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A brief and general evaluation of the proposed General Anti Avoidance Regulations: Section 80A of the Income Tax Act

Introduction

I am an associate professor at Rhodes University, Grahamstown. I am also a tax practitioner and tax commentator. I have recently written articles in the Sunday Times newspaper on the proposed General Anti Avoidance Regulations.

I do not represent any client or interest group in making the following representations. They are made only in the spirit of the ongoing process of tax reform in South Africa.

The need for a new set of General Anti Avoidance Regulations 'GAAR' in South Africa.

The tax playing arena has undergone considerable change over the past 10 years. Thus, it is important that GAAR be reconsidered in order to evaluate its contribution to the new South Africa as we are today as opposed to how South Africa was when GAAR was last evaluated. In this regard the following is noted

- The massive changes to specific provisions of the Income Tax Act implemented while the Honorable Minister of Finance, Trevor Manuel, has been in office has put an end to many questionable tax planning practices of our past.
- South Africa is no longer as heavily reliant on GAAR as was the case in the past.
- The reduction in tax rates, coupled with new thinking in the arenas of corporate governance and responsibility have contributed to substantially reduce the 'appetite' for aggressive tax planning that existed some 10 years ago.
- Nevertheless, GAAR remains necessary, more as a guideline to taxpayers as to the 'limit of the envelope', than a tool to attack taxpayers. GAAR communicates the line of thinking and tolerance of SARS.

In my view, the new GAAR contained in section 80A does little more than effectively communicate the limits of tax planning as they are sought to be applied by SARS today.

The deficiencies of the existing section 103

The existing section 103 is creating significant uncertainty in South Africa today:-

- The 'abnormality provisions' are almost impossible to interpret, let alone apply consistently to all taxpayers.
- Taxpayers and SARS are involved in substantial and costly legal disputes that are not being resolved.
- There is substantial difference of opinion in the interpretation of the provisions.
- The case precedents concerning section 103 are somewhat 'long-in-the-tooth' and need to be reconsidered.
- The provisions have not been updated to keep pace with International GAAR developments.

Thus, there is simply no question of it not being the right time to reconsider GAAR.

Section 80A: Concessions made

It is important to note that section 80A has allowed for some major concessions over the proposals contained in the discussion paper of November 2005. Thus, it is quite obvious that SARS has not only followed an extensive and proper consultative process, but has also indeed reacted to some of the advice and commentary that has been raised by participants.

It is noteworthy that the following questionable clauses, *inter alia*, suggested in the November 2005 discussion paper have been abandoned:-

- General reference to complexity
- Reference to fee structure
- The presence of tax haven arrangements
- The imposition of penalty charges

Section 80A: Targets

Section 80A has been confined to General Anti Avoidance principles and only extended in the arenas where the vast majority of the uncertainty inherent to section 103 exists today, being

- Commercial substance
- Round Trip Financing
- Tax indifferent and accommodating parties

- Connected persons

It is suggested that these are the very areas where GAAR had to become more specific as section 103 contained absolutely no guidance in their regard.

Much has been made of the 'frustration provision' of section 80A(c)(ii). And indeed, this provision, viewed in isolation, is somewhat intimidating.

However, the 'frustration provision' must be considered in the conjunction with the preamble to the section. Thus it is simply necessary for the taxpayer to demonstrate that the sole or main purpose of the transaction was not to obtain a tax benefit and the frustration provision is of no force or effect.

Section 80A Taxpayer protection

It is all too easy to imagine SARS inspectors applying the new Section 80A in a heavy handed manner. However it is encouraging to note that SARS has built in a fair and properly considered degree of taxpayer protection into section 80A so as to ensure the fair and consistent treatment of taxpayers.

The notice provisions of section 80H are admirable. Taxpayers will be given the opportunity to defend themselves before GAAR is applied.

Even if SARS does apply GAAR, the taxpayer is in a position to request that SARS justifies its decisions. Thereafter the taxpayer is still left with a range of procedures to defend against the application of section 80A.

Failure to observe the above procedures will leave SARS vulnerable to review in terms of the Promotion of Administrative Justice Act.

In addition to the above it is worth noting that on 2 October 2006 the 'Advanced Rulings' provisions of section 76B were finally brought into effect. These provisions provide taxpayers who may be in doubt with regard to the application of section 80A, the opportunity of entering into negotiations with SARS before any damage is caused.

Conclusion

Considering section 80A in its entirety, it is submitted that:-

- SARS has spent nearly two years researching the provisions contained in section 80A.
- A proper consultative process has been indeed followed and concessions have been made that eliminate some of the harsher provisions contemplated in the November 2005 discussion paper.
- The provisions contained in section 80A have been confined to the very issues that have caused section 103 to fall short of its objectives.

- Adequate provision has been made for taxpayer protection.

In view of the above I submit that section 80A is a substantial improvement on the existing section 103.

Yours faithfully

Professor Matthew Lester