

**ATTRIBUTING TAX LIABILITY OF A DELINQUENT COMPANY TO ITS
REPRESENTATIVE TAXPAYER: A LEGAL COMPARRISON OF SOUTH AFRICA
AND AUSTRALIA**

by

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DECLARATION

I, **JOHAN CORNELIUS ELS** hereby declare that the dissertation is my own, unaided work. It is being submitted in partial fulfilment of the prerequisites for the degree of Masters in Tax Law at the University of Pretoria. It has not been submitted before for any degree or examination in any other university.

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7 September 2016

ABSTRACT

The South African Revenue Service has for many years found it difficult to collect sufficient amount of tax from a limited taxpayer base. It has therefore sought to increase the range of its collections efforts by including in legislation several aggressive collections actions such as attributing a tax liability of a company to its representative taxpayer. It appears from reading the enabling provisions of the Act that the legislature omitted to determine the exact manner in which such tax debt should be attributed. This is precariously done by issuing the representative taxpayer with a notice informing him/ her of his/ her suspected liability and thereafter blindly attributing the tax debt without notice of assessment.

If compared to the South African Companies Act, Act 73 of 2008 it becomes apparent that in instances where a director has been found to have violated his fiduciary duties and contributed or caused a debt to be unpaid he would only become liable through the operation of law. Simply an aggrieved party must upon application to the relevant court prove gross negligence, fraud or an unconscionable abuse by the director concerned before the court will deem such person to be liable. The courts have the benefit of decided cases to assist them in making an objective determination whether a person becomes liable or not.

Contrary to the South African Revenue Service's its Australian counterpart has through their legislators found it wise to, in similar circumstances, impose a penalty to a suspecting defaulting director. The director would be given a determined amount of time to remedy the default after which, if left unpaid, a penalty equal to the liability would be imposed upon the director. The Australian Tax Authority has also sought to include various defences a suspecting defaulting director may rely on to refute any claim of liability. This approach is seen to be pragmatic and pro-active as it allows the Australian Tax Authority to mitigate any real loss it may incur.

In my dissertation, I will evaluate and compare the different approaches of attributing a liability of the delinquent company to its representative in differing fields of law and jurisdictions. In the comparison, it will be shown that the manner in which a tax debt is attributed to a representative taxpayer is just as important for the reason a revenue authority would want to attribute a tax debt to a representative taxpayer. The purpose of the comparison is to highlight the effectiveness of the different approaches and the burden of proof that needs to be overcome by a complaining party. In the dissertation, it will become

evident that, despite moral and judicial justification for attributing a tax debt of a delinquent company to its representative taxpayer, there are debilitating shortcomings in the South African Revenue Service's current approach.

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CHAPTER I

ATTRIBUTING A TAX LIABILITY OF A DELINQUENT COMPANY TO THE REPRESENTATIVE TAXPAYER OF THAT COMPANY

I. RESEARCH PROBLEM BACKGROUND OF THE STUDY

The Commissioner for the South African Revenue Service (hereinafter referred to as the Commissioner) is finding it increasingly difficult to collect and maintain revenue collection from a relatively conservative and small taxpayer base in a slowing economy. Taxpayers, who for the purpose of this research are primarily corporate entities, will often postpone or evade the payment of tax, be that willingly or not. This is evidenced by the 2014/15 collections target, based on a 2.9% GDP growth outlook, which was set at R993.6 billion in the February 2014 Budget announcement. Subsequent to this announcement the real GDP growth was revised down to 1.4% in the February 2015 Budget. This was as a result of tentative global economic performance and domestic supply side constraints. The latter included the impact of strikes in the mining and manufacturing sectors as well as prospects of significant load shedding. Furthermore, the slump of the oil price in the second half of the 2014/15 year reduced the profit outlook for fuel companies, while imports overall were in a downward spiral. As a result, in the February 2015 Budget, the 2014/15 Revenue estimate was revised downwards by R14.6bn to R979bn. Regardless of the reason, the Commissioner is aware that, if left unchecked the effect of such delinquency may be devastating not only to fiscal growth but also to investor confidence¹.

The burden to collect tax therefore increases and the Commissioner is desperately seeking to maintain a position of not forgoing any tax and to collect as much through the means of collections actions created in the tax acts the Commissioner administers. But what

¹ Minister of Finance, 2015 Budget Speech, 25 February 2015 at 1 *'Today's budget is constrained by the need to consolidate our public finances, in the context of slower growth and rising debt. And so we must intensify our efforts to address economic constraints, improve our growth performance, create work opportunities and broaden economic participation. We need to achieve these goals if our National Development Plan is to be realised. On the one hand, our development path is limited by the resource constraints of the current economic outlook. On the other hand, it seeks to lift these constraints by strengthening public institutions, supporting innovation and making markets work better and investing in infrastructure and our people. The 2015 budget is aimed at rebalancing fiscal policy to give greater impetus to investment, to support enterprise development, to promote agriculture and industry and to make our cities engines of growth.'*

if the Commissioner is unsuccessful to collect tax from a trading and delinquent corporate entity?

The Commissioner has in recent years, in an effort to increase tax compliance, moved to expand its collections efforts. This includes collections action against the personal estate of the known representative taxpayers of a delinquent company. This, in particular, was the case in an unreported case in the Witwatersrand Local Division ruling where the SARS had attributed the Value Added Tax (VAT) Liability of the Close Corporation to the member thereof.

II. RATIONALE OF THE STUDY

Prima Facie, attributing the liability of a legal person, poses a legal challenge to the independence of the legal person and those natural persons who are mandated to act on its behalf. The writer will herein attempt to determine whether the Commissioner may legally attribute the tax liability of a delinquent company to the representative taxpayer of that company. The research problem will presuppose that the Commissioner has in the performance of his primary functions² attempted to recover an unpaid tax amount from a (tax delinquent) company, and or its debtors (where applicable) with little or no success. It will be necessary to determine why tax legislation requires such a drastic legal remedy, in particular where the Commissioner may, and is not barred from, approaching a competent court for an order to finally liquidate and wind-up the affairs of a company³. If found that sufficient reasons exist to justify the existence of such legal provision the writer intends to determine:

- The requirements in law that must be met; and
- Whether such legal provision would pass constitutional scrutiny.

III. ASSUMPTIONS AND LIMITATIONS

The writer would not assume any fact or point in law, yet he intends to limit the scope of his research to the following aspects in respect of this topic:

- Corporate legal entities;

² s 4 of the South African Revenue Service Act, Act 34 of 1997

³ Companies Act, Act 61 of 1973, Companies Act, Act 71 of 2008

- s 96(7) of the Income Tax Act, s 48(6) of the Value Added Tax Act and s 155 of the Tax Administration Act; and
- Trading companies which are either solvent or insolvent but not yet finally wound up

IV. RESEARCH QUESTIONS

This research will respond to the following questions:

a) *Regarding the current tax statute*

May the SARS attribute a tax liability of a legal person to its appointed representative? and *ifso*

b) *Regarding the current tax jurisprudence*

Have the courts in South Africa been asked to answer this question? If so what did the court decide?

c) *Regarding the international ratio iuris*

Is this an international standard practice? How is this pursued in other jurisdictions and how does it compare to the South African approach?

d) *Regarding the common law*

Does the liability of common law exist in Common Law?

Have the courts been asked to address the issue under common law and if so what did the courts decide?

e) *South African Tax Law*

Does SARS actively practice the principle of attributing a tax liability of a corporate entity, if so what approach does it make use of?

What are the specific circumstances under which the SARS may attribute a tax liability of a legal person to its appointed representative? and

Who carries the burden of proof in attributing the liability?

What are the fundamental and formal requirements which must be met before the SARS may attribute a tax liability to the tax representative?

What is the legal effect of attributing the tax liability?

What remedies can the Commissioner pursue in the alternative?

What would be the cost and the benefit to the Commissioner in attributing a tax liability?

What remedies does the tax representative have against a decision to attribute the liability to him or her?

How does the position as set out in tax legislation differ from those in the companies Act?

How have the courts treated this issue?

f) Principles of Administrative Law

Does the Promotion of Administrative Justice Act, Act 53 of 2002 (PAJA) play a role in the Commissioner's decision to attribute the tax liability of a corporate entity to a tax representative? And if so how? Should it not be a factor that the Commissioner, as a creature of statute and an organ of the state, must consider in its decision to attribute a liability?

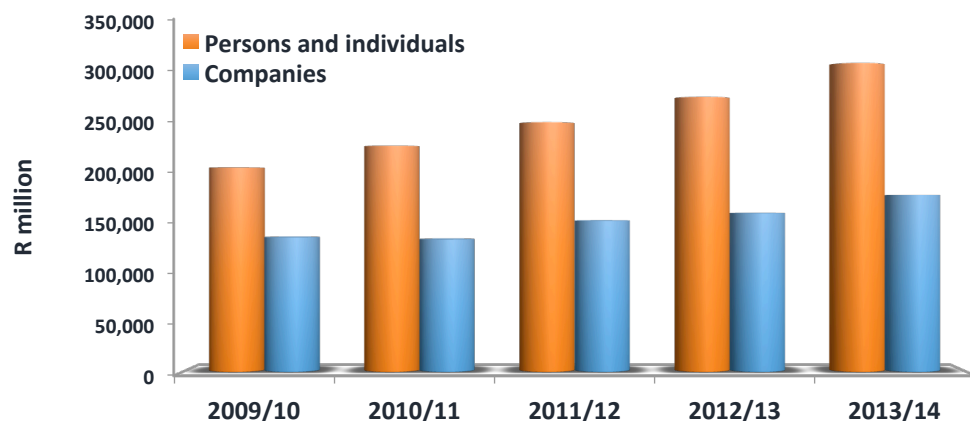
g) Principles of Constitutional Law

Does the attribution of a tax liability pass constitutional scrutiny?

V. MOTIVATION FOR RESEARCH

a) Background

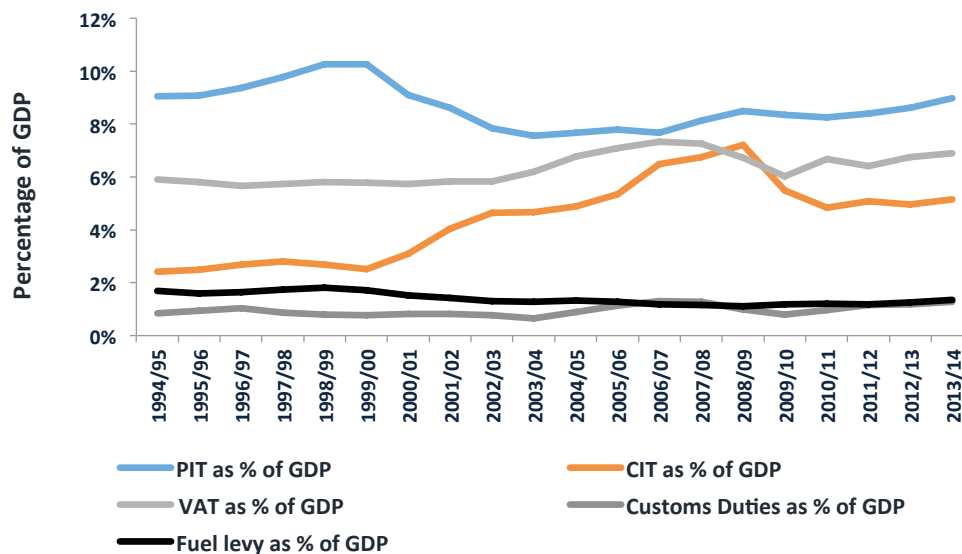
The Commissioner in its *Annual Performance Plan for 2015/ 2016*⁴ identified a risk in the global and local economic instability and the pressure it creates on the Commissioner's ability to fulfil its primary function to cost effectively and efficiently collect revenue. The Commissioner's argues in its Annual report that its research and empirical data shows that taxpayer's attitude towards compliance and their attitude to comply is influenced by the public's confidence in government. It is rational to infer that non-compliance on the part of the taxpayers can not only be ascribed to perception but most often than not taxpayers are responsible, deliberately or not, for their own delinquency. In the Commissioner's *Tax Statistic Report for 2014*⁵, the Commissioner provides a comparison between persons, individuals and companies as contributors to the national *fiscus*. It is interesting to note that the biggest contributor to the national *fiscus* appears to be the persons and/ or individuals whilst business and industry account for nearly half of the value of the former, and it also seems that the gap between these two contributors is growing larger year on year.



⁴ SARS *Annual Strategic Plan 2015/2016*, RP61/2015

⁵ National Treasury and SARS, *2014 Tax Statistics Publication*, November 2014

A further comparison done by the Commissioner, in relation to GDP, highlights the burden on the persons and individuals even more.



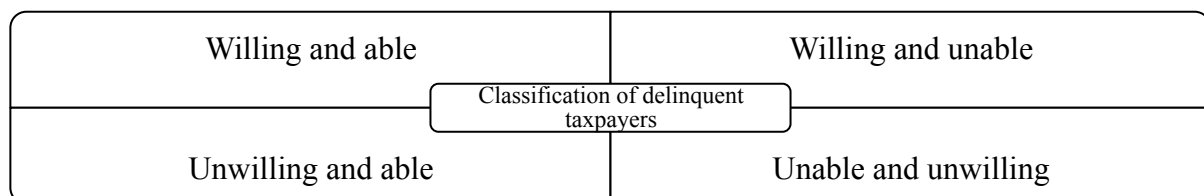
It is inferred from the diagram above that the compliance and recovery from persons and individuals are on the rise but remains below the highest mark of 10% achieved during the late 1980's. Unlike persons and individuals, companies and industry have experienced a dramatic decline from the highest mark of 7,5% achieved during 2008/2009 year. It appears that companies and industry are intent on maintaining a 5% mark. The relevance of the distinction between these two contributors may lie in the debt book of the Commissioner. This debt book comprises of all delinquent taxpayers, but no empirical data is provided by the Commissioner in any of its reports differentiating between each of the known contributors as to the percentage it occupies. It can only be assumed that the ratio would be similar to the comparison between persons, individuals and companies as contributors to the national *fiscus* as set out above. The difference may only be that despite the quantity, companies and industry may far exceed the value of the portion of unpaid tax compared to the portion of unpaid tax of persons and individuals.

According to the Commissioner's Annual Strategic Plan for 2015/2016 the current actual debt book as a percentage of GDP stands at 10,79%. This 2,79 % Higher than what the Finance Minister has agreed to as an agreed target of 8% for the 2015/2016 year and 4,76% higher than the acceptable International standard. This means that the Commissioner's task to collect without fail a staggering amount of arrear taxes by means of legal recovery action

from a small but significant contributor with the likelihood of forgoing an adverse percentage of unpaid tax.

The Commissioner has therefore, without elaborating much, marked as a priority objective and initiative for the 2015/2016 year, the use of all litigation tools at its disposal to achieve its objectives. If this were to include an extreme measure such as attributing an unpaid tax debt of a delinquent company to the known representative taxpayer it may have several consequences which may not just affect the actual yield of recovery but also contribute to diminishing a taxpayer confidence in the government’s ability to ensure just and fair administrative action as envisaged in the provisions of the Constitution of the Republic of South Africa. From a tax administration perspective, the Commissioner does not have the luxury to forgo any tax that is due. In fact, it will only force the Commissioner to make every effort to not only expand its taxpayer base but also expand and make use of each and every available remedy to collect whatever tax from whatever source as far as the law may permit.

