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MONTHLY NEWS

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Companies: How to Manage Your Greater Tax Risk in 2021

If you think compliance is expensive - try non-compliance." (Paul McNulty, former US Deputy Attorney General)

The extent of corporate taxes – from income tax, employment taxes and value added tax (VAT) to dividend taxes, capital gains taxes, transaction taxes and other indirect taxes – along with the operational aspects such as data and reporting systems and related technicalities, guarantee complexity and time-consuming processes for companies, which in turn increases compliance costs.

This also compounds other tax risks such as under-estimation; underpayments; overpayments; not applying the correct tax savings and incentives; tax penalties – such as the 10% late payment penalty; the inability to meet tax obligations; and assessments and audits.

Compliance costs are another growing tax risk. Studies suggest that companies spend hundreds of hours and tens of thousands of Rands each year on internal tax compliance costs such as labour or time devoted to tax activities and incidental compliance expenses, and on external tax compliance costs like tax practitioners' fees.

In addition, tax issues can place a company's reputation and brand at risk. An example would be a company losing a tender on a large contract because it was unable to provide a tax clearance certificate, perhaps due to a technical or minor non-compliance issue. Companies also face the risk that a tax issue could attract negative attention from the media, civil society or competitors, as growing numbers of stakeholders ranging from customers to potential investors increasingly support only companies perceived to be contributing their fair share to the country and community in which it operates.

Why tax risk management will be even more critical in 2021

All these tax risks will be amplified in 2021 for a number of reasons, including increased tax liabilities; intensified taxpayer scrutiny; and the further entrenchment of SARS' powers.

In the 2020 Medium-Term Budget Policy Statement, Finance Minister Tito Mboweni announced government-projected tax increases of R5 billion in 2021/22; R10 billion in 2022/23; R10 billion in 2023/24; and R15 billion in 2024/25. Companies need to factor these tax increases into their future planning and budgeting.

Taxpayers will also find themselves under greater scrutiny and likely to be subject to more punitive measures in 2021. Human errors and simple mistakes, which are not uncommon given the complex processes and strict deadlines involved, stand now to be harshly punished even if unintentional. The Tax Administration Laws Amendment Bill, 2020 (awaiting Presidential signature to become law) provides that for certain tax crimes you can be convicted if you acted either "wilfully or negligently", where previously proof of wilfulness (intention) was required. This means that a court could find a taxpayer guilty of an offence without proof of wilfulness, so that even inadvertent errors could be penalised with a maximum penalty of up to two years' imprisonment.

Along the same lines, companies can also expect an increase in the number of tax audits, as well as more detailed, expensive, and time-consuming investigations and audits. These are likely to focus on SMMEs, business owners, trusts and high net worth individuals.

Furthermore, SARS' already extensive powers - including asset forfeiture powers – continue to be entrenched. Just two examples from recent court rulings illustrate: the Gauteng High Court confirmed a taxpayer's obligation to be vigilant when filing a tax return and liability for appropriate penalties when falling short of this duty, while a North High Court judgement set an important precedent by re-affirming SARS' right to liquidate a taxpayer to recover debt where an assessment is under appeal.

How to manage your tax risk

- ***Plan for tax compliance***

  A well-defined tax strategy, aligned with your overall business strategy and the specific tax challenges facing your business, is important. As the business grows, a re-assessment of the corporate vehicle or tax structure may be required.

  Detailed planning is also required for the tax year ahead, providing ample time for processes required for proper record-keeping to ensure tax returns are complete and accurate, and that the numerous tax deadlines can be met.

  Planning should also incorporate identifying and implementing relevant tax relief and incentives and assistance. Just one example is turnover tax that provides administrative relief for micro businesses by replacing Income Tax, VAT, Provisional Tax, Capital Gains Tax and Dividends Tax for businesses with a qualifying annual turnover of R1 million or less.

- ***Budget for tax compliance***

  Proper budgeting is required to ensure all the various tax liabilities can be met before or on the stipulated deadlines, while also factoring in the effect of the annual tax increases announced in the latest Medium-Term Budget Policy.

