Recent case law

Nondabula v Commissioner: SARS (2018 (3) SA 541 (ECM) (27 June 2017))

"Victory" for taxpayer after SARS fails to fulfil its duties

1 Introduction

The South African Revenue Service (SARS) is tasked with effectively and efficiently collecting taxes (s 3(a) of the South African Revenue Service Act 34 of 1997). In turn, these collected taxes are used by government to develop the economy of the country and regulate employment levels (Croome *Taxpayers' Rights* (2010) 3).

Section 92 of the Tax Administration Act 28 of 2011 (TAA) ensures that SARS collects the correct amount of tax by providing for the issuing of an additional assessment, if the assessment that was originally issued in relation to a specific tax period was not in accordance with the relevant tax provisions and was to the detriment of SARS or the *fiscus*. SARS may estimate this additional assessed amount based on information that is readily available to SARS (s 95(1) and 95(2) of the TAA). Whenever SARS issues an additional assessment, section 96(1) of the TAA provides that SARS must issue a notice of assessment in relation to assessed taxes. This notice must contain, *inter alia*, the date of the assessment, the assessed amount, and the period in terms whereof the assessment is issued, and when the assessed amount must be paid. Where SARS has estimated the amount of outstanding tax based on information it has at its disposal (s 95(2) of the TAA), the notice of assessment should also contain a statement indicating the grounds for the assessment (s 96(2)(a) of the TAA). This statement should make it possible for the taxpayer to establish the legal and factual basis for the assessment (*SARS Dispute Resolution Guide* (28 October 2014) 31).

In *Nondabula v Commissioner: SARS* 19 SATC 333 (*Nondabula*), the court had to consider whether SARS could proceed in fulfilling its task of collecting assessed taxes if it did not furnish a notice of assessment as required. This is an important aspect to consider as allegations pertaining to an illegal "rogue" investigation unit set up by SARS and the emerging public debate in this regard has brought the extent of SARS powers under scrutiny (see Sikhane Investigation report – conduct of Mr Johan Hendrikus van Loggerenberg South African Revenue Service (2014) 5-7; Sunday Times (2016-05-15) 1; Business Day Live (2015-03-02) in this

How to cite: Fritz '*Nondabula v Commissioner: SARS* (2018 (3) SA 541 (ECM) (27 June 2017))' 2019 *De Jure Law Journal* 181-188
http://dx.doi.org/10.17159/2225-7160/2019/v52a11

regard). This case note reflects on whether the court came to a correct conclusion and the future implications thereof.

2 Facts and judgment

In the present matter before the Eastern Cape Local Division (Mthatha), the taxpayer, Nondabula, sought confirmation of a rule *nisi* that was granted to interdict SARS from using its power to appoint a third party to collect an outstanding tax debt. This outstanding tax debt emerged from an additional assessment, which was issued by SARS on 1 March 2016 (par 1, 4 & 14). This outstanding tax debt first came to the taxpayer's attention by way of a statement of account dated 4 April 2016 (par 5). The statement of account did not contain any indication of how the amount of outstanding tax had been determined (par 5), and it also did not contain a statement indicating the grounds as required in terms of section 96(2)(a) of the TAA (par 20).

The applicant lodged an objection relating to the assessed tax, where after SARS responded that the taxpayer could not request that penalties be waived and declare a dispute in the same objection (par 9). It therefore seems that the merits of the taxpayer's objection were not considered.

Subsequently, SARS forwarded a letter to the taxpayer demanding that the outstanding tax be settled within ten days (par 4). In response, the taxpayer requested SARS to reconsider the assessment and to note the objections which he had lodged (par 10). This request was to no avail, as SARS did not provide an indication of how the outstanding tax debt had been calculated, and continued to oppose the taxpayer's objections on technical grounds (par 10).

Thereafter, SARS issued another statement of account reflecting an outstanding tax debt, which was less than the tax debt initially indicated.

None of the correspondence addressed to the taxpayer by SARS provided any indication of how the amount had been calculated. Furthermore, the legal basis for the outstanding tax was not indicated (par 5 & 14).

The court observed that no interaction with a taxpayer is required either when an additional assessment in terms of section 92 of the TAA is issued or when an estimation is based on information readily available to SARS (par 21). However, the court held that section 96 sets out what information *must* be contained in the notice of assessment (par 21). SARS could not simply decide to deviate from the required information provided for in the section as SARS is expected to adhere to "its own legislation" (par 26).

The court considered SARS decision to issue a third party appointment notice in terms of section 179 of the TAA, despite not furnishing a notice of assessment, as unlawful and contrary to the rule of law (par 22).