The Commissioner’s efforts in revenue collection are however always subject to the provisions of s 4 of the South African Revenue Service Act read with s 195 of the Constitution of South Africa. The gist and the effect of the latter are that despite the fact that the Commissioner may not forgo any tax, he must ensure that he performs his functions in the most cost effective and efficient manner whilst promoting administrative efficiency and making sure his decisions are at all times to the best advantage of the state. This is arguably one of the most precarious of all tasks of any bureaucracy. Similarly, the ability of the company to pay any amount of tax must be differentiated from its willingness to be compliant. A company’s willingness in comparison to its ability can be distinguished as



indicated the diagram below:

The ability and willingness of the company may either be a direct or indirect consequence of either the policies and procedures (accounting policies and business strategy etc.) created by

the board of directors or as a result of external circumstances or the conduct of third parties (debtors, creditors or legislative changes etc.) related to that company⁶. Despite the company's solvency and liquidity position at the time of demand of the tax liability, various factors will convince the Commissioner that it will be unable to collect the tax from the company. At the same time, if it would be correct in law to attribute a tax liability to the representative taxpayer such exercise would be futile if the person to whom the liability is attributed to, owns inadequate assets and/ or resources to pay the tax liability of the company. It is therefore safe to conclude that the Commissioner is compelled to apply the same principle it would when collecting a tax from the company. The Commissioner would be required by law to perform his duties to collect revenue in the most cost effective and efficient manner and its decision to attribute the liability must be to the best advantage of the state. In short, the benefit in such action must exceed the cost.

b) Approach and method

The writer will attempt to apply a combined approach and method to the research proposal. The writer will in this research proposal conduct an analytical approach wherein a particular court decision would be analysed and thereafter he will attempt to conduct a comparative review of the international tax law, the South African tax laws and common law with the latter. Thereafter the writer will conduct a critical analysis of current South African tax legislation and existing case law.

c) Structure/ Chapters

The structure will be set out as follow:

- I. Chapter I Attributing a tax liability of a delinquent company to the representative taxpayer of that company
 - I. Research problem Background of the Study
 - II. Rationale of the study
 - III. Assumptions and limitations
 - IV. Research Questions

⁶ See diagram attached and marked as JCE 1

- V. Motivation
- II. Chapter II Attributing a tax liability in terms of s155 of the Tax Administration Act, Act 28 of 2011
 - I. Introduction
 - II. The Liability of a Representative Taxpayer
 - III. The Personal Liability of a Representative Taxpayer
 - IV. General Principles
 - a. Disregarding the legal independence of the Principal Taxpayer
 - b. The Commissioner's decision
 - c. Burden of Proof
 - d. A Relationship of Trust
 - V. Determining personal liability in terms of s 155 of the Tax Administration Act
 - a. Procedural fairness
 - b. Substantive Fairness
 - c. Factors not relevant to the Commissioner's decision
 - d. Factors relevant to the Commissioner's decision
 - e. The Effect of the Commissioner's decision
- III. Chapter III: Director's personal liability in terms of the Companies Act, Act 71 of 2008 and at common law
 - I. Introduction
 - II. General Principles
 - a) Legal Independence
 - b) Legal Capacity and Authority
 - c) Director's duties
 - III. Approach under the Companies Act of 1973
 - a) When it appears that the business of the company is carried on recklessly/ burden of proof
 - b) Any business of the company
 - c) Recklessly
 - d) Intent to Defraud/ Fraudulent purpose
 - e) Knowing Party
 - IV. Approach under the Companies Act of 2008
 - V. The Gore Case and the meaning of 'unconscionable abuse'

- IV. Chapter IV: Director Penalty Notice – An Australian Approach
- I. Introduction
 - II. The Global Economy *versus* Taxpayer Compliance
 - III. A director’s liability for corporate faults and defaults - An Australian Approach
 - a) Background
 - b) Australian Policy Consideration
 - IV. Australian Tax Position – s 269 of the Taxation Administration Act, 1953
 - a) Purpose
 - V. The four Components of Directors liability
 - a) Director’s obligations
 - b) The Notice
 - c) The Penalty
 - d) The Effect of the penalty of the Director’s obligation ending before the end of the Notice period
 - VI. Defences
 - a) Illness
 - b) All reasonable steps taken
 - c) Superannuation guarantee charge – reasonable arguable position
 - VII. Conclusion
- V. Chapter V: Comparative Analysis
- I. Introduction
 - II. Frame of Reference
 - III. Grounds of Comparison
 - a) International ratio *iuris* – An Australian perspective
 - b) South African Company *ratio iuris*
 - c) South African Tax *ratio iuris*
 - IV. Theory
 - a) Substantive similarities and dissimilarities
 - b) Substantive Similarities
 - c) Substantive Dissimilarities
 - d) Procedural Similarities and dissimilarities
 - e) Procedural Similarities

f Procedural Dissimilarities

V. The causal nexus

VI. Chapter 6: Conclusion

CHAPTER II

ATTRIBUTING A TAX LIABILITY IN TERMS OF S 155 OF THE TAX ADMINISTRATION ACT, ACT 28 OF 2011

I. INTRODUCTION

The general rule in any tax regime is that a Company as a principal taxpayer ultimately acquires liability under a relevant tax Act to either charge, declare, deduct and/ or withhold an amount of tax in respect of income it had derived¹, remuneration paid to an employee² or goods or services supplied to a vendor in the furtherance of its enterprise³. It cannot be ignored that a principal taxpayer would be unable to fulfil its statutory obligations in respect of a tax Act without a duly authorised and delegated representative taxpayer⁴ to act for and on its behalf. This, however, does not result in the principal taxpayer being relieved from any liability, responsibility or duty imposed under a tax Act by reason of the fact that the taxpayer's representative failed to perform such responsibilities or duties; or is liable for the tax payable by the taxpayer⁵. Yet it seems that, notwithstanding the latter, the legislator intended or anticipated circumstances under which a representative taxpayer may be liable for a tax debt incurred by a principal taxpayer.

Having carefully evaluated and considered the construct of the provisions under which the Commissioner may rely upon in deeming a representative taxpayer to be liable, it is the writer's view from reading these particular provisions that one must distinguish between the liability⁶ and the personal liability⁷ of a representative taxpayer. The necessity to distinguish between these two constructs is that each construct affects the representative taxpayer differently.

II. THE LIABILITY OF A REPRESENTATIVE TAXPAYER

s154 of the *Tax Administration Act* ("s 154") states that a representative taxpayer is, as

¹ s 5(1) of the Income Tax Act, Act 58 of 1962 (Repealed),

² Para 2 to 11 of the 4th Schedule of Act 58 of 1962 (Repealed) *ibid* note 1

³ s 7(1) of the Value-Added Tax Act, Act 89 of 1991

⁴ s 154(1) of the Tax Administration Act, Act 28 of 2011

⁵ s 154(3) of Act 28 of 2011 *ibid* note 4

⁶ s 154 of Act 28 of 2011 *ibid* note 4

⁷ s 155 of Act 28 of 2011 *ibid* note 4

regards the income, and monies to which the representative taxpayer are entitled to or has the management or control of such monies, transactions concluded by the representative taxpayer for or on behalf of the principal taxpayer; and anything else done by the representative taxpayer, in such capacity subject to the same duties, responsibilities and liabilities of the principal taxpayer he represents and he is also entitled to any abatement, deduction, exemption, right to set off a loss, and other items that could be claimed by the principal taxpayer; and liable for the amount of tax specified by a tax Act⁸. The liability of a representative taxpayer therefore becomes a matter where it is necessary to determine who attracts a liability for a tax under a Tax Act imposed and who is personally liable for such tax⁹.

Some writers hold the view that the representative taxpayer merely steps into the shoes of a principal taxpayer both in regards to payment of a tax liability and in respect of a liability to comply with all other obligations of the principal taxpayer under a Tax Act¹⁰. A representative taxpayer¹¹ may, therefore, be assessed in respect of any tax incurred by the principal taxpayer, but such assessment is regarded as made upon the representative taxpayer in such capacity only¹². This corresponds to the view of Delpont as set out in the preceding chapter. To recount, Delpont states that if a director had given his consent to act for and on behalf of the company, only the company and the third party (SARS) will acquire rights and obligations as to each other.

It is the writer's view that an assessment issued under the provisions of s 154 to a representative taxpayer will not result in or constitutes to be a tax debt due by a representative taxpayer in his personal capacity¹³. It merely suggests that the intended assessment is issued to a person responsible for accepting such assessment on the principal taxpayer's behalf. It further suggests that the representative taxpayer would be the appropriate person to take the necessary steps in terms of the company policies and/ or procedures to pay or respond to such

⁸ s 154(1) of Act 28 of 2011 *ibid* note 4

⁹ s 152 of Act 28 of 2011 *ibid* note 4

¹⁰ David Clegg *et al*, *Income Tax in South Africa, Liability of representative taxpayer for assessed and self-assessed taxes* at para 27.21.2, available at <http://www.mylexisnexis.co.za>

¹¹ s 153 of Act 28 of 2011 for the definition of a representative taxpayer

¹² s 154(2) of Act 28 of 2011 *ibid* note 4

¹³ *Op cit* note 10 at para 27.21.2, *Persons liable for the payment of tax: public officers, Secretary of Finance v Esselman*, 50 SATC 1, 1988 (1) SA 594 (SWA) "That, having regard to ss 5 and 43 of Ordinance 5 of 1974 and to the dictionary meaning of 'payable', liability to income tax exists prior to the making of an assessment" It therefore follows that a principal taxpayer incurs the liability prior to assessment and such liability is one that the representative taxpayer assumes in his representative capacity.

assessment accordingly. Thus, the tax liability in this instance can only be recovered from the assets belonging to the person represented which may, for whatever reason, either be in the representative taxpayer's possession or under his management or control¹⁴.

III. THE PERSONAL LIABILITY OF A REPRESENTATIVE TAXPAYER

s 155 of the *Tax Administration Act* (“s 155”) states that a representative taxpayer is personally liable for tax payable in the representative taxpayer's representative capacity, if, while it remains unpaid¹⁵, the representative taxpayer alienates, charges or disposes of amounts in respect of which the tax is chargeable¹⁶; or the representative taxpayer disposes of or parts with funds or money, 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 monies¹⁷. The enabling provision does not indicate whether the representative taxpayer attracts the liability in his personal capacity by way of assessment or otherwise. It is inferred from the wording of the section that in order to attribute a principal taxpayer's tax liability to the representative taxpayer, that it requires a decision on the part of the Commissioner in the performance of its statutory function, which is supported by a factual determination. The factual consideration requires an assessment of certain facts, which are relevant to the unpaid tax liability and the conduct, or intention of the representative taxpayer¹⁸.

IV. GENERAL PRINCIPLES

a) *Disregarding the legal independence of the Principal Taxpayer*

As indicated *supra*, the enabling provision does not indicate whether the representative taxpayer attracts the liability in his personal capacity by way of assessment or otherwise. However, from evaluating s 155 and in comparing it to s 20(9) of the *Companies Act*¹⁹, it appears that the legislator has sought to give the Commissioner the statutory power and authority to disregard the legal independence of the principal taxpayer by enabling it to lift or pierce the corporate veil under certain

¹⁴ s 160(2)(a) of Act 28 of 2011 *ibid* note 4

¹⁵ s 155(1) of Act 28 of 2011 *ibid* note 4

¹⁶ s 155(1)(a) of Act 28 of 2011 *ibid* note 4

¹⁷ s 155(1)(b) of Act 28 of 2011 *ibid* note 4

¹⁸ *ibid* note 17

¹⁹ Act 71 of 2008

circumstances which would allow the Commissioner to deem the representative taxpayer to be personally liable for the unpaid tax of the principal taxpayer²⁰.

b) *The Commissioner's decision*

A decision by the Commissioner to attribute a tax liability to a representative taxpayer must be preceded by a principal taxpayer's failure to pay an amount of tax due and the Commissioner's failure to collect that amount from the principal taxpayer by means of the appropriate recovery actions available to the Commissioner.

c) *Burden of Proof*

It is suggested that having regard to the Commissioner's failure to collect from the principal taxpayer, s 155 requires the Commissioner to make a factual and empirical determination regarding its inability to collect the amount in comparison to the manner in which the tax liability was incurred. As a general rule, the Tax Administration Act places the burden of proof regarding a liability to tax on the person chargeable to tax to refute any such claim of liability by the Commissioner²¹. The question is whether this is also true in the case where the Commissioner seeks to attribute a tax liability of a principal taxpayer to the representative taxpayer based upon a *prima facie* case? According to the *dicta* of *South Cape Corporation (Pty) Ltd v Engineering Management Services (Pty) Ltd*, Corbett, JA²² stated that an onus in its truest sense is only represented when a duty is cast on a particular litigant, in order to be successful, of finally satisfying the Court that he is entitled to succeed on his claim or defense. The onus can never shift from the party upon whom it originally rested. This must be distinguished from the burden of adducing evidence in rebuttal which may shift or transfer in the course of the case between the plaintiff and the defendant depending upon the measure of proof furnished by the one party or the other.

²⁰ ML Benade et al, *Die Maatskappybegrip, Verontagsaming deur die wetgewer*, available at <https://www@mylexisnexis.co.za>, 'Soms ignoreer die wetgewer ook die beginsels rakende afsonderlike korporatiewe persoonlikheid van die Maatskappy. Dit gebeur dikwels in gevalle waar die wetgewer persone anders as die maatskappy aanspreeklik stel vir die skulde van die maatskappy as 'n sanksie vir die nie-nakoming van 'n statutêre verpligting.'

²¹ s 102 of Act 28 of 2011 *ibid* note 4

²² 1977 (3) SA 534 (A) at 548, See also *Pillay v. Krishna and Another*, 1946 A.D. 946 at 952-3; *Brand v. Minister of Justice and Another*, 1959 (4) S.A. 712 (A.D.) at 715,

If it is true that s 155 establishes a *prima facie* claim by the Commissioner (plaintiff) of the representative taxpayer's liability (defendant) in respect of the principal taxpayer's unpaid taxes, then the overall onus rest upon the Commissioner (plaintiff) to prove such liability²³. This is affirmed by the fact that in the absence of any rebutting evidence by the representative taxpayer (the defendant), his liability for the unpaid tax of the principal taxpayer would be conclusive. However, the issue of burden of proof has always been a matter where one must consider the substantive law. It is patently obvious from reading s 155 that in order to give legal effect to the aim and purpose of this section the Commissioner must prove a deliberate act or decision on the part of the representative taxpayer to dispose of monies or funds to which tax was chargeable or of funds or monies which could have been used to pay the unpaid tax with. The Commissioner therefore carries an evidentiary burden to adduce evidence to prove a *prima facie* case against the representative taxpayer.

It is necessary to interpolate at this juncture to emphasize that, unlike proceedings in terms of the Companies Acts, the Commissioner's decision to attribute the tax liability to a representative taxpayer under s 155 does not lie with a competent court to, on application by an interested person, objectively consider whether the representative taxpayer is personally liable or not. Firstly, this is relevant because it is evident from legal precedent that the courts are often reluctant to disregard the legal independence of a principal taxpayer without good cause. Yet, if the facts justify such a decision, the court would be an appropriate forum wherein either party to such application would be given an opportunity to properly ventilate the matter. The court, in consideration of the facts before it, would have the benefit of a plethora of legal precedent to guide and direct it in making the correct decision. Secondly, a matter, which was brought before the court on application by a plaintiff, would first have to survive the court's scrutiny to determine whether he has successfully discharged the burden of proof. If he did, then the burden would shift to the defendant to rebut the claim of the plaintiff, if not the defendant could argue and request Absolution from the instance.

²³ Rule 39(12) of the uniform rules of the High Court, see also *Pillay*-case *ibid* note 23 wherein the court stated that the burden of proof rests upon him who asserts, proves and it rests not upon him who denies, since a denial of a fact cannot naturally be proved provided that it is a fact that is denied and the denial is absolute.

