REPUBLIC OF SOUTH AFRICA

IN THE TAX COURT OF SOUTH AFRICA
(HELD AT MEGAWATT PARK, JOHANNESBURG)

CASE NO: 35476

(1)	REPORTABLE: YES/NO
(2)	OF INTEREST TO OTHER JUDGES: YES/NO
(3)	REVISED.
15 March 2023	………………………...
DATE	SIGNATURE

In the matter between:

TAXPAYER DK **APPLICANT (RESPONDENT)**

and

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **RESPONDENT (APPLICANT)**

J U D G M E N T

MANOIM J:

[1] The taxpayer in this matter has an appeal pending before this court against an assessment from SARS. The appeal has yet to be heard as its progress has been slowed down due to a number of interlocutory applications.

[2] The present matter concerns two further interlocutory applications brought at the behest of SARS. The one is an application to amend it pleadings i.e., its rule 31 statement, the other for further discovery in terms of rule 36(6). Both applications are interrelated. For this reason, I heard them at the same time and deal with them in the same judgment.

Background

[3] At issue in the appeal is an assessment SARS did on the taxpayer. The taxpayer is a businessman who is the sole director and shareholder in a number of firms which are referred to as the Taxpayer DK Group.

[4] In August 2022 I heard an application by SARS in which it sought to have the case referred back to it for reconsideration and assessment. I, for reasons given in that decision, refused the application.[1] Thereafter the matter went ahead with trial preparation including a meeting of experts. The experts could not agree on the extent of the documentation required. SARS' expert filed his report in which he stated he required certain documentation to be able to complete his report. That led to a further case management meeting on 26 January 2023. The upshot was that I gave SARS an opportunity to request further discovery and file an amendment to its rule 31 statement. As a result, the trial which was meant to proceed in the week of 20 February 2023 was postponed in order to resolve the discovery and amendment issues.

[5] The applications for amendment and discovery have now been brought. The taxpayer opposes both. Despite the exchange of affidavits neither party has made any concessions to the other. Two issues drive the difference in approach of the parties in this matter. The first, is SARS' scepticism of the taxpayer's version that he had made good faith errors in respect of the loan accounts of one of his entities, Company A, and hence they had to be rewritten, rendering what was taxable in his hands, no longer. The second, is the taxpayers' belief that SARS wants to resurrect the opportunity to subject him to an audit *de novo.* These different departure points identify the core issue in this case before I get down to the detail.

[1] The judgement can be found on CaseLines at 016-3.

Amendment application

[6] It must be borne in mind that the application for amendment has come very late in this case. Indeed, to repeat the point that but for these applications the appeal would have proceeded to be heard during this period. SARS justifies the necessity for its amendments as consequence of my decision to refuse its application for referring the taxpayer's matter back for reconsideration and assessment. SARS still wants to be able to argue this point on appeal. In terms of section 129(2)(*c*) of the Tax Administration Act 28 0f 2011 (the TAA) one of the orders a court may make on hearing an appeal, is to refer the assessment back to SARS for further examination and assessment.

[7] In SARS' rule 31 statement this was done by way of a point *in limine* contained in a short paragraph. The amendment to paragraph 3.1 deletes this paragraph and replaces it with a lengthier formulation of the issues.[2] This amendment clarifies the position that SARS will contend for in the appeal and I consider it will aid the litigation.

[8] The next amendments are motivated according to SARS to delineate between what SARS alleges was told to it during the Objection and Appeal process by the taxpayer and what is contended for now. Since part of SARS case is premised on an inconsistency between these versions it wants its pleadings to carefully set out this distinction. Thus, this delineation function has led to two types of amendment. The first is to amend the rule 31 statement in some paragraphs by the insertion of a prefatory sentence in each one which states:

> "Regarding issues canvassed during the "Objection and Appeal Process", on the merits, the "Issues in Dispute" are as follows: Paragraphs 3.2–3.4 to be repeated".

[9] The second part of delineation is to repeat the same text but without prefatory text. This is motivated by the need to deal with the process problem; i.e., to distinguish between what served before SARS in the assessment stage and what followed afterwards during the ADR stage. This it seems is aimed at giving SARS the ability to argue for the matter to be referred back and hence it is a cautious approach to the pleading. It is SARS case that the present version of the taxpayer which SARS labels his fourth version only emerged during the ADR stage and thus after the "Objection and Appeal" process.

[10] The taxpayer raised no serious objection to these amendments apart from suggesting that they were vague (a criticism that I don't consider has been fully made out). I consider they improve the pleadings by clarifying SARS position. The taxpayer benefits from this clarity as does SARS.

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[2] A new 3,1 with three subparagraphs 3.1.1 to 3.1.3.