Furthermore, the court held that SARS had failed to comply with the constitutional obligations that SARS, as an organ of state, has in terms of section 195 of the Constitution of the Republic of South Africa, 1996 (Constitution). Firstly, SARS had not acted in an accountable manner (s 195(1)(f) of the Constitution), as it had not complied with the relevant legislation. Secondly, SARS had not acted transparently, as it had failed to provide the public, in this case the taxpayer, with "timely, accessible and accurate information" (s 195(1)(g) of the Constitution; par 24).

Based on the foregoing, the court concluded that the conduct of SARS had been both unlawful and unconstitutional. Accordingly, the court confirmed the interdict prohibiting SARS from appointing a third party in terms of section 179(1) of the TAA. Also, SARS was ordered to pay costs in the matter.

3 Analysis of the judgment

3 1 General observations

In the preceding judgment of *SARS v Pretoria East Motors (Pty) Ltd* (291/12) [2014] ZASCA 91 (12 June 2014) (par 11) the Supreme Court of Appeal remarked as follows:

> As best as can be discerned, Ms Victor's approach was that if she did not understand something she was free to raise an additional assessment and leave it to the taxpayer to prove in due course at the hearing before the Tax Court that she was wrong. Her approach was fallacious. ... In the case of income tax, it must be based on proper grounds for believing that there is undeclared income or a claim for a deduction or allowance that is unjustified. It is only in this way that SARS can engage the taxpayer in an administratively fair manner, as it is obliged to do. It is also the only basis upon which it can, as it must, provide grounds for raising the assessment to which the taxpayer must then respond by demonstrating that the assessment is wrong.

This remark highlights the importance of the notice of assessment, namely to facilitate engagement with an informed taxpayer. Without such a notice the taxpayer would be prompted to request reasons for the assessment (rule 6 of the Rules promulgated under s 103 of the Tax Administration Act 28 of 2011 as contained in GN 550 in *Government Gazette* 37819 (11 July 2014)) and possibly proceed with dispute resolution. Early engagement between SARS and a taxpayer is beneficial, as the taxpayer would have the opportunity to show that the additional assessment was incorrect, without venturing into the often long and costly option of dispute resolution. Accordingly, the notice of assessment ensures that uncertainties are eliminated and only actual disagreements proceed to dispute resolution. Thus, the issuing of a notice of assessment is crucial in an effective tax administration system.

3 2 Peremptory wording

The importance of issuing a notice of assessment is demonstrated in section 96(1) of the TAA provides that SARS "must" issue this notice.

Consequently, SARS has not discretion regarding whether to furnish this notice or not. Unfortunately, the TAA does not stipulate the consequences if SARS fails to comply with this requirement. Botha (*Statutory Interpretation – An Introduction for Students* (2012175-176) remarks that any ensuing action, by a party who has failed to act in accordance with a peremptory wording, would be null and void.

Based on this, the court's decision to interdict SARS from proceeding with ensuing action, appointing a third party, is correct. However, the court did not only rely on the peremptory wording to reach its decision. It considered two aspects of the Constitution, namely the rule of law and the basic values and principles of public administration should be adhere to.

3 3 Rule of law and section 195(1) of the Constitution

One of the founding values of the Constitution contained in section 1(c) thereof is the supremacy of the rule of law. The rule of law, and, more specifically, the principle of legality, which forms part of the rule of law (*Fedsure Life Assurance Ltd v Greater Johannesburg Transitional Metropolitan Council* 1999 1 SA 374 (CC) par 56 & 58), dictates that government must act in accordance with "pre-announced, clear and general rules" (*Dawood v Minister of Home Affairs; Shalabi v Minister of Home Affairs; Thomas v Minister of Home Affairs* 2000 5 BCLR 837 (CC) 842; *Affordable Medicines Trust v Minister of Health of the RSA* 2005 6 BCLR 529 (CC) par 108; Bekink *Principles of South African Constitutional Law* (2012) 62. See, also: Dicey *Introduction to the Study of the Law of the Constitution* (1959) 193; *Fedsure Life Assurance Ltd v Greater Johannesburg Transitional Metropolitan Council* 1998 12 BCLR 1458 (CC) 1482; *Pharmaceutical Manufacturers Association of SA: in re ex parte President of the RSA* 2000 2 SA 674 (CC) par 19-20; Fritz *An Appraisal of Selected Tax-Enforcement Powers of the South African Revenue Service in the South African Constitutional Context* (LLD thesis 2017 UP) 37). Thus, SARS must act in accordance with legislative provisions such as section 96 of the TAA.

Moreover, this value demands that the conduct of government, in this instance SARS, may not be arbitrary (Fritz 38). Currie and De Waal (*The Bill of Rights Handbook* (2013) 540-547) state that "arbitrary" generally involves not following fair procedure, being irrational or having no good reason. It is submitted that SARS' conduct in *Nondabula* was arbitrary for two reasons. One, SARS did not follow fair procedure when it failed to provide the grounds for the additional assessment in a notice of assessment as required in terms of section 96(1) of the TAA. Two, SARS' conduct was irrational as it reduced the additional assessed amount over the course of time without any explanation. This creates the impression that the initial assessed amount was not on firm grounds, or perhaps groundless, which resulted in SARS unceremoniously reducing the amount.