Companies also need to budget for compliance costs including the internal cost of labour or time devoted to tax activities, incidental expenses, and the resources, systems and continuous upskilling required to meet ever-changing tax obligations. The budget should also provide for external costs such as tax practitioners' fees; external reviews of the tax function; and even tax risk insurance to cover the cost of immediate expert assistance and support from a team of tax professionals in the case of a SARS' tax audit.

- ***Call on expert professional services***

  Given the increase in compliance complexity and costs, the expertise of accounting officers and auditors is vital in determining the taxable income and the amount of tax to be paid.

  Advice from a tax professional can ensure an appropriate tax strategy is formulated to proactively manage your tax risk in the long-term, saving time and money and avoiding expensive tax mistakes, while keeping in line with the ever-changing tax obligations.

  Be sure to choose a specialist who is appropriately qualified and experienced, as well as a member of a professional controlling body that enforces strict standards, such as SAICA (South African Institute of Chartered Accountants).

Benefits of professional tax risk management

Failure to manage tax risk effectively will negatively impact on an organisation's profitability. However, beyond managing tax liability, there are further benefits to managing a business' tax risks.

One of these is more accurate records resulting from tax compliance obligations. This improves the availability of up-to-date information and insight into the financial position of the business and its profitability – enabling accurate, timeous financial management which is crucial to business success. In addition, tax compliance has become both a corporate governance and a reputational issue and can create both shareholder value and stakeholder trust. These benefits, along with tightly managed tax liabilities, will certainly assist companies as they build back after the economic upheaval of 2020.

Five Mistakes to Avoid When Investing Offshore

"An investment in knowledge pays the best interest" (Benjamin Franklin)

It can be tempting to look at South Africa and the bad news that seems to hit us like freight trains one after another, and immediately consider moving all your money offshore. There is however far more to consider than simply your gut feel, and predictions of woe as investing offshore comes with a lot of difficulties and more than a few unique problems.

Here we look at some of the most common errors people make, to steer you clear of losing your investments.

1. ***A bank account is not an investment***

   Perhaps the largest mistake that new offshore investors make is panicking. In their emotional state they open an offshore bank account and start moving money overseas, but this is a mistake.

   Bank accounts, particularly in Europe, often pay less than 1% interest and any money that is sitting in one is certainly not even keeping up with South African inflation. As with local investments offshore investors should be looking to craft a diverse portfolio that includes quality global equities to ensure they aren't just throwing money away.

2. ***Understand the market***

   Before leaping into an offshore investment, it’s important to have a clear picture of the currencies, returns, fees and taxes associated with the different options, and the respective risks that might need to be managed from the outset.

   In many jurisdictions fees can end up being a significant player in the profitability of the investment, to the point where they may result in an ongoing shrinkage of offshore assets. This is particularly true if an investment is held in the name of a company, trust or pension, where director or trustee fees will usually be charged on top of the advisory fees.

   On top of this, investors in many European countries often pay significantly more in fees for absolutely no added benefits, compared to local investors.

3. ***Rental properties aren't simple***

   Many people consider buying a rental property in a foreign country the ideal investment, especially if they are considering emigrating there at some stage. A number of countries also offer passports to investors provided they purchase property in those countries, which can also lead to this kind of investment.

   There are, however, a number of ways that a rental property can end up becoming a money sinkhole instead of offering the expected stable returns.

   International property investors should not simply buy into whichever development the internet or sales agents are suggesting. Do your homework and fully understand the laws, taxes and unique conditions around the country, city and suburb you hope to invest in. Even if the property you are about to buy seems like a good deal, if it is in an area where there is too much rental housing and you struggle to find a tenant, it will end up costing you a small fortune instead.

   Investors need to also make sure they do their research on the companies they are working with to ensure they are not uncertified or unscrupulous. Fortunately for investors there is the Association of International Property Professionals (AIPP), an international body that is committed to regulating the industry. If you partner with an AIPP member, you are assured that they have been vetted and approved.

   Arranging finance in a foreign country is possible, but again comes with a need for caution. What is the track record of the company offering the finance and just what are the terms they are offering in their contracts? Laws in other countries may not be the same when it comes to finance, and there may not be the same protections that are on offer in SA relating to allowable interest rates and what happens in the event of a default.

