite a substantial increase. This monetary amount is based on the actual savings that will materialise during the year based on a verified baseline. There is no rationale to provide an over-generous incentive of this nature for multiple years on the same baseline as it could defeat the policy rationale of "encouraging a process of continual improvement" of the baseline. It should also be noted that the payback period, without the tax incentive, for many energy efficiency projects is less than two to three years.

Comment: The policy and regulation relating to the energy saving incentive should be amended to include fuel switching e.g. grid to solar as a measurable energy saving technological improvement.

Response: Not accepted. The comment is outside the scope of the 2015 Budget Proposals and subsequent proposed amendments to the Act. The scope of this incentive was design to kick start investments in energy efficiency savings as part of the low-hanging fruits to reduce the high energy and carbon intensity of the economy. It should be noted that this incentive has been designed as part of the revenue recycling initiatives of the carbon tax policy, is being implemented ahead of the implementation of the carbon tax policy and is a way to mitigate the financial impact of the carbon tax and at the same time reap the benefits of reduced energy use and greenhouse gas emissions. Renewable energy projects are specifically excluded to eliminate the likelihood of projects receiving concurrent benefits from government incentives that are catered for through other incentive mechanisms.

Comment: Several challenges relating to both the administration and issue of certificates by SANEDI are being experienced by industry. The process is considered more onerous than originally anticipated.

Response: Noted. SANEDI has made significant progress with the verification of the reported or intended energy efficiency savings. This is a process that requires careful scrutiny and cannot be unduly fast tracked. The experience in the current year of operation will enhance administration of the project going forward. SANEDI will also assist with training and increasing the number of measurement and verification agents.

6. INCOME TAX: INTERNATIONAL

6.1. Revision of the definition of foreign partnership

(Main reference: section 1, definition of foreign partnership)

Comment: In the 2015 Draft TLAB, amendments were proposed by including in the definition of a *"foreign partnership*" the following words "any partnership, association, body of persons or entity is not liable for or subject to any tax on income *other than tax levied by a municipality or local authority, in that country*". The proposed amendments to address the anomaly are welcomed however the wording *"local authority"* may be misconstrued to refer to taxes levied by the national revenue authority (and not only by the municipal revenue authority).

Response: Accepted. Amendments will be made in the definition of "foreign partnership" to capture the underlying purpose.

6.2. Removing Capital Gain Tax rules applicable to cross issue of shares and introducing counter measures to address tax-free migrations

(Main reference: section 9H and paragraph 64B of the Eighth Schedule to the Act)

Comment: The 2015 Draft TLAB proposal to reverse the 2013 amendment to paragraph 11(2)(b) of the Eighth schedule is welcomed. However, there is a concern regarding the proposal to deny the participation exemption in respect of disposals to connected persons as the proposal is too broad and will have the unintended consequence of limiting the ability of foreign multinationals to re-organise their investments. It is suggested that the proposed amendment be withdrawn or be significantly narrowed to target the perceived abuse.

Response: Not accepted. The policy rationale for the introduction of a participation exemption was intended to encourage South African multinationals to repatriate their foreign dividends and gains back to South Africa. It was not aimed at facilitating offshore restructurings. Removing the proposal to deny participation exemption in respect of disposals to connected persons will expose the fiscus to abusive tax free disposals of foreign operations of South African companies to their non-resident connected persons.

Comment: The 2015 Draft TLAB proposes that the claw back should apply in relation to participation exemption that applied within 3 years of migration of residence. The 3 year period is longer than the 18 month period contained in other claw back provisions in the Act, for instance, those relating to corporate rollover relief provisions. It is therefore proposed that the claw-back should only apply to participation exemptions within 18 months of migration and not within three years.

Response: Not accepted. The period of 18 months is too short in the given circumstances. During a workshop held on 26 March 2015 with taxpayers, there was a consensus regarding the claw-back period. A 3 year period was viewed to be a more reasonable period than the 5year period that was originally proposed.

Comment: The claw-back of the participation exemption should apply only on migration of residence and not on a company becoming a headquarter company.

Response: Comment misplaced. The claw-back of the participation exemption does not apply on a company becoming a headquarter company and only applies on migration of residence.

6.3. Withdrawal of special foreign tax credits for service fees sourced in South Africa

(Main reference: Section 6*quin*)

Comment: The 2015 Draft TLAB proposes to repeal Section 6*quin* foreign tax credit rebate in respect of South African sourced service fees income with effect from 1 January 2016. While the comments by National Treasury in relation to the repeal of section 6*quin* are noted and have some merit, South African investors face serious obstacles when they invest in African countries as some of these countries levy withholding taxes contrary to tax treaties. Section 6*quin* acts as a legitimate measure to mitigate double tax faced by taxpayers in doing business with the rest of Africa and as an incentive to make South Africa attractive as regional service hub. It is therefore proposed that section 6*quin* should not be repealed, or to the extent that it is repealed, there should be further grace period of a year so that the repeal only comes into operation on 1 January 2017.

Response: Not accepted. Section 6*quin* is a departure from international tax rules and tax treaty principles in that it indirectly subsidies countries that do not comply with tax treaties. South Africa is the only country in the world that provides for this kind of tax concession. While the enactment of section 6*quin* relief was well intended, it has resulted in a significant compliance burden on SARS as some taxpayers are exploiting this relief by claiming it even for other income such as royalties and interest that are not intended to be covered under section 6*quin*. Further, the Davis Tax Committee Interim Report on Action 6 entitled "Preventing Treaty Abuse", in its discussion of section 6*quin* entitled "Base erosion resulting from South Africa giving away its tax base", states that South Africa has effectively eroded its own tax base as it is obliged to give credit for taxes levied in the paying country. That said, the mutual agreement procedure available in tax treaties as a mechanism to resolve disputes of double taxation assist in this regard and SARS has started to resolve some of these disputes through this process. As a concession, in order to mitigate double tax faced by South African taxpayers in doing business with the rest of Africa, amendments will be proposed to the current provisions of section 6*quat* (1C) to allow a deduction of foreign taxes which are proved to be paid or payable without taking into account the option of mutual agreement procedures under a tax treaty.

6.4. Reinstatement of the Controlled Foreign Company diversionary income rules

(Main reference: section 9D)

Comment: The 2015 Draft TLAB proposes to reinstate diversionary rules on the CFC outbound sale of goods that were deleted in 2011. The proposed reinstatement of these rules is unfortunate as these rules resulted in many unintended consequences. In addition, these rules do not work as taxpayers can easily do restructuring to break these rules and only unwary taxpayers will be inadvertently hit by the rules. Further, for outbound sale of goods, the transfer pricing rules are sufficient to address the concern. Alternatively, similar rules to those currently applying to imported goods should be introduced, for example, high tax exclusion and a permanent establishment exclusion.

Response: Not accepted. While transfer pricing rules can be applied to prevent the shifting of income offshore through the sale of goods and services, the CFC diversionary rules are more effective in preventing shifting of profits through these transactions. Transfer pricing auditing processes by their nature often take a long time to be finalised. CFC diversionary rules are necessary as a back-up to transfer pricing rules to deal with base erosion practices.

Comment: The diversionary rules in respect of CFC outbound sale of goods sourced from South Africa should be narrowed to exclude regional sale of goods and not to only be limited to country-specific sales.

Response: Noted. While it is possible to consider, the option of excluding regional sales of goods leads to the practical concerns of how to define the term "*region*" and how to limit the risks where the other parties might be located in low tax jurisdictions.

6.5. Definition of interest for withholding tax purposes

(Main reference: section 50A)

Comment: The 2015 Draft TLAB proposes that the definition of the term "*interest"* for withholding tax purposes should be *"interest"* as defined in section 24J(1). Interest as defined in section 24J(1) is too wide and includes sale and leaseback arrangements. It is proposed that the definition of *"interest"* for withholding tax purposes should be limited to paragraph (a) of section 24J(1) *"interest*" definition. This will exclude sale and leaseback arrangements.

> *Response:* Partially accepted. The definition of the term *"interest"* for withholding tax purposes will be revised and will be limited to paragraphs (a) and (b) of the definition of *"interest"* in section 24J(1).

Comment: The proposed definition of the term "*interest"* for withholding tax purposes should be prospective and must be aligned with the date of release of the draft TLAB or be effective from 1 January 2016 or 1 March 2016 instead of 1 March 2015 in order to avoid any retrospective application of the provisions.

> *Response:* Accepted. The effective date for the proposed definition of the term *"interest"* for withholding tax purposes will be prospective and will be applicable with effect from 1 March 2016.

7. VALUE-ADDED TAX

7.1. Enterprise supplying Commercial Accommodation: Monetary threshold adjustments

(Main reference: section 1(1): Definition of "commercial accommodation" and proviso (ix) to the definition of "enterprise")

Comment: The 2015 Draft TLAB proposes to increase the threshold from R60 000 to R120 000 in respect of businesses supplying commercial accommodation to register for VAT. The increase of this threshold to twice the existing amount is excessive and will result in many vendors having to de-register, thus triggering an exit VAT which could be rather substantial. In order to alleviate this burden, it is proposed that a 12-month repayment period of relief is given to vendors who will have to deregister in terms of section 8(2) of the Act as a result of the proposed amendment. It is further recommended that SARS not levy interest on the capital due.

