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The South African Revenue Service
Lehae La SARS
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BY EMAIL: policycomments@sars.gov.za

COMMENTS TO THE DRAFT GUIDE OF THE VOLUNTARY DISCLOSURE PROGRAMME: TAX ADMINISTRATION

Dear Sirs/Madam,

We have attached the Tax Administration Technical Work Group's comments to the Draft Guide of the Voluntary Disclosure Programme ("**the Draft Guide**") which was published on 20 October 2021. The comments cover submissions made on a policy level (Part A), the meaning of "voluntary" considering Purveyors South Africa Mine Services (Pty) Ltd v CSARS (135/2021) [2021] ZASCA 170 (Part B), as well as specific comments to the guide (Part C).

We appreciate the opportunity to participate in the process and would welcome further dialogue.

Please do not hesitate to contact us should you need further information.

Yours sincerely

E Rossato

Elle-Sarah Rossato
Chair of the Tax Administration Technical Work Group

PART A – SUBMISSIONS IN RESPECT OF LEGISLATIVE PROPOSALS

Voluntary Disclosure Programmes ("**VDP's**" or "**VDP**" in singular form) globally are seen as a pathway to tax compliance. This is the cornerstone of submissions made below. Per the Draft Guide's Explanatory Note:

> *"The voluntary disclosure programme (VDP) was introduced as a permanent measure to increase voluntary compliance in the interest of enhanced tax compliance, good management of the tax system and the best use of the SARS resources. The VDP is intended to encourage taxpayers to voluntarily disclose tax defaults."* (our emphasis)

Considering the above, we submit that the VDP as it is currently interpreted by SARS and ultimately most recently by the Supreme Court of Appeal[1] ("**Purveyors v CSARS**"), is rather narrow and not conducive to the Explanatory Note's aim. As it stands, it begs the question: does the VDP per the Tax Administration Act 28 of 2011 ("**the TAA**") aim to only collect taxes that have been understated or is it aimed at collating the full and complete tax profile of a particular taxpayer? The latter would seem more beneficial to ensure accurate tax records and information for the benefit of both the South African Revenue Service ("**SARS**") and the taxpayer.

From a taxpayer's perspective, it would be encouraging to correct any erroneous submission to SARS to not only be penalised by virtue of interest, at the very least, for understated taxes, but also ensuring that SARS has the taxpayer's complete tax profile. Ensuring accurate taxpayer information would, in turn, be helpful to SARS in the long term for purposes of forecasting of tax collections and National Treasury's Budget purposes. It would also assist in monitoring taxpayers' fluctuations and declarations of taxes to SARS.

With tax compliance as the cornerstone of VDP applications, we submit that there are objective parameters within which a VDP application could be considered, i.e. it will the outcome ensure that the taxpayer's full and complete information and that taxes are accurately captured by SARS versus a generally one-sided approach to the VDP regime.

[1] *Purveyors South Africa Mine Services (Pty) Ltd v CSARS* (135/2021) [2021] ZASCA 170

PART B – INTEPRETATION OF SCA JUDGMENT IN RE PURVEYORS V CSARS: THE MEANING OF "VOLUNTARY"

Detailed factual description

The issue for determination in Purveyors v CSARS was effectively what the meaning is of the words "voluntary" and "disclosure" in the context of VDP.

Following the SCA judgment, the word "voluntary" means: "*performed or done of one's own free will, impulse or choice; not constrained, prompted, or suggested by another*" (our underlining).

It follows then, also from the SCA judgment that an application will be made voluntarily if: "*errant taxpayers … come clean, out of their own volition and **without any** prompting*" (our underlining and emphasis) (paragraph 20 of the judgment) and further that if an application was "*prompted by … the advice it received from its …* [advisors]" [our insertion] (paragraph 30 of the judgment) it would not be voluntary.