   Applicable laws need to be checked regarding tenancy too. Are there protections in place if your tenant does not pay the rent? What happens if someone refuses to move out or damages the property? The best solution is to team up with a reputable letting agent who knows the laws, and who has your best interests at heart to ensure you don't fall foul of some trick of local law. Of course, using an agent results in additional costs, but in the scheme of things this is likely to be money well spent.

   In short, research and research again. This is not something to rush into because you saw a flashy Power-point presentation.

4. ***Double Taxation***

With the laws around taxation of foreign income recently changing there is a lot of uncertainty, and numerous rumours have arisen as to just when tax is applicable, whether disclosure is necessary and just how much is due. The basic rule is that South African tax residents are subject to tax on their worldwide income regardless of where that income derives or whether it has already been subject to tax in the country where it was earned.

It gets more complicated though, because the South African government has numerous Double Tax Agreements (DTA) with various countries, which seek to prevent double taxation. These are not always helpful however as they don't always protect the investor from paying two sets of taxes.

The DTA signed with the UK for example clearly outlines in Article 6(1) and 6(3) that where a South African receives rental income from letting immovable property in the UK, such income may be taxed by the UK. It does not however say that South Africa is then not allowed to also tax the income. Article 21 tries to provide protection from double taxation, but there are numerous limitations.

This is then further complicated by the fact that there are some domestic laws which seek to help prevent double taxation in some circumstances, but these laws don't always apply and come with onerous documentary requirements. Basically, consult an accountant to go through the particulars of your case to determine if any tax is owed and what to do about previously undisclosed income to avoid falling foul of the law.

5. ***Waiting for the right time to invest***

Perhaps the simplest error to correct is the one where, having already decided to invest offshore, the investor decides to hold onto their money, waiting for the right time to jump into the foreign market.

It may seem wise to wait for the Rand to strengthen or the global equity markets to offer up some value, but this is advised against. Commonly, when people are waiting to move funds, they place large sums of money in money market funds, sometimes for years, looking for the right time to jump in, all the while accruing local income taxes at the marginal rate. This more than undoes all the good that a small strengthening of the Rand could present.

If you are going to do it, there is no better time than the present.

What Should You Do If a Creditor Tries to Liquidate Your Business?

Due to the recession, there are a rising number of local companies in financial distress and facing threats or applications from creditors to liquidate their businesses.

The latest Statistics South Africa (StatsSA) figures released in November show that the total number of liquidations increased by 33.2% in the three months ended October 2020 compared with the three months ended October 2019.

Werksmans Attorneys head of insolvency, business rescue and restructuring Dr Eric Levenstein said during an interview that a company in distress faced with the possibility of liquidation needed to get advice as soon as possible.

Get professional advice as soon as possible

“My advice is do not wait if your company is struggling, or your creditors are applying pressure, go get professional advice. If you leave it too late, then your company faces one option – liquidation,” Levenstein added.

He said it was vital for small business owners to confront the situation and take drastic action to fix their battling company and ensure it survived.

Shepstone & Wylie Attorneys head of litigation Andrew Donnelly has specialist knowledge about insolvency, business restructuring and business rescue.

He said during an interview that when the owners of a small company faced a court application from a creditor to liquidate their business for alleged unpaid debts, they must first check its legality and determine if the creditor’s claims for outstanding debt were valid.

If there was a dispute about the validity of the application, then the company owners should oppose the liquidation, he added.

Stephan Venter is a Cliffe Dekker Hofmeyr lawyer who focuses on insolvency, corporate recovery, and business rescue.

He said during an interview that when reviewing a liquidation application, it was important for small business owners to determine whether their companies were commercially insolvent, since this was what a court would focus on when deciding whether or not the court should order the company liquidated.

To answer this question, the owners must consider if the company could pay its debts as and when they became due and payable, he added.

“It is expensive to go to court, so a creditor will normally only apply to the court for a company’s liquidation once they have exhausted all other informal options, and if there is a reasonable prospect to recover amounts owing to them once the company is liquidated,” Venter said.

