

CAN X BE LIABLE FOR THE TAX DEBT OF Y?

Can a director, shareholder, member or representative taxpayer of a company be held personally liable for the tax debts of an entity? Or for that matter, can any person be held personally liable for the tax debts of another person or entity that is owing to the fiscus? Previous inconsistencies between provisions in the various tax Acts dealing with the recovery of taxes have now been resolved in the Tax Administration Act. Let's take a look.

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Introduction

Can a director, shareholder, member or representative taxpayer of a company¹ be held personally liable for the tax debts of an entity? Or for that matter, can any person be held personally liable for the tax debts of another person or entity that is owing to the fiscus?

Prior to the Tax Administration Act ("TAA") that came into effect on 1 October 2012, the various tax Acts such as the Income Tax Act ("ITA"), Value Added Tax Act ("VAT Act"), Skills Development Levies Act etc., each contained its own provisions in respect of dealing with the recovery of taxes due. Although the provisions were largely analogous, there were a number of differences which, in certain circumstances, lead to inconsistencies in the treatment of the same taxpayer in respect of the different types of taxes due.

The TAA however repealed the various administrative provisions² and incorporated a list of generic provisions that are applicable to all the tax Acts, into a single piece of legislation. In so doing, it removed a number of provisions which were previously duplicated in the respective tax Acts. This was done in an attempt to simplify and align the differing provisions of the various tax Acts. The provisions, for example, contained in sections 91A to 100 of the ITA, and sections 47 to 49 of the Vat Act, pertaining to representative taxpayers and agents, have been repealed by the TAA and are now dealt with in Chapter 11 of that Act.

The TAA did more than simply re-align certain administrative provisions; it also added a couple of provisions of its own. The effect of these inclusions, as will be pointed out, may have some dramatic consequences on the statutory landscape when imposing, for instance, personal liability on one person in respect of another person's tax liabilities.

¹ As defined in section 1 of the Income Tax Act No. 58 of 1962.

² See section 271 of the TAA.

True personal liability for the tax debts of another

An example of the difference brought about by the application of the TAA can be illustrated by comparing the applicable provisions of the TAA, with the now repealed provisions of paragraph 16(2C) of the Fourth Schedule to the ITA, and similarly section 48(9) of the VAT Act. The wording of these latter two sections is virtually identical and merely differs as to the type of tax levied, i.e. either the withholding of employees' tax or VAT respectively, as would be the case in many other equivalent statutes. For illustrative purpose we refer to the wording of section 16(2C) of the Fourth Schedule, which reads as follows:³

“Where an employer is a company, **every shareholder and director who controls or is regularly involved in the management of the company's overall financial affairs** shall be personally liable for the employees' tax, additional tax, penalty or interest for which the company is liable.”

[Emphasis added]

The applicable section of the TAA replacing the above provisions is that of section 180 which reads as follows:

“A **person** is personally liable for any tax debt of the taxpayer to the extent that the person's **negligence or fraud** resulted in the failure to pay the tax debt **if-**

(a) the **person** controls or is regularly involved in the management or overall financial affairs of the taxpayer; and

(b) a senior **SARS official is satisfied** that the person is or was negligent or fraudulent in respect of the payment of the tax debts of the taxpayer.”

[Emphasis added]

Comparison of the old and the new position:

From the above excerpts, the following is noticed:

1. Certainly the most noticeable difference from the preceding legislation is that the failure to pay a tax debt must now, in the opinion of a senior SARS official, stem from either negligence or fraud. This test is subjective as it refers to the discretion of “a senior SARS official” being so “satisfied”. Nevertheless one would assume that our courts would require objective grounds upon which such a decision is

³ Please note that the wording of the VAT Act also specifically includes “members” in addition to directors and shareholders as referred to in this extract.

based and not merely allow the exercise of an unfounded discretion. This two-pronged test is a significant deviation from the previous position which did not require the presence of negligence or fraud and places an added burden on the revenue authority to prove the existence of these facts.

2. Another divergence is that the repealed provisions narrow the potentially liable person(s) to those who are members, directors and shareholders of the entity. Conversely, the TAA has a much wider scope, given that it refers to “a person” that need not be a member, shareholder or director of the entity. The wider scope of the TAA can however be said to be tempered by the negligence or fraud requirement as referred to in the previous paragraph.
3. A further difference is that the TAA does not specifically refer to penalties and interest (as did the repealed sections of the VAT Act), but it should reasonably be inferred from the definition of “tax” and “tax debt” in section 1 of the TAA that such amounts do indeed form part of the tax debt due.
4. The use of the word “extent” in section 180 of the TAA also infers the notion that a person’s liability may be apportioned in relation to the “extent” of such a person’s negligent or fraudulent activities. How such an apportionment is to be made is however not clear.

The test as to whether a person can be held personally liable for the tax debts of another essentially boils down to firstly, whether that person is in control or regularly involved in the management of the finances of that entity; and secondly, whether the failure to pay the tax debt due resulted from their negligence or fraud. Should any person fall foul of these provisions they would be personally liable to SARS for the repayment of such debt without recourse to the entity.