This appears to be simply not the case when reading s 155. In comparison to the South African Company law, it is suggested that the legislator boldly thought of the Commissioner and/or its officials to be well equipped and capable of objectively evaluating the facts to determine whether a representative taxpayer is personally liable or not. The failure by the legislature to provide an adequate mechanism for the Commissioner to exercise its discretion in this regard exposes the fact that the legislator had failed to take into account that it had rather precariously given the power of such decision to a SARS official who is primarily appointed, delegated and tasked to collect the tax liability of that principal taxpayer. Effectively, the plaintiff is also the judge and jury in the decision. As stated in the latter paragraph, s 155 does not provide a mechanism by which a representative taxpayer should be notified of the Commissioner's intended decision deeming him to be liable for the unpaid tax of the principal taxpayer. It can only be assumed from reading s 155 and s 184(2) that the Commissioner is required to notify a representative taxpayer of his decision that he may be liable for the unpaid tax of that principal taxpayer.

The decision by the Commissioner may, therefore, constitute an administrative act, which would be subject to the principles of an administrative review by a court. The issue of an administrative act will be discussed in greater detail *infra*.

d) *A Relationship of Trust*

Until recently the Commissioner has substantiated its decision with the mistaken belief that statutory tax constituted “*trustee funds*”. This mistaken belief allowed for the Commissioner to believe that a trust relationship existed between an employer and/ or vendor as “*trustees*” in relation to the Commissioner. An employer and vendor are at all times duty bound to deduct, charge, collect and pay such monies to the Commissioner²⁴. This assertion created the presumption of automatic liability of the representative employer or vendor in consequence to their fiduciary duty to the

²⁴ Beric Croome & Lynette Olivier, *Director's personal liability for company's debts*, Tax Administration, Juta, 2010, at 242 to 244

company²⁵. This is evidenced from the unreported case of *Peretz v CSARS*²⁶. In this case, the applicant sought an order rescinding a default judgment granted against him in respect of Value-Added Tax owing by a company Restomont Trading CC. The Applicant was the sole member of the close corporation. Mbha, J indicated that the Commissioner had exhausted its recovery collections action against the close corporation, without recovering any amount of tax. Accordingly, the Commissioner proceeded to write a letter to the Applicant advising him of his personal liability. Mbha, J determined that the Applicant was personally liable in that it was obvious that tax was due at a relevant period when there was money available in the close corporation's bank account, but that such monies were never used to pay that tax²⁷. Mbha, J continues in his judgment to emphasise the provisions of the VAT Act as far as they relate to the representative vendor²⁸. He further concludes that a liability for VAT arose under s 28(1) when a taxpayer had its two-monthly duty to pay its tax. The personal liability for tax arose when the representative vendor disposed of funds under his control instead of paying tax²⁹.

However, in the case of *Director of Public Prosecutions, Western Cape v Parker*³⁰ Pillay, J completely rejected any such notion. Pillay held that s 7(1) of the VAT Act did not, either expressly or impliedly, create a relationship of trust between the VAT vendor and SARS. On the contrary, it was clear that the relationship created by the VAT Act was one of a debtor and his creditor and at the time the Respondent was charged, s 40 of the Act was still in operation and that section pertinently described VAT 'when it becomes due or is payable' as a 'debit to the State.' Consequently, it was clear that the VAT Act provided for a debtor-creditor relationship as between the vendor and SARS. The concept that a trust relationship between the vendor and SARS

²⁵ *Peretz, Leon Yehuda v Commissioner for the South African Revenue Services, WLD*, under case number 92/1236, unreported, the writer attempted to obtain the actual court records from the court but was informed that the case number cited on the judgment in the writer's possession is incorrect

²⁶ Op cit note 20

²⁷ ibid note 20 at para 19

²⁸ ibid note 20 at para 28, Mbha, J also bases his judgment on his understanding that the VAT Act is based upon self-assessment and a statutory imposed obligation to pay which arises on a monthly or two monthly basis. According Mbha vendors are involuntary tax collectors; the duty to pay arises *ex lege* and is not dependent upon any form of assessment. He also makes reference to the provisions of section 48(1), 48(2) and 48(3) of The VAT Act in an attempt to create a nexus between the tax liability and the sole member's duty to pay the tax on behalf of the vendor. No factual determination other than the comparison of the VAT tax returns and the bank statements of the close corporation was used to determine the personal liability of the sole member.

²⁹ Ibid note 20 at para 32

³⁰ 77 SATC 224, or 2015 1 All SA 525 (SCA) at para 9 and para 15 to 16

forms the bedrock of the Appellant's argument is clearly unsustainable. It is clear that the VAT Act is a scheme with its own directives, processes and penalties and the relationship that it creates between SARS and the registered vendor is *sui generis*, one with its own peculiar nature. The VAT Act does not confer on the vendor the status of a trustee or an agent of SARS and, if it did, the vendor would either have to keep separate books of account or alternatively would have to be sufficiently liquid at any given time in order to cover the outstanding VAT but the VAT Act makes no provision for this situation nor did it seek to compel a vendor to keep separate books of account in respect of VAT. The same is true of PAYE in terms of the provisions of the Fourth Schedule to the Income Tax Act.

V. DETERMINING PERSONAL LIABILITY IN TERMS OF S 155 OF THE TAX ADMINISTRATION ACT

Mbha, J was partially correct to conclude in the *Peretz*-case by stating that from reading the provisions of s 48(6) of the VAT Act, the Commissioner may under certain circumstances recover the tax from the representative taxpayer³¹. However, the learned judge fails to identify these circumstances in his judgment. In fact, Mbha J's decision was purely based on the fact that there were sufficient monies in the bank of the principal taxpayer to pay the tax at the time a tax return was due³². The judgment in the *Peretz*-case is perilous in that it inadequately concludes and presumes certain circumstantial truths and it is devoid of any proper evidence gathering in determining by way of an empirical analysis of the true facts the reason for the liability, the financial capability of the principle and representative taxpayer in relation to the conduct of the representative taxpayer. The judgment also clearly highlights the incorrect presumption of a trustee relationship as set out in the *Parker*-case³³ *supra*. How then should the Commissioner proceed to determine the personal liability of a representative taxpayer?

³¹ Ibid note 25 at para 14

³² Ibid at para 16 and para 18 where Mbha, J concludes '*It is obvious that the tax was due at a relevant period when there was money available in Restomont's bank account but same was never utilized to pay that tax. Furthermore, the applicant subsequently become personally liable for the tax in accordance with the provisions of s 48(6) of the (VAT) Act*'

³³ Ibid note 30

One cannot ignore the fact that for the Commissioner to continue in such a manner it would first need to satisfy the requirements of procedural and substantive fairness³⁴. It is suggested that these requirements are all embracing and not exclusionary.

a) *Procedural fairness*

Everyone has the right to administrative action that is lawful, reasonable and procedurally fair, and if a person's rights have been adversely affected by the administrative action he has the right to be given written reasons³⁵. An administrative action is defined to be any decision³⁶ taken or failure to take a decision by an organ of State³⁷ when exercising a power in terms of the Constitution or a provincial constitution or exercising a public power or performing a public function in terms of any legislation³⁸. In order to give effect to a procedurally fair administrative action the Commissioner must give the representative taxpayer adequate notice of the nature and purpose of the administrative action, a reasonable opportunity to make representations, a clear statement of the administrative action, adequate notice of any right of review or internal appeal, and adequate notice of the right to request reasons for the decision³⁹.

b) *Substantive Fairness*

The reason for the Commissioner's decision must be made in terms of an empowering provision substantiated by fact. The facts the Commissioner must rely on will be discussed in greater detail herein *infra*. The Commissioner is a creature of statute and as the administrator of tax legislation, it is considered to be an administrative organ of

³⁴ s 33 of the Constitution, 1996

³⁵ s 33 of the Constitution, 1996

³⁶ s 1 of the Promotion of Administrative Justice Act, Act 3 of 2000 defines it to be 'any decision of an administrative nature made, proposed to be made, or required to be made, as the case may be, under an empowering provision, including a decision relating to making, suspending, revoking or refusing to make an order, award or determination; giving, suspending, revoking or refusing to give a certificate, direction, approval, consent or permission; issuing, suspending, revoking or refusing to issue a license, authority or other instrument; imposing a condition or restriction; making a declaration, demand or requirement; retaining, or refusing to deliver up, an article; or doing or refusing to do any other act or thing of an administrative nature, and a reference to a failure to take a decision must be construed accordingly.'

³⁷ s 2 of the South African Revenue Service Act, Act 34 of 1997 'the South African Revenue Service is hereby established as an organ of state within the public administration but as an institution outside the public service.'

³⁸ Act 3 of 2000 *ibid* note 37

³⁹ s 3(2) of Act 3 of 2000 *ibid* note 39

State⁴⁰ the primary objective of which it is to collect revenue⁴¹ for and on behalf of the State. The Commissioner carries a statutory obligation to perform its function in the most cost efficient and effective way and in accordance with the values and principles mentioned in s 195 of the Constitution⁴². Any decision of the Commissioner, as to the personal liability of a representative taxpayer, would constitute a decision taken under an empowering provision as envisaged in the Promotion of Administrative Justice Act⁴³.

c) *Factors not relevant to the Commissioner's decision*

Upon careful evaluation of the provisions of s155, it is apparent that two (2) factors would not be relevant to the Commissioner in making its decision. The first of these are that the representative taxpayer has personally benefitted from the non-payment of tax and secondly, the fact that the tax debt is uneconomical to pursue or irrecoverable from the principal taxpayer. The fact that the representative taxpayer has personally benefitted is not a requirement of his personal liability but may be an element in the consideration of the Commissioner. However, if the representative taxpayer had benefitted in the scheme of such things, it would serve as an extenuating circumstance to attribute the liability to him for the purpose of possible criminal prosecution and/or the eventual surrender of his personal estate.

Although s155 states that a tax liability of a principal taxpayer must remain unpaid before it could attribute that liability to the representative taxpayer, it does not explicitly require for the tax liability to be irrecoverable in relation to the principal taxpayer and the assets it may have. It is suggested that perhaps the Commissioner may even, as far as it could not recover a certain portion of the tax liability from the principal taxpayer, under certain circumstances recover the remaining portion from the representative taxpayer. This has not yet been tested before the court but remains a risk to any representative taxpayer.

⁴⁰ Ibid note 39

⁴¹ s 3(1)(a) of the South African Revenue Service Act, Act 34 of 1997

⁴² s 4(2) of Act 34 of 1997 ibid note 42

⁴³ Act 3 of 2000 ibid note 37

d) *Factors relevant to the Commissioner's decision*

Contrary to the aforementioned, s 155 requires the Commissioner to consider two (2) objective factors in its decision-making process. These factors can be divided into factors inherent to and factors analogous to the decision to attribute the tax liability to the representative taxpayer. The first factor inherent to the decision is the requirement of intent to evade the payment of tax by the representative taxpayer. The intent of the representative taxpayer can be inferred from a disposal of funds or monies to which either tax is chargeable or monies or funds, which could have been used to pay the unpaid tax of the principal taxpayer. Tax evasion has on many occasions been the topic of deliberation by our courts and must be distinguished from tax avoidance⁴⁴. At its foundation tax evasion implies inherently unlawful methods to reduce or postpone a liability. Contrarily, tax avoidance implies that a taxpayer has a plan or scheme to achieve payment of a lesser amount of tax⁴⁵. It is not the aim and purpose of this research study to cover the legal principles associated with tax avoidance. s155 does advocate an element of tax evasion in the form of a deliberate decision on the part of the representative taxpayer to dispose of funds or monies in order for the principal taxpayer to evade the payment of tax. Evasion occurs when the Commissioner is not informed of all the facts relevant to an assessment of tax. Innocent evasion may lead to a reassessment. Fraudulent evasion may lead to a criminal prosecution as well as reassessment⁴⁶. It is true that tax evasion is characterised by fraud and deceit, and may also result from a *bona fide* attempt to arrange a taxpayer's tax affairs to avoid or reduce a tax liability. It is inferred from the latter that although such rearrangement may be *bona fide*, the avoidance may be considered to be negligent in the manner in which it proceeded to rearrange its affairs⁴⁷.

It would seem that fraud⁴⁸ and negligence⁴⁹ would be prevalent in the Commissioner's

⁴⁴ AP De Koker *et al* SILKE on Income Tax, Tax Avoidance – *Distinction between tax evasion and tax avoidance*, Ch 19.1, available at <http://www.myexisnexis.co.za> last accessed September 2015

⁴⁵ Op cit note 38

⁴⁶ *C of IR v Challenge Corp Ltd (1986) 2 NZLR 513 (PC) at 561*

⁴⁷ Op cit note 38

⁴⁸ s 155(a) op cit note 7 states that '*A representative taxpayer is personally liable for tax payable in the representative taxpayer's representative capacity, if, while it remains unpaid, the representative taxpayer alienates, charges or disposes of amounts in respect of which the tax is chargeable*' and may require the

decision to attribute a tax liability to a representative taxpayer in his personal capacity. Considerations of fraud and negligence are familiar legal principles, which the courts have deliberated upon frequently. The question, which one needs to answer, is whether the representative taxpayer attracts personal liability by means of *dolus directus* or *dolus eventualis*?

Knowing the legal consequence of *dolus directus* regarding the liability of the representative taxpayer, it is necessary for the aim and purpose of this research study to focus on *dolus eventualis*. In *S v Brown [2015] 1 All SA 452 (SCA)* the court was tasked to consider fraud conducted by an asset manager who, on behalf of investors, managed an asset whilst he had a mandate to do so. The court found that in this particular case, it was necessary to consider the principles of fraud as it relates to *dolus eventualis*. Accordingly, a person will act with an intention in the form of *dolus eventualis* if the commission of the unlawful act or the causing of the unlawful result is not his main aim, but he subjectively foresees the possibility that, in striving towards his main aim, the unlawful act may be committed or the unlawful result may be caused and he reconciles himself to this possibility.

In the case of *Commissioner for South African Revenue Service v Metlika Trading Ltd and Others 72 SATC 241* the Commissioner launched an application to the High Court where it sought an order for the lifting of the corporate veil of a transferee company or alternatively the reversal of the transfers of assets made by that company. Ledwaba, J determined that the main issue before the court was whether the transfer of assets had been effected with dishonesty or improper motive in order to frustrate SARS from collecting outstanding taxes due. Ledwaba, J found that the evidence clearly showed that the transfer of assets was aimed at stopping the Commissioner from tracing and attaching assets for tax purposes. The court was not asked by the Commissioner to consider the provisions of s155. However, having regard to the aforementioned *dicta*, it provides assistance when one considers the aim and purpose of s 155 in as much as a representative taxpayer dispose of funds or monies in

Commissioner to prove an intention to defraud. Fraud is defined by Hunt, *The South African Criminal Law and Procedure*, 2nd Edition, Volume 2 at 255 as ‘*the unlawfully making, with intent to defraud, a misrepresentation which causes actual prejudice or which is potentially prejudicial to other(s)*’

⁴⁹ s 155(b) *ibid* note 7 states that ‘*A representative taxpayer is personally liable for tax payable in the representative taxpayer’s representative capacity, if, while it remains unpaid the representative taxpayer disposes of or parts with funds or monies, 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 monies*’ and may require the Commissioner to prove negligence on the part of the representative taxpayer in not paying a tax of the principal taxpayer.

respect of which tax is chargeable and/ or if tax could legally have been paid from such funds or monies.