It is unclear whether a taxpayer who applies for VDP after having been prompted to do so or it having been suggested by advisors or anybody other than SARS to do so would still be doing so voluntarily. Stated differently, if the taxpayer receives advise to the effect (from someone other than SARS) that it/she/he has made an understatement and VDP is suggested in order to mitigate exposure to penalties and prevent criminal prosecution, whether, in these circumstances, the application would still be voluntary, especially if the taxpayer has been warned by the advisor that I might face penalties if otherwise discovered by SARS.

Whilst it is accepted that the facts in the SCA case was that SARS warned the taxpayer of penalties, it seems firstly that Purveyors was also warned by consultants of the penalties (i.e. someone other than SARS) and secondly, the wide definition provided by the court suggests that the meaning of voluntary may stretch to exclude from VDP relief, those applications where the cause of compulsion underpinning that application was something or someone other than SARS.

Further, SARS often issues media releases informing taxpayers about the VDP and informing taxpayers that they face penalties if their non-compliance is not remedied *via* VDP. It is unclear whether, in light of the definition provided by the court on the meaning of "voluntary", whether applications submitted by taxpayers in response to such media releases can be said to be made without any prompting and out of a taxpayer's own volition.

Nature of business/persons impacted

Taxpayers impacted are potentially all taxpayers applying for VDP relief, especially those applying for relief with assistance of professional service firms, and tax practitioners in particular, and those disclosing defaults following media releases by SARS that warns of penalties and recommends VDP instead.

Proposal

It is proposed that the VDP guide be updated to include SARS' view and/or interpretation of the SCA judgment on the issue detailed above so as to provide certainty and limit the potential for disputes about what the correct interpretation of the SCA judgment should be. Failing that, it is suspected that advisors may be reluctant to suggest VDP as, in doing so, advisors may inadvertently be the cause of a VDP application being rejected (bearing in mind that the very incentive to get taxpayers to disclose through VDP is the relief against penalties and criminal prosecution and hence advisors are likely to inform taxpayers of this incentive - as does SARS in its media releases - in an attempt to convince taxpayers to apply for relief). We suspect that if advisors become reluctant to recommend VDP, the amount of VDP applications are likely to decline drastically.

PART C: COMMENTS RELATING TO THE DRAFT GUIDE:

1. PROBLEMS WITH VOLUNTARY DISCLOSURE PROGRAMME (VDP) PROVISIONS

[Applicable provisions: Sections 225-233 of the TA Act]

1.1. **Reason for the introduction of the provisions into the TA Act**

1.1.1. According to the Memorandum on the Objects of the Tax Administration Bill 2011, the main purpose of such a framework was to enhance voluntary compliance and was in the interest of the good management of the tax system and the best use of SARS' resources.

1.1.2. The voluntary disclosure programme ("**VDP**") thus serves an important policy objective, which is to bring more taxpayers, assets and income into the South African tax net. It is important to note that the VDP is not a tax amnesty, in that there is no relief from the actual underlying taxes. There is also no relief from interest payable on the relevant taxes or relief from an exchange control perspective. The only relief is in relation to certain penalties that could potentially otherwise apply.

1.1.3. However, in practice there are various technical/practical issues with the VDP tax provisions. This is highly problematic within the current context, since uncertainty or perceived inequity in relation to the VDP has the result that taxpayers are disinclined to apply for VDP. Given these risks, taxpayers frequently rather adopt a "catch me if you can" approach.

1.1.4. We note that VDP was discussed during the Annexure C workshops held in 2017, at which time SARS arranged a subsequent meeting in January 2018 to discuss these issues. Whereas SARS expressed the view that the vast majority of taxpayer concerns could be resolved by means of an operational guide / standard operating procedure document, there has been no such document published to date. In addition, we note that more recently, SARS has conducted their own research project into the VDP regime with the aim of gauging taxpayers' experiences associated with the VDP, however, we are unaware of the outcome of such research project.

