

PARLIAMENT

The National Credit Amendment Bill
and taxation issues

17 October 2017

INTRODUCTION

SARS' response on two issues is requested:

- Should taxes be included in a debt relief programme proposed by the amendment to the National credit Act?**

- What tax consequences follow debt relief?**

SHOULD A DEBT RELIEF PROGRAMME UNDER THE NCA INCLUDE TAX DEBTS?

1

There are **fundamental distinctions** between commercial or trade debt and tax debt:

□ Private debt

- Originally incurred voluntarily and arises through a contract between the debtor and the commercial enterprise.
- Commercial debt is therefore a private debt.
- Debt relief of commercial/trade debt has a commercial or “private” impact.

□ Tax

- Is incurred by operation of statute.
- Tax is not an optional liability and every person is subject to the same rules.
- Tax is a social compact between the State and residents and traders in the country:

In exchange for taxes the Government provides fundamental services to the country’s people – from roads and transport to schools, safety and social grants.

SHOULD A DEBT RELIEF PROGRAMME UNDER THE NCA INCLUDE TAX DEBTS?

2

Extending debt relief to taxes will **imbalance** the **equity** of the **SA tax system**

- ❑ The **effectiveness** of a tax system relies on, *inter alia*, the **equity** of the tax system:
 - People in the **same position** are **taxed the same** – so, no person is treated more favourably than another ; and
 - People pay tax **proportionally**.

- ❑ **Achieving** and **maintaining equity** in a tax system is a complex balance.

- ❑ If the **equity**, or the **perception** of equity is **disturbed**, there is a **direct impact** on the willingness of taxpayers to **comply**.

Simply put: If a taxpayer believes that a “neighbour” is not paying

Tax then the taxpayer is less likely to pay voluntarily

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3

- Debt relief is **akin** to a **voluntary disclosure programme** adopted by a tax authority
 - When a special voluntary disclosure programme for tax is adopted by a country, it is first extensively considered by the **financial cluster**, including National Treasury and SARS.
 - A special dispensation for **tax relief** has consistently been contained within **tax legislation**.

SHOULD A DEBT RELIEF PROGRAMME UNDER THE NCA INCLUDE TAX DEBTS?

4

- The **tax legislation** already contains adequate **provisions** that afford **debt relief** for tax debtors who are **financially distressed**
 - If a tax debt is irrecoverable then SARS may **write off** the debt (s197 TAA)
 - Even though tax is required to be paid in full and on the due date, SARS may grant a tax debtor an **instalment arrangement** (s168 TAA)

The **factors** that SARS must consider, that are prescribed in law, include:

- A debtor's **liquidity**; and
- Whether **collections** actions would be **harsh**
- SARS may **compromise** a tax debt when the tax debtor is distressed.
(s200 TAA)

When compromising a tax debt, SARS must **consider**, *inter alia*:

- The **value** of the tax debtor's **assets**; and
- Whether a compromise may adversely affect
broader taxpayer compliance

SHOULD A DEBT RELIEF PROGRAMME UNDER THE NCA INCLUDE TAX DEBTS?

5

- ❑ There is a comprehensive **regulatory framework** to authorise instalments; compromise and write-off of taxes; which the NCA does not provide.

- ❑ Because tax debt is owed to the fiscus; SARS controls the application of “debt relief” through
 - Internal **policies** and **processes**;
 - **Designation** of specific officials who are authorised to write-off or compromise tax debts;
 - **Committees** exist to debate and consider each write-off or compromise to ensure the legislation is followed strictly;
 - The Commissioner is required by legislation to **annually report** on certain “debt relief” measures to the **Auditor General** and the **Minister of Finance**.

SHOULD A DEBT RELIEF PROGRAMME UNDER THE NCA INCLUDE TAX DEBTS?

6

- ❑ If the **NCA** is extended to **include tax debts** it will **subvert** and **overwrite** tax **legislation** and **principles** that **already accommodates** tax relief to distressed debtors

- ❑ There are possible **implications** for the **debtor** and the **lender** depending on the surrounding circumstances of the debt

For example

- The amount of the **debt reduction** could be a **recoupment** – (section 19 Income Tax Act) which amount of recoupment may be **added back** to the taxpayer's **gross income** (section 8(4)(a) Income Tax Act)
- There may be a **Capital Gains Tax implication** whereby the **base cost** of an asset is to be **reduced** by the amount of the **debt reduction** (paragraph 12A(3)(b)) of the Eighth Schedule to the Income Tax Act)
- The amount of the **debt reduction** would be a **bad debt** deduction for the lender; claimable against gross income – the result is reduction in a lender's taxable income and a **reduced amount of tax liability**

SUMMARY

- ❑ **Tax** is a **social compact** between the State and its citizens
- ❑ **Tax** is **different** to commercial or private debt
- ❑ The **forgiveness** of a **tax debt** can **impact** on **tax compliance**
- ❑ The **reduction** of **tax debts** should **remain** within the **tax legislation**
- ❑ The **reduction** of **tax debts** must **give effect** to **tax principles** and therefore should be contained only in tax legislation

SUMMARY

- ❑ **Existing tax legislation** provides **debt reduction** and **postponement measures** to accommodate tax debtors who are in **financial distress**
- ❑ These provisions are **appropriate** to **tax principles** & therefore there is **no need** for **tax forgiveness** contained in **non-tax legislation**
- ❑ There are **tax consequences** to the **borrower** and the **lender** if there is debt forgiveness **BUT** the **surrounding circumstances** must be considered in detail
- ❑ The tax consequences of debt reduction requires a more in-depth explanation

END