It becomes increasingly evident that a decision to attribute a tax liability of a principal taxpayer to the representative taxpayer is not as plain as the principal taxpayer having sufficient funds in its bank account at the time the tax liability was due⁵⁰. The Commissioner's approach must include both an objective and subjective consideration as to the merits of the case. Each case must be considered on its own merits. Objectively, the Commissioner must consider whether the conduct of the representative taxpayer constitutes an improper motive wherein it was the aim and purpose of the representative taxpayer to misrepresent the ability of the principal taxpayer's to pay its tax liability⁵¹. Subjectively, it must consider whether the conduct of the representative taxpayer was intended to frustrate the Commissioner from collecting the tax due to the State⁵². In short, one must determine whether the representative taxpayer was reckless in his conduct in managing the tax affairs of the principal taxpayer?

In the case of *S v Van Zyl*⁵³ the court had to determine the meaning of 'recklessly'. Although the facts of this case relate to the driving of a motor vehicle Steyn, J determined that to act (drive) recklessly is established by proof of conduct amounting to 'gross negligence'. Steyn, J further stated that in such instance it was not necessary to prove that a person concerned was aware of the risk and was indifferent to its possible consequences. To subjectively attribute a tax liability to a representative taxpayer requires the Commissioner to take into consideration certain analogous factors. These analogous factors are whether the principal taxpayer is continuing its trade, whether it persists in its non-compliance, the expected yield in recovery from the assets of the principal taxpayer and from the assets or estate of the representative taxpayer and the cost associated with the collection thereof.

⁵⁰ Ibid note 25 at para 14

⁵¹ *Orkin Brothers Ltd v Bell & Others 1921 TPD 92*, in *S v Van As 1976 (2) SA 921 (A)* the court held that the test for recklessness was objective in so far as the defendant's actions are measured against the standard of the notional reasonable person.

⁵² In *S v Van As* ibid note 52 the court held that the test is subjective in so far as one can postulate that the notional being as belonging to the same group or class as the defendant, moving in the same spheres and having the same knowledge or means to knowledge.

⁵³ 1969 (1) SA 553 (A), Steyn, J also referred to the English *dicta* of *Shawinigan Ltd v Vokings & Co Ltd 1961 (3) All English Law Reports 386 (QB)* wherein MGaw, J submitted that the term "recklessly" meant deliberately running an unjustifiable risk.

e) *The Effect of the Commissioner's decision*

The Commissioner has the same powers of recovery against the assets of a person who is personally liable under s 155, s 157 or this Part as the Commissioner has against the assets of the taxpayer and the person has the same rights and remedies as the taxpayer has against such powers of recovery⁵⁴. The Commissioner must provide a person with an opportunity to make representations before the person is held liable for the tax debt of the taxpayer in terms of s 155 if this will not place the collection of tax in jeopardy⁵⁵. It is noted from the *dicta* in the *Peretz* case that the Commissioner, after having failed to collect the tax liability from the principal taxpayer, wrote to the representative taxpayer informing him of his liability in terms of s 48 (6) of the VAT Act for the unpaid tax of the principal taxpayer⁵⁶. The Commissioner, despite the representative taxpayer's claim that he had not received the letter firstly caused a certified statement to be filed in the name of the representative taxpayer with the Registrar of the relevant competent court for an amount equal to the unpaid tax of the principal taxpayer⁵⁷ exactly the day after the Commissioner issued instructions to the Sheriff of the court to execute a warrant of execution for the "judgment" amount⁵⁸. From the aforementioned *dicta* it is suggested that the Commissioner may, subsequent to a decision to hold a representative taxpayer personally liable for the tax of the representative taxpayer, recover that amount from him by means of an issuing of a certified statement filed with the relevant competent court in the name of the representative taxpayer which shall have the same effect as a civil judgment⁵⁹, issuing a notice of third party appointment to the banking institution or debtors of the representative taxpayer instructing them to pay any monies it may have or hold for or on behalf of the taxpayer to the Commissioner⁶⁰, instruct the sheriff of the court to attach and sell any available assets the representative taxpayer may have in favor of the tax liability and lastly it may even petition a relevant court for an order to finally wind-up and sequestrate the personal estate of the representative taxpayer in favor of

⁵⁴ s 184(1) of Act 28 of 2011 *ibid* note 4

⁵⁵ s 184(2) of Act 28 of 2011 *ibid* note 4

⁵⁶ *Ibid* note 26 at para 12

⁵⁷ *Ibid* note 26 at para 20

⁵⁸ *Ibid* note 26 at para 21

⁵⁹ s 172 of Act 28 of 2011 *ibid* note 4

⁶⁰ s 179 of Act 28 of 2011 *ibid* note 4

the tax liability⁶¹.

It is suggested that any decision by the Commissioner wherein it would rely upon its discretion to recover a tax liability from whomever, the recovery action of the Commissioner must result in a return, which would exceed the cost of the recovery of a tax liability⁶². The right of recovery against the personal assets or estate of the representative taxpayer also possess questions regarding legitimacy thereof and whether it does not infringe upon any rights of the representative taxpayer. The first of these questions are whether or not the attribution of the tax liability is not an unlawful deprivation of property? Croome states that the various statutes under which taxes are payable constitute laws of general application applicable to all taxpayers⁶³. These laws do not discriminate unfairly on one or more grounds found in s 9 of the Constitution. Croome also relies on the *dicta* of *First National Bank of South Africa t/a Wesbank v Commissioner, South African Revenue Service and Another*⁶⁴. In this matter before the Constitutional Court Ackermann, J held that “*taxation could not amount to deprivation or expropriation*”. It must be pointed out that the taxation of a taxpayer materializes from the fact that the taxpayer is the person chargeable to tax in consequence to a duty imposed upon the taxpayer to either charge, declare, deduct and/ or withhold an amount of tax in respect of income it had derived⁶⁵, remuneration paid to an employee⁶⁶ or goods or services supplied to a vendor in the furtherance of its enterprise⁶⁷. There is no such duty upon a representative taxpayer in his representative taxpayer and it can only be suggested, in the absence of legal precedent, that any recovery action the Commissioner initiates or commences with against his property in terms of the provisions of the Tax Administration Act, may be an unlawful deprivation of his property in violation of s 25 of the Constitution.

The Second question, which arises, is whether the Commissioner may conduct an inquiry into taxpayer’s affairs without violating the taxpayer’s rights to privacy? The issue of both the principal taxpayer and representative taxpayer’s right to privacy runs parallel to the

⁶¹ s 177 of Act 28 of 2011 *ibid* note 4

⁶² See also s 200 to s205 of Act 28 of 2011 *ibid* note 4

⁶³ See reference to Croome *op cit* note 26, at 19 to 20

⁶⁴ 2001 (3) SA 310 (C), see also *Metcash Trading Ltd v Commissioner for South African Revenue Service and Another*, 2001 (1) SA 1109 (CC)

⁶⁵ s 5(1) Act 58 of 1962 (Repealed) *ibid* note 1,

⁶⁶ Para 2 to 11 of the 4th Schedule to Act 58 of 1962 (Repealed) *ibid* note 2

⁶⁷ s 7(1) Act 89 of 1991 *ibid* note 3

requirement of procedural fairness as discussed herein *supra*. In order to overcome an issue of infringement of a privacy and to comply with all of the requirements of administrative law, it is perhaps prudent to look at initiating the process of attributing a tax liability to the representative taxpayer by way of an inquiry in terms of the provisions of the Tax Administration Act. In terms of Part C of Chapter 5 to the Tax Administration Act, a senior SARS official may authorize a person to conduct an inquiry for the purposes of the administration of a tax Act after which a judge may, on application made *ex parte* and supported by information supplied under oath or solemn declaration and establishing the facts on which the application is based, grant an order in terms of which a person described would be designated to act as presiding officer⁶⁸. The most notable reported case wherein the courts dealt with an inquiry can be found in the *dicta* of the infamous case of *The Commissioner for the South African Revenue Service v D King and Others*⁶⁹ although to workings of the inquiry was not subject matter of the case. According to Croome the aim and purpose of an inquiry would be to allow the Commissioner to obtain information after it has unsuccessfully attempted and exhausted all other less invasive means to obtain the same information⁷⁰.

In terms of the Tax Administration Act a judge may grant an order authorizing an inquiry if he is satisfied that there are reasonable grounds to believe that a person has failed to comply with an obligation imposed under a tax Act or committed a tax offence; and relevant material is likely to be revealed during the inquiry which may provide proof of the failure to comply or of the commission of the offence⁷¹. However, the order the Commissioner seeks must designate a presiding officer before whom the inquiry is to be held, identify the person who's alleged non-compliance or offence is to be inquired, identify the alleged non-compliance or offence with reasonable specificity to set the scope of the inquiry; which must be provided to the presiding officer⁷². The presiding officer may, by notice in writing, require a person, whether or not chargeable to tax, to appear before the inquiry, at the time and place designated in the notice, for the purpose of being examined under oath or solemn declaration; and produce any relevant material in the custody of the person⁷³. The inquiry is in terms of

⁶⁸ s 50 of Act 28 of 2011, this section is preceded by s 74C of Act 58 of 1962 (repealed) *ibid* note 1

⁶⁹ Unreported TPD case number 4745/02

⁷⁰ Croome *op cit* note 26, at 155

⁷¹ s 51(1) of Act 28 of 2011 *ibid* note 4

⁷² s 51(2) of Act 28 of 2011 *ibid* note 4

⁷³ s 53(1) of Act 28 of 2011 *ibid* note 4

the provisions of the Tax administration Act private and confidential⁷⁴ and a person may not refuse to answer a question during an inquiry on the grounds that it may incriminate the person⁷⁵.

⁷⁴ s 56(1) of Act 28 of 2011 *ibid* note 4
⁷⁵ s 57(1) of Act 28 of 2011 *ibid* note 4



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CHAPTER III

DIRECTOR'S PERSONAL LIABILITY IN TERMS OF THE COMPANIES ACT, ACT 71 OF 2008 AND AT COMMON LAW

I. INTRODUCTION

The liability of a director finds its origins in the purpose for which a legal entity has been brought into existence. The purpose of the legal entity determines the particular duties a director would be tasked with by the board of directors, which in turn would be subject to certain objective standards set by statutory and/ or common law¹. A company as an independent legal entity has a statutory duty to timeously pay a tax assessment and/ or submit and pay tax returns within the prescribed period of time. Failure to do so will render the company civilly liable to collection action and/ or administrative penalties.

It is trite law that a legal entity is only able to comply with the statutory tax obligations as far as it has the legal capacity to do so. The company therefore appoints certain natural persons who will be responsible to act for and on its behalf to ensure that the company at all times act within the restrictions and provisions of any tax acts administered by the Commissioner. It is always the company who is accountable to the Commissioner to comply with all of the statutory obligations a tax Act may impose upon it. Conversely, it is the appointed representative who is accountable to the company to act in good faith and in the best interest of the company and who is responsible for ensuring that the company remains compliant in respect of its tax affairs. A failure by a company to remain compliant may result in that company bearing the brunt of the Commissioner's robust collections action and/or it may even face criminal investigations. If the company representative acts in breach of his given authority and has caused the company a certain amount of harm or financial loss in consequence thereto that person may be, in terms of the Companies Act, at common law or the provisions of a tax Act liable in his personal capacity for the debts of the company.

¹ Piet Delpont, *The New Companies Act Manual, Corporate Governance: Director's Rights and Duties* available at <http://www.mylexisnexis.co.za>, accessed on 10 October 2015, at para 6.1

The purpose of this research study would be to determine to what extent the SARS could manoeuvre onto the plain of attributing a tax liability of a delinquent company to a director of that company in his personal capacity within the ambit of company law, if at all.

II. GENERAL PRINCIPLES

a) *Legal Independence*

The established principle of legal independence² of a corporate entity is inescapable. It renders a corporate entity relevant and gives the existence of such entity significance too; as far as it has the legal capacity to do so, act amongst and with other personas. The independence of the corporate entity is also its greatest constraint. According to Piet Delport (Delport),³ a company cannot, despite its independence, act in its own name. To legally commit it, the natural persons duly appointed and authorised to do so must perform the company's actions on its behalf⁴. The legal independence of a corporate entity is, however, not absolute and can be ignored under certain circumstances⁵. This will be discussed in greater detail *infra*.

b) *Legal Capacity and Authority*

From the date of incorporation of a company it becomes a juristic person, which exists continuously, it has all of the legal capacity of an individual except to the extent that it is incapable of exercising such power by itself or where the Memorandum of Incorporation directs otherwise⁶. The foundational determinant in the establishment of liability of a company or director is the principle of capacity or authority. The presence or the absence of authority will ultimately determine whether a director has, in representing the company and through his actions, bound the company in its dealings with third parties⁷, in this instance the SARS. According to Delport the principles of agency is quite simple. Delport states that if a director had consent to act

² *Salomon v Salomon and Co Ltd* [1897] AC 22 (HL), s 8(2) of the Constitution of the Republic of South Africa, 1996

³ *Ibid* note 1, *Introduction and Background*, 2nd Ed, 2011, Ch 1

⁴ See note 10 *supra*, Cilliers & Benade, *Die Gevolge van afsonderlikheid in Korporatiewe Reg*, 1987, at page 8, 'Niemand is as lid bevoeg om handelinge namens die maatskappy aan te gaan nie. Alleen diegene wat ooreenkomstig die statute as verteenwoordigers van die maatskappy aangestel is, kan die maatskappy bind.'

⁵ *Ibid* note 2

⁶ s 19(1)(a) and s19(1)(b) of the *Companies Act*, Act 71 of 2008

⁷ s 20(1) *ibid* note 6

for and on behalf of the company, only the company and the third party (Commissioner) will acquire rights and obligations.

Contrarily if the director acts outside of his given authority the company is not bound by his actions. This requires the third party (Commissioner) to make certain that the director was at all times acting within his given authority⁸. A director can either be given express and/ or implied authority to act for or on behalf of the company. The difference is with express authority any action by a director is considered to be the action of the company, whereas with implied authority the action of the director is regarded to be that of his own.

Good company governance dictates that resolutions should be properly taken at general meetings or meetings of directors after due and proper deliberation. The question as to whom must register the company for tax and who shall be responsible for the management of those taxes is one, which should form part of the first board meetings subsequent to the incorporation of the company. However, in instances where this course was not strictly followed, directors were still able to bind a company⁹. In respect of tax compliance, the premise of authority lies in the statutory duty imposed upon a company to register¹⁰, submit or to declare¹¹ and pay¹² any amount of tax due to the *fiscus*¹³. Implied Authority is, however, regarded to be an act in representation not because the director acts on behalf of another but because the director acts on the company's behalf in consequence to the legal nature of their relationship. The relationship requires the director and the company to, amongst each other, confer the legal effect of the actions of the party on whose behalf the action was concluded¹⁴. The latter perfectly captures the relationship between a company, its directors and the Commissioner. The Commissioner may therefore be reasonable to assume that a director of a company has the necessary authority to act for and on behalf of that company¹⁵.

⁸ Representation, *Ibid* note 2, Ch 5, para 4.1

⁹ *De Villiers and another NNO v BOE Bank Ltd* [2004] 2 SA ALL 457 (SCA) par 52

¹⁰ s 22 of the Tax Administration Act, Act 28 of 2011, s 22 of the Income Tax Act, Act 58 of 1962 as amended, s 23 of the Value-Added Tax Act, Act 89 of 1991 as amended

¹¹ s 25 to 27 of Act 28 of 2011, s 66 of Act 58 of 1962, as amended, s 28 to s 29 of Act 89 of 1991 as amended

¹² s 162 of Act 28 of 2011, s 90 of Act 58 of 1962, as amended, s 38 of Act 89 of 1991 as amended

¹³ s 169(1) of Act 28 of 2011

¹⁴ DJ Joubert, *Die Suid Afrikaanse Verteenwoordigingsreg*, 1979 at 1

¹⁵ s 66(1) *ibid* note 6, 'The business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that this Act or the company's Memorandum of Incorporation provides otherwise.'

c) *Director's duties*

According to Henochsberg, the Companies Act places a positive obligation upon the directors or the board of directors to manage the company¹⁶. Henochsberg continues to state that the powers conferred upon a director apply from the moment the director is appointed and the appointment is in respect of the board collectively. The management powers are therefore inextricably linked to the position of a director¹⁷.