1.2. **Period of disclosure for VDP**

1.2.1. **Detailed factual description/ The legal nature of the problem**

1.2.1.1. There is currently no limitation of period in relation to a disclosure in terms of the VDP. In contrast, section 29 of the TA Act requires that a taxpayer should ordinarily retain tax related records for a period of five years from the date of submission of the relevant tax return (or five years from the date of the end of the relevant tax period, where no return was required to be submitted).

1.2.1.2. This period is extended in terms of section 32 of the TA Act, where there is an audit, investigation, objection or appeal. Whereas the burden of proof in tax matters is ordinarily on taxpayers, the taxpayer is not obliged to retain documents past the record retention period, and accordingly ordinarily SARS cannot assess a taxpayer to tax in relation to these earlier periods (where tax records may have supported the taxpayer's tax submissions, but the taxpayer has lawfully no longer retained these records).

1.2.1.3. As a result of the record retention period, a taxpayer will often not have records relating to periods prior to the record retention period. In practice, in VDP matters, SARS has required that a taxpayer estimate its tax liability for these earlier periods, alternatively SARS has alleged that the failure to declare tax liabilities for earlier periods, results in the disclosure not being "full and complete in all material respects" as envisaged in section 227(c) of the TA Act. This is problematic in that ordinarily the record retention period would protect a taxpayer from tax liability in relation to these earlier periods, and the taxpayer does not have appropriate records to defend itself.

1.2.1.4. It should be noted that, in the first voluntary disclosure program (that ran from 2010 to 31 October 2011), there was a limitation of five years in relation to the period for disclosure. In current practice, the meaning of "full and complete" is applied inconsistently at the SARS VDP unit. In some cases SARS officials have requested that certain applicants make the disclosures going 10 years back, even if the applicant can reasonably pinpoint the date of default. In other cases, SARS accepts the date of the default without any questions.

1.2.1.5. There are also technical legal issues in relation to VDP extending back to multiple past periods. For example, the normal period of limitation for issuing assessments is 3 years from assessment for income tax matters and five years for VAT matters. For SARS to assess prior to these periods, exceptional circumstances such as fraud, misrepresentation or non-disclosure would need to be present. It would accordingly be the exception rather than the rule for SARS to be able to issue any tax assessments for these earlier periods. In the circumstances, it appears unfair and unreasonable to require taxpayers to disclose and pay taxes in relation to these earlier periods, or face rejection of their VDP application.

1.2.1.6. Given these perceived inequities or risks, taxpayers frequently decide not to make VDP disclosures regarding tax positions arguably incorrectly adopted in earlier periods, and rather simply "fix this going forward". This significantly negatively impacts the uptake of the VDP. This is arguably opposite to one of the main purposes of the VDP which is to enhance voluntary compliance.

1.2.2. **Nature of the business/ persons impacted**

1.2.2.1. The taxpayers[2] impacted by the lack of clarity in this regard can be either:

1.2.2.1.1. non-compliant taxpayers who wish to come forward and regularise their defaults; or

1.2.2.1.2. Compliant taxpayers of good standing who have in good faith discovered an error resulting in a default, which they now wish to regularise.

1.2.3. **Proposal**

1.2.3.1. The period for disclosure of information and documentation relating to a VDP should be limited to the record retention period in section 29 read with 32 of the TA Act and aligned with the five-year limitation rule in the first voluntary disclosure program (that ran from 2010 to 31 October 2011).

1.3. **No objection and appeal process for rejections of VDP applications**

1.3.1. **Detailed factual description/ The legal nature of the problem**

1.3.1.1. The SARS VDP Unit may reject an application for VDP relief if it is of the view that the requirements in sections 226 and 227 of the TA Act are not met.

1.3.1.2. Such decisions by the VDP Unit are not currently subject to objection or appeal under Chapter 9. The remedy for a taxpayer in these circumstances, who disagrees with such a decision must take the matter on judicial review to the High Court. Because of

[2] Note: Due to the complexity of the VDP regime, our feedback is that mostly high net worth taxpayers or medium to large corporate taxpayers are making use of the provision as they can afford tax practitioners. This coupled with the other notes on VDP is resulting in massive losses of revenue to the fiscus.

the cost and delay involved in such a process, few taxpayers are willing or able to do so.