> *Response:* Noted. The policy intention is not to over-burden vendors who will now fall out of the VAT net. Section 167, read together with section 187 of the Tax Administration Act provides for the vendor to enter into a payment arrangement with SARS. However, the Tax Administration Act also provides for SARS to levy interest and penalties on the total repayment amount. The vendor may apply for the remission of the penalties, but not the interest amount. This is to take account of the time value of money.

7.2. Zero-rating: Goods delivered by a cartage contractor

(Main reference: section 11(1)(*m*)(ii))

Comment: The 2015 Draft TLAB seeks to align the provisions of section 11(1)(*m*)(ii) of the VAT Act with SARS Interpretation Note 30 (Issue 3). However, there is a legislative mismatch between the VAT Act, Interpretation Note 30 and Regulation R316 published in Government Gazette No. 37580. The Act requires that the cartage contractor be registered for VAT but the Interpretation Note and the Regulation do not require this.

Response: Accepted: Amendments will be made in section 11(1)(*m*)(ii) of the VAT Act to remove the requirement for the cartage contractor to be registered for VAT.

7.3. Zero-rating of services: Vocational Training

(Main reference: section 11(2)(*r*))

Comment: The 2015 Draft TLAB proposal amends section 11(2)(*r*) by clarifying that vocational training is zero rated including instances where such training is provided through a third party vendor for the benefit of an employer who is not resident in South Africa. However, the wording in the proposed proviso to section 11(2)(*r*) is likely to cause significant confusion and debate as to whether the services are "for the benefit of an employee or another person".

Response: Accepted. In order to address the unintended confusion further clarity will be provided in this regard in the Explanatory Memorandum.

7.4. Time of supply: Connected Persons (Undetermined Amounts)

(Main reference: sections 9(2)(*a*) and 10(4)(*a*))

Comment: In instances where the recipient vendor is partially taxable, the 2015 Draft TLAB proposes to deem the consideration to be open market value in cases where the supply is between connected persons and consideration cannot be determined at the time of supply. In this regard, the concern is that the market value may be difficult to quantify at the time of supply.

Response: Noted. The vendor may utilise section 3(4) of the VAT Act to make an application to the Commissioner to approve any alternative method of calculation in such instances where the open market value cannot be determined.

7.5. Repealing the zero-rating for the National Housing Programme

(Main reference: sections (8)(23) and 11(2)(*s*))

Comment: The 2015 Draft TLAB proposes to abolish the current provisions contained in section 8(23) read together with section 11(2)(*s*) of the VAT Act of zero rating for the supply of goods and services in terms of the national housing programme contemplated in the Housing Act, 1997. Since section 8(23) will now no longer exist, it could be deemed that the definition of *"grant*" in section 1(1) will now include payments made in terms of the National Housing Programme and hence zero-rated in terms of section 11(2)(t), read together with section 8(5A).

Response: Accepted: An amendment will be proposed to the definition of "*grant*" in section 1(1) in order to clarify that payments in terms of the National Housing Programme are excluded from this definition and hence will always be standard-rated.

7.6. Removing the reference to "shareholder" as defined in the Income Tax Act

(Main reference: section 1(1), definition of "connected person", subparagraph (d)(ii))

Comment: The Income Tax Act was revised and no longer contains a definition of *"shareholder".* Therefore removing the reference to *"shareholder"* from the VAT Act is logical. However, the consequential removal of the reference to the *"shareholder*" in the Vat Act is not merely a technical amendment since the word *"shareholder*" in the VAT Act is still used and now requires a definition.

Response: Accepted*:* A new definition of *"shareholder*" is to be added to section 1(1) of the VAT Act.

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8. Transfer Duty Act, 1949 (TDA)

8.1. Administrative non-compliance penalty

(Main reference: section 4; clause 1)

Comment: The conversion of the "time-value of money" penalty into an administrative non-compliance penalty introduces a late payment penalty for a tax that falls outside the class of taxes where such a penalty already exists. This penalty should be reconsidered.

Response: Accepted. Proposal will be withdrawn for reconsideration.

9. Income Tax Act, 1962 (ITA)

9.1. Transition to self-assessment

(Main reference: section 3; clause 2)

Comment: SARS does not appreciate the legal implications as well as the socio-economic implications of migrating to self-assessment for taxpayers. Much of this is as a result of its migration without law to support that approach to date. Self-assessment does not only impact on the taxpayer but also on SARS and how it performs its functions. The migration will also see SARS not requiring the services of assessors but auditors, the latter which it is submitted require a different skills set.

The Memorandum of Objects refers to both Australia and the UK as examples of successful implementation of the self-assessment system. Australia has now had two review committees since 1988 to seek a balance between taxpayers' rights and obligations which had been overly burdensome on the taxpayer in the initial migration. Furthermore, it is also acknowledged that self-assessment is administratively burdensome on the taxpayer. In this regard the UK in its budget speech 2015 in April 2015 has undertaken to scrap the self-assessment system to "allow business to do business and not tax administration". SARS' conclusion that the system was successful therefore seems misplaced.

Response: Not accepted. The practical migration to a self-assessment system has been underway for decades. The Margo Commission noted in its 1986 report that; "It may be questioned whether South Africa, under the present system, does not have the worst of both worlds, namely a de facto self-assessment system (as few returns are in fact assessed in the old-fashioned sense) which achieves none of the advantages of a proper self-assessment system." The Commission went on to recommend a move towards self-assessment, which was subsequently supported by the Katz Commission. The migration involved incremental changes as third party data became more accessible to SARS and reliable, which resulted in the pre-population of returns. This, together with the practice that supporting documents need only be submitted if requested by SARS, substantially reduced the administrative burden on taxpayers in completing returns. It is fully appreciated that the final migration to income tax self-assessment does not only involve legislative amendments, but also requires operational, administrative (forms and processes) and systems review and adjustment, which is currently underway.

According to the OECD Tax Administration 2015 report, more than half of the 56 revenue bodies surveyed confirmed that their personal income tax system is designed and based on self-assessment principles. Apart from the developing countries mentioned in the Memorandum of Objects, African countries that have adopted self-assessment systems are Kenya, Malawi, Nigeria and Zambia. Finally, with respect to the UK proposal to do away with annual tax returns and replace them with digital tax accounts, the official HM Revenue & Customs publication in this regard notes that; "taxpayers will still be responsible for ensuring their tax bills are right and telling HMRC about information that is not reported by other means." This has led at least one commentator to suggest that; "In reality, this appears to be just an updated digital version of the current online tax return system."

Comment: Although the discretions of the Commissioner in respect of the determination of tax liability should be deleted in general, certain omissions remained e.g. section 11*(e)*.

Response: Partially accepted. SARS is in the process of removing discretions but this is a phased approach. The particular example provided has highlighted an inconsistency between the TALAB and TLAB that will be addressed.

Comment: The effective date of the deletions proposed by this amendment must be aligned with the effective date of the consequential amendments to the discretions in the corresponding provisions in the TLAB.

Response: Accepted. The TALAB and TLAB self-assessment amendments effective dates will be aligned.

9.2. Treatment of withholding payment on sales of immovable property by non-residents if no return is submitted

(Main reference: section 35A; clause 3)

Comment: For an amount to be a final income tax payable, it should be preceded by some form of assessment. It is submitted that the proposed amendment should deem payment to constitute a self-assessment if no return is submitted.

Response: Accepted. The proposed amendment will be reworded accordingly.

9.3. Definition of personal service provider

(Main reference: paragraph 1 of Fourth Schedule; Clause 6)

Comment: The term "settlor" (which is akin to a trustee under SA legislation) is not a term generally used in relation to trust law in South Africa and is not a defined term for purposes of the proposed amendment. It is proposed that the term "settlor" should be defined with clear precision within the context that it is intended.

Response: Comment misplaced. The term is encountered in SA case law and reference works. A settlor is the person (also known as the founder) who determines the contents of the document in terms of which the trust is established and governed.

9.4. Replacement of discretion by application process

(Main reference: paragraph 5 of the Fourth Schedule; Clause 7)

Comment: Clarity is sought on whether the removal of the discretion and replacement with a directive implies that the directive process will be expanded to accommodate these applications and the forms revised for directive applications. It is submitted that SARS must clarify the prescribed form and manner to be followed in order to submit such an application to SARS in the draft legislation or the Memorandum of Objects.

Response: Partially accepted. An enabling provision similar to that used in the Tax Administration Act will be inserted by adding the words "in the prescribed form and manner". Attempting to prescribe the form and manner in detail will be inflexible and inconsistent with the approach generally followed in tax Acts.

9.5. PAYE: Additional medical tax credits for over 65s

(Main reference: paragraph 9 of the Fourth Schedule; Clause 8)

Comment: This amendment is welcomed.

Response: Noted.

9.6. Amendment to definition of remuneration

(Main reference: paragraph 11A of Fourth Schedule; Clause 9)

Comment: Though remuneration includes certain capital amounts, it does not include as a general rule capital gains as envisaged in the Eighth Schedule. Section 8C of the Income Tax Act, does include capital distributions and this amendment aims to include these as being subject to PAYE and not the future capital gains. Please confirm that our understanding is correct.

Response: Noted. The scope of the proposed amendment is limited to amounts referred to in section 8C which are required to be included in the income of employees. It does not refer to capital gains under the Eighth Schedule.