[11] The more spirited opposition from the taxpayer came in respect of the second aspect of the amendment to introduce a higher understatement penalty (USP) which reads as follows:

> "In respect of the "Fourth Version" advanced post "The Objection and Appeal Process" SARS is justified to ask the court to impose USP at 125% Gross Negligence — Obstructive Behaviour as the facts will show that the Appellant consistently and without any reasonable explanation misrepresented the facts in such a manner as to establish a case for "Gross Negligence" as contemplated in Item (v), column 4 (Obstructive Behaviour).
>
> The Appellant's conduct does not constitute "*Bona-Fide* Inadvertent error as contemplated in s222(1) of the TAA as his conduct as evidenced in the declarations made during the Objection & Appeal Process" and post appeal, is illustrative of a conscious, elaborate and well thought effort as opposed to an innocent error."

[12] SARS motivated the increased penalty amendment in this way. If the taxpayer is found to have altered his financials on these facts, then the concealment is worthy of a higher level of penalty for the understatement. But this is not a new aspect to the case brought on by my August decision. This has always been SARS position and it has not motivated sufficiently for why the amendment should be made now. Given the prejudice to the taxpayer it cannot be allowed at this stage of proceedings.

Discovery

[13] Prior to considering the specific requests in the discovery application I need to consider the debate between the parties about the ambit of SARS' rights to request discovery. Mr OM who appeared for SARS argues that this right stems for the definition of "*relevant material*" contained in section 1 of the TAA, read with section 3, which states:

> "relevant material" means any information, document or thing that in the opinion of SARS is foreseeably relevant for the administration of a tax Act as referred to in section 3;"

[14] Section 3 then gives SARS wide powers to carry out the administration of a Tax Act. This power, is defined, inter alia, in terms of section 3(2), to include the power to:

> "(*a*) obtain full information in relation to—
>
> (i) anything that may affect the liability of a person for tax in respect of a previous, current or future tax period;
>
> (ii) a taxable event; or
>
> (iii) the obligation of a person (whether personally or on behalf of another person) to comply with a tax Act;

(*b*) ascertain whether a person has filed or submitted correct returns, information or documents in compliance with the provisions of a tax Act;"

[15] Ms Counsel who appeared for the taxpayer argued that in an appeal the court is confined to ordering discovery in terms of the Tax Court rules only. Hence the court is limited to considering the application in terms of rule 36(6), not section 1 read with section 3 of the TAA. Rule 36(6) states:

> "If either party believes that, in addition to the documents disclosed, there are other documents in possession of the other party that may be relevant to a request under subrule (1) or (2) or the issues in appeal, as the case may be, that have not been discovered, then that party may give notice of further discovery…"

[16] I agree with this contention by the taxpayer. There is a distinction between the powers SARS exercises qua investigator and the rights it has to discovery as a litigant in an appeal. In terms of the former, given these are investigative powers it is understandable that these powers are wide. But the same latitude is not accorded to SARS as a litigant in an appeal. For this reason, the right to discovery is determined by the normal standard applied to a litigant in accordance with the Tax Court's rules.

[17] I find that the following document requests exceed the discovery rights of the litigant. These are items, 4, 14, 15 and 16 which relate to financial information of the taxpayer in foreign jurisdictions (4, 14 and 15) or in the case of 16 have not been shown to be relevant to the current dispute. The application for discovery of these items is dismissed.

[18] While adopting this approach narrow's the ambit of relevance it does not entirely decide the matter. This is because one of the issues as it is framed by the taxpayer is:

> "The misstatement in Company A's 2014 unaudited annual financial statements, dated 12 November 2014, prepared by GHB Consulting Accountants, was that the mortgage loan facilities advanced by the financial institutions, Nedbank Limited and the Standard Bank of South Africa Limited, secured by Company A as mortgagor, had been merged together with the appellant's shareholder loan account in the disclosure of Company A's unaudited financial statements."[3]

[3] See appellant's (taxpayer's) rule 32 statement, CaseLines 017-6, paragraph 19.

[19] In his grounds of appeal, the taxpayer frames his issues *inter alia* as follows:

> "26.1 The amount classified by SARS as an understatement of income for funds advanced by the appellant to Company A in the 2014 and 2015 years of assessment **is overstated and incorrect**. The amount does not constitute gross income as defined. The correct extent of the funds advanced by Company A constitutes capital and not revenue.
>
> 26.2 The amount classified by SARS as an understatement of interest income in the 2014, 2015, 2016 and 2017 years of assessment **is overstated and incorrect**. The amount does not constitute gross income as defined."

(My emphasis)

[20] I now apply this approach to the requests. Certain documents have already been given to SARS by the taxpayer. At my request the taxpayer's legal team prepared a table of these documents, including where they could be found in the record. I have annexed this document as part of this order as Schedule A.