1.3.1.3. Many practitioners believe that certain decisions by the VDP Unit incorrectly narrow the qualification criteria for VDP. With the inability to access the normal objection and appeal process in relation to rejections of VDP applications, taxpayers are disinclined to "risk" a VDP application in various circumstances. Once again, this defeats the main purpose of the VDP regime which is, *inter alia*, aimed at encouraging/ enhancing voluntary compliance (see also note 1 on previous page).

1.3.2. **Nature of the business/ persons impacted**

1.3.2.1. This provision affects taxpayers whose VDP applications have been rejected on the basis that it does not meet a requirement/s for a valid VDP. This is unfair, as certain aspects of the current VDP legislation are unclear and open to different interpretations by the taxpayer and by SARS. If a complaint taxpayer identifies an error which they voluntarily seek to regularize with the VDP Unit and their interpretation of "full and complete" disclosure differs from SARS' interpretation resulting in the rejection of the VDP, the complaint taxpayer will potentially only be left with the costly remedy of approaching the High Court in a review application. This is unduly harsh.

1.3.3. **Proposal**

1.3.3.1. Decisions concerning qualification for VDP relief in terms of Part B of Chapter 16 of the TA Act should be subject to objection and appeal. We set out below reasons why, in our view, the objection and appeal process should be available to taxpayers (rather than a High Court review process).

1.3.3.2. <u>Justice prohibitively costs</u>

1.3.3.2.1. For larger taxpayers, an appeal to Tax Court or review in the High Court may well be similarly affordable. However, the situation is dramatically different for "smaller" taxpayers.

1.3.3.2.2. In relation to smaller disputes, taxpayers following the objection and appeal process would have their matter heard by the tax board. This involves fewer formalities and lower cost,

making justice more financially accessible for "smaller" taxpayers.

1.3.3.2.3. This is a real concern in relation to all potential disputes, where taxpayers are obliged to follow the High Court review process, regardless of their financial resources and the size of their dispute.

1.3.3.3. ADR process

1.3.3.3.1. The Alternative Dispute Resolution process has been implemented as part of the normal objection and appeal process. This appears to be fulfilling an important function, in reducing the need for costly litigation, and helping the parties reach a mutually agreeable conclusion.

1.3.3.3.2. This process can be anticipated to have a similar beneficial impact on disputes regarding the availability of VDP. However, ADR does not form part of the High Court review process and is therefore currently unavailable for taxpayers who dispute SARS' rejection of their VDP application.

1.3.3.3.3. Whereas it is possible that similar positive resolution could be achieved in a less formal manner, when requesting SARS to review their decision, the ADR mechanism is already set up with skilled and experienced staff and known processes. In the circumstances, it appears most appropriate to utilise these existing channels, as part of the objection and appeal process.

1.3.3.4. Taxpayer secrecy

1.3.3.4.1. In an objection and appeal process, the taxpayer maintains secrecy. In contrast, in a High Court review process, the taxpayer is exposed to commercial and reputational risks in relation to their private taxpayer information becoming public.

1.3.3.4.2. The risk of the VDP application being rejected (which would have the impact of penalties being imposed), combined with the commercial and reputational risks associated with challenging this rejection of the VDP application by means of a public court process, is a material disincentive to taxpayers. This can, in certain instances, result in taxpayers adopting a "find me first" attitude to past tax non-compliance.

1.3.3.5. It is submitted that this amendment should apply retrospectively, so that applications incorrectly rejected in recent times can be reconsidered.

1.4. **Lack of clarity on the meaning of "Notice" of an audit**

1.4.1. **Detailed factual description/ The legal nature of the problem**

1.4.1.1. According to the Explanatory Memorandum on the Tax Administration Laws Amendment Bill, 2016, this amendment inserted a requirement that a person seeking voluntary disclosure relief must be given notice of the commencement of an audit or criminal investigation into the affairs of the person as opposed to the requirement that the person has become aware of a pending audit or criminal investigation or that the audit or criminal investigation has commenced. The proposed amendment was aimed at clarifying the application of the section.