Comment: The provision has been amended with more generic wording "amount referred to in section 8C" rather than using the word gain. However, in the deeming provision it then refers again to gain or that amount which does not broaden the scope but merely adds confusion as the more general wording would already include any gains in section 8C. It is submitted that the wording should read: "…amount referred to in section 8C which is required to be included in the income of the employee, **[the amount of that gain or]** that amount must …".

Response: Comment misplaced. The commentator overlooked the reference to "gain" in paragraphs *(a)* and *(b)*. The deeming provision applies to paragraphs *(a)*, *(b)* and *(c)* and therefore now refers to "the amount of that gain" (in paragraphs *(a)* and *(b)*) "or that amount" (in paragraph *(c)*).

9.7. Consequential changes

(Main reference: paragraph 13 of Fourth Schedule; clause 12)

Comment: Paragraphs 13 and 14 should be amended to include a remedy for the employee to be able to comply with his or her income tax obligations and obtain credit for PAYE withheld where the employer has failed to submit its PAYE declaration or issue IRP5s. Furthermore, it must be clarified that it is SARS who should compel the employer to comply.

> *Response:* Not accepted. The comment does not relate to the substitution of the reference to obsolete paragraph 11C(5) with paragraph 14(5). Paragraph 14(5) already allows the Commissioner to "direct otherwise" and permit an employer to issue IRP5s even if the employer's PAYE declaration has not been submitted. Doing so introduces a significant risk, however, since SARS is not in a position to verify that the credits it grants in terms of the IRP5s relate to PAYE that was actually paid by the employer. Failure to submit bi-annual employer reconciliation return (EMP501) may, in terms of paragraph 14(6) of the Fourth Schedule, result in an administrative penalty under Chapter 15. Failure by an employer to issue an IRP5 is an offence in terms of paragraph 30 of the Fourth Schedule.

9.8. Provisional tax estimates

(Main reference: paragraph 19 of Fourth Schedule; clause 16)

Comment: By removing the discretion of the Commissioner all companies would be required to file provisional tax returns. This would mean that dormant companies, nominee companies, etc. would also be required to file provisional tax returns, notwithstanding the fact that these entities would never be liable for tax. This would place an unnecessary administrative burden on SARS and taxpayers.

> *Response:* Accepted. The wording "unless the Commissioner directs otherwise" will be inserted.

Comment: SARS' decision to increase an estimate for provisional tax purposes should be subject to an internal remedy, so a taxpayer need not incur the substantial costs of applying to the High Court for relief. The internal remedy of objection and appeal is a more practical and cost effective than a High Court application. Furthermore, a taxpayer will not be able to claim a refund of an overestimated amount by SARS, which could potentially have a negative impact on the taxpayer's liquidity. Interest is also only paid from the period commencing six months after year end leaving the taxpayer out of pocket with respect to the interest between the date of the provisional tax payment and six months after year end.

> *Response:* Not accepted. The taxpayer will receive prior notice of the fact that SARS is reviewing the estimate when it is given an opportunity to justify its original estimate. If liquidity concerns arise, the instalment payment provisions of the Tax Administration Act are available. If the taxpayer is dissatisfied with the estimate by SARS, there is an internal remedy available to it under section 9 of the Tax Administration Act to request a review of the estimate by SARS. If necessary, the taxpayer would also be able to request that the estimate be reviewed by the Tax Ombud. Finally, consideration is being given to the payment of interest up to the "effective date" on that part of SARS' increase in the estimate that exceeds the amount finally assessed. Such a provision would, however, raise the question of the circumstances under which analogous interest would be

charged. A review interest paid and charged under these circumstances will be undertaken with a view to possible amendments in the 2016 legislative cycle.

Comment: Paragraph 19(1)*(c)* compels the taxpayer to seek approval from SARS before an estimate for an amount less than the basic amount may be used. As the taxpayer has no control over how long SARS may take to respond, paragraph 19(1)*(c)* must provide for a minimum time period before the estimate is due for the application to be made. The taxpayer should have 14 days, from the date of the notice from SARS that the request is accepted or rejected, to submit the estimate.

Response: <u>Accepted.</u> Paragraph 19(1)*(c)* has now been amended to remove the Commissioner's discretion. The estimate must, instead, be justified under the circumstances.

9.9. Penalty for underpayment as a result of underestimation

(Main reference: paragraph 20 of Fourth Schedule; clause 17)

Comment: It is proposed that the threshold be increased to R2 million in order to maintain the threshold in real terms.

Response: <u>Noted</u> for 2016 Budget Review.

Comment: Proposed amendments to paragraph 20(2A) will have draconian implications for provisional taxpayers who do submit a second provisional tax return, but do so late. In this regard it is unclear whether the remittance relief in paragraph 20(2) would apply as the submission is deemed to be an estimate of an amount of nil taxable income and therefore is arguably not calculated seriously. It is proposed that paragraph 20(2) should be amended to clarify that even where paragraph 20(2A) applies, if the taxpayer does submit an estimate then the discretion should continue to apply in respect of the penalty relief.

Response: <u>Partially accepted.</u> The proposed amended has been redrafted to provide provisional taxpayers a six or seven month window from one provisional tax payment to the next to correct the situation before the nil estimate is triggered. To avoid the paragraph 20(1) penalty, a provisional taxpayer need only to submit a seriously calculated and accurate estimate before or with the subsequent payment of provisional tax.

10. Customs and Excise Act, 1964 (C&E Act)

10.1. Alignment of prescription periods to general prescription period

(Main reference: section 99; clause 24)

Comment: Amend sections 76(4); 76B(1)*(b)*; 76B(1)*(d)* and 76B(1)*(e)* accordingly (i.e. amend the two year period to three years).

Response: Noted. Sections 65 and section 66 of the Customs and Excise Amendment Act, 2014, have effected the suggested amendments to sections 76(4); 76B(1)*(b)*; 76B(1)*(d)* of the C&E Act. A review of the remaining prescription periods will be undertaken with a view to possible amendments in the 2016 legislative cycle.

11. Value-Added Tax Act, 1991 (VAT Act)

11.1. Documentary proof

(Main reference: section 16; clause 25)

Comment: The proposed amendment seems to envisage two public notices, one for circumstances that could apply and one for alternate documentation. It is proposed that all information should be included in a single public notice.

Response: Noted. The information will be published in the format considered most appropriate for ease of use and understanding.

Comment: The term public notice is not defined in the VAT Act but only in section 1 of the Tax Administration Act. It is proposed that the term "public notice" should either be defined in the VAT Act or reference be made to the definition of the term in the Tax Administration Act.

Response: Partially accepted. Reference will be made to "as may be prescribed by the Commissioner" so as to align the wording with the approach followed in the rest of the VAT Act.

Comment: To make the legislative references consistent and prevent interpretative differences between the Tax Administration Act and the VAT Act, it is proposed that the word "furnished" in section 16(2)*(f)* and *(g)* should be replaced with word "submitted" as used in Chapter 4 of Part A of the Tax Administration Act.

Response: Not accepted. The wording is consistent with the wording elsewhere in the VAT Act.

Comment: The effective date of the amendment should be made clear as applying to tax periods ending on or after the date of promulgation to avoid a negative impact on taxpayers in relation to past tax periods.

Response: Accepted. An effective date of 1 April 2016 is proposed, and the amendment will apply to tax periods commencing on or after that date.

11.2. Prescription

(Main reference: section 41; clause 27)

Comment: The proposed amendment introduces a reference to section 99(2) of the Tax Administration Act, while paragraphs (*aa)* to *(cc)* have not been deleted, with the effect that these requirements are extended and duplicated. Section 41 should be amended to align to the new requirements proposed in section 99 of the Tax Administration Act as to when prescription would apply.

Response: Accepted. The proposal has been amended to delete paragraph *(d)* of section 41 as the process is regulated under the Tax Administration Act.

12. Mineral and Petroleum Resources Royalty (Administration) Act, 2008

12.1. Penalty for underestimation of royalty payable

(Main reference: section 14; clause 31)

Comment: Given the duplication between the section 14 penalty and the understatement penalty under the Tax Administration Act, if SARS applied the penalty in terms of the Tax Administration Act, it is submitted that the repeal of section 14 should be made retrospective to 1 October 2011. If SARS applied the section 14 penalty, it is submitted that any penalties in terms of the Tax Administration Act should be expressly excluded from 1 Oct 2011 to the effective date of amendment.

Response: Not accepted. On review the penalty is more akin to a penalty for an underpayment of provisional tax as a result of underestimation in terms of paragraph 20 of the Fourth Schedule to the Income Tax Act. The amendment will be revised to provide the Commissioner the power to remit part or entire amount of the penalty on a basis similar to that contained in paragraph 20(2).

13. Tax Administration Act, 2011 (TAA)

13.1. Definition of international tax standard

(Main reference: section 1; clause 32)

Comment: Regarding the new definition of "international tax standard", to what extent has SARS researched and verified that no data protection laws would be contravened?

Response: Noted. The most important data protection law in this context is the Protection of Personal Information Act, 2013 (POPI), which has yet to fully commence. This Act essentially seeks to protect personal information obtained and processed by public and private bodies. In the context of collecting and retaining personal information, POPI allows this if it is done under a statutory power do so. In the case of SARS, this will be its information gathering powers under Chapter 5 of the Tax Administration Act.