[21] However, it is not clear to me whether the documents submitted in response to the request in paragraph 1 include the journal entries referred to. I agree with SARS that these entries are relevant to the issues in dispute contemplated in paragraph 26 of the rule 32 statement. SARS places in dispute the explanations given by the Taxpayer that these entries were errors and refers, as I mentioned earlier, to the so-called four versions given to SARS. Whilst the taxpayer denies he has given four versions this is a fact in issue to be determined in the appeal and hence relevant for discovery purposes.

[22] SARS relies on the case of *GB Mining & Exploration SA Pty Ltd v CSARS* to support its contention that in cases where a taxpayer contended that its financial statements contained incorrect information which SARS ought not to have relied upon, evidence of supporting documentation would have to be submitted. The court put it this way:

> "In the event of incorrect information being included in the balance sheets or accounts, evidence would have to be furnished to explain the precise nature and extent of the incorrect information and how it was included. All the relevant supporting documentation to verify the correct information would have to be submitted … together with a full explanatory note to clarify the amendment." [4]

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[4] (90-3/2012) [2014] ZASCA 29 at p.12.

[23] The journal entries sought are examples of such supporting documentation and SARS is entitled to seek their discovery. To the extent then that the documents already disclosed in Schedule A do not contain the journal entries referred to in paragraphs 1.1 to 1.6 they must be discovered. The same principle of supplying supporting information that can enable verification applies to items 2, 3, 5, 6, 8 and 9.

[24] Item 12 is a request for BJP the taxpayers' accountants' invoices to him. It's not clear why these would divulge relevant information. This request is too refused.

[25] Item 13 relates to correspondence between his accounting firm BJP and the auditing firm at the relevant time. Some of this information may be relevant but framed as it is overbroad and would require the discovery of much irrelevant documentation because it contains no restrictions as to content and to duration. What might be relevant is any correspondence between them regarding the reconstruction of the financial statements during the period when the error was realised and when it was corrected. However, I am reluctant to rewrite this request in this manner as it would amount to more than a pruning of the request but a rewrite. For this reason, this request is also, as presently framed, refused. The same can be said of the request in item 11 which is the correspondence between BJP and the taxpayer from inception of the relationship to date. Had this been pared down it might contain relevant material but as presently formulated it is overbroad.

[26] In contrast, item 10, which is overbroad, can be pared down to the essential items which is referred to after the word "including" that appears in the third line of that request. In other words, here while the request starts off broadly it is then narrowed by the term 'including' and words that follow, which allows me to do the surgery without a substantial rewriting of the request. I have also narrowed the period of request to the starting year being 2012, consistent with the other requests and not 2004.

[27] Items 7.2 to 7.4, which deal with communications between the accountant and the auditor are much more in point to the issue of the restatement of the accounts and hence I have allowed them.

Costs

[28] Neither party has been entirely successful. Each will bear its own costs.

Order

[29] In the result the following order is made:

Amendment application

In respect of SARS application to amend its rule 31 statement dated 25 January 2023

1. The amendments sought in paragraphs 1, 2, 4 and 6–10 of the notice of intention to amend (the NOIA) are granted.

2. The amendments sought in paragraphs 3 and 5 of the NOIA are refused.

3. There is no order as to costs.

Discovery application

In respect of SARS discovery application in terms of rule 36(6) of the TAA rules dated 31 January 2023

1. The documents set out in Schedule A and said to have been produced must be produced if not already in the possession of SARS. In addition to those documents the following must be produced:

    a. In relation to item 1, the documents referred to in paragraphs 1.1 to 1.6.

    b. In relation to item 2, the documents referred to in paragraphs 2.1 to 2.5.

    c. In relation to item 3, all the documents described.

    d. In relation to item 5, an affidavit from the taxpayer or responsible person with knowledge of this fact to say the 2012 AFS is not available.

    e. Item 6.

    f. In relation to item 7, only items 7.2 to 7.4.

    g. In relation to item 8 to the extent not already given.

    h. In relation to item 9 limited to bank accounts in South Africa for 2012 to 2017.

    i. In relation to item 10 limited to the following:

        i. All the documents received from, and correspondence with, the construction company/ies and others involved with the development

of any properties of Company A, that were used in the reconstruction of the records for 2012 to 2017.

2. The request for discovery of the following items is dismissed-
   a. Item 4 in respect of 4.1 to 4.6
   b. Items 11, 12, 13, 14, 15 and 16.
3. There is no order as to costs.

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N. MANOIM
Judge of the High Court
Gauteng Division
Johannesburg

Date of hearing: 21 February 2023
Date of judgment: 15 March 2023