CALL FOR COMMENT: DRAFT INTERPRETATION NOTE: INCOME TAX ON SECTION 23(o): CORRUPT ACTIVITIES, FINES AND PENALTIES

General comment
While we acknowledge the need for an Interpretation Note on section 23(o), we are not sure why an Interpretation Note on section 23(o) is more important than for example an Interpretation Note on a complex section like section 9D and many other sections. It would be helpful to understand how SARS decides to prioritise the issuing of Interpretation Notes.

1. Purpose
The Purpose should be expanded to state the following:

This note clarifies the prohibition on the deductibility of expenditure incurred in respect of -

- a corrupt activity; or
- a fine or penalty imposed as a result of an unlawful activity undertaken by a taxpayer or a representative of a taxpayer in order to obtain a benefit for the taxpayer.

2. Corrupt activities: s23(o)(i)

2.1 The Note does not deal with losses suffered by a taxpayer as a consequence of being a victim of a corrupt or unlawful activity, the tax deductibility of which will be dependent on the specific circumstances of the case. It would be helpful to taxpayers if the Note dealt with this issue.
2.2 The statement that a conviction is not necessary is concerning. It almost seems "guilty until proven innocent". It is not always clear cut whether an activity falls within the scope of corrupt activities.

It is important that the Note tackles complex examples. A typical example is pharmaceutical companies rewarding doctors via gifts to prescribe their drugs. It is common practice for pharmaceutical companies to have conferences in for example five star ski-resorts in Europe, all expenses paid for by the companies, where doctors are wined and dined. The doctors attend technical seminars but more than half of the time is for example spent skiing. Does this amount to a "corrupt activity"?

In practice this is going to be difficult to apply as taxpayers engaging in these kinds of activities are unlikely to admit it and will have many reasons other than bribery for giving the gifts.

2.3 The examples given in 4.1 are mainly examples of bribes (refer to the definition in Annexure A) and whether they amount to corrupt activities will depend on the presence of “any gratification” in this regard. The Note does not deal with this.

2.4 The conclusion to the last example (Nigerian prisoners) does not follow from the facts. It is not clear that they were in fact carrying on a trade and section 23 would therefore not have arisen as the expense will not have qualified under section 11 in the first place.

2.5 It is not the deduction of all expenditure incurred in respect of all illegal activities that is prohibited, but only those incurred in respect of activities contemplated in chapter 2 of the Prevention and Combating of Corrupt Activities Act 12 of 2004.

3. Payments of fines and penalties as a result of an unlawful act (section 23(o)(ii))

3.1 Section 23(o) does not refer to the Conventional Penalties Act. Whilst it is considered that the conclusion in the 4.2.1 is correct (not all penalties result from an unlawful act), it may well present a problem. Section 23(o)(ii) does not refer to the definition in the Prevention of Organised Crime Act:

"Unlawful activity" is defined to mean “any conduct which constitutes a crime or which contravenes any law whether such conduct occurred before or after the commencement of the Act and whether such conduct occurred in the Republic or elsewhere”.

In National Director of Public Prosecutions v Levy and others [2004] 4 All SA 103 (W) the Court opted to apply the phrase “unlawful activity” in its broadest sense, in order to give effect to the purpose of its express wording.
3.2 The Note (paragraph 4.2.1. and 4.2.2) does not provide sufficient guidance to identify penalties which may be allowed to be deducted and will not be prohibited by section 23(o).

**Conclusion:**
The disclosure burden on taxpayers is material. It is possible for activities of this nature to be deliberately hidden from the public officer by officials within an organisation as they believe that the business benefit outweighs the risk.

If the taxpayer separately discloses items which fall within section 23(o), what will the criminal consequences be for that taxpayer?

If the taxpayer fails to disclose such items, and it later transpires that an amount was expended which falls within section 23(o), it would appear that SARS will be within their rights to accuse the taxpayer of material non-disclosure, with the result that the tax assessment for that year will not prescribe.

Whilst we applaud all attempts to rid our society of corruption, we need to be practical with regard to the potential consequences of section 23(o) for all taxpayers. The potential criminal consequences of adhering to the provisions of the section (and disallowing the deduction of these types of expenses) need to be carefully considered.

Please do not hesitate to contact me should you require further information.

Yours faithfully

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Annexure A

BRIBERY

Is the unlawful and intentional taking or giving, or procuring the taking or giving, of any money or valuable consideration; or office, place or employment; or gift, loan or promise of such, or of an advance of money; for the performance or non-performance of any public duty, or for false judgment or evidence, or for the performance of some unjust or illegal act.

To bribe or attempt to bribe an official is a crime by Roman-Dutch law (The State v Aaron H 146; 10 CLJ 238):

“Under our common law, therefore, the crime of bribery includes the making of a gift to an official in order to influence him to do something in conflict with his duty. I use the word ‘includes’ advisedly because it is not necessary for the purposes of this appeal to attempt to define the full scope of the crime”

(per TINDALL, JA in R v Sacks 1943 AD 423):

“As I have indicated, bribery implies a voluntary gift; extortion implies at least a transfer of property induced by illegitimate pressure upon the transferor”

(per MATTHEWS, AJP in R v Muller 1934 NPD 146).

“It is not necessary to prove that the person bribed did what he was bribed to do. The essentials of the crime are receipt of the bribe and that it was given and received as an inducement” (Green v R 1926 (1) PH H44 (AD)).

See also R v Patel 1944 AD 511. “The crime may be committed by offering gifts to an official of the State to engage his assistance even where that does not fall within his official functions” (R v Chorle 1945 AD 487).

See the recent cases collected in 1968 SALJ 399 and see S v Van der Westhuizen 1974 4 SA 61 (C). The elements of this crime discussed in S v Gouws 1975 1 SA 1 (A); S v Narker 1975 1 SA 583 (A).

In connection with an election, see Van Rhyn v Du Plessis 1974 3 SA 605 (A). See BRIBE; CORRUPTLY; OFFICIAL; OMKOPING; VALUABLE CONSIDERATION.