In the context of the exchange of taxpayer information by SARS under the various tax treaties, such as Double Taxation Agreements and Tax Information Exchange Agreements, the transfer of personal information is permissible under section 17 of POPI if the recipient of the information is subject to a binding agreement which provide an adequate level of protection. All of SA's international tax agreements impose strict confidentiality and disclosure provisions on the treaty partners, based on OECD and UN standards.

13.2. Administration of tax acts

(Main reference: section 3; clause 33)

Comment: SARS can only exchange taxpayer information with another country under a bilateral or multilateral international tax agreement, as defined in the Tax Administration Act. Hence, the word "only" should be inserted between retain and exchange of information: "SARS may retain and only exchange the information…".

Response: <u>Accepted.</u> The reference to exchanging the information has been deleted, since any such exchange will take place under an international tax agreement that is incorporated into domestic law under the provisions of the relevant tax Act.

13.3. Delegation of powers and duties

(Main reference: section 6; clause 34)

Comment: The reference to "a person" can include a person other than a SARS official delegated by the Commissioner. It is submitted that it would be outside the scope of the enabling legislation for the Commissioner to delegate powers beyond SARS officials and hence it is proposed that the words "a person" should be replaced with "a SARS official".

Response: <u>Accepted.</u> "Person" will be replaced by "SARS official". Further clarity will be provided by inserting a cross-reference to subsection (3)*(a)*, *(b)* or *(c)*.

13.4. Legal proceedings involving Commissioner

(Main reference: section 11; clause 35)

Comment: The proposed amendment appears to be nonsensical as it provides for an outright exclusion which is overridden by specific exclusion. It is proposed that the provision should rather state that only such persons who have been empowered by the Tax Administration Act to authorize such proceedings may do so, as no exclusive right for the Commissioner was intended as per these proposals.

Response: <u>Accepted.</u> The proposed amendment will be reworded to address the concern.

13.5. Registration to furnish third party returns

(Main reference: section 26; clause 37)

Comment: In the furtherance of legal certainty, and for ease of reference, SARS should by government notice publish the names of institutions required to register as a person required to submit a return, with specific reference to the specific intergovernmental agreement in terms of which this is enabled.

If the intention is that the administration of this provision should be coordinated and enforced in line with international treaties, then this should be specifically clarified either in the main body of the legislation or via public notice.

> *Response:* Partially accepted. A public notice will be published indicating the classes of persons required to register and submit a return. The public notice will only apply to persons that SARS has jurisdiction over.

Comment: Affected parties should be properly consulted as to the obligation and financial burden required from them and the reasonability of information sharing agreements.

> *Response:* Noted. In the context of the OECD Standard for Automatic Exchange of Financial Account Information in Tax Matters, SARS is in the process of consulting with the affected financial institutions as it did with the implementation of the FATCA Intergovernmental Agreement with the US, which is an international tax agreement.

Comment: "International standard" should be revised to read "international tax standard" as that term is defined in section 1 of the Tax Administration Act.

> *Response:* Accepted.

13.6. Reportable arrangements

(Main reference: section 34; clause 38)

Comment: With a clear obligation to report listed arrangements being placed on the parties, it is submitted that there is no need to extend a reporting obligation in relation to such arrangements to a promoter. In fact, it may be more appropriate to require parties to all arrangements to report and remove the reporting obligation from the promoter. The inclusion of a promoter in the definition of a participant should be removed or limited to section 35(1) reportable arrangements.

> *Response:* Not accepted. The proposal does not extend the reporting obligation – the promoter was included from the introduction of the reportable arrangement scheme. The promoter has the most insight and knowledge of the structure which it organises, sells, designs or manages. Also, it should be noted that section 37(3) absolves a participant (including a promoter) from reporting if that participant obtains a written statement from any other participant that the other participant has disclosed the reportable arrangement.

Comment: The proposed addition to the definition of "participant" of "any other person who is a party to an "arrangement" listed in a public notice as referred to in section 35(2) widens the net of reportable arrangement legislation. It is not clear what the policy thinking was and why this penalty is warranted. The definition accordingly seems vague and is casting the net arbitrarily too wide.

Response: Not accepted. The purpose of the change to the definition of 'participant' is to clarify the responsibility for reporting of listed arrangements. Section 37(3) provides participants with relief from reporting where another participant in the arrangement has already reported it. Furthermore, SARS notes that it does not consider a bank to be a party or participant to, or promoter of, an arrangement merely because the bank has received and acted on an instruction from a client to make payment of any amount out of an account held by that client with that bank.

13.7. Procedure when legal professional privilege is asserted

(Main reference: section 42A; clause 40)

Comment: There is no reason why questions must be answered about the document if it could simply and efficiently be referred to an attorney on the panel who will be able to determine if it is subject to legal privilege or not. It is proposed section 42A be deleted and the already established procedure in terms of section 64 be applied to all cases where legal professional privilege is asserted as this will ensure that a uniform process applies for all claims to privilege for Chapter 5 as a whole. Alternatively where a taxpayer or person alleges legal professional privilege in respect of a document, request the practitioner who drafted the document to confirm the privilege under oath or solemn declaration.

Response: Not accepted. The first objective of section 42A is to resolve the matter between SARS and the taxpayer as opposed to starting with an adjudicative and generally more protracted process. This approach is followed elsewhere in the Act, for example section 66 which provides that a taxpayer subjected to a search and seizure and who intends to bring an application for the return of the seized relevant material or costs of damages, must first request this from SARS and only if SARS refuses, bring a High Court application.

Applying this approach to assertions of legal professional privilege regarding relevant material required by SARS, which happen fairly often, means there will be a process to handle the volumes of such matters. If SARS and the taxpayer agree that the material is privileged, alternative methods such as redaction of the privileged part and providing SARS with the remainder can be pursued. This will substantially reduce the number of cases that require adjudication by an independent legal practitioner or the High Court.

The underlying difficulty with the comment is that it proposes a model where SARS does not even have a basic set of information to enable it to determine whether a document qualifies for legal professional privilege. In the absence of this information SARS has no basis for determining whether it agrees or not with the taxpayer's assertion of privilege or a decision in this regard by an independent legal practitioner or court. The courts have warned against overreliance on a "judicial peek" to decide matter of confidentiality in decisions of the High Court in the case of privilege in a tax matter and the Constitutional Court in the case of promotion of access to information.

Comment: The particular information sought under the present draft of section 42A, in particular subparagraphs *(a)*, *(c)*, *(e)*, *(h)* and *(i)* are so intrusive that these requirements may effectively compel a taxpayer to waive legal privilege in the particular document by requiring the taxpayer to disclose information about the content of the privileged document. It is proposed that the wording be revised to give proper context as to what information will satisfy the requirements set out therein. Alternatively the following words can be inserted at the end of section 42A(1): *"provided that the provision of such information would not be tantamount to disclosure of the substance of the relevant material."*

Response: Accepted. Taxpayers concerns with the possible breadth of the information initially required are recognised. The information required in terms of the proposed amendment will be reduced in order to avoid any perception that SARS is seeking access to the content of the legal advice or the risk that it may inadvertently be disclosed.

Comment: It is uncertain what is meant by the term "client". Legal professional privilege belongs in each case to the person seeking legal advice and it cannot be waived by a third party.

Response: Accepted. The term "client" will be deleted.

Comment: The proposed new subsection refers to a "legal practitioner" which term is not defined for purposes of the Tax Administration Act. It is proposed that the term be defined in the Act, alternatively, reference should be made to the definition contained in the Legal Practice Act, 2014 (Act No. 28 of 2014).

Response: Accepted. The term "legal practitioner" will be replaced with the term "author". There is thus no need for a definition as proposed.

13.8. Request for relevant material

(Main reference: section 46; clause 41)

Comment: By virtue of the fact that a request for information under oath or solemn declaration is intrusive, it is contented that the proposed removal of "senior" should not be proceeded with and that it should be required that a senior SARS official must direct that relevant material be provided under oath or solemn declaration.

Response: Accepted. The opening words to section 46(2) will remain a "senior SARS official".

Comment: The sourcing of relevant information under oath seems merely to circumvent the inquiry provisions. The fact that criminal investigations can be conducted in this way also alludes to SARS attempting to circumvent judicial oversight in its information gathering proceedings. It is proposed that section 46(7) should be deleted as there are remedies for SARS to acquire this information in both civil and criminal proceedings.

Response: Not accepted. The ambit of a tax authority's information gathering powers is self-evidently wide, which principle has been confirmed in case after case in comparable jurisdictions. The obtaining and use of information under oath or solemn declaration is a common practice in most civil and criminal investigations. It also protects a person by adding evidentiary value to what was said and protects the person from allegations that he or she provided different information.

In the context of criminal matters, the person is protected both under section 44, which obliges SARS to conduct the investigation with due recognition of the taxpayer's constitutional rights as a suspect in a criminal investigation, as well as section 72(2), which provides that an admission by the taxpayer of the commission of a tax offence obtained from a taxpayer under Chapter 5 is not admissible in criminal proceedings against the taxpayer, unless a competent court directs otherwise.

Comment: SARS would be in a position to request relevant material in respect of any connected person, which means that SARS would be able to impose this additional burden on a taxpayer that holds as low as 20 per cent shareholding in a foreign entity. It would be extremely difficult to convince a connected but not controlled foreign entity to make such relevant material available to SARS.