A director's duties at common law must be approached in such a manner, by having regard to the duties imposed upon him and evaluating those duties both subjectively and objectively. Subjectively, it would require a director to at all times act honestly. Objectively, his actions would be subject to far narrower guidelines than just the transparency of his integrity¹⁸. It is then so that a director must perform his duties in the best interest of the company whilst not exceeding the capacity of the company or his agency or the restrictions of an act, with the ultimate aim of achieving the benefit the company was created for¹⁹.

The duties and standards of conduct relevant to a director of a company are set out in the provisions of s 76 of the Companies Act²⁰. It is important to note that these duties do not exclude those imposed by common law and those under common law will still apply. Having regard to the fact that the statutory duties relevant to a director could be differentiated between positive and negative duties, it will be the aim of the writer to only focus on the negative duties with specific reference to reckless trading. The reason for the writer's decision is that the principles related to reckless trading under s 20(9) of the Companies Act of 2008 relate closely to the provisions of the former s424 of the Companies Act of 1973 and in particular to the provisions of s 155 of the Tax Administration Act.

¹⁶ DJ Joubert op cit note 14; Henochsberg, Commentary s 66(1), 2011, available at <http://www.mylexisnexis.co.za>, last accessed at 10 October 2015 'The significance of the power to manage to business and affairs in terms of s 66 is two-fold. In the first instance this power (and obligation) is now original and not delegated (from the shareholders through the Memorandum of Incorporation) as it was under the 1973 Act (through the articles).

¹⁷ DJ Joubert op cit note 14, Henochsberg op cit note 16

¹⁸ Ibid note 1, at para 6.2.2

¹⁹ Op cit note 2

²⁰ Ibid note 6

III. APPROACH UNDER THE COMPANIES ACT OF 1973

When it appears, whether it be in a winding-up, judicial management or otherwise, that any business of the company was or is being carried on recklessly or with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the Court may, on the application of the Master, the liquidator, the judicial manager, any creditor or member or contributory of the company, declare that any person who was knowingly a party to the carrying on of the business in the manner aforesaid, shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Court may direct²¹. According to Henochsberg²² the policy consideration for s424 was expressed in the Supreme Court of Appeal's decision of *Ebrahim and Another v Airport Cold Storage (Pty) Ltd*²³. Henochsberg provides a summary of the court's decision stating that s 424 retracts the fundamental attribute of corporate personality, namely separate legal existence, with its corollary of autonomous and independent liability for debts, when the level of mismanagement of the corporation's affairs exceeds the merely inept or incompetent and becomes heedlessly gross or dishonest. The provision in effect exacts a *quid pro quo*: for the benefit of immunity from liability for its debts, those running the corporation may not use its formal identity to incur obligations recklessly, grossly negligently or fraudulently²⁴. The legislature has therefore sought to punish directors for the deliberate and delinquent behaviour of the company and to compensate affected creditors²⁵.

A successful application does not result in the director being responsible to the company with the result that he would now be liable to pay a certain amount in favour of the body of creditors, much rather appears that a director would be liable in his own capacity to the extent that the court may declare²⁶. Henochsberg continues in relying on several cases setting out the fundamental factors of s 424. These factors are discussed in greater detail below.

²¹ s 424 ibid note 6

²² Henochsberg ibid note 16, *Liability of directors and others for fraudulent conduct of business*

²³ 2008 (6) SA 585 (SCA)

²⁴ Henochsberg op cit note 22

²⁵ *In re William C Leitch Brothers Ltd* [1932] 2 Ch 71 at 79, see *Terblanche NO v Damji* 2003 (5) SA 489 (C) at para 511 in which the Court held that '[t]he remedy created by s 424 is a punitive one and a director can attract liability for the debts of the company without proof of any causal connection between his sanctioned conduct and those debts.'

²⁶ *Ex Parte Liquidator, Vautid Wear Parts (Pty) Ltd* 2000 (3) SA 96 (W) at para 103

a) *When it appears that the business of the company is carried on recklessly/ burden of proof*

S 424 may find its application in circumstances where the business of a company was or is being carried on recklessly and/ or with the intent to defraud the company's creditors and is not limited to the company's financial affairs only²⁷. Henochsberg states that a court may, on application by any envisaged applicants, declare that the respondent is to be personally responsible, without limitation of liability, for all the liabilities of the company²⁸. A court would, however, not grant an order based solely on a *prima facie* case but would require the applicant to satisfy the burden of proof on a balance probabilities²⁹. The Supreme Court of Appeal also had held that proof of a casual link between the relevant conduct of a Respondent and the liabilities of a company in respect of which a declaration of personal liability is sought, is not required³⁰.

b) *Any business of the company*

The true application of s 424 does not distinguish between a single transaction can cause liability to be attributed to director of that company or whether it requires that the business as a whole must be conducted in a reckless or fraudulent manner³¹. Henochsberg states that for the purposes of s 424 a business is carried on even if it

²⁷ *Gordon and Rennie NNO v Standard Merchant Bank Ltd* 1984 (2) SA 519 (C) at para 528, *Body Corporate of Greenwood Scheme v 75/2 Sandown (Pty) Ltd* 1999 (3) SA 480 (W) at para 487

²⁸ *Solomon*- case op cit note 2

²⁹ *Joh-Air (Pty) Ltd v Rudman* 1980 (2) SA 420 (T) at 426–427; *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA) at 142, *Fourie v Newton* 2010 JDR 1437 (SCA) at para 45, '[i]n evaluating the conduct of directors, courts should not be astute to stigmatize decisions made by businessmen as reckless simply because perceived entrepreneurial options did not in the event pan out. What is required is not the application of the exact science of hindsight, but a value judgment bearing in mind what was known, or ought reasonably to have been known, by individual directors at the time the decisions were made. In making this value judgment, courts can usefully be guided by the opinions of businessmen who move in the world of commerce and who are called upon to make these decisions in the performance of their functions as directors of companies, and by experts who advise businessmen in the making of such decisions or who evaluate them at the time they are made'

³⁰ *Philotex* – case ibid note 29, at para 142

³¹ *Gordon and Rennie NNO v Standard Merchant Bank Ltd* 1984 (2) SA 519 (C) at para 528 'When one looks at the words of s 424(1) in their context, there is . . . no reason to interpret them in such a way as to exclude a single reckless or fraudulent transaction from the ambit of the section. The intention of the Act is plainly to render personally liable any person who is knowingly a party to the carrying on of any business of the company in a reckless or fraudulent manner . . . having regard to the purpose of the section and the evil which the Legislature sought to combat by means of the section, there is no justification for thinking that Parliament intended to exclude from liability a director who has committed a massive fraud on a single occasion but to render liable a director who has stolen small amounts of money on a few occasions. If a transaction is part of the business of the company and it is executed recklessly or with intent to defraud creditors of the company or for any fraudulent purpose, it matters not . . . that it is done once or as part of a series of acts. In either case the guilty person may be visited with personal responsibility in terms of the section'

does not involve active trading. The courts have carefully determined the meaning of “*carrying on of a business*”. It was best summarised by Goldstone JA³², determined that the carrying on of a business is always a question of commercial reality in the light of all the circumstances of the case and not merely looking at the accounts and making a mechanical comparison of assets and liabilities. Goldstone JA continues to state that such a consideration must be viewed from the perspective of someone operating in a practical business environment. This would further require a consideration of the company’s financial position in its entirety, which would include the nature, and circumstances of its activities, its assets and liabilities etc.

c) *Recklessly*

It is trite law that when adjudicating whether the conduct of a person is reckless or not, the test to be applied is objective which relies heavily on the standard of conduct of a reasonable person³³. It is important to remember the case of *S v Van AS* wherein the learned judge found that one cannot ignore that there is also a measure of subjective consideration insofar as the notional reasonable person is envisaged to be moving in the same spheres and having the same access to knowledge as the party concerned³⁴. The meaning of reckless in the context of s 424 must be distinguished from a director or person acting negligently. If any value must be given to the conduct

³² *Ex parte De Villiers & Another NNO: In re Carbon Developments (Pty) Ltd (in liquidation)*

³³ Henochsberg ibid note 16, *Liability of directors and others for fraudulent conduct of business*

³⁴ 1976 (2) SA 921 (AD) at 928, Fourie – case op cit note 29, at para 28, “[t]he test for recklessness has both objective and subjective elements. It is objective, to the extent that the defendant’s actions are measured against the standard of conduct of a notional reasonable person. Accordingly, a defendant’s honest but mistaken belief as to the prospects of payment of a claim by the company when due is not determinative of whether he was reckless; if a reasonable person or business in the same circumstances would not have held that belief, the defendant’s bona fides is irrelevant. The test is subjective, to the extent that it must be postulated that the notional person belongs to the same group or class as the defendant, moving in the same sphere and having the same knowledge or means of knowledge. In the context of s 424, the court should have regard, amongst other things, to the scope of operations of the company, the role, functions and powers of the directors, the amount of the debts, the extent of the company’s financial difficulties and the prospects, if any, of recovery. If when credit was incurred a reasonable man of business would have foreseen that there was a strong chance, falling short of a virtual certainty, that creditors would not be paid, recklessness is established”

of a director who is negligent in the performance of his duties, his negligence must at the very least equate to gross negligence for s 424 to be applied³⁵.

As indicated *supra*, a director is amongst others tasked to perform his duties in the best interest of the company whilst not exceeding the capacity of the company or his agency or the restrictions of an Act, with the ultimate aim to achieve the benefit the company was created for³⁶. It is therefore safe to conclude that in instances where a director acts in such a manner that equates to a lack of genuine concern for the company or its prosperity such action could be considered to be reckless³⁷. Most relevant to the aim and purpose of this research study would be the *dicta* of *Ozinsky NO v Lloyd*³⁸ wherein Van Deventer J determined:

‘If a company continues to carry on business and to incur debts when, in the opinion of reasonable businessmen, standing in the shoes of the directors, there would be no reasonable prospect of the creditors receiving payment when due, it will in general be a proper inference that the business is being carried on recklessly.’

The practical application of the test requires one to have regard to the scope of the operations of the company, the role, functions and powers of the directors, the amount of the debts, the extent of the company’s financial difficulties and the prospects, if any, of recovery³⁹. In carefully evaluating and considering the relevant *dicta* and legal principles cited herein, it appears that without any suspicion that a director’s conduct is not anything more than his failure to comply with the duties given to him under the Companies Act, he cannot be found to be anything but negligent⁴⁰. Conversely, if there appear to be suspicions regarding particular transactions which question the integrity of the director’s conduct and leads to

³⁵ *Philotex* – case op cit note 29, at 144, *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W), *Fourie* – case op cit note 29 ‘[a]cting ‘recklessly’ consists in ‘an entire failure to give consideration to the consequences of one’s actions, in other words, an attitude of reckless disregard of such consequences’, *Triptomania Twee (Pty) Ltd v Connolly* [2003] 1 All SA 374 (C) at para 378: ‘*Recklessness in this context is not limited to the more onerous test inherent in the concept of dolus eventualis. Gross negligence without a conscious or wilful regard for the consequences will be sufficient to bring a respondent within the scope of the section.*’

³⁶ *Solomon* – case op cit note 2

³⁷ *L&P Plant Hire BK v Bosch* 2002 (2) SA 662 (SCA) at 677

³⁸ 1992 (3) SA 396 (C), *Philotex* op cit note 29, at para 146 Howie, J stated that, although the approach postulated in the *Ozinsky* case is an evidential test and not a statement of substantive law, it accords ‘recognition to the difference between negligence, on the one hand, and recklessness, at least in the form of gross negligence, on the other.’

³⁹ *Philotex* – case op cit note 29, at para 144

⁴⁰ *Henochsberg*, *ibid* note 16, *Liability of directors and others for fraudulent conduct of business*, General

evidence that he had failed to comply with the duties given to him then it would, in applying the appropriate test, be difficult to conclude that he was not reckless.

d) *Intent to Defraud/ Fraudulent purpose*

According to Henochsberg, s 424 applies irrespective of the nature of the conduct provided that there was, or is, a carrying on of the business of the company with intent to defraud any creditor of the company or anyone else's creditor or a carrying on of the business for any fraudulent purpose, even if that purpose does not involve the defrauding of any particular creditor⁴¹. Fraudulent intention is when a company incurs debts whilst carrying on its business when at the time its directors have full knowledge that there is no reasonable prospect that the creditors of the company will ever receive payment⁴². Inversely, it has been found that there would be no intention to defraud if the directors knew that the company is unable to pay but it does not disclose this fact out of their firm believes that the possibility exists that the company may be able to trade out of such a position⁴³. The courts have, however, found that such belief must be a genuine belief that '*the clouds of prosperity will roll away and the sunshine of prosperity will shine on them again*'⁴⁴.

Similarly, an intention by the directors to give voidable or undue preference to certain creditors is not equivalent to an intention to defraud other creditors⁴⁵.

e) *Knowing Party*

Section 424 also is only applicable to a person who had personal knowledge of the facts from which the conclusion has been drawn that the business of the company was carried on recklessly and/ or with the intention to defraud creditors⁴⁶. As stated in the foregoing paragraphs a director must perform his duties in the best interest of the

⁴¹ Henochsberg op cit note 40

⁴² *Heneways Freight Services (Pty) Ltd v Grogor* 2007 (2) SA 561 (SCA) at para 4,

⁴³ *Ozinsky* op cit note 38, at 415–418, confirmed on appeal 1995 (2) SA 915 (AD) (see esp. at 918), in *Ex parte De Villiers* op cit note 32, Goldstone, J stated that '*the mere carrying on of business by directors does not constitute an implied representation to those with whom they do business that the assets of their company exceed its liabilities. The implied representation is no more than that the company will be able to pay its debts when they fall due*'

⁴⁴ *Heneways Freight Services (Pty) Ltd v Grogor* 2007 (2) SA 561 (SCA) at 569, *De Villier's case* op cit note 32, at para 504B

⁴⁵ *Simon NO v Mitsui and Co Ltd* 1997 (2) SA 475 (W) at 525 to 526

⁴⁶ Henochsberg *ibid* note 33

company whilst not exceeding the capacity of the company or his agency or the restrictions of an Act, with the ultimate aim to achieve the benefit the company was created for⁴⁷. Goldstone, J summarised the position regarding a director in the Howard case *Howard v Herrigel NO*⁴⁸ by stating,

'A director has an affirmative duty to safeguard and protect the affairs of the company. In my opinion, it follows that. . . [a director] may well be a 'party' to the reckless or fraudulent conduct of the company's business even in the absence of some positive steps by him in the carrying on of the company's business. His supine attitude may, I suppose, even amount to concurrence in that conduct. Whether such an inference could properly be drawn will depend upon the facts and circumstances of the particular case.'

In other cases, the court found that where a director did not partake or had no knowledge of the day-to-day operations of the business, the director would not be a knowing party as envisaged in s 424⁴⁹.

IV. APPROACH UNDER THE COMPANIES ACT OF 2008

If, on application by an interested person or in any proceedings in which a company is involved, a court finds that the incorporation of the company, any use of the company, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity, the court⁵⁰ may declare that the company is to be deemed not to be a juristic person in respect of any right, obligation or liability of the company or of a shareholder of the company or, in the case of a non-profit company, a member of the company, or of another person specified in the declaration⁵¹; and make any further order the court considers appropriate to give effect to a declaration⁵². It appears that the legislature has moved to codify the principles regarding the instances where a court may ignore the separate legal personality of a delinquent company.