In *President of the Republic of South Africa v South African Rugby Football Union* (CCT16/98) 1999 ZACC 11 (*SARFU*) the court pointed towards another element of the rule of law. Public administration, of which SARS forms part of (s 195(2) of the Constitution read with s 2 of the SARS Act 34 of 1997) "must act in good faith and must not misconstrue" its powers (*SARFU* par 148). The court in *Nondabula* (para 24) shared a similar sentiment when it declared that SARS contravened the rule of law by not complying with its duties in terms of section 195(1) of the Constitution when it failed to furnish the taxpayer with the required information.

The question arises why the court considered it necessary to highlight the unconstitutionality of SARS' conduct, whilst simply relying on the peremptory wording of section 96 would suffice. It is submitted that in the current discourse where the extent of SARS' powers and conduct play an important role, the court had to emphasise that although it is important for SARS to collect taxes this must be done within the parameters of the Constitution.

3 3 Confirming the interdict – no other satisfactory remedy

An interdict is seen as a drastic remedy (Devenish 432) and should be granted only when similar protection cannot be achieved by "any other ordinary remedy" (*Setlogelo v Setlogelo* 1914 AD 221 227).

For purposes of ascertaining whether there was another satisfactory remedy available to the taxpayer, two actions of SARS should be considered. Firstly, SARS issued an estimated additional assessment and failed to comply with the procedural requirements thereof as envisaged in section 96 of the TAA. Secondly, SARS appointed a third party in terms of section 179 of the TAA.

(a) Failure to comply with section 96 of the TAA

In principle, a taxpayer could force SARS to comply with legislative provisions, in this instance section 96 of the TAA, by way of a mandatory interdict against SARS, known as a *mandamus* (Dendy 1063; Hoexter *Administrative Law in South Africa* (2007) 495). Nonetheless, this relief would possible not have been granted as an interdict requires there to be no other satisfactory remedy. In this instance, the taxpayer could use provisions in the Promotion of Administrative Justice Act (PAJA) 3 of 2000 to ensure compliance.

The issuing of an assessment constitutes administrative action. This is relevant, as such act falls within the purview of PAJA, which was enacted to give effect to the constitutional right to administrative action that is lawful, reasonable and procedurally fair as envisaged in section 33 of the Constitution (preamble to the PAJA).

In terms of section 3(2)(b)(iii) of the PAJA, an administrator must give a person who is subject to an administrative action a clear statement of the administrative action. This requirement is echoed in section 96 of the TAA, specifically in relation to SARS and assessments.

Furthermore, sections 6(2)(b) and 6(2)(c) of PAJA identify a failure to comply with a procedure or condition in terms of an empowering provision and a procedurally unfair action as grounds for review in terms of section 8 of PAJA. In turn, section 8(1)(a)(ii) of PAJA stipulates that a court that reviews such a qualifying action may order the administrator – in this instance SARS – to act in a certain manner. In *Nondabula*, the court could have ordered SARS to furnish the taxpayer with the required details in relation to the additional assessment in order for him to grasp the legal and factual basis for the assessment.

It is clear that the taxpayer had a remedy at his disposal in relation to SARS' failure to comply with section 96 of the TAA. However, the interdict sought by the taxpayer in *Nondabula* relates to the subsequent action of SARS in appointing a third party in terms of section 179(1) of the TAA. Consequently, the fact that the taxpayer could have had SARS' non-compliance remedied, cannot result in the court refusing to confirm the final interdict based on other suitable remedies available as this matter has evolved beyond the failure to furnish a notice of assessment.

(b) Appointment of a third party

The decision to appoint a third party is considered an "administrative action" in terms of PAJA (*Contract Support Services (Pty) Ltd v SARS* [1998] 61 SATC 338 349). Consequently, such action also needs to be lawful, reasonable and procedurally fair as envisaged in section 33 of the Constitution and in PAJA. The action on the part of SARS is thus reviewable in terms of section 6(2)(e)(v) of PAJA, as it acted in bad faith by proceeding with enforcement of a tax debt while not yet having provided the taxpayer with the required information. This conduct cannot simply be attributed to possible inadequate training that should be excused. Surely, if a taxpayer requests certain information on numerous occasions, the SARS official(s) dealing with the matter, should seek guidance within SARS. Also, SARS is required to be accountable (s 195(1)(f) of the Constitution) and provide the public with accurate information in a timeous manner (s 195(1)(g) of the Constitution). Therefore, more is and must be expected from SARS.