Response: Comment misplaced. The application of the proposal is restricted to paragraph *(d)*(i) of the definition of "connected person" in the Income Tax Act, i.e. it will only apply to a connected person where more than 50% of the equity shares or voting rights are involved.

Comment: SARS cannot force a non-resident (i.e. off-shore entity) to provide relevant material in terms of the Tax Administration Act as this act is not applicable outside of the borders of South Africa. The off-shore entity would only be obliged to provide the relevant material in those instances where a bilateral or multilateral tax treaty exists between South Africa and the country of the non-South African entity, and in accordance with the terms of that treaty. Such mechanisms are the appropriate instruments under which to obtain information held by non-residents.

Response: Noted. This provision is not enforceable against non-residents but against the resident company in the relevant group. If the information is not available to the resident, it suffers a limited adverse consequence since the only sanction is that it may not later produce information that is not available to it.

Comment: The proposed amendment aims to prohibit the taxpayer from relying on relevant material held by a non-resident connected person if it was not produced when initially requested. The foreign company would be well within its rights to refuse to provide information to another party, particularly if the information is regarded as commercially sensitive. Furthermore the taxpayer is in no position to compel the foreign company to provide the relevant material. It would be administratively unfair to penalise the taxpayer if the foreign company (e.g. parent or fellow subsidiary) refused to provide the relevant information.

The prohibition is subject to review by a competent court, but it is limited to exceptional circumstances in respect of which SARS follows a very narrow interpretation. Furthermore, if SARS obtains the information through other means, such as an international treaty, SARS would be able to use the relevant material in subsequent proceedings but the taxpayer will be barred from doing so.

> *Response:* <u>Partially accepted.</u> The underlying rationale for the proposal is information asymmetry, since SARS is not in a position to judge whether information is not provided for tactical or legitimate reasons. The amendment merely proposes that, where the taxpayer indicates that it has not been able to obtain the information from its foreign connected person, it is held to this assertion.
>
> The proposal is largely based on the Canadian legislation in this regard, in particular given the fact that it has a similar constitution. Other countries e.g. Germany and the USA deal with this information asymmetry more strictly by imposing a penalty on the local taxpayer if foreign information is not provided.
>
> Regarding the sanction that may result from a failure to provide the offshore information and the limitation of the court's discretion to "exceptional circumstances", this limitation will be changed to read "unless a competent court directs otherwise on the basis of circumstances outside the control of the taxpayer and any connected person…".
> The sanction that the information may not be "produced or used" has also been limited to "produced". Should SARS be able to obtain the information under a tax treaty, which is a more protracted process, both parties may use it subject to the conditions of confidentiality imposed under the treaty.

Comment: A request for information cannot be extended to the Bank as third party where a client of the Bank also holds an account at a connected off-shore entity of that bank as such information can only be obtained by SARS from the foreign Revenue Authority through the relevant article in the double tax agreement.

> *Response:* <u>Comment misplaced.</u> If it is an independent third party's account, not being able to introduce information in this regard will not prejudice the local bank since it will have no impact on its tax affairs.

Comment: If SARS proceeds with the proposed amendment, it must be made clear that the provisions operate prospectively to requests made on or after date of promulgation.

Response: Accepted.

13.9. Production of relevant material in person

(Main reference: section 47; clause 42)

Comment: The proposed amendment allows SARS to not only require the taxpayer whose tax affairs are under verification or audit to be interviewed but also, third parties such as current employees of the taxpayer or persons who hold office in the taxpayer to be interviewed. The current provision does not allow SARS to require a third party to attend an interview in respect of the tax affairs of a taxpayer under investigation and the intention as indicated in the initial purpose of section 47 was to expedite and end the process of verification and audit and not to be used as a process to gather further information or extend the audit and verification process.

The proposal provides SARS with excessive power and the ability to gather incorrect and incriminating hearsay information from third parties, who may at times not have the necessary knowledge in the specific tax related affairs under investigation. This may result in inadmissible evidence such as hearsay evidence (which is inadmissible in court precisely because it is unreliable), irrelevant evidence and evidence that is not placed in the proper context being elicited, as the person may effectively be cross-examined without being protected by the rules of evidence and without the constitutional safeguards in relation to inquiry procedures.

SARS may want to cross examine witnesses during a trial on what was supposedly said by a person in an interview who may or may not have had personal knowledge of the transactions in question.

Response: Partially accepted. The proposed amendment will be reworded to ensure that the original purpose still applies, although the ambit of the enquiry is extended to current verifications or audits.

Just as is the case of external auditors or forensic investigators contracted by the legal entity, SARS should be in a position to interview employees or office holders of the legal entity. The proposed amendment aims to clarify which persons may be interviewed or requested to submit relevant material where the person whose tax affairs is under verification or audit is a company or other legal entity. As such, these persons are not independent third parties in relation to the legal entity. A legal entity comprises of people, and if they have knowledge of the tax affairs of the legal entity that employs them, they are obviously the people that SARS needs to interview for purposes of the verification or audit. However, it may be necessary to interview them first to determine *if* they have such knowledge.

It is the function of SARS auditors to evaluate the various sources of information which are placed before them to ascertain the correct tax liability. SARS auditors are regularly confronted by discrepancies between documents, statements and other information available to them which they must reconcile in order to clarify issues of concern regarding the tax liability of the taxpayer.

A person required to attend the interview is protected against self-incrimination by virtue of section 72(2) of the TAA, which provides that an admission by the taxpayer of the commission of a tax offence obtained from a taxpayer under Chapter 5 is not admissible in criminal proceedings against the taxpayer, unless a competent court directs otherwise.

The admissibility of the information provided and the rules of evidence are matters for a court to decide, should a tax appeal ensue. If SARS bases an assessment on inadmissible evidence, it would lose the case if the assessment is disputed. Furthermore, asking questions during an interview to obtain clarity and relevant material does not amount to cross-examination, the object of which is generally to test the veracity of evidence or to discredit a witness *before a court*.

Comment: The TAA currently allows for SARS to have witnesses subpoenaed and cross-examined under oath or solemn declaration by using the formal process of an inquiry provided for under Part C of Chapter 5 of the TAA. This inquiry procedure is subject to certain requirements which constitutionally safeguard taxpayers from arbitrary, abusive or unduly invasive behaviour by SARS officials. If section 47 is to have any proper purpose at all (to distinguish it from an inquiry), it must be to provide an efficient and fair procedure to render further information-gathering processes unnecessary, that is, to bring the investigation to an early end. The provision is too intrusive and violates the taxpayer's constitutional right to just administrative action, right to privacy and right against self-incrimination.

Response: <u>Not accepted.</u> It would be wholly impractical to only use the formal enquiry proceedings under order of a judge to interview persons. A section 47 interview is intended to be far more informal and expedited. This is precisely why, in contrast to formal enquiries, the section's scope does not extend to independent third parties, it may not be used for criminal matters and further procedural rules are not required. Regarding procedural safeguards, see response above.

Comment: The verification and audit process may be unduly protracted as it will result in the interview becoming part of an on-going information gathering process for further audit and investigation, which could drag the process out for years to come.

Response: <u>Not accepted.</u> As set out above, the purpose of section 47 is precisely the opposite.

Comment: The proposed amendment further eliminates the purpose of a public officer as the person who in this regard would be the relevant person to contact. It is submitted that should SARS wish to conduct an audit or verification, prior notice to the public officer of the taxpayer must be supplied.

Response: Not accepted. It would be extremely unlikely that the public officer would know everything about the business, particularly in a large business. Other sections in Chapter 5 of the TAA, such as sections 46 (requests for relevant material) and 48 (field audit), do not limit SARS to only question the public officer or, for that matter, an office holder such as the Chief Financial Officer. Section 49, which deals with the obligations of the taxpayer during a field audit, specifically provides that SARS may question the taxpayer (of which the public officer will be the representative taxpayer) or "any other person" on the premises. The public officer is generally SARS' first point of contact but is by no means the only person that may be questioned for purposed of the audit. Prior notice of a field audit *is* given under section 47.

13.10. Assistance during field audit or criminal investigation

(Main reference: section 49; clause 43)

Comment: In the event where a person misunderstands a specific question or bases his answer on his perception of the facts; providing the information under oath or solemn declaration may lead to the individual committing perjury. It is therefore unclear how in practice SARS would want to implement this adversarial process where an employer would have to discredit an unwitting employee because SARS compelled them to give answers to questions they may not have had the correct or full information to. It is proposed that this amendment be deleted.

Response: Not accepted. The ambit of a tax administration's information gathering powers is self-evidently wide, which principle has been confirmed in case after case in comparable jurisdictions. The obtaining and use of information under oath or solemn declaration is a common practice in most civil and criminal investigations, including in comparable jurisdictions (see, for example, the Australian Tax Office audit manual which clearly provides for obtaining information in this manner). Providing information under oath or solemn declaration also protects a person by adding evidentiary value to what was said and protects the taxpayer from allegations that he or she provided different information.

The SA Police Service notes that; "Perjury consists in the unlawful and intentional making of a false statement in the course of a judicial proceeding by a person who has taken the oath or made an affirmation…" In certain circumstance a false oath or solemn declaration may constitute defeating the course of justice, for purposes of which there must have been a clear intent to provide false information. Neither would appear to be applicable to the examples provided.