⁴⁷ Solomon – case, op cit note 2

⁴⁸ 1991 (2) SA 660 (A) at para 674, and see *Ebrahim v Airport Cold Storage (Pty) Ltd* 2008 (6) SA 585 (SCA) at para 23–24

⁴⁹ Henochsberg ibid note 33, *Fourie v Braude* 1996 (1) SA 610 (T) at para 614

⁵⁰ s 20(9) ibid note 6

⁵¹ s 20(9)(a) ibid note 50

⁵² s 20(9)(b) ibid note 50

The courts have also considered the legal effect of the provisions of section 20(9) and have stated that although the principle of piercing is now codified within the Act, it should be seen as complementing common law principles rather than replacing it⁵³. The most relevant *dicta* regarding section 20(9) of the Companies Act is *Ex Parte Gore NO [2013] JOL 30155 (WCC)* (the Gore case) wherein the application was launched under the common law, alternatively relief was sought in terms of the provisions of section 20(9) of the Companies Act.

It is not the aim and purpose of this research study to fully dissect and give account of the principles of piercing or lifting of the corporate veil as the grounds on which the courts will pierce the corporate veil have been difficult and it had grappled with the correct approach to adopt in determining whether to pierce the corporate veil or not⁵⁴. However, the *dicta* in the aforementioned Gore case assists the writer in his examination of the relevant principles applied both internationally and locally and as far as it pertains to the common law and the provisions of section 20(9) of the Companies Act.

V. THE GORE CASE AND THE MEANING OF ‘UNCONSCIONABLE ABUSE’

The basis for the application, in this case, was the allegation that the relevant business of the group was conducted through the holding company with little or no regard to the distinction between that company’s legal personality and that of its subsidiaries. The presiding Binns-Ward, J early in his ruling considered the circumstances under which the English courts were prepared to pierce the corporate veil, although it has been a question that has been left open by the UK Supreme Court⁵⁵. In particular Binns-Ward, J has singled out and referred to the *dicta* of *Faiza Ben Hashem v Shayif and Another*⁵⁶. In this decision Munby, J set out seven principles one should consider if one opted to pierce or lift the corporate veil⁵⁷.

Without paraphrasing all seven principles, it is evident therefrom that any consideration and decision to lift or pierce the corporate veil one cannot merely disregard the

⁵³ Henochsberg, *ibid* note 33, *Validity of Company Actions; Ex parte application of Gore NO [2013] JOL 30155 (WCC)* para 34

⁵⁴ *Ex parte Gore*, *op cit* note 53, para 20 wherein judge Binns-Ward referenced Cassim et al (ed) *Contemporary Company Law*, (2ed) (Juta), 2012

⁵⁵ *Gore* case *op cit* note 53, para 22

⁵⁶ (2008) EWHC 2380 (FAM)

⁵⁷ *Faiza Ben Hashem v Shayif and Another* *op cit* note 57 at para 22 and Fn 56 at para 159-164

commercial reality a company finds itself in. This somewhat relates to the decision of *Ex parte De Villiers & Another NNO* where Goldstone JA *supra* stated that such a consideration must be viewed from the perspective of someone operating in a practical business environment. It would further require a consideration of the company's financial position in its entirety, which would include the nature and circumstances of its activities, of its activities, its assets and liabilities etc.⁵⁸. Binns-Ward, J states that the courts have shown an acute appreciation that juristic personality is a statutory creation and that the separate existence remains a figment of law, liable to be curtailed or withdrawn when the objects of their creation are abused or curtailed⁵⁹. Binns-Ward, J further states that in his view the determination to disregard the distinctness in terms of a company's separate legal personality, the court must in each case reflect a policy based decision and weigh the importance of giving effect to the legal concept of juristic personality. It must acknowledge the material; practical and legal considerations that underpin the legal fiction and it must also compare the latter to the adverse moral and economic effects of countenancing an unconscionable abuse of the concept of the founders, shareholders or controllers of the company.

In his judgment Binns-Ward, J had taken it upon himself to consider with great care the legislator's words in the term '*unconscionable abuse*'⁶⁰. According to the learned judge, the use of the term was done with the aim and purpose to create a firm but flexible basis for the remedy, which would in his view ultimately operate to erode the philosophy, that piercing or lifting of the veil should operate with a theoretical deduction rather than empirical observation. The term therefore suggests conduct in relation to the formation and use of companies diverse enough to cover all descriptive terms such as "sham", "device", "stratagem" etc.

Accordingly, the Binns-Ward decision further suggests that a remedy of piercing or lifting of the veil under section 20(9) may be initiated by an interested person⁶¹ whenever there appears to be an illegitimate use of the concept of the juristic personality which would have the effect

⁵⁸ *De Villiers* - case Op cit note 32

⁵⁹ *Gore* -case ibid note 54 at para 29

⁶⁰ *Gore* -case ibid note 54 at para 34

⁶¹ *Gore* -case ibid note 54 at 35: '*The term "interested person" is not defined. I do not think that any mystique should be attached to it. The standing of any person to seek a remedy in terms of the provision should be determined on the basis of well-established principle*', Binns-Ward, J in this regard also refers to the decision of *Jacobs en 'n ander v Waks en andere* 1992 (1) SA 521 (A) at 533J-534E, and, of course, if the facts happen to implicate a right in the Bill of Rights, section 38 of the Constitution

that a third party would be adversely affected in such a way that it should not be tolerated. The remedy under section 20(9) can therefore no longer be considered to be exceptional or drastic and is to be regarded as supplemental to the common law rather than substitutive⁶².

⁶² Op cit note 61



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CHAPTER IV

DIRECTOR PENALTY NOTICES – AN AUSTRALIAN APPROACH

I. INTRODUCTION

The principle of attributing a delinquent company's tax liability to a director of that company is a complex area of enquiry and is known in various international jurisdictions, but interestingly not applied in all. It is also true that jurisdictions differ in their respective approaches in enforcing the principle. Some revenue authorities seek strict compliance with revenue laws by either attributing such a tax liability to the director in his personal capacity, where others follow a more simplistic approach by issuing directors with a penalty notice equal to the tax liability of the delinquent company. The latter is of specific significance to the Australian approach. It appears the reason why the principle of penalizing and/or attributing a delinquent company's tax liability to a director of that company, is more often a matter of policy considerations influenced by the strength of the global economy and the impact thereof on taxpayer compliance and taxpayer morale in a particular jurisdiction at any specific time¹².

II. THE GLOBAL ECONOMY VERSUS TAXPAYER COMPLIANCE

As early as 2009 John Brondolo (Brondolo) had determined in an IMF Staff Position Note that the global financial economic crisis would present major challenges to many revenue administrations³⁴. In his note Brondolo indicates that the various forms of non-compliance give rise to tax gaps, which could possibly represent foregone government revenue. As with most revenue administrations, reducing and eliminating these gaps become vitally important during difficult economic times⁵⁶ and may require enforcement action of varying kinds.

¹ Michael Keen *et al*, *Current Challenges in Revenue Mobilization: Improving Tax Compliance*, IMF Staff Report, April 2015, at 6: “*The Extent of Compliance with the legal obligations it imposes powerfully affects the Revenue Yield, Efficiency and fairness of any tax system. Noncompliance undermines revenue, distorts competition . . . compromises equity. These effects interact. Governments anxious for revenue may concentrate their efforts on more compliant taxpayer's, amplifying distortions and perceptions.*” and at page 14, Dealing with the Compliance Challenges of the Crisis.

² *ibid* Note 1 at 7 “By compliance is meant, broadly, meeting legal obligations imposed by a tax system.”

³ John Brondolo, *Collecting Taxes During an Economic Crisis: Challenges and Policy Options*, IMF Staff Position Note, 14 July 2009, Kindle Edition, at location 64 of 842

⁴ *ibid* note 1, at 12

⁵ *ibid* note 3, at location 87 of 842

It is important to understand what considerations revenue administrations take into account in determining what contributes to an increased risk of non-compliance. Brondolo in his note identified three major risk areas⁷, first the lack of credit or financing options available to taxpayers which may contribute to taxpayers being more than tempted to use tax evasion as an alternative source of finance for their operations⁸; secondly, the taxpayers who are financially distressed may perceive the risk of tax evasion to be minimal compared to the potential of avoiding bankruptcy; and thirdly, a shift in economic activity due to an economic crisis. Brondolo continues by stating that social norms may reinforce these three conditions as taxpayers may perceive that revenue administrators are less stringent in enforcing tax laws or that other taxpayers are evading taxes more, making it less risky and more socially acceptable to evade taxes⁹.

⁶ *ibid* note 1, at 7 ‘The focus is thus on (illegal) evasion, deliberate, or from ignorance and error, rather than (legal) avoidance. But the distinction is not always clear-cut, and among the risks that RAs must manage, more for some taxpayer groups (the very wealthy, for instance) than others, are those from avoidance activities which cross some line of legal acceptability.’

⁷ *Ibid* note 3 at para 86, para 95, para 104, ‘Although some aspects of taxpayer compliance may actually improve during an economic downturn, there is good reason to believe . . . that compliance will worsen in important respects’

⁸ *Ibid* note 1 at 12, Compliance appears to have worsened sharply as a consequence of the 2009-09 crisis, though experiences varied widely, ‘This is one might expect: Cash strapped firms may well find delaying or omitting payment of their liabilities to be a relatively cheap source of finance.’

⁹ *Ibid* note 1, at 16, *Calculus of Voluntary Compliance*, The standard framework for thinking about noncompliance stresses deterrence as the central way to improve it.

III. A DIRECTOR'S LIABILITY FOR CORPORATE FAULTS AND DEFAULTS - AN AUSTRALIAN APPROACH

a) *Background*

According to Karen Wheelwright¹⁰ (Wheelwright), the issue of director's personal liability for corporate fault in Australia is a complex area of inquiry. She highlights that the liability of directors arises principally under the legislation, which is wide-ranging and resembles a diversity of approaches to determine liability¹¹. Wheelwright affirms that the High Court of Australia has endorsed the established legal principle in *Salomon v Salomon*¹² wherein the Honourable Court found that upon registration a company is a legal entity that is separate from its shareholders and managers. Australian law (as in South African law) has adopted from and developed by English law the legal rules for attributing the acts of humans to a company¹³. Wheelwright states that in consequence directors can bind a company as a primary organ when they act collectively as a board.

Following Wheelwright *supra*, Dr Helen Anderson¹⁴ (Anderson) wrote an article¹⁵ in 2009 wherein she explained the different approaches followed by several jurisdictions dealing with corporate fault and default in comparison to Australia. Anderson affirmed Wheelwright's assertions that director's liability is a contentious issue. In Anderson's article¹⁶ she indicates that when money is in short supply, a company can be tempted to treat tax instalments as working capital to finance its operations rather than remitting them as required. Anderson's remarks appear to correspond with the major risk areas identified by Brondolo *supra*¹⁷. Anderson continues to state that in such instances if a company is unable to trade out of financial difficulties and becomes insolvent, the loss either falls to the employee or to the revenue authority. She further states that, in order to deter such behaviour, Australia had in

¹⁰ Professor, Faculty of Law, Monash University, Australia

¹¹ Helen Anderson, *Director's Personal Liability for Corporate Fault: A Comparative Analysis*, (2008), Chapter 2, at 45

¹² *Salomon v Salomon & Co* (1987) AC 22

¹³ *Ibid* note 11 at 48

¹⁴ Associate Professor and Head of Department of Business Law and Taxation, Monash University, Australia

¹⁵ Dr. Helen Anderson, *Director's Liability for Corporate Faults and Defaults – An International Comparison*, Vol 18, (2009)

¹⁶ *ibid* note 15, At 11, Part B, *Similarities in Unremitted Employee Tax Installment Laws Across Selected Jurisdictions*

¹⁷ *Op cit* note 7

1993 enacted legislation whereby it could impose harsh liabilities on directors for unremitted tax instalments¹⁸. Australian company directors are, since the enactment of the legislation, potentially liable for unremitted tax instalments, which they deduct from their worker's salaries in the event that the company does not pay the tax in a timely manner¹⁹.

b) *Australian Policy Consideration*

According to the Law Society of New South Wales, the Australian policy behind the director penalty provisions²⁰ is explained within paragraph 2.12 of the Explanatory Memorandum to the Tax Laws Amendment Bill 2010 (Austl)²¹, which is paraphrased below:

Paragraph 2.12

'Sections 9 and 10 of Part IV of the ITAA 1936 introduced a new regime in 1993 to enable the Commissioner to recover certain tax debts earlier and more effectively. The new regime imposes a duty on directors to cause the company to forward amounts withheld from payments to employees and some other creditors to the Commissioner. The duty is enforced by penalties equal to unpaid amounts. The penalty is automatically remitted if the company meets its obligations, or promptly goes into voluntary administration or liquidation.'

The penalty regime reflects the public duty on directors to ensure that amounts withheld from payments to third parties are promptly forwarded to the Commissioner. The public duty arises because withheld amounts are similar in nature to amounts held on trust. That is, the directors are in a position of trust and have a duty to protect those monies until they have been forwarded to the Commissioner.'

¹⁸ Jane Trethewey, *Changes to Directors Penalty Regime*, 2012, 'On 29 June 2012, legislation amending the directors' penalty provisions in Section 269 of Schedule 1 to the Taxation Administration Act 1997 (Cth) (TAA) and associated measures was enacted'

¹⁹ s 222AOB to s 222AQD of *Income Tax Assessment Act*, 1936(Austl)

²⁰ Denis Barlin and Michael Bennett, *The Tax Perspective*, in Young Lawyers The Law Society of New South Wales, *Director's Duties*, 2011; The directors penalty regime contained in Part IV of s 9 of the 1936 Act (containing sections 222ANA to 222AQD) was replaced as from 1 July 2010 by Section 1 of Schedule 1 to the Taxation Administration Act 1953 (Cth) (containing s 269-1 to 269-55). This was inserted by Tax Laws Amendment (Transfer of Provisions) Bill 2010 (Cth)

²¹ Explanatory Memorandum to the Tax Laws Amendment Bill 2010 (Austl)

IV. AUSTRALIAN TAX POSITION – S 269 OF THE TAXATION ADMINISTRATION ACT, 1953

The Australian Taxation Office (ATO) expects taxpayers to pay their tax-related liabilities as and when they fall due for payment. If a tax-related liability remains unpaid after its due date, the ATO's assumes responsibility to initiate the most appropriate action to collect that debt as soon as practicably possible²² The enabling provisions, which allows the ATO to enforce Director Penalty Notices (the notices), can be found in the provisions of s 269A to s 269D as set out in Chapter 4 of Schedule 1 of the Taxation Administrative Act, 1953 (TA Act, Austl).

a) *Purpose*²³

The Australian legislature indicates²⁴ in a historical note to s 269, that the purpose of this particular section is to enforce, by way of penalties²⁵, a director's duty²⁶ to ensure that a company either meets its obligations under ss 16-B and s 268 in Schedule 1 to the TA Act (Austl) and Part 3 of the Superannuation Guarantee Administration Act 1992; or to ensure that it goes promptly into voluntary administration in terms of the provisions of the Corporations Act, 2001 or into liquidation. Keeping in mind that the ATO commits itself, as a matter of course, to take into account the individual circumstances of each tax debtor to ensure that any recovery strategy is effective and appropriate for collecting that particular tax-related liability²⁷. The Australian legislature continues in its statement that the section applies in relation to an amount a company purports to withhold under s 12, but is not required to withhold, as if the company were required to withhold the amount²⁸.

