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When Can Taxpayers Rely On Prescription Of Assessments?

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INTRODUCTION

As is widely known, the general principle is that SARS may not reopen an income tax assessment after three years have expired since the date of issue. This is colloquially referred to as "prescription". In the case of self-assessment, such as VAT and PAYE declarations by employers, the period is five years.

However, the Tax Administration Act, 2011 does allow SARS to ignore prescription, where there is an amount that was not assessed for tax and the full amount of tax chargeable was not so assessed was due to fraud, misrepresentation, or non-disclosure of material facts. In the case of self-assessment, the requirements are stricter in that there must be fraud, intentional or negligent misrepresentation, intentional or negligent non-disclosure of material facts, or the failure to submit a return (or if no return is required, the failure to make the required payment of tax).

Prior to the Tax Administration Act applying, the relevant rules, as far as income tax was concerned, were contained in the Income Tax Act, 1962, but the rules now are not very different to those that applied then. Under those old rules (what is now) the Supreme Court of Appeal pointed out that there are two elements involved before SARS can ignore prescription, namely, first, SARS must show – and the burden of proof is on SARS – that there was fraud or misrepresentation or non-disclosure of material facts; and, secondly, SARS must show that the failure to assess was "due to" one of those three factors alleged. In other words, the onus is on SARS not only to prove the existence of, what might be called, the misconduct by the taxpayer, but also that the failure by SARS to assess was a result of that misconduct, i.e. the two were causally connected.

PRACTICAL APPLICATION

This issue came up for adjudication in the Tax Court in a matter, where we recently acted for a client. In that case SARS had sought to ignore prescription on the basis of non-disclosure of material facts. While not admitting that there was such non-disclosure, we enquired from SARS on behalf of the client – as is allowed in terms of the rules – how such non-disclosure caused the non-taxation, because it was common cause that the tax return had never been the subject of a verification or audit by SARS during the three-year period following the issue of the assessment. SARS's response was that the mere fact of non-disclosure caused the non-taxation.

Being dissatisfied that this did not represent a proper response to enable our client to formulate a proper objection, an application to the Tax Court was launched to compel SARS to provide a proper reason. The outcome of that application is not of great relevance here, as it is highly technical in nature, but what is of relevance is the judge's analysis of the provisions and how they are to be interpreted. The judge stated as follows:

> *"Put in simple terms, what caused SARS in its original assessment and during the period of three years thereafter not to assess the full amount of tax chargeable? If this came about because of the material non-disclosure, then the additional assessment is competent. If the [failure to assess the correct amount of tax chargeable] came about for other reasons* ***such as neglect by SARS*** *or*

> *some conduct of the taxpayer not amounting to misconduct, then the additional assessment is not competent and cannot be made." (My emphasis.)*

While this judgment does not deal with the merits, and objection must still be lodged against the assessment, the judge has sent a clear message. It is not enough for SARS to allege that the mere existence of non-disclosure (or fraud or misrepresentation) in the tax return is sufficient to give rise to the non-taxation of the relevant amount. There has to be more. And if, as in the case here, no-one at SARS even looked at the tax return during the three years subsequent to the assessment being raised, SARS can hardly argue that the failure to raise an assessment within the three-year period was "due to", what the judge referred to as, the "misconduct".

And interestingly, it happens that, pursuant to an audit or verification by SARS they do discover that there has been non-disclosure or misrepresentation, but the relevant information is given to SARS well within the three-year period, thereby "curing" such non-disclosure or misrepresentation. If SARS does nothing with that information, i.e. does not reassess the taxpayer, and three years go by, once again, SARS can hardly rely on the fact that there was such "misconduct", given that their failure to reassess within the three-year period was due to, in the words of the judge, "neglect by SARS".



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