In the context of criminal matters, the person is protected both under section 44, which obliges SARS to conduct the investigation with due recognition of the taxpayer's constitutional rights as a suspect in a criminal investigation, as well as section 72(2), which provides that an admission by the taxpayer of the commission of a tax offence obtained from a taxpayer under Chapter 5 is not admissible in criminal proceedings against the taxpayer, unless a competent court directs otherwise.

Comment: It is unclear why section 49(1)*(c)* is required if section 46(7) already exists. On what basis is broader powers required?

> *Response:* Not accepted. Section 49 relates to a field audit under section 48 and not a request for information under section 46.

13.11. Inquiry order

(Main reference: section 51; clause 44)

Comment: Section 51(1) refers to section 50(2). It is submitted that the reference should be to section 50(1).

> Response: Accepted.

13.12. Reduced assessments

(Main reference: section 93: clause 48)

Comment: The provisions of the proposed subsection (3) apply to the whole of section 93 and not only to the circumstances contemplated in section 93(1)(*d*). It is assumed that this is an oversight and that it is not intended that taxpayers are expected to request a reduced assessment in the case of matters resolved through the dispute resolution or settlement processes.

> Response: Accepted.

Comment: On the question of the proposed 6 or 12 month timeframes, the very nature of errors is that they go undetected for extended periods of time. Experience has shown that SARS applies the term “exceptional circumstances” exceedingly strictly. As such, the likelihood is that taxpayers will be regarded by SARS officials as not qualifying for the extended period contemplated in section 93(3) and, by definition, for the extended period to lodge an objection in terms of section 104. It is unclear how this represents a balance of rights in SARS seeking self-assessment system of taxation. Hence, the three year period should be retained.

> *Response:* Accepted. The three year period will be retained and SARS will attempt to mitigate the risks presented by older requests for correction through its risk management systems. In order to ensure that substantive issues are properly channelled through the objection and appeal system, the phrase “readily apparent” will be added to the requirement that there be an “undisputed error”.

Comment: In order to make the provision workable, the time within which the reduced assessment must be requested in the case of an undisputed error must be calculated from the date of the assessment containing the error, instead of the date of the previous year's assessments.

> *Response:* No longer applicable. A technical correction will however be made section 99(2)*(d)* to ensure that a request for correction that is received shortly before the expiry of the three year period may be actioned by SARS after the expiry of the period.

13.13. Withdrawal of assessment after prescription

(Main reference: section 98; clause 49)

Comment: One of the clear purposes of the provision was to allow a taxpayer to correct an error in a return where it would otherwise face an inequitable result. Errors are frequently only identified long after a return is filed and the tax assessed, hence this provision was to provide for a remedy in such circumstances where prescription had applied. The proposed amendment will narrow the scope of the provision to cases where there was an adverse assessment. Consequently, the proposed amendment unnecessarily limits taxpayer rights as there continues to be a real need to find redress in situations where there was an "undisputed factual error" by a taxpayer in a return.

> *Response:* <u>Not accepted.</u> This is an exception to the prescription periods that is to the benefit of the taxpayer and is uncommon internationally. The justification for narrowing of the grounds for a section 98(1)*(d)* withdrawal to matters beyond the control of the taxpayer remains for the reasons stated in the Memorandum of Objects.
>
> As the outcome of a successful request under section 98(1)*(d)* is not a withdrawal but the issue of a reduced assessment, this remedy should not have been included under section 98 but the section that provides for reduced assessments, i.e. section 93. The wording of section 98(1)*(d)* will be included under the taxpayer's actual remedy in the case of undisputed errors, i.e. to request a reduced assessment under section 93. If a taxpayer qualifies for a reduced assessment under the proposed new section 93(1)*(e),* this will fall under a new exception to prescription under section 99(2)*(e)*.

13.14. Extension of period of limitations for issuance of assessment

(Main reference: section 99; clause 50)

Comment: Taxpayers are entitled to certainty after a prescribed period that an assessment will no longer change. It is submitted that the relevant three and five year prescription periods set out in section 99(1) are reasonable periods for SARS to complete any tax audits and are in line with international norms. The current prescription periods provide certainty to both SARS and taxpayers and to extend the relevant periods would jeopardise the objective of section 99 and undermine the element of certainty.

> *Response:* <u>Not accepted.</u> SARS concedes that finality is important but internationally the period allowed varies from jurisdiction to jurisdiction. This is a targeted proposal which deals with a small number of cases. Other jurisdictions have also increased the time for specific matters, such as Australia where the prescription period for transfer pricing audits is seven years (previously unlimited) or Canada where it is six or seven years depending on the type of taxpayer. The

United States of America suspends prescription while a “designated summons” issued by the Internal Revenue Service is litigated.

Comment: The proposed provision gives SARS the power to extend prescription by an “appropriate period”. There is no indication of what an appropriate period is, leaving this entirely to the subjective discretion of SARS officials. Given that an outer limit is imposed for complex matters, similarly, an outer limit should be imposed for information disputes. In this regard, we would suggest that prescription should not be extended beyond a period of 6 months after the relevant material is provided to SARS.

> *Response:* <u>Partially accepted.</u> The extension will be for a period approximate to the delay encountered in obtaining information from the taxpayer.

Comment: Current legislation already sufficiently empowers SARS to appropriately combat situations where taxpayers fail to respond to SARS’ queries in an attempt to force prescription. SARS can either disallow the expenditure under query/include into taxable income potential income under query by raising a valid additional assessment before prescription or alternatively raising an estimated assessment. The taxpayer would then be required to object to such assessment should the taxpayer wish to do so.

> *Response:* <u>Not accepted.</u> The application of the law in complex matters requires SARS to be satisfied of various jurisdictional factors which it cannot ascertain if it is not in possession of all the relevant facts. The complexity of such matters has been demonstrated to the Committee.

Comment: If the provision stands, the information requests must be submitted at least six months before prescription, otherwise SARS can use the information request itself to extend prescription.

> *Response:* <u>Partially accepted.</u> SARS is obliged to allow a reasonable period for the provision of information and may grant an extension to do so if reasonable grounds exist to do so. The proposal will be changed to require prior notice of the extension of a minimum of 30 days (for information related extensions) or 60 days (for complex matter extensions) before the expiry of the prescription period.

Comment: Reference to a “reasonable period” for the provision of relevant material may be problematic. This is subjective and it is often found in practice that SARS makes requests for the provision of large volumes of information to be provided by taxpayers with inordinately short deadlines of as little as two days. Hence it is proposed that the minimum period within which taxpayers must provide relevant information before which the provision cannot be invoked should be prescribed.

> *Response:* <u>Partially accepted.</u> The proposal will make specific reference to the period allowed to respond to the request and an extension under section 46(5).

Actions of the nature described are also unlikely to survive the scrutiny by the Commissioner when approval for the extension of prescription is sought.

Comment: Taxpayers are within their rights to dispute the entitlement of SARS to certain information or documents requested. To this end the extension of prescription should not apply where a taxpayer fails to provide relevant material timeously having disputed SARS' entitlement thereto with just cause.

Response: Not accepted. Whether or not the information entitlement dispute is based on just cause not to provide the information, the time taken by the dispute will reduce the time available to SARS to obtain all relevant material and to ensure that the correct amount of tax has been paid. SARS' legislative function is to audit – this cannot happen during an information entitlement dispute.

Comment: As currently formulated, it is possible for a SARS official to extend prescription on the basis that SARS is considering the application of the GAAR. It is submitted that this is too low a threshold to be applied in this regard. Before prescription can be extended it must be readily apparent that the audit is a complex matter. SARS should be required to provide the taxpayer with reasons as to why it intends to extend prescription, why an audit is regarded as complex and give the taxpayer an opportunity to make representations prior to prescription being extended.

Response: Partially accepted. The reference to complex matters will be withdrawn. The grounds for the decision will be included in the notice to extend prescription in order to demonstrate that the jurisdictional requirements for the extension have been met. Procedural fairness is implicit.

Comment: SARS should not be permitted to commence an audit shortly before the expiry of prescription and then be able to extend prescription on the basis that the matter is complex. Taxpayers' rights should not be adversely affected where SARS has been lax in fulfilling its duties timeously within the prescribed prescription period. To this end, it is submitted that it should be a prerequisite for the extension of prescription that SARS has issued notification of audit relating to the specific matter at least 6 months prior to prescription.

Response: Partially accepted. A notice period of at least 60 days will be provided for. As a practical matter, an audit is generally underway before it is possible to identify a complex matter.

Comment: Concern is raised with regard to the use of the term "matter of analogous complexity" as it is a subjective matter of opinion and what is a complex matter for one person is a simple matter for another. This term raises the risk of abuse by SARS officials simply alleging that a matter is complex.

Response: Accepted. The reference to complex matters will be withdrawn and replaced with a reference to the application of the doctrine of substance over form, the application of a general anti-avoidance rule, the taxation of hybrid entities or instruments and transfer pricing.

Comment: The ability to extend prescription for a period of up to three years is considered to be excessive. This amounts to a doubling of the prescription period in the case of SARS assessment from three years to six years and for self-assessment will result in a prescription period of up to eight years. This undermines the very principle behind prescription of bringing finality to matters. Should SARS proceed on this matter, for complex matters, it should be extended by no more than 12 months which, even in the most complex of matters, should provide SARS with sufficient time to complete its audit and raise an assessment.