Further, that for the purpose of this section the company's superannuation guarantee charge for a quarter under the Superannuation Guarantee Act, 1992 is treated as being payable on the

²² Practice Statement Law Administration, PS LA 2011/18, *Enforcement measures used for the collection and recovery of tax-related liabilities and other amounts*, (2011) Annexure B, at 1

²³ *ibid* note 22, 'The recovery of personal liabilities that company directors may incur in relation to their company's liabilities for PAYG withholding (or another remittance provision) or SGC disclosures to other parties when dealing with parallel liabilities'.

²⁴ Guide to s 269 available at <https://www.law.ato.gov.au>, last accessed on 3 November 2015

²⁵ See Fn 18 *supra*, s 269-5 *op cit* note 19, *History Note*, a penalty recovered under the Section is applied towards meeting the Company's obligation.

²⁶ ss 252(1) of the *Income Tax Assessment Act 1936*

²⁷ *Ibid* note 22

²⁸ s 269-10(2) *op cit* note 19

day by which the company must lodge a superannuation guarantee statement for the quarter under s 33 of that Act, even if the charge is not assessed under that Act on or before that day²⁹. s 269-10(1) of the TA Act, 1953 provides a table setting out the circumstances under which this particular section would apply:

Table 3.1 – Table setting out the scope of s269³⁰

The Obligations that directors must cause the company to comply with		
Item	Column 1	Column 2
	This Section Applies if, on a particular day, a company is a company registered under the Corporations Act, 2001, and on the initial day	And the company is obligated to pay to the Commissioner on or before a particular day
1	The company withholds an amount under Section 12	That amount in accordance with Subsection 16-B
2	The company receives an alienated personal services payment	An amount in respect of that benefit in accordance with Section 13 and Subsection 16-B
3	The company provides a non-cash benefit	An amount in respect of that benefit in accordance with Subsection 16-B
4	The company is given notice of an estimate under Section 268	The Amount of the estimate
5	The quarter ends	Superannuation guarantee charge for the quarter with Superannuation Guarantee Act 1992

V. THE FOUR COMPONENTS OF DIRECTORS LIABILITY

In reading s 269 of the TA Act, 1953 one would find that it presupposes five (5) components, a mixture between substance and form, to be present and which are relevant to give legal effect to a Director Penalty Notice issued to a director. These five (5) components are identified as: the director's obligations³¹, the penalty³², the notice issued to directors³³; the effect of the penalty³⁴ and the defences directors may come to rely on³⁵.

²⁹ s 269-10(1) *op cit* note 19

³⁰ s 269-10(1) *op cit* note 19

³¹ s 269-15 *op cit* note 19

³² s 269-20 *op cit* note 19

³³ s 269-25 *op cit* note 19

³⁴ s 269-30 *op cit* note 19

³⁵ s 269-35 *op cit* note 19

These four (4) components will be discussed in greater detail *infra*.

a) *Director's obligations*

The director's obligations are generally defined in the TA Act, 1953 and are extended by those obligations imposed by the Corporations Act³⁶.

b) *The Notice*

The Commissioner is obligated by law to give notice of a penalty to a director of a delinquent company. The Commissioner is prohibited from commencing with proceedings to recover from a director a penalty payable under the ss269-25(1) until the expiry of 21 (twenty-one) days after the Commissioner gives a director written notice under this section³⁷. The Notice issued to a director must set out the following information; what the Commissioner thinks is the unpaid amount of the company's liability under its obligation; and it must state that the director is liable to pay to the Commissioner, by way of penalty, an amount equal to that unpaid amount because of an obligation you have or had under this section and it must explain the main circumstances in which the penalty will be remitted.

c) *The Penalty*

A director of a delinquent company may be liable to pay a penalty³⁸ if, at the end of the due day, the director of the company is still under an obligation under s 269-15³⁹; and if the director was under that obligation at or before that time⁴⁰. A director will

³⁶ s 269-15(1) *op cit* note 19, 'The directors of the company (from time to time) on or after the initial day must cause the company to comply with its obligations', *The Corporations Act, 2001*; *ibid* note 11, at 47, 'The Act places significant statutory duties on directors. These duties supplement director's fiduciary obligations.' and at page 48, 'Director's actions may also bind the company under other principles of attribution . . . the directors may be regarded as the directing mind and will of the company so that their acts and intentions are regarded in law as acts and intentions of the company itself.'

³⁷ s 269-25(1) *op cit* note 19; *Deputy Commissioner of Taxation v Meredith [2007] NSWCA 354* – 'by letter dated 27 July 2004, the Commissioner of Taxation gave notice to the Opponent of her liability and the available options to discharge the liability. The Opponent said that she had not received the notice, that if it had been delivered she would have received it, and that therefore it had not been delivered. If it had not been delivered, she was not liable. On 27 October 2006, Quirk DCJ found on the balance of probabilities that the penalty notice had not been delivered and dismissed the Commissioner's claim for an amount of \$67,576.'; *Deputy Commissioner of Taxation v Gruber Matter No Ca 40766/97 [1998] NSWSC 64* (24 March 1998)

³⁸ s 269-20(1) *op cit* note 19

³⁹ s 269-20(1)(a) *op cit* note 19

⁴⁰ s 269-20(1)(b) *op cit* note 19, According to the note published by the ATO, paragraph (1)(b) applies even if a person stopped being a director before the end of the due day, See s 269-15(2) *op cit* note 19

also be liable to pay a penalty if⁴¹, after the due day, a person became a director of the company and came to be under the obligation under s269-15⁴²; and if the director is, after 30 (thirty) days, still under that obligation⁴³. The amount of the penalty under this section is equal to the unpaid amount of the delinquent company's liability under the obligation⁴⁴.

- d) The Effect of the penalty of the Director's obligation ending before the end of the Notice period.

Subject to ss 2, a penalty of a director under this section is remitted if the directors of the company stop being under the relevant obligation under s 269-15 before the Commissioner issued that director with a notice of penalty under s 269-25 or within 21 (twenty-one) days after the Commissioner gives the director notice of the penalty under the same section⁴⁵.

VI. DEFENSES⁴⁶

A director is not liable to pay a penalty under the section if he is able to successfully rely on one of the following defences:

- a) *Illness*⁴⁷

A director would ordinarily not be liable to pay a penalty if because of an illness or for some good reason it would have been unreasonable to expect the director to take part, if he did not take part in the management of the company at a time when the person was a director of the company and the directors of the company was under an obligation under s 269-15(1) of the TA Act, 1953 (Austl).

- b) *All reasonable steps were taken*⁴⁸

A director is not liable for a penalty if he took all reasonable steps⁴⁹ to ensure that the directors caused the company to comply with its obligations, or the directors caused an

⁴¹ s 269-20(3) *op cit* note 19

⁴² s 269-20(3)(a) *op cit* note 19

⁴³ s 269-20(3)(b) *op cit* note 19

⁴⁴ s 269-20(5) *op cit* note 19

⁴⁵ s 269-30(1) *op cit* note 19

⁴⁶ *Op cit* note 22, Annexure B, *Statutory Defenses*, at para 54

⁴⁷ s 269-35(1) *op cit* note 19

⁴⁸ s 269-35(2) *op cit* note 19

administrator of the company to be appointed under s 436A, s436B or s436C of the Corporations Act, 2001; or the directors caused the company to begin to be wound up within the meaning of the Corporations Act; or there were no reasonable steps a director could have taken to ensure that anyone of those things happened.

c) *Superannuation guarantee charge – reasonable arguable position*⁵⁰.

A director will not be liable to a penalty under s 269 to the extent that the penalty resulted from the company treating the Superannuation Guarantee Act 1992 as applying to a matter or identical matters in a particular way that was reasonably arguable, if the company took reasonable care in connection with applying that Act to the matter or matters.

VII. CONCLUSION

In evaluating the Australian approach, it appears that the enabling provisions require the ATO to satisfy two fundamental requirements. The two requirements are procedural and substantive correctness. These two requirements become more exposed when one examines s269 of the TA Act, 1953 more closely.

⁴⁹ s 269-35(3) *op cit* note 19, This section deals with what is considered to be reasonable steps. It states that for the purpose of this subsection the ATO must have regard to when and for how long the person was a director and for how long did he took part in the management of the company, and all other circumstances.

⁵⁰ s 269-35(3) *op cit* note 19



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CHAPTER V

A COMPARATIVE ANALYSIS

I. INTRODUCTION

In the preceding Chapters, the relevant principles to the South African Tax, Company and International law has been set out and discussed as far as it related to the existence, function and duties of a Company as a separate legal entity *viz-a-vis* the duties and obligations of a director as the delegated appointed representative of a company. However, to fully understand the aim and purpose of this research study it is necessary to compare and analyse the applicable principles of each field of law against that of the other. It will become apparent from this analysis that the argument in each is based upon similar legal principles but as a result of differing jurisdictions, interpretation by the courts or the lack thereof the application differs in practical application.

II. FRAME OF REFERENCE

In considering the aim and purpose of this research study it is necessary to identify the legal standard for the study. The *dicta* of *Salomon v Salomon & Co Ltd*¹ is considered to be the universally accepted legal precedent when determining issues regarding the legal independence of a company. The House of Lords has determined to be set as follow:

‘It seems to me impossible to dispute that once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are’.

It will be observed that in each of the legal jurisdictions and/ or genres of law the consequence of legal independence of a company creates certain statutory duties or obligations at common law, which the directors of that company must adhere to when acting for and on behalf of that company. The responsibility given to the directors can be measured and scrutinised depending upon the particular circumstances at that time and if it is

¹ *Salomon v Salomon & Co* (1987) AC 22

determined that the director has acted *contra* his duties he may find himself accountable to the company or creditors of that company depending upon his intent. The consequence of his actions may vary in that his to be unduly liable or he may even attract liability in his personal capacity. It will further be observed that in each of the legal jurisdictions and/ or genres of law scrutiny of director's actions commences in differing ways. The effect of the manner in which it is done may perhaps bring scrutiny upon the legality of the process. Whether it will pass such scrutiny would ultimately depend upon how the affected person would react to such proceedings and whether he would require the court to intervene on his behalf.

III. GROUNDS OF COMPARISON

a) *International ratio iuris – An Australian perspective*

Very few revenue authorities escape the burdens of a struggling economy or the effects of a recession. A global downturns of the economy place an immeasurable strain on a revenue authority to collect tax from its taxpayer base who themselves feels the strain of a downturn in economic activity. Such a strain may prompt a taxpayer to seek ways in which it could either pay a lesser amount of tax or avoid paying it altogether. If this is the case a revenue authority must then be prepared and have the necessary mechanisms at its disposal to protect its taxpayer base and sources of revenue without creating a bigger tax gap.

The Australian revenue authority, the ATO and the laws that govern its functions are comparable to that of its South African Counter Part. It too has a Tax Administration Act, which has passed scrutiny over time and has been amended accordingly. From reading the Australian tax administration act it is apparent that the ATO is primarily focused on early intervention. The ATO is of the view that by engaging with its taxpayer's early it could help the taxpayers to manage their obligations and prevent their tax debt from escalating. Yet if a taxpayer chooses not to engage with the ATO it is prepared to use stronger measures to ensure a level playing field for all taxpayers and reinforces community confidence in the Australian tax system. According to the ATO their approach is sufficiently robust that it would withstand economic lows and highs². The ATO's approach for corporate faults and/ or

²'Our Approach to collecting debt' available at <https://www.ato.gov.au> accessed on 3 Nov 2015

defaults is to enforce, by way of penalties³, the duty of a director⁴ to ensure that a company either meets its obligations under ss 16-B⁵ and s 268 in Schedule 1 to the Tax Administration Act (*Austl*) and Part 3 of the Superannuation Guarantee Administration Act 1992⁶; or goes promptly into voluntary administration under the Corporations Act 2001 or into liquidation. The Australian approach does not require a formal process of lengthy legal proceedings which is subject to evidence gathering or a strict burden of proof, but it is rather based upon a prima facie case of non-compliance whereby the delinquent taxpayer (principle) taxpayer is notified of its non-compliance and given an opportunity to remedy that non-compliance. The accountability to remedy the non-compliance however vests with the director as the representative of the taxpayer to ensure its compliance with the appropriate tax obligations. If the non-compliance is not remedied and the director fails to show good cause for such failure, he would suffer an imposition of a penalty equal to the amount of the tax liability incurred as a result of the non-compliance of the company. It appears that the Australian approach is directed to being punitive and precautionary rather than reactionary.

b) *South African Company ratio iuris*

The South African company law has been the subject matter of deliberation within the South African courts for many years and the courts (and any institution administering the Act) have been duty bound to promote the spirit, purpose and objects of the applicable Company Acts⁷. The case of Salomon⁸, as within the Australian narrative, is the central theme in South African Company law. The significance of company law lies in two specific characteristics, the first being the true purpose for which the company was created for and the second the relationship created between the director and the company it represents. The relationship between the director and the company imposes certain duties upon the director to act in such a way that the company achieves the objectives it was created for.

³ note 18 supra, s 269-5 of the Tax Administration Act, 1953 (Austl), History Note ‘a penalty recovered under the Section is applied towards meeting the Company’s obligation’.

⁴ ss 252(1) of the Income Tax Assessment Act 1936 (Austl)

⁵ The obligation to pay withheld amounts to the Commissioner

⁶ The obligation to pay superannuation guarantee charge

⁷ Piet Delpont *et al*, *The Purpose of the Companies Act*, Chapter 1, *The New Companies Act Manual*, 2 ed, 2011

⁸ *Op cit* Note 1

In the end it must be evident that a company carries on a business as a principal. The company can never be an agent of its directors. If this is the case then a director's liability emanate from the very purpose for which the company was created for⁹. One simply cannot assume the true intentions of a director by a mere superficial observance of the facts as they plainly appear. The development of legislation within the ambits of Company law has created three circumstances through which a director may attract liability in his personal capacity. The first circumstance is when it appears that any business of the company was or is being carried on recklessly or with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose¹⁰, the second being where the incorporation of the company, any use of the company as an entity, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity¹¹ and thirdly a director will attract liability at common law where he had failed to act with appropriate bona fides, honestly and in the best interest of the company.

In each of these circumstances it is required of an affected or interested person to, upon application to the relevant competent court, prove on a balance of probabilities that the conduct of the director was either fraudulent, reckless or constituted an unconscionable abuse of the juristic personality of the corporate entity. By ventilating these matters before a competent court requires a consideration of fact with the intent of an empirical observation and not with a theoretical idealistic approach of what the application of the law should be. A further benefit lies therein that in an examination by the courts, the court has the luxury to rely upon a plethora of legal precedent and established legal principles that could guide the court in making a decision that would not only be just but would also aim to promote the spirit, purpose and objects of the applicable Company Acts¹².

c) *South African Tax ratio iuris*

The South Africa tax position differs not much from the position under the South African Company law. A principal taxpayer would be unable to fulfil its statutory obligations in respect of a tax Act without a duly authorised and delegated

⁹ ibid note 1 at 323, 337–340

¹⁰ s 424 of Act 69 of 1973

¹¹ s 20(9) of Act 71 of 2008

¹² The New Companies Act Manual, Piet Delpont *et al*, Chapter 1, The Purpose of the Companies Act, 2nd Edition, 2011

representative taxpayer¹³ to act for and on its behalf. This, however, does not result in the principal taxpayer being relieved from any liability, responsibility or duty imposed under a tax Act.

In terms of South African Tax legislation, one must distinguish between the liability and personal liability of a representative taxpayer¹⁴. The purpose of the distinction is that the manner in which he attracts liability and the effect of the liability his liability differs. If it is determined that a representative taxpayer is liable for the tax of a taxpayer, the representative taxpayer would only be liable to such an extent in his representative capacity. Therefore, he would only be liable to pay the liability with such funds or monies of the taxpayer which he may have in his possession or which is under his control, and which could be used to pay the tax liability. Contrarily, if it is determined that the representative taxpayer is personally liable for the tax liability of the taxpayer then that amount may be recovered by the Commissioner from his personal estate.