Levenstein said that what often happened was that the board of directors anticipated the possibility of a liquidation application because of their creditors getting aggressive about unpaid bills.

“The directors then file for business rescue by a board resolution, and that puts a stop to the liquidation application for the time being. It is a defensive strategy. It doesn’t mean that the business rescue will be successful, but at least there is an opportunity to talk to your creditors. To set aside the business rescue, a creditor would have to apply to the court,” he added.

Donnelly said that only companies and close corporations could apply for business rescue. If there was already a pending application for liquidation, then the company must apply to the court for an order allowing for business rescue, he added. Donnelly said that when the owners of a distressed company applied to the court to have their company placed into business rescue, they must have a plan to save the business. The business rescue plan would require the approval from creditors holding 75 per cent of the value of the claims, Donnelly said.

“If there is no plan, then liquidation may be the only option,” he added.

Many well-known companies have gone into business rescue

Well-known local companies that have recently gone into business rescue include Comair, Edcon, Phumelela Gaming and Leisure, SAA and SA Express.

If a creditor brought a justified liquidation application and the company was insolvent with no hope of rescue, then the courts would approve the winding up, Donnelly said.

Small owner-managed or family businesses often look at their companies emotionally, and they try to save their businesses at all costs regardless of the facts.

"The best course of action often would be to make the hard decision and close the business," he added.

Donnelly cautioned that while creditors might use the threat of liquidation to aid the payment of their debts, they had to have rational grounds for a liquidation application.

Levenstein said that tactically a creditor wanting payment could threaten the company that owed money with liquidation.

"Creditors that are owed money would apply pressure and to ensure the repayment of outstanding debt," he added.

Creditors see liquidation as a quick way to get their money

Creditors seeking payment for their debts were increasingly applying for liquidation rather than business rescue as they saw liquidation as a quicker way to get their debts settled, Donnelly said.

"The problem with business rescue is that it can drag on. Creditors find that very frustrating because the company continues trading, but legislation prevents them from enforcing their claims," Donnelly said.

Larger companies have a better chance of surviving than small to medium companies because business rescue was expensive, Levenstein said. It was important for company directors to consider whether they were incurring needless debt that they could not afford to pay back, he said.

In such a situation, the company directors could face accusations of reckless trading and be sued in their personal capacities, he added. Donnelly said that before a company went into business rescue, the first person the company's directors should talk to was their banker.

If the banker heard about a business rescue of a small company through the grapevine, he or she would get a nasty surprise and go into a defensive mode where they would focus on debt recovery rather than trying to help the distressed company, he added.

Communication with a company's bankers was even more important if the company was likely to need post-commencement finance from their bank to stay afloat, Donnelly said.

Other options for distressed businesses

A company facing the possibility of liquidation has several options other than a business rescue or a court-sanctioned liquidation.

The first was to negotiate an informal repayment plan with the creditor bringing the liquidation application, Donnelly said.

The second option was for a distressed business to pursue an informal restructuring, Levenstein said.

An informal restructuring takes place when a company changes the structure of the company, exits from non-performing entities, sells off assets, reduces staff, and cuts costs to make the company more efficient, Venter said.

"The most important thing is to have a good relationship with your creditors when proceeding with informal restructuring options," he added.

Levenstein said that the dangers of an informal restructuring were that all of the company's creditors needed to agree to it.

"You cannot have one creditor disagree, and then the company pays the other creditors because then you prefer certain creditors ahead of other creditors, which the law does not allow," he said.

"The other problem is that one of those creditors could apply to the court for the company's winding up with liquidation. This situation would come amid the company's admission that it cannot pay its creditors and so this could invite a liquidation. So informal restructuring can work, but the problem is that there is no moratorium on creditor claims like in business rescue," Levenstein added.

The third option for a company in distress was to pursue a voluntary liquidation, which Donnelly pointed out could offer big cost savings when compared with a court-sanctioned liquidation.

Voluntary liquidations are much more prevalent than compulsory applications as StatsSA figures show that during the ten months ending October this year, there were 162 compulsory liquidations compared to 1,448 voluntary liquidations.