> *Response:* <u>Partially accepted.</u> The extension will remain at three years in the case of an assessment by SARS and reduced to two years in the case of self-assessment, which in total will amount to six years for SARS assessments and seven years for self-assessments for the specified matters.

Comment: While it may be implicit, it should be made explicit in the provision that the extension of prescription relates only to the matter under audit and is not of a general nature.

> *Response:* <u>Partially accepted.</u> The provision will be reworded to make it more specific.

Comment: The Commissioner's decision to extend prescription should be subject to objection and appeal.

> *Response:* <u>Not accepted.</u> A decision to extend prescription, as has always been the case where an extension was based on fraud, misrepresentation or non-disclosure of material information, would form part of the objection and appeal against the assessment.

13.15. Jurisdiction of tax board

(Main reference: section 109; clause 52)

Comment: While this is a very good idea in principle, the practical implementation thereof needs to be considered. Attention should be given to address the specific triggering events for joining disputes.

> *Response:* <u>Accepted.</u> The proposed amendment will be deleted in light of the fact that the threshold of the tax board is to be increased to R1 000 000 by the Minister.

13.16. Settlement of dispute

(Main reference: section 146; clause 55)

Comment: It is submitted that the cost of pursuing the full debt and not partial debt recovery by settlement seems short sighted as this remains only a factor to be considered, not a compulsion.

Response: Not accepted. The recoverability of the tax debt constitutes unnecessary criteria to determine if a settlement should be concluded. Under the pay-now-argue-later principle, the recovery of the disputed tax is separated from the pursuance of the objection and appeal. The proposed amendment follows this approach.

13.17. Liability of third party appointed to satisfy tax debts

(Main reference: section 179; clause 57)

Comment: The constitutionality of this section (which the proposed automation of the process will make even worse) in light of the recent case of University of Stellenbosch Legal Aid Clinic and Others v Minister of Justice and Correctional Services and Others (16703/14) [2015] ZAWCHC 99 is contested. In that case it was held that certain provisions of the Magistrates Court Act, relating to emolument attachment orders were held to be unconstitutional on the grounds that they failed to provide for judicial oversight. Section 179 contains no judicial oversight or safeguards whatsoever and the issue of a notice in terms of this section is left to the whim of a senior SARS official.

It is proposed that the amendment to section 179(1) be withdrawn and appropriate safeguards should be introduced, including the exhaustion of other collection mechanisms first and judicial oversight.

Response: Partially accepted. A distinction should be drawn between civil debts and statutory debts. Prior judicial oversight is not required under the TAA nor is it required in most jurisdictions with similar powers. The OECD Tax Administration 2015 report on 56 jurisdictions indicates that tax administrations in 50 of the jurisdictions are permitted to collect taxes from third parties and only one requires a court order to do so. The proposed amendment will be redrafted to allow for prior notice and opportunity to apply for debt relief, for example by an instalment payment agreement, compromise or reduction of the amount to be paid to SARS under section 179 based on basic living expenses or, in the case of business, serious financial hardship. However, prior notice will not be given if a senior SARS official is satisfied that to do so would prejudice the collection of the tax debt.

Comment: In practice the administration of this provision includes the collection of debts in respect of which a dispute has been instituted and where a request for suspension of payment has been lodged. In practice it has been seen that SARS' system does not keep track of requests for suspension of payment of disputed tax debts and it would accordingly be impossible for this to be taken into account in any systems parameters at present.

Response: Accepted. Operational and system changes are underway to address this issue.

Comment: SARS has suggested that where the notice has been given in error, a refund can be requested. This is not a solution as once the money is taken out of a taxpayer's bank account, the damage is done.

> *Response:* Partially accepted. Under the redrafted wording, the tax debtor would have adequate warning and opportunity to seek debt relief as set out above. If it is not sought or the taxpayer does not qualify for it, the money will be paid to SARS in satisfaction of the outstanding tax debt.

Comment: SARS has not considered the practicalities and cost of administration to appointed third parties agents. Statistics by the Banking Association of South Africa confirmed that each bank receives between 4 000 and 8 000 agent appointments on a monthly basis. The cost to action 1 appointment is more than R200. To this SARS has now added the burden of the proposed 72 hours preservation that will lead to extreme compliance costs to banks and is time consuming.

> *Response:* Accepted. These statistics should be seen in the light of the magnitude of SARS' debt book. The proposed 72 hours preservation will be withdrawn.

Comment: In terms of section 179(2)*(a)* the bank must inform SARS of the reason it cannot recover the amount. Banks don't have a facility to keep an AA88 and action over a period provided by SARS other than to deduct and pay immediately. Section 179(2)*(b)* requires the Bank to inform the taxpayer of the notice. Due to volumes the Bank will only be able to notify the client/taxpayer if this notification is built into the Bank's system.

> *Response:* Accepted. The proposed requirement for the third party to notify the taxpayer will be withdrawn.

Comment: Though section 179(4) provides for SARS to on application apply a basic living expenses allowance, no such procedure exists with SARS imposing this obligation on employers in many instances. More importantly, no time frame is prescribed for SARS to access and repay the amounts.

> *Response:* Accepted. A prior notice requirement will be inserted, as set out above.

13.18. Refunds of excess payments

(Main reference: section 190; clause 60)

Comment: Application of section 190(6) should be extended to include the right to object and appeal against a failure by SARS to effect a refund, or take a decision not to refund, within a specified time frame e.g. 21 days, where the refund is properly refundable and if so reflected in an assessment (as per section 190(1)*(a)*).

Response: Comment misplaced. If a refund under section 190(1)*(a)* is not paid, this is an administrative matter that may be taken up directly with SARS and, if necessary, the Tax Ombud.

Comment: Provisions are clear insofar that a refund may only be withheld where the audit or verification relates to the refund itself, yet SARS applies the provision in practice for any outstanding audit, even for unrelated periods, as a justification for withholding a refund. This needs to be clarified in the legislation.

Response: Comment misplaced. If it is clear from the wording of section 190 that this is not permissible, this is an issue that must be resolved operationally.

Comment: It is proposed to change the wording from "within three years from the date of the assessment" to "within three years from the date of payment". It would be unfair on taxpayers to limit the potential future refund of an advance or other payment of assessed taxes to the date of payment (which would precede the date of assessment). Hence the proposed amendment should be amended not to prejudice a taxpayer aiming to claim a refund of an amount where the payment made in respect of an assessment is made before the date of such assessment.

Response: Accepted. The proposal will be amended to refer to date of payment or date of assessment, whichever is the later.

Comment: It is unsure how one would determine when an amount was paid erroneously as in all cases amounts paid to SARS in respect of an assessment are based on some calculation or understanding of the assessment or the assessment to be raised.

Response: Comment misplaced. The legal position is clear. How erroneous overpayments are detected is determined by SARS' systems and by the taxpayer's own review of payments made.

Comment: The provision should be amended to provide guidance as to the type of security required by SARS and for the Commissioner to prescribe procedures to apply for security by public notice.

Response: Not accepted. No amendment to section 190(3) is proposed. Be that as it may, the type of security that would be acceptable will differ from case to case and be based on the circumstances of each matter.

Comment: Currently SARS reviews the alleged suspicious transactions reported and requests the Bank to reserve the amount and within 48 hours SARS provides an AA88 to recover the tax debt. It has also happened that SARS confirms that it is fraud and then after a hold has been placed only weeks later requests the banks to lift the hold as it is not fraud. SARS can therefore direct the bank to lift the hold and therefore it cannot only be when a competent court directs.

Section 190(5A)*(b)* also obliges the Bank to "immediately report to SARS the suspicion and the grounds on which it rests". Any alleged suspicious transactions are identified through the bank's risk engines. Due to the increased risk of fraud syndicates, the "grounds" on which the suspicion rests is confidential and cannot be shared.

> *Response:* Accepted. It will be made clear that SARS may also release the amount and the requirement to report the grounds for the suspicion will be deleted.

13.19. Reportable arrangement penalty

(Main reference: section 212; clause 62)

Comment: While the reduced penalty for parties to a listed reportable arrangement is welcomed, it is questioned why the promoter of such an arrangement should face the far higher penalties that apply in terms of section 212(1). The reduced penalty should apply for all listed arrangements. This provision should be clarified.

> *Response:* Not accepted. The higher penalty is justified by the fact that the promoter organises, sells, designs or manages the structure.

Comment: It is also questioned as to which penalty will apply when a party to a listed reportable arrangement derives a tax benefit from the arrangement and is therefore also a participant on this basis. Will the penalty in section 212(1) apply or that in section 212(3)? This provision should be clarified.

> *Response:* Noted. A person referred to in paragraph *(c)* of the definition of 'participant', i.e. a party to a listed arrangement, cannot also be a person referred to in *(a)* or *(b)* of the definition, given the fact *(c)* begins with the phrase "any other person". If it is a section 35(1) reportable arrangement and a person is a person referred to in paragraphs *(a)* or *(b)* of the definition, the section 212(1) penalty will apply. If it is a section 35(1) arrangement and a listed arrangement under section 35(2) and the person is a person referred to in paragraph *(c)* of the definition, the section 212(3) penalty will apply.