1.4.1.2. Practically, it appears that SARS' interpretation regarding what constitutes "notice" involves an element of subjectivity. As a result, taxpayers are disinclined to "risk" a VDP application in various circumstances.

1.4.2. **Nature of the business/ persons impacted**

1.4.2.1. In practice it appears that there are differing views as to what constitutes notice of audit, for example:

1.4.2.1.1. whether an IT14SD which is a supplementary declaration requested from the taxpayer by SARS is regarded as being part of SARS' audit process; or

1.4.2.1.2. if a taxpayer has been given notice of an audit, whether or not the default would not otherwise have been detected during the audit.

1.4.3. **Proposal**

1.4.3.1. A potential solution would be for SARS to specifically indicate that the "notice" (in whichever form it may be), is in fact a 'notice' for purposes of section 226(2) of the TA Act, which then creates an objective determination and eliminates uncertainty for taxpayers considering a VDP application.

1.4.3.2. We propose a cross-reference in section 226 to section 42 of the TA Act to ensure certainty and consistency.

1.4.3.3. In addition, we propose that a definition of "audit" be included in the TA Act so as to clarify the confusion created in practice due to the lack of clarity in respect of this term.

1.5. **"Voluntary" nature of VDP application**

1.5.1. **Detailed factual description/ The legal nature of the problem**

1.5.1.1. One of the requirements for valid voluntary disclosure in terms of section 227 of the TA Act is that the disclosure must "be voluntary".

1.5.1.2. The classification of a disclosure as "voluntary" involves substantial subjectivity, which creates uncertainty and reduces the uptake of the VDP. Practically, it appears that SARS' interpretation regarding what constitutes "voluntary" disclosure is such that VDP applications are quite broadly rejected.

1.5.1.3. In addition, in the recent case of *Purveyors South Africa Mine Services (Pty) Ltd v Commissioner for the South African Revenue Service* (61689/2019) [2020] ZAGPPHC 409 (25 August 2020), the court did not adequately elaborate on the meaning of "voluntary". Furthermore, the Judge dismissed the taxpayer's application for leave to appeal (with costs and without reasons) despite marking the original judgment as reportable and of interest to other judges.

1.5.1.4. It appears that the lack of clarity in this regard makes taxpayers disinclined to "risk" a VDP application in various circumstances.

1.5.2. **Nature of the business/ persons impacted**

1.5.2.1. SARS has been known to consider a VDP application as not being voluntary, if the taxpayer has received a request for relevant material in terms of section 46 of the TA Act (even where there has been no audit notification, in other words there is no actual audit underway).

1.5.2.2. Similarly, SARS has been known to consider a VDP application as not being voluntary, if it involves a period where a tax return is outstanding or even lately that an IT14SD has been issued and

where the taxpayer has already been notified that the relevant tax return is outstanding, or even where a taxpayer approached a SARS official to clarify a tax position.

1.5.3. **Proposal**

1.5.3.1. The recent rejections of VDP applications are against the spirit of the VDP programme and it impacts tax morale negatively. Instead of encouraging taxpayers to regulate their tax affairs, they are deterred from doing so and eventually SARS would not have the full picture of taxpayers' affairs.

1.5.3.2. Currently, the criteria of "voluntary" is very subjective and based on whether the VDP controller believes that the application meets the requirement or not. It is proposed that the requirement that the disclosure be voluntary be defined with reference to the lack of notification of audit, so that the only criterion in this respect is the lack of notification of audit (established as an objective standard as set out above). This will create an objective determination and eliminate uncertainty for taxpayers.

1.6. **The VDP must not "result in a refund"**

1.6.1. **Detailed factual description/ The legal nature of the problem**

1.6.1.1. One of the requirements for valid voluntary disclosure is that the disclosure must "not result in a refund due by SARS".

