TAX SHOCK, HORROR NEWSLETTER

Davey's Locker

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Voluntary disclosure programme

And foreign assets

by Tony Davey

Legal certainty

A person with foreign assets making a voluntary disclosure in order to regularize his or her tax position has, in my view, a legitimate expectation as to the certainty of the tax result.

The spirit of the voluntary disclosure programme (VDP) offered by the Tax Administration Act is surely to encourage taxpayers with offshore taxable income to enter fully or more fully into the tax system, but at a determinable cost, capable of being evaluated in advance.

Under the VDP, undisclosed taxable income on offshore investments (interest, dividends, rentals and realized capital gains) is certain and measurable and thus subject to tax, with interest, but without the imposition of understatement penalties. Less certain are outcomes under the latest position adopted by the SARS VDP unit on:

- ☐ The prescription period for re-opening assessments.
- ☐ The acquisition funding of offshore assets (whether such assets were funded with pre-tax or post-tax monies).
- ☐ The funding of assets transferred into an offshore trust (whether such a transaction is a donation or loan).

Record-keeping

The reality in practice is that residents have seldom kept historic records, for fear of self-incrimination. And offshore trustees were not required by the law of tax-haven jurisdictions to register trusts, render tax returns or produce financial statements.

In most instances the only available information is a valuation statement of the investments. Thus it is often not possible for a VDP applicant to comply with the documentary requirements of SARS, and an application might as a result be cancelled or withdrawn.

In the event that SARS should subsequently proceed to making an estimated assessment, under s 102(2), it bears the onus of proof. Here I rely on para 6 of the SARS publication 'Voluntary Disclosure Programme' GEN–VDP–02–G01 revision 1 of 1 October 2012, which states that VDP information remains confidential and 'is not shared with any other division of SARS'.

VDP tax cost

The VDP does not forgive actual tax or interest on late payments but only understatement penalties.

Thus, for example, if the capital originally funding a trust is considered to be a donation (instead of an interest-free loan), 20% donations tax plus interest remains due and payable under the VDP. Assuming an 8% annual simple interest rate and a ten-year period since inception of the trust, this equates to 36%—and if a twenty-year period is involved, 52%—of the original capital!

Add to this the Reserve Bank's penalty, which in my experience is usually 20% if the monies are retained abroad and 10% if remitted, your original capital (and possibly investment growth, which has been notoriously poor abroad) may be largely eroded.

Pragmatic solution

An approach of benign tolerance is required by SARS of *bona fide* VDP applications, unless there are glaring anomalies in an applicant's version. For example, an interest-free loan to an offshore trust could, under domestic common law, have been made under an oral contract. If required, the oral agreement could now be recorded in writing.

Failing a benign approach by SARS, we need another tax and forex amnesty.