

The compromise of tax debt: fact or fable?

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In current economic times, some taxpayers may prefer to follow the “head-in-sand” approach when it comes to outstanding tax debts it has no means of paying. Unfortunately, this approach will not make the tax debt go away, but rather give rise to interest being levied in respect thereof.

In certain limited instances it may be possible for the taxpayer to enter into a compromise arrangement with SARS in terms of Chapter 14 of the Tax Administration Act No. 28 of 2011 (“the TAA”).

A compromise is defined in section 192 of the TAA as an agreement entered into between the South African Revenue Service (“SARS”) and a “debtor” (i.e., a taxpayer with a tax debt) in terms of which the debtor undertakes to pay an amount which is less than the full value of the tax debt in full satisfaction thereof and SARS undertakes to permanently “write off” the remaining portion subject to certain conditions imposed.

Although the process of considering the applicability of the compromise provisions having regard to the stringent requirements and preparing a voluminous application in this regard can be quite cumbersome, in the current economy, certain taxpayers may find that they adhere to the requirements of a compromise and could therefore obtain a permanent write-off of a portion of their tax debt.

A compromise may be approved by SARS if the purpose of the compromise is to secure the highest net return from the recovery of the tax debt and the compromise is consistent with considerations of good management of the tax system as well as administrative efficiency.

We summarise below some of the most pertinent aspects a taxpayer should consider in determining whether a successful compromise of tax debt may be possible.

Requirements for a compromise:

A request by a debtor for a tax debt to be compromised must be signed by the debtor and supported by a detailed statement setting out *inter alia*:

- the assets and liabilities of the debtor reflecting their current market value;
- the amounts received by or accrued to the debtor in the 12 months preceding the compromise request;
- the assets which have been disposed of in the preceding 3 years (or such longer period as SARS may require), together with their value, the consideration received or accrued, the identity of the person who acquired the assets and the relationship between the debtor and the transferee of the assets;
- the debtor's future interest in any assets or assets subject to the exercise of a discretionary power by another person;
- the assets of which the debtor (alone or with other persons) has a direct or indirect power of appointment or disposal, whether as trustee or otherwise;
- details of any connected person in relation to the debtor;
- the debtor's present sources and level of income and the anticipated sources and level of income for the next three years, with an outline of the debtor's financial plans for the future;
- the debtor's reasons for seeking a compromise.

In addition, the debtor must warrant that the information provided in the application is accurate and complete.

SARS may require that the application be supplemented by further information.

Consideration of compromise application

In considering the compromise application, SARS must have regard to:

- the value of the debtor's present assets;
- future prospects of the debtor, including arrangements which have been implemented or proposed which may have the effect of diverting income or

assets that may otherwise accrue to or be acquired by the debtor or a connected person in relation to the debtor;

- past transactions of the debtor;
- the position of any connected person in relation to the debtor.

Circumstances where it is not appropriate to compromise tax debt

SARS may not agree to the compromise of a tax debt if-

- the debtor was, within a preceding period of 3 years, a party to a compromise agreement with SARS (in *Agricultural and Industrial Mechanisation (Pty) Ltd* (83 SATC 1) it was held by the Tax Court that a business rescue plan involving a settlement with SARS is not a compromise in terms of the TAA);
- another creditor has initiated liquidation proceedings against the debtor;
- the compromise will prejudice other creditors or if other creditors will be placed in a position of advantage due to the compromise;
- it may adversely affect broader taxpayer compliance;
- where the debtor is a company (including a close corporation) and SARS has not first explored action against or recovery from the personal assets of third parties who may be liable for the debt.

Circumstances in which someone other than the debtor can be held liable for the tax debt

- Financial management of the debtor can be held liable to the extent that any such person's negligence or fraud resulted in the failure to pay the tax debt.
- In certain circumstances, shareholders of the debtor can be held liable for the tax debts if such entity is being voluntarily liquidated.
- Where a connected person in relation to the debtor received assets from the debtor at below the fair market value of such assets, such transferee may in certain circumstances be held liable for the tax debt of the debtor.
- If a person knowingly assists in dissipating a debtor's assets in order to obstruct the collection of tax debts.

Although it is evident from the above that SARS will only agree to the compromise of a tax debt in limited circumstances, taxpayers finding themselves in a position where they cannot pay tax debt and have no reasonable prospects of being able to do so in future, should consider whether a compromise arrangement may be possible in the circumstances.

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Should you have any queries on this matter, please feel free to contact your PKF relationship partner or firm.

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