It appears that a decision whether a representative taxpayer is either liable or personal liability appears to not at all be dependent upon the Commissioner making formal application to a court for an order declaring the representative either liable or personally liable. The consideration of a representative taxpayer's liability and/ or personal liability merely requires the Commissioner to make a determination based upon certain facts, (i.e. a disposal of funds/ monies to which either tax was chargeable or funds/ monies which could have been used to pay the tax), at its disposal where after it notifies the representative taxpayer by notice of its alleged liability or personal liability and inviting a reply to negate any allegation of liability. The effect of the Commissioner's unilateral decision to attribute a tax liability to the representative taxpayer in his personal capacity results in the Commissioner assuming the powers of the courts and it allows itself to have the same powers of recovery against the assets of the representative taxpayer as against the assets of the principal taxpayer¹⁵.

¹³ s 154(1) of the Tax Administration Act, Act 28 of 2011

¹⁴ s 154 and s 155 op cit note 13

¹⁵ s 184 op cit note 13

IV. THEORY

In the careful evaluation of the position as it relates to the International, South African Company law and tax law it becomes apparent that there are certain aspects that are substantively and procedurally similar and dissimilar. The similarities and dissimilarities are set out in the tables below:

a) *Substantive similarities and dissimilarities*

The substantive principles emphasise the relationship between the company as the principal and the director as its representative or agent. The representative taxpayer's failure to act in a manner that would be in the best interest of the principal may possibly be underpinned by the principles of negligence, fraud or reckless on the part of that principal. The similarities are found in the company, an independent legal person and as the principal, always remain the debtor who has incurred and who remains liable for the tax liability. The liability in most instances has been incurred as a failure to pay tax as a consequence of the conduct of a person. The conduct of the person who is responsible for the failure to pay tax is subject to various legal tests all intended to determine whether there was any fraud, negligence or intent to postpone or evade the payment of tax.

b) *Substantive Similarities*

	International Ratio Iuris	South African Company Ratio iuris	South African Tax Ratio Iuris
Principal debtor	The Company	The Company	The Company
Basis	Legal Independence of a Company, Salomon v Salomon, Developed from English Law	Legal Independence of a Company, Salomon v Salomon, Developed from English Law	
Causa	Failure to pay tax	Failure to Act	Failure to pay tax
Requirements	Liability to pay tax arises <i>ex lege</i> , failure or omitting of paying tax timeously	Fraud, recklessness, abuse of the company	Unpaid tax, disposal of money, intent to postpone or evade the payment of tax
Other	None	Section 20(9) of Companies Act, 2008 codification of piercing of the corporate veil	

c) *Substantive Dissimilarities*

The dissimilarities are dependent on legislation, legal precedent or policy considerations in different jurisdictions. In some instances, a revenue authority may only pursue a penalty of equal value against the defaulting party, in others the full debt is recoverable from the representative. Even the manner in which legal action is initiated or commenced with differs. In some instances, a mere notice or penalty would suffice, in others due to the complexity of the facts it would require a creditor to make application to a court to obtain an order for the specific relief it seeks to remedy the default, loss and or damages suffered. In some instances, the representative is entitled to certain defenses where as in other circumstances no defenses exist.

	International <i>Ratio Iuris</i>	South African Company <i>Ratio iuris</i>	South African Tax <i>Ratio Iuris</i>
Director is liable for?	To a penalty equal to the amount of tax not paid, the company remains liable for the unpaid tax	The debts of the company	Unpaid tax of the company
Distinguishing factors	None	None	Liability and personal liability of a director
Components	1. Director's obligations 2. A Notice 3. A Penalty 4. Effect of the Penalty before the end of the notice period	1. When it appears 2. Any business of the company 3. Recklessly 4. Intent to defraud 5. Knowing Party 6. Unconscionable abuse 7. Gross dishonesty	1. Disposal of monies chargeable to tax or monies which could have been used to pay tax 2. Intent to postpone or evade payment of tax
Defenses	1. Illness 2. All reasonable steps taken 3. Reasonable arguable position present	Estoppel, <i>Turqand</i> Rule	None
Other	None	May recover the unpaid tax from director's personal estate	May recover the unpaid tax from director's personal estate

d) *Procedural Similarities and dissimilarities*

The procedural principle distinguishes between two types of processes in pursuing the representative for the debts of the principal; those are the formal and rudimentary

approach. The rudimentary approach originates from the position of a single major creditor, being the revenue authority, which notifies the representative of a principal delinquent company of non-compliance with a statutory duty prior to attributing the liability to that representative. Whereas in the formal approach the proceedings commence by way of an application to a court by any affected person or interested party in consequence to a failure to act. The rudimentary approach however is subjective and may be subject to manipulation and without any measure of control or oversight may be completely biased towards the representative taxpayer. Below are two tables indicating the similarities and dissimilarities in each approach.

It is noted that the issuance of a notice in the commencement of such proceedings is a procedural similarity, which is a common feature in the genre of tax law. The notice is issued by the same party who will decide the merits of the must set out the reasons for the step provide the recipient thereof with an opportunity to refute any allegations contained therein or to remedy any non-compliance on the part of the principal or company. Interestingly the complainant or issuer of the notice is also the adjudicator of the recipient's reply, which may place a question mark on the impartiality thereof.

e) *Procedural Similarities*

	International Ratio Iuris	South African Company Ratio iuris	South African Tax Ratio Iuris
Proceedings	Issuing of a notice		Issuing of Notice of Assessment or Personal Liability
Party initiating proceedings	Australian Tax Office		Commissioner for the South African Revenue Service

The formal approach differs from the latter in its entirety. Within the South African company law, an interested or affected party must approach a court by presenting its case under the notice of motion. The complaint must contain factual assertions based upon adequate evidence which may be refuted by the defendant by cross-examination or rebutting evidence of his/ her own. The court will then decide based on the evidence led before it and whether the complainant has satisfied the burden of proof that he has succeeded or not. In such proceedings, it is much less likely that an impartial or bias decision will be made which could impact upon the rights and legitimate expectations of the defendant.

f) *Procedural Dissimilarities*

	International <i>Iuris</i>	Ratio	South African Company <i>Ratio iuris</i>	South African Tax <i>Ratio Iuris</i>
Proceedings			Application under Notice of Motion to a competent court	
Party initiating proceedings			Sec 424 – Master, Liquidator, Judicial Manager, Creditor or member Sec 20(9) – Any interested person	

V. THE CAUSAL NEXUS

Each approach as discussed in this research study finds its origins within the principle of legal independence of a corporate entity. A corporate entity exists for a specific purpose and due to its nature requires a person to act on its behalf to achieve a specific purpose, whether that is to provide goods or services or to adhere to certain obligations it has with creditors and its employees.

It is only when persons, who act for and on behalf of that corporate entity, uses the corporate entity for a purpose other than what it was created for, that the legal independence of the entity has been breached. In such an instance there was a willful and deliberate act by that person, contrary to the duties imposed upon him, whereby he has misrepresented facts or failed to act in the best interest of the corporate entity for whatever reason, which was to the detriment of the entity or those who have an interest in the entity. It is only then when the conduct of those persons becomes the subject matter of a plaintiff's complaint which must undergo the rigours of scrutiny by those who have authority to do so.

Having compared the different fields of law, jurisdictions and approaches with one another, it becomes apparent that the issue of a directors' personal liability for the debts of the company he/ she represents that there is no clear cut way to deal with the issue. The differences between these allow for an opportunity to evaluate the effectiveness of the current approach and in what manner it could either be done away with or improved. The issue of personal liability is set to take a far more prominent role in revenue administration subsequent to the publishing of the recent Panama Papers. It is anticipated that revenue

authorities would seek more collaboration between one another to mitigate the outflow of any desperately needed revenue and to close the tax gap as a result of such outflows.

CHAPTER VI

CONCLUSION

The collection of tax is probably the most perilous function tax administrators in any bureaucracy. A revenue authority must instil confidence in an economy but also make every effort to collect as much tax as possible from its taxpayer base. It is a precarious position for any corporate entity. The corporate entity is obligated to charge, deduct, declare and/ or pays certain amounts of tax for or on behalf of the state to the tax administrator. Depending upon the accounting system of the corporate entity the administration of its tax obligations may consume substantial amounts of its cash flow and as a result, the duty to pay taxes remains an ever-present risk to any profit a corporate entity is to make. In some ways, the revenue authority becomes the unwanted shareholder of that corporate entity.

From the inception of the imposition of tax and the consequential collection of tax, taxpayers have sought ways to pay less tax or to avoid paying it all together. Contrarily revenue authorities had to keep up and are required to evolve with the efforts of the taxpayer base. In many ways, a tax administrator has assumed the role of gatekeeper who has mutated into a type of super creditor who has in more ways than one become consumed with exposing and eliminating tax gaps to expand its taxpayer base or sources it could collect tax from. The recent frenzy surrounding the publication of the Panama Papers is sufficient proof that governments and tax administrators alike are desperate to close any possible tax gap it can find in order to increase the amount of tax it could collect.

The Australian Tax Office appears to follow a more pragmatic approach. It has created a Director Penalty Notice issued at the instance of unpaid tax liability. The ATO's enforcement of the Director Penalty Notice achieves more than one goal. First, it reminds a responsible representative of a default of the defaulting taxpayer. Giving the defaulting taxpayer an opportunity to remedy the non-compliance within a specified period of time. The risk to the *fiscus* is abated in that the defaulting taxpayer would immediately comply and pay the amount of tax due or the ATO would collect, as a penalty, a similar amount from the director. The Director Penalty Notice therefore serves also to be punitive measure in nature in that it punishes a director, responsible to act for and on behalf of a defaulting taxpayer, for its failure to act in accordance with its duties. Lastly, it also seeks to deter future behaviour. The Director Penalty Notice is a cost effective measure, which does not duplicate a tax, nor does

it overburden an already effective administration of a tax system, as it is easily enforceable. The non-compliance event is sufficient proof to trigger the issuance of a director penalty notice to the director compelling it to ensure that the defaulting taxpayer complies with its statutory duties. Despite the subjectivity of this enforcement action it also provides the director with an opportunity to provide a defence to refute any allegation of liability. The proactive nature of the Director Penalty Notice is a feature that any administration especially the Commissioner must take note of.

It is true that not all cases may require such a pragmatic approach. In some instances, the facts are more complex and require a more delicate and comprehensive approach. The intricacy of the facts, which relates to a default of payment or an obligation, may in many instances be underlined by the interpretation and application of a particular provision of a document or legislation or it may even be influenced by the intent of those involved or even circumstances the parties find themselves in. Dissecting these facts and understanding the true legal consequence thereof requires a court, not a tax administrator task with the duty to enforce compliance, to distinguish fact from fiction and to determine the appropriate recourse. The courts provide parties with the opportunity to ventilate their position in accordance with the well-known principle of *audi alteram partem* rule. Although each case must be decided upon its own merit a court has the benefit of legal precedent upon which it could rely in guiding it to make a decision and therefore contributing to the development of *jurisprudence*.

There is no caveat against the Commissioner to use the courts in instances where a taxpayer defaults to pay tax or to, under the notice of motion makes application to a competent court commencing with proceedings to pursue directors of a delinquent corporate entity who had failed to pay any amount of tax. In fact, it is evident that the Commissioner is not indifferent to such proceedings as it makes use of the courts to issue with the clerk or the registrar of that court a certified statement in the name of the taxpayer who has failed to pay a tax. It also makes use of the officers of the same courts to execute warrants of execution and it also calls upon the courts to either liquidate or sequester an estate of a delinquent taxpayer. The only constraint is that, where the Commissioner already deals with a debtor who struggles to keep its commitments, it becomes a difficult decision to commence with lengthy and expensive litigation to pursue a representative taxpayer for the same amount of tax and who in all probability would have insufficient resources to pay such tax or would

make every effort to oppose such motion. The position becomes more troubling as the length of time to collect the tax liability may be extended considerably. The natural consequence of a further delay in the recovery of the tax liability is that the tax liability would only increase due to the accrual of interest. The effect is that time and legal cost spent in pursuing any person other than the defaulting taxpayer by attributing the tax liability to such person will reduce any yield or dividend the Commissioner may expect to collect should it be successful with its application.

To allow for greater revenue authority and with an attempt to make it easier for taxpayers to comply with its obligations, the legislator enacted the Tax Administration Act, Act 28 of 2011. In it the Commissioner was given extraordinary and far-reaching powers to fulfil its statutory mandate. In terms of enforcement, the Commissioner was not only afforded the same recovery powers as any other creditor but it also separated itself to a higher level. Allowing itself additional powers to appoint third parties to pay any funds or monies a taxpayer may hold for or on behalf of the taxpayer to the Commissioner in satisfaction of the tax liability. It also expanded the reach of the Commissioner in terms of the source it may collect a tax from. In this instance the representative taxpayer.

Having regard to the provisions of section 155 of the TA Act the Commissioner is well and all entitled to initiate recovery action against the representative taxpayer if that representative taxpayer had disposed of monies or funds which were either chargeable to tax or could have been used to pay a tax due to the *fiscus*. But is it as plain as that? It is not. It is a costly, time-consuming and reactive approach. Under such circumstances, the Commissioner would already have spent a considerable amount of time and resources attempting to collect the unpaid tax from the defaulting taxpayer with variable success. Taking into account the primary function of the Commissioner it begs the question whether the Commissioner may without any due diligence in respect of the prospect of any success of recovery against the personal estate of the representative taxpayer proceed to attribute a tax liability to such a person? Ultimately the Commissioner must determine whether the attribution of the tax liability will allow it to cost effectively and efficiently collect the revenue it is primarily tasked to collect?

What remains a veiled issue is how the Commissioner would collect a tax debt from a representative taxpayer in his personal capacity if that tax debt originated primarily in the

production of income and or in the furtherance of the enterprise of the company? It is accepted that a tax debt originates only in two ways, first, a tax debt originates when a taxpayer declares its taxable income for any period of tax by way of an original return and secondly a tax debt may be incurred by way of assessment issued by the Commissioner. It is a legal impossibility for a tax debt to be incurred and/ or attributed in any other manner.

The manner in which a tax debt originates causes the taxpayer to be entitled to certain rights depending on the outcome of the return he submits or the assessment which he is issued with. For instance, if a tax return was submitted indicating that he is entitled to a credit or refund the taxpayer can expect to receive such credit or refund inclusive of interest. Contrarily if the taxpayer is liable to pay an amount he may dispute the liability and cause to be delivered to the Commissioner a notice of objection.

However, in attributing a liability of a principal taxpayer to the representative taxpayer without there being an assessment may cause the Commissioner some difficulty to enforce its decision to deem the representative taxpayer to be liable. It is suggested that in order to allow the Commissioner the authority to attribute the liability it would be required to create a tax debt by means of an estimated assessment. It is further suggested the estimated assessment would in all probability contain an apportionment of the principal tax liability to the representative taxpayer, as it would be unlikely that the representative taxpayer would be the single reason why the principal taxpayer remains indebted to the Commissioner.

The Commissioner would be, in the issuing of the estimated assessment, be required to clearly identify the particular tax period and the conduct of the representative taxpayer which caused the principal taxpayer to remain indebted to the Commissioner. The assessment must comply with the requirements as set out in s 96(1) of the Act.

In issuing an assessment as suggested herein and above it will cause the Commissioner to comply with its statutory duties and which will be consistent with the considerations of good management of a tax system and administrative efficiency.

For the time being it remains to be seen if the Commissioner would pursue the personal liability of a representative taxpayer by causing an assessment to be issued. However, it appears that for it will continue for now too, until it is challenged in a court of law, blindly attribute the tax liability of a principal taxpayer to its representative.

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