Venter said that a voluntary liquidation could involve the sale of the assets and wind-down of a distressed company by an appointed liquidator.

If a company filed a special resolution with the Companies and Intellectual Property Commission in line with the relevant sections of the Companies Act, then the company would be placed under voluntary liquidation, he added.

The owners of a company could place it under voluntary liquidation even though its creditors do not agree or support the initiative, Venter said.

A fourth option is for the company directors to enter into a compromise with all of its creditors or a class of its creditors in terms of Section 155 of the Companies Act.

Venter said that a compromise was where a company comes to an arrangement with its creditors, for instance, to reduce the debt it owed them or to pay the amount owed to the creditors over an extended period. A compromise aimed to allow a company to improve its financial position, he added.

"If seventy-five per cent of the creditors in value approve the compromise, the court sanctions it and then it becomes binding on all existing shareholders. Properly used a compromise can be a very effective way of saving and restructuring a struggling company," Donnelly said.

But Levenstein said that the problem with Section 155 was that there was no moratorium against creditor claims.

Once the court approved the liquidation application, then the Master of the High Court would select a liquidator, Levenstein said.

Liquidation was the end of the company because the liquidator would shut it down, sell all the assets and the creditors would get a final liquidation dividend, he added.

Donnelly said that liquidation would tarnish the reputations of the owners of a business and could impair their ability to win the support of clients, investors, and financial institutions for other business ventures in the future.

However, a factor of liquidation was that the liquidator could probe any allegations of mismanagement by the company's directors, he added.

The Way Forward: More Virtual Meetings?

> ***"Any sufficiently advanced technology is indistinguishable from magic" (Arthur C. Clarke, English science writer and inventor)***

Virtual meeting platforms have their pros and cons, but the standout advantages seem to be their cost effectiveness, time saving capabilities and their ability to host large numbers of attendees at very small cost.

The options available to companies looking to use these platforms are vast. The South African Institute of Chartered Accountants (SAICA)'s recommended list of virtual meeting software and platforms for accounting professions and their clients include:

- CrowdCast
- Google Hangouts
- GoToMeeting
- Hopin
- Microsoft Teams
- Skype
- Zoom.

Auditable voting tools

Furthermore, one of the useful tools of a platform like Zoom and Microsoft Teams, for example, is their polling system, which could be used in a meeting that requests voting or Q&As.

Virtual meetings pass the legal test and are admissible in court

Earlier this year, the Johannesburg Labour Court ruled that it is fully legal for employers to negotiate retrenchments with employees through Zoom.

The watershed ruling handed down by judge Graham Moshoana, in an urgent application brought by the Food and Allied Workers Union (FAWU) against South African Breweries (SAB), effectively gave credence to virtual meetings as legally recognised replacements for, or equivalent to, conventional face-to-face meetings in appropriate cases.

The resources used in face-to-face meetings can be put to better use

The average meeting requires money - from catering, human resources and fuel to even flights and accommodation. You can host a virtual meeting with literally thousands of attendees almost for free, with the only cost considerations being software, data and the availability of a laptop or computer.

This is ideal for businesses with a lot of employees. For example, if you are using Zoom for Webinars, it can allow up to 10,000 virtual attendees to sign up.

Virtual meetings afford a chance to save the conversation online

The meetings' recordings are capable of remaining available for the attendees to refer back to and replay the content for clarity at their own discretion without extra charges.

This can improve the quality of output.

The downsides

On the downside, the quality of the conversation depends on external factors, typically beyond the administrator's control. These could include data processing speed, audio visual quality, and the quality of network reception.

Consider virtual meetings more in your business and put your resources to better use - ask your accountant how to achieve this to maximum effect.

Your Tax Deadlines for January 2021

- 7 January - PAYE submissions and payments
- 25 January - VAT manual submissions and payments
- 28 January - Excise Duty payments
- 29 January - VAT electronic submissions and payments
- 29 January - CIT provisional payments

2021
happy new year

"Have a Healthy, Happy and Successful 2021!"

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