Personal liability of a representative taxpayer

The TAA provides in section 155⁴ that a representative taxpayer (as defined in section 153 of this Act) may be held personally liable in his/her/its representative capacity in instances where the tax debt remains unpaid and where:

“(a) the representative taxpayer alienates, charges or disposes of amounts in respect of which the tax is chargeable; or

⁴ This section replaces the repealed amongst others section 97 of the ITA and paragraph 16 of the Fourth Schedule to the ITA.

(b) the representative taxpayer disposes of or parts with funds or moneys, which are in the representative taxpayer's possession or come to the representative taxpayer after the tax is payable, if the tax could legally have been paid from or out of the funds or moneys."

The above excerpt is fairly self-explanatory and falls in line with the above mentioned rationale behind the personal liability contained in section 180 of the TAA, i.e. the negligent or fraudulent actions of a representative taxpayer in this case.

Liability of a representative taxpayer in such capacity

Section 169 of the TAA, as read with sections 151(b), 153 and 154, imposes provisions enabling the recoverability of a tax debt from a representative taxpayer, where such person is not personally liable in terms of section 155 of the TAA.

A representative taxpayer may be assessed, in terms of section 154 of the TAA, for the income to which the representative taxpayer is entitled; monies to which the representative taxpayer is entitled or has management or control over etc., but such assessment is regarded to be made on that representative taxpayer in such capacity only.

Such a recovery is however not true "personal liability" and is limited to the assets belonging to the person represented which are in the representative taxpayer's possession or under his management and control (as per section 169(2)(a) of the TAA).

In respect of representative taxpayers, the TAA does not deviate from the preceding legislation to a great extent.

Personal liability of shareholders

Section 181 of the TAA provides for instances where a company is wound up by means other than an involuntary liquidation, without it having satisfied its tax debts (including its responsibilities as responsible third party,⁵ withholding agent⁶ or a representative taxpayer,⁷ employer or vendor).

In such instances, the persons who were shareholders within one year prior to its winding up are jointly and severally liable. This liability is, however, limited to the extent to which they received assets of the company as shareholders within one year prior to its winding

⁵ See section 184 of the TAA.

⁶ See section 179 of the TAA.

⁷ See section 169 of the TAA.

up, and the extent to which the tax debt existed at the time of receiving the asset, or would have existed had the company complied with its obligations under a tax Act.

It should be noted that the liability of the shareholder is second to that of the company and that a shareholder, who in terms of this provision is liable to SARS, may avail himself of any rights against SARS as would have been available to the company.

With regard to shareholders in the context of this section, it is worth noting that, owing to the wide definition of “company” and “shareholder” in section 1 of the ITA, these provisions would equally apply to the members of close corporations.

Liability of transferees for the tax debts of others

The TAA provides in section 182 that connected persons (“the transferee”) who receive an asset from a taxpayer for little or below market value consideration, is liable for the tax debt of the taxpayer. Such liability shall however be limited to the lesser of the tax debt existing at the time of receipt of the asset or would have existed had the transferor complied with its obligations under a tax Act; or the fair market value of the asset less the consideration paid.

This provision only applies to assets received one year prior to SARS’s notification of the liability due by the transferee.

Liability of persons assisting in dissipation of assets

Persons who knowingly assist in dissipating a taxpayer’s assets in order to obstruct the collection of a tax debt of that taxpayer is, in terms of section 183 of the TAA, jointly and severally liable with the taxpayer for the outstanding debt. The extent of such liability is however limited to the reduction of the assets available to pay the taxpayer’s debt.

Criminal liability

It would be quite easy to argue that the most burdensome form of personal liability that a person may have, arising from the tax debt of another, is that of criminal liability.

Chapter 17 of the TAA sets out a list of criminal offences which include *inter alia* the following offences outlined in section 234 of the TAA. If a person is found guilty of contravention thereof, that person may be fined or imprisoned for a period of up to two years. The listed offences include, amongst others, non-compliance with section 179 to

182 of the TAA, some of which having been discussed earlier.⁸ These provisions pertain to the liability of a third party who has been appointed as an agent of SARS, the personal liability for financial management of tax debts, shareholders liability and the liability of a transferee.

The dissipation, as well as the assistance in such dissipation, discussed in the immediately preceding section, has as consequence not only incurring personal liability but also criminal liability.⁹

Conclusion

As is evident from the above discussion regarding the application of the TAA, and without even looking into the common law or other statutory provisions such as the Companies Act, the personal liability of one person for the tax liability of another which is owing to the fiscus is a very real prospect and it is abundantly clear that personal liability goes much wider than applying simply to the directors or representative taxpayers of such entities.

For assistance in this regard, contact Johan at JohanG@stbb.co.za.

⁸ See section 234(n) of the TAA.

⁹ See section 234(m) of the TAA.

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