1.6.1.2. A tax position adopted erroneously, or other errors could affect multiple tax periods. This could potentially result in reductions of tax liability in certain periods and increases in tax liability for other periods.

1.6.1.3. Because of the periodic nature of tax, it could then be argued that the default results in a refund in relation to a particular tax period, such that the VDP application is rejected (either as a whole, or as regards that period only).

1.6.1.4. In practice, SARS has been known to instruct taxpayers to apply for VDP only in relation to periods where the "default" results in increased tax liabilities, and to submit a request for correction or objection in relation to the periods where the "default" results in reduced tax liabilities.

1.6.1.5. However, there are significant challenges associated with taxpayers attempting to have their tax assessments revised to correct overpaid taxes. There is accordingly a real risk to the taxpayer that they may be obliged to make payment of the underpaid taxes in one period, only to have the claim for overpaid taxes in another period rejected in the other period. In these types of situations, taxpayers are strongly disincentivized to make any disclosure whatsoever to SARS, and the more common response is for taxpayers to decide to "let sleeping dogs lie".

1.6.2. **Nature of the business/ persons impacted**

1.6.2.1. This provision impacts taxpayers who, for example, made an error that affects multiple tax periods, and which could potentially result in reductions of tax liability in certain periods and increases in tax liability for other periods.

1.6.3. **Proposal**

1.6.3.1. Where the same issue results in an "understatement" in certain tax periods, and overpaid taxes in other tax periods, SARS should be authorized to accept the VDP application and process all relevant revised assessments so that only the net underpaid taxes are considered and forms part of the VDP agreement and ultimately paid to SARS.

1.6.3.2. In this respect, section 227(e) of the TAA should be amended to refer to "not resulting in a refund on a net basis" across all relevant affected tax periods; alternatively, "refund" should be better clarified under Section 225 of the TAA.

1.7. **VDP and prescription rules**

[Applicable provisions: section 99 of the TA Act, sections 225 to 234 of the TA Act]

1.7.1. **Detailed factual description/ The legal nature of the problem**

1.7.1.1. The VDP draft guide that was published recently (October 2021) indicates SARS's approach to years of assessment where there was a non-disclosure of information but does not result in tax chargeable for the particular year of assessment. SARS's view is that section 99 of the TA Act does not override the Voluntary Disclosure provisions.

1.7.1.2. Upon reading the legislation it seems to be a fair assumption to make if an application is submitted for a year in question that does not result in tax payable, and it is the only year for which a VDP application has been made.

1.7.1.3. In cases where multiple years are concerned though it does pose a problem in that any year which may be affected by a prior year adjustment that results in a tax chargeable will not be subject to prescription rules on the basis of non-disclosure but the subsequent year where the prior year adjustment would result in less tax chargeable would be subject to the limitation periods because such non-disclosure does not result in an amount chargeable to tax. SARS has already taken this approach in a VDP application submitted over multiple years to determine a tax liability without taking into account the years of assessment where taxes should have been reduced due to prior year adjustments. This would happen in cases dealing with foreign gains and losses and adjustments which are timing differences or where assessed losses carried forward to subsequent years of assessment require adjustment.

1.7.1.4. This approach appears to be prejudicial to the taxpayer and would deter a taxpayer from making disclosure under the VDP, especially since the legislation does not cater for an override of the limitation provisions contained in section 99 of the TA Act. Whilst SARS should be placed in the position it would have been, the section should not result in prejudice to a taxpayer that does come forward on a voluntary basis to be prejudiced for being forthcoming, especially in cases where the non-disclosure was not done intentionally and only identified in later years.

1.7.2. **Proposal**

1.7.2.1. It is proposed that the legislation be amended so that the VDP provisions override the limitations provision contained in section 99 or to amend section 99 of the TA Act to make it not applicable to years of assessment that are considered under the VDP programme as valid voluntary disclosure applications.

ENDS