13.20. Voluntary disclosure programme (VDP)

(Main reference: sections 226 and 227; clauses 64 and 65)

Comment: The clarification that an audit or investigation must relate to the default to be disclosed is welcomed. This will go a long way towards making the VDP more attractive, particularly for large companies which are usually always subject to some tax audit. Given that this amendment is stated to be a clarification, we submit that it should be made retrospective to 1 October 2012 and that those taxpayers that have been denied VDP relief or have had to pay understatement penalties on the basis that they are subject to an audit unrelated to the default disclosed should be allowed the appropriate VDP relief.

Response: Not accepted. The proposed amendment is intended to broaden the scope for VDP applications and the ambit of the relief thereunder based on public representations. The reference to a clarification will be corrected.

Comment: It is submitted that it should be made explicit in section 40 that SARS should be required to inform a taxpayer in writing as to the nature of the enquiry (inspection, verification or audit) and, in the case of an audit, the information required to be provided to the taxpayer in terms of section 42. Similarly, section 43 should be amended to explicitly require that SARS must inform a taxpayer that they are subject to a criminal investigation, including the scope thereof. Following on from this, section 226(1) should be amended so as to refer back to the notices referred to above.

Response: Comment misplaced. The requirements of sections 40, 42 and 43 apply in any event. Regarding the proposal that section 43 should be amended to oblige SARS to inform a taxpayer that he or she is a suspect, this is already regulated under section 44(1) and relevant law as to the rights of a suspect. This includes the right of the taxpayer to be informed that he or she is a suspect in a criminal investigation, at which point the taxpayer will be aware of the commencement of a criminal investigation.

It is also common knowledge that it is SARS' practice is to commence an audit with a letter of engagement. Verification is not referred to in the context of VDP – only audit or criminal investigation. Any activity before a letter of engagement, speaks to whether the application is "voluntary", which is a different issue.

Comment: The language used in section 226 (and 223) is inconsistent in that it refers to an investigation rather than a criminal investigation. In the interests of consistency and not creating the impression that the term has a different meaning in the context of the VDP and understatement penalties the wording should be aligned. Both section 226 and section 223 should be amended to refer to a criminal investigation.

Response: Not accepted. The word "investigation" must be interpreted in the context of the relevant section and the scheme of the Act. It is generally used in the Act in the context of criminal investigation, particularly where used together with audit, i.e. "audit or investigation" such as is the case in sections 48(2), 48(4), 223 and 226 of the Act.

Comment: The proposed relaxation of the requirements for a valid voluntary disclosure is welcomed. However, it must be pointed out that the proposed paragraph (d) would still not be met where there is no substantial understatement and the other behaviours in the table are also not present. This raises the question as to why it should be a requirement at all that the VDP is linked to understatement penalties. It should be sufficient to qualify for the VDP if there has been a default with no reference to understatement penalties. It is therefore submitted that, rather than being amended, paragraph (d) should simply be deleted.

Response: Not accepted. The primary benefit of a successful VDP application is the reduced understatement penalties in columns 5 and 6 of the understatement penalty percentage table in section 223. The linkage is thus a logical one.

Comment: Furthermore, the definition of a default in section 225 does not cater for the situation where a taxpayer is in an assessed loss position, both before and after the disclosure of an income tax matter, that results in the assessed loss being overstated. In this regard, there is a lacuna in the law as such a taxpayer could be subject to understatement penalties in terms of section 222. The definition of a default should be amended to include this scenario.

Response: Noted. The question of whether the definition should be extended to an assessed loss scenario will require further review, which will form part of the 2016 legislative cycle.

Comment: Sections 863 to 873 of the Customs Control Act, 2014, provides for voluntary disclosure relief in respect of a duty in terms of the Customs Duty Act, 2014 or a duty or levy in terms of the Excise Duty Act, 1964. Section 873 of the Customs Control Act, 2014, created an anomaly in respect of section 277 in that duty in terms of the Customs Duty Act, 2014, does not extend to value-added tax on importation of goods. The question in this instance is to whom such applications should be directed. In the circumstances it is recommended that section 227*(b)* be amended to read: "*(b)* involve a default which has not occurred within five years of a similar default by the applicant or a person referred to in section 226(3)<u>, but excluding any unintended default on a customs declaration</u>.".

Response: Not accepted. VDP for customs and excise matters is regulated under the Customs Control Act, 2014, which already provides that that the VDP provisions of the TAA apply *mutatis mutandis* for customs and excise matters.

13.21. Delivery of documents

(Main reference: sections 251 and 252; clauses 68 and 69)

Comment: The problem is not with delivery to an e-Filing page in general, but with the proposition that sending it to an e-Filing page is sufficient on its own to constitute effective delivery. This is especially so in matters where legal action will be taken against the taxpayer. This has serious implications in that time periods may lapse which would effectively remove the taxpayer's remedies to object or take appropriate action. Many taxpayers do not check their e-Filing page on a regular basis. It is submitted that delivery to e-Filing should be accompanied by a notice to that effect delivered in terms of any of the other delivery methods.

Response: Partially accepted. The SARS e-Filing system already provides for separate notice of a delivery of a document or notice on a taxpayer's e-Filing page, mostly effected through an email or SMS. However, the electronic communication rules issued under section 255 will be amended to specifically provide that if delivery is to be made to taxpayers' e-Filing pages, SARS will be obliged to provide the taxpayers with the option to choose to receive notification by email or SMS as well. However, it remains taxpayers' obligation to inform SARS of their current contact details, including email address or cell phone number to ensure the email or SMS notification is received.

Comment: In addition to the above, the retrospective application of this amendment to 1 October 2012 would have the effect of retrospectively rectifying deficiencies in delivery and could negatively impact on the vested rights of taxpayers and/or result in adverse implications for them. The effective date of the amendment should be prospective with effect from date of promulgation.

Response: Partially accepted. The proposed amendment will come into effect on the date that the electronic communication rules issued under section 255 were published, i.e. 25 August 2014

Comment: Any correspondence to a company must be sent directly to the company's e-filing profile which includes the public officer's business profile and not to the personal profile of the public officer. However, SARS often sends company correspondence to the private addresses of the public officer which poses a confidentiality risk.

Response: Not accepted. Under section 246 of the Act a public officer is responsible for all acts, matters, or things that the public officer's company must do under a tax Act, and in case of default, the public officer is subject to penalties for the company's defaults. Thus, if no response is received to correspondence send to the place appointed by a company under section 247 at which SARS may deliver communications, the obvious alternative would be to send it to the business address of the public officer. If the latter details are not available, there can be no reason not to send the communication to a private address of the public officer.

13.22. Transitional rules

(Main reference: section 270; clause 72)

Comment: The proposed amendment is unclear for the following reasons:

- interest on an understatement penalty imposed under section 222 has always been interpreted as being calculated with effect from the "effective date of the tax understated" as stated in section 187(3)*(f)* - i.e. the date on which the provisional tax should have been paid as set out in section 89*quat* of the Income Tax Act. We are therefore of the view that the insertion of (a) is not necessary;
- it is unclear whether interest on understatement penalties must then be imposed and waived on the same basis as interest on additional tax imposed under section 76 of the Income Tax Act was imposed and waived under section 89quat(2) and (3) of the Income Tax Act.

It is proposed that the amendment be re-drafted in order to make it clear that interest on understatement penalties (in respect of periods before 1 October 2012) must be imposed and waived on the same basis as interest on additional tax under the previous regime. This will deal with the unintended consequences of the retrospective effect of understatement penalties referred to in the Explanatory Memorandum.

Response: Not accepted. The calculation of interest for purposes of additional tax differs from that of the new understatement penalty regime. Interest on the amount of unpaid tax accrues from the date that the tax should have been paid. In the case of an understatement penalty, interest is calculated from the date the understated tax should have been paid. This is in addition to the interest which accrued from the "effective date" of the understated tax, i.e. the date it should have been paid, and will be payable under section 187(1) read with section 187(3)*(a)* once the TAA interest regime comes into operation (section 187(3)*(a)* has not yet commenced).

The remittance of additional tax under section 76(2) will still apply for the period intended by the proposed amendment. The fact that Chapter 12 is not promulgated in full means that section 89*quat*(2) and (3) of the Income Tax Act remain in force until such coming into operation, as is explained in Interpretation Note 68.

13.23. New amendments not contained in the draft Bill published for comment

- Amendment of section 64K to remove return obligation imposed on foreign recipients of exempt foreign dividends as such obligation is not enforceable.
- Amendment of section 21 of the Value Added Tax Act as a consequence of amendments to section 20.
- Amendment of section 1 of Tax Administration Act – specific inclusion of OECD Standard for Automatic Exchange of Financial Account Information in Tax Matters and Country-by-Country Reporting for Multinational Enterprises in the definition of "international tax standard", as well as the replacement of designation of such standards in a public notice by the Commissioner with regulation made by the Minister of Finance: This will provide greater certainty to taxpayers.
- Amendment of evidentiary burden under section 235(2) of the Tax Administration Act. Pursuant to further review section 235(2) will be further clarified to ensure that it cannot be argued that it is more akin to a reverse onus, which has been held to be unconstitutional.
- Amendment to definition of "default" in section 225 of the Tax Administration Act - this is consequential to the other voluntary disclosure programme changes in Part B of Chapter 16.