Apart from a review in terms of PAJA, the taxpayer could also have taken the matter on review on the grounds that the conduct of SARS was contrary to the rule of law (see above). Hoexter (225) points out that a review based on the principle of legality, which forms part of the rule of law, corresponds with the grounds for review in terms of PAJA. However, as "PAJA is now the primary or default pathway to review" (Hoexter 114), it would have been more appropriate for the taxpayer to have

commenced review proceedings in terms of PAJA than based on the principle of legality.

From the above discussion regarding possible remedies available in this matter, it is clear that the taxpayer could have taken the conduct on the part of SARS on review based on several different grounds. However, if the taxpayer had opted for relief by taking the matter on review, SARS would have still been able to collect the assessed amount by way of a third-party appointment as section 164(1) of the TAA provides for the "pay now, argue later" rule. This means that even if an objection, appeal or review has been lodged in relation to a tax debt, SARS may proceed with enforcing the payment of this disputed tax debt. Accordingly, the court was correct in granting the final interdict in *Nondabula* as there were no other satisfactory relief available to the taxpayer.

3 4 Cost Order

Whilst the cost order granted by the court would absorb some of the costs incurred by the taxpayer, the taxpayer could still be liable for a substantial amount in legal costs. As the court did not specify what type of cost order had been granted, it is deemed to be on a party-and-party scale (Theophilopoulos, Van Heerden & Boraine *Fundamental Principles of Civil Procedure* (2015) 447). As such, SARS would only be liable to pay costs that were "necessarily and properly incurred, for the attainment of justice, or for defending of that party's rights" (*Lead Practice Manual: Legal Costs* (2016) 17), which would result in the taxpayer having to pay his attorney any other costs not covered in terms of the party-and-party scale. Accordingly, awarding a party-and-party cost order in this matter does not mean that the taxpayer would not be liable for any costs incurred as a result of SARS not complying with the explicit requirements set out in section 96 of the TAA.

The matter of *Reid v Royal Insurance Co Ltd* (1951 1 SA 713 (T)) (*Reid*) serves to indicate that, in some circumstances, a court may order a party to pay more than just the "necessary and properly incurred" costs. In *Reid*, the court held that the applicant had misunderstood the purpose of particulars of claim, which had caused a delay in proceeding with the matter (720). As a result, the court held that the plaintiff should not "suffer by having to pay out of his own pocket any portion of the costs to which it was subjected" (720) and awarded costs on the attorney-and-client scale. This means that the applicant had to pay all costs, which the plaintiff's attorney would have been able to justifiably recover from the plaintiff (Theophilopoulos 447).

In *Cambridge Plan AG v Cambridge Diet (Pty) Ltd* (1990 2 SA 574 (T)), the court went even further by awarding a cost order for punitive reasons. *In casu*, the court stated that an order on an attorney-and-own-client scale, which was awarded in this matter, signified the court's utmost disapproval of the circumstances that had given rise to the action or the actions of the losing party (589). This cost award would thus

require the losing party to pay the costs as agreed upon by the winning party and its attorney (Theophilopoulos 447). However, the court in *Enslin v Gallo* (1984 1 PH F27 (D)), as referred to in *Cambridge Plan AG v Cambridge Diet (Pty) Ltd* (1990 3 All SA 836 (T) 862), recognised that the party against whom an attorney-and-own-client order is granted is not a party to the contract between the winning party and his or her attorney. This aspect must therefore be taken into consideration when a court exercises its discretion relating to a cost order, as the court has to ensure that its order is fair to both parties. (See *Fripp v Gibbon & Co* 1913 AD 354; *Vryenhoek v Powell* 1996 2 SA 621 (CC) 624B-C; *Naylor v Jansen* 2007 1 SA 16 (SCA) 23F-28F in this regard.)

Considering the different costs orders and relevant case law, it is apparent that whenever a taxpayer approaches a court, even if SARS is to blame, it will have a financial impact on the taxpayer, unless the taxpayer's legal representative is able to successfully argue for an attorney-and-own-client cost order. Although this may be true for other types of litigation, the extent of SARS' powers, *inter alia* the "pay now, argue later" rule and third party appointments, forces a taxpayer to approach a court as it cannot simply be ignored.

4 Conclusion

The case of *Nondabula* highlights the fact that the duty of SARS to collect taxes does not mean it can forsake its obligations imposed by legislation. SARS must act in accordance with the rule of law and has to adhere to the standard enshrined in section 195(1) of the Constitution. As such, the "pay now, argue later" rule can only apply if SARS has furnished a notice of assessment as required in terms of section 96(1) of the TAA. Thus, failure on the part of SARS to provide legal and factual basis for the assessment prevents SARS from using its array of enforcement powers. Although the taxpayer had to pay a cost to interdict SARS, the clarity gained for the benefit of future disputes with SARS is invaluable and a victory for taxpayers.

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