

New laws to increase disclosure

THE new reportable arrangements legislation in the Income Tax Act, 1962, was brought into effect on April 1 to address the fact that the South African Revenue Service (SARS) was of the view that the type and number of the transactions disclosed to SARS under the previous legislation — section 76A — proved disappointing.

It was SARS's intention that section 76A would provide it with an early warning of arrangements that were potentially tax driven.

However, section 76A proved unsuccessful, as only about 100 transactions, many of which involved ordinary hybrid instruments, were reported during the time that section 76A was in force. The legislation affecting reportable arrangements was revised by linking the provisions to the new General Anti-Avoidance Rules (GAAR), specifically to link it to factors that are indicative of a lack of commercial substance for GAAR purposes.

Section 80M of the new laws defines a reportable arrangement as any arrangement which gives rise to a tax benefit and where that arrangement:

- Provides for interest, finance costs, fees or other charges that are partly or wholly dependent on the assumptions relating to the tax treatment of that arrangement (other than a change in law);
- Has any of the characteristics of, or characteristics which are substantially similar to, the indicators of a lack of commercial substance under the GAAR;
- Is or will be disclosed by any participant as a financial liability for purposes of generally accepted accounting practice but not for income tax purposes;
- Does not result in a reasonable expectation of a pre-tax profit for

any participant; or

- Results in a reasonable expectation of a pre-tax profit for any participant that is less than the value of those tax benefits to that participant on a present value basis.

A tax benefit is defined as including any avoidance, postponement or reduction of any liability for tax. A reportable arrangement also includes hybrid equity and debt instruments, with the prescribed period being 10 years (previously five years).

Arrangements that are unlikely to be tax driven, such as ordinary loans, leases and collective investment schemes, and share transactions, continue to be excluded from the above provisions. The new legislation also excludes arrangements where the tax benefit derived does not exceed R1m or where the tax benefit is not the main or one of the main benefits of the arrangement.

Should a transaction qualify as a reportable arrangement, it must be disclosed within 60 days after any amount is received or paid by or to any party to the arrangement.

Although the disclosure requirements have been amended, they remain onerous. In particular, the following information is required to be disclosed in respect of a reportable arrangement:

- A detailed description of all the steps and key features;
- A detailed description of the assumed tax benefits for all participants, including but not limited to tax deduction and deferred income;
- The names, registration numbers and registered addresses of all participants;
- A list of all the agreements (previously a complete set of the agreements was required to be furnished to SARS); and
- Any financial model that em-

bodies its projected tax treatment.

The responsibility to disclose a reportable arrangement is placed on the promoter, being the person who is principally responsible for organising, designing, selling, financing or managing that reportable arrangement. Failure to adequately and timeously disclose a reportable transaction carries a penalty of R1m.

It is imperative that the application of the new legislation be made clear with regards to the effective date. Although it is understood that the new law comes into force on April 1, the application thereof to existing transactions is not so clear and potentially leads to an ambiguous situation which arguably provides SARS with some scope to contend that existing transactions would be affected.

An example is the case of an existing arrangement, entered into three years ago, which has and continues to give rise to ongoing payments. The arrangement was not, however, required to be reported in terms of the old section 76A. If the above transaction now meets the definition of a reportable arrangement, in terms of section 80M, the question arises as to whether the transactions now becomes reportable in section 80O, even though it was entered into prior to April 1. A strict application of new legislation would result in a disclosure obligation in respect thereof.

In this regard, SARS, in a media release dated April 9, attempted to clarify the position by saying that "...it is the first flows which are most relevant for the purposes for the legislation, so arrangements where they took place before April 1 2008 need not be reported in terms of the new legislation but may well be reportable in terms of the previous legislation".

SARS CLOSES MORE LOOPHOLES

- New reportable arrangements were brought into effect on April 1
- Section 80M of the new legislation defines a reportable arrangement as any arrangement which gives rise to a tax benefit
- A tax benefit is defined as including any avoidance, postponement or reduction of any liability for tax
- A reportable arrangement also includes hybrid equity and debt instruments, with the prescribed period being ten years
- The new legislation excludes arrangements where the tax benefit derived from the arrangement does not exceed R1m or where the tax benefit is not the main or one of the main benefits of the arrangement



It is therefore understood, that in the above example, even though the arrangement gives rise to ongoing payments, to bring it into the disclosure obligation provisions of section 80O, since the "first flows" as referred to in the press release, took place prior to April 1, the transaction would not be reportable in terms of the new legislation. It is also understood that transactions which were reported in terms of section 76A, need not be re-reported in terms of

the new legislation.

Promoters, who may not necessarily be tax advisors, are required to have a thorough knowledge of these provisions, particularly with regard to their responsibilities to report qualifying arrangements, since failure to adequately disclose a reportable arrangement within the prescribed period, carries a hefty penalty for all participants.

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