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BE PREPARED AS GOVERNMENT TAKES AIM AT TRUSTS

***"Let me tell you how it will be
There's one for you, nineteen for me
'Cos I'm the taxman, yeah, I'm the taxman"
(The Beatles – 'Taxman')***

For many years government has been hostile to trusts. In the latest draft Bill of 2016 taxation amendments, a provision has been inserted on trusts.

Be aware that this has not passed into law but it will have a fundamental impact on trusts if enacted as it stands. **This early warning gives you more time to consult with your tax adviser.**

The proposed changes:

1. An individual or a connected entity that makes an interest-free or low interest rate loan to a trust will be taxed from 1 March 2017 (if the provisions are passed unaltered). The tax will be the difference between the SARS interest rate of 8% (note this is subject to change) and the interest amount charged,

2. If you are taxed under this provision, you have 3 years to recover the tax paid from the trust. If the tax is not recovered, the taxed amount is treated as a donation in your hands as taxpayer.

An example illustrates

Assume you make a R1 million tax-free loan to a trust.

In the next tax year you will be liable for tax on R80,000 (8% of R1 million). Let's further assume that tax payable on this is R32,000 (40% of R80,000)

If 3 years then elapse and the R32,000 is not recovered from the trust, you will be taxed on a donation of R32,000 and will pay tax of R6,400 (20% donations tax on R32,000)

Note that the interest cannot be offset against your annual interest exemption of R23,800. Neither can the donations tax be part of your annual R100,000 donation tax exemption.

Be prepared!

For many years, one of the tenets of establishing a trust has been for the founder to finance it by an interest-free loan with no adverse tax consequences. If the new tax Bill is enacted as is, this will change. **Be prepared!**

DUE DILIGENCE: IT'S MORE THAN JUST COMPLIANCE

We tend to think of due diligence as a boring bit of compliance when buying or selling a business.

Often auditors come and hunch over files for a few days or weeks and then give you a report on their findings.

But in today's fast-moving world due diligence can be a considerable asset to your business. Think of how quickly a social media comment can damage a business – having a process to prevent this, or, if it happens, a process to respond quickly, can prevent or at least limit harmful effects on your business.

What is due diligence?

It is really the process of taking due care that any major decision will add value to your business. Aligned to this is being prepared to react to any event such as the social media example above.

What you would do when undertaking due diligence varies with the task needed. For example if you are appointing a new director there would be:

- Advertising for the position,
- Interviews,
- A short list,
- Final interviews, and
- Detailed checks including detailed referee questioning, criminal and credit checks, and social media screening (for any evidence of behaviour prejudicial to the organisation) and so on.

With buying a business there would be:

- Detailed compliance tests – such as all laws obeyed, taxes paid, no major legal issues, all patents renewed and all contracts in order,
- Detailed checks on current management,
- Checks on controls and finances,
- Human Resource policies are comprehensive and working well,
- New product strategy, and
- All business processes in order.

Use checklists

We live in a busy fast-moving world so set up checklists for the types of due diligence you use.

Remember that in the final analysis these checklists are only a guide. Management makes the final determination after reviewing checklists.

By doing a thorough job of due diligence, management gains important knowledge - this can be used to leverage things such as an improved deal.

The bottom line - due diligence is much more than just compliance, it's a valuable management tool.

BUSINESS RESCUE – HOW WELL IS IT DOING AND HOW CAN WE IMPROVE IT?

Business Rescue (BR) is one of the cornerstones of the "new" Companies Act. It is generally agreed that the BR section of the Act is based on global best practice and is of a very high standard.

Virtually all business owners will go through difficult times at some stage in their career – knowing how BR works could be the saviour of your business.

What is Business Rescue?

When a business is facing difficulties, it can invoke business rescue which results in a business rescue practitioner putting into practice an agreed rescue plan (involving key stakeholders such as banks, creditors, shareholders, employees etc). During this process, the company is legally protected from creditors' claims.

The final result is the business returns to normal trading (if the action plan is successful) or is liquidated if the plan is unsuccessful.

How is it doing?

Up to March 2016, 2,148 businesses had entered BR and 1,129 cases were still in process. Of 1,019 completed instances, 310 or just over 30% were proving to be successful.

Whilst this marks a step–up from the previous Companies Act's Judicial Management process, it is a good time to take stock of BR.

3 steps to improving the rescue rate

1. Almost all commentators want to see an improvement in the calibre of BR practitioners. Banks cite issues in this regard as a reason why they are not prepared to advance funds when businesses go into BR.

   Potential solution: Get the CIPC to raise standards for business rescue practitioners to be accredited as qualified. The CIPC has begun to do this.

2. Many of the businesses which went into BR should not have done so.

   Potential Solution: Get the business rescue practitioner (or independent specialists) to do an in-depth analysis of the business before commencing BR. Apart from directors, involving other stakeholders will improve this process. If this analysis supports BR, then it should be given the green light.

   In the statistics above, many of the companies were poor candidates for BR and should have been liquidated. Thus, this process will enhance

the potential for a successful BR.

3. Financiers who fund companies in liquidation should become preferred creditors in the event of liquidation. This will encourage banks to be more amenable to taking the risk of lending to BR entities.

Of course the best way to avoid BR is to be proactive. Always have forward-looking cash flows and continually scan the environment for potential risks.

A NIGHTMARE ON SARS STREET: THEY'RE USING DEBT COLLECTORS TO RECOVER TAX

Our two worst nightmares are owing SARS money and being pursued by debt collectors. These nightmares are fusing into one as SARS have contracted debt collectors to recover amounts due to SARS that are older than four years.

Why would SARS use debt collectors?

Some commentators have expressed surprise that SARS would take such a step as they are amongst the best debt collectors around. They have legal remedies such as issuing effective emolument orders to employers to divert part of their employees' salaries to SARS. In fact, they can go further and have more powers than any debt collecting agency.

Revenue authorities have not always been successful when outsourcing collections – a case in point is the United States where they have twice tried outsourcing and each time have withdrawn as costs exceeded the amount of revenue collected.

There is a significant degree of confidentiality required. Legislation restricts the information that can be divulged to third parties and legal specialists have questioned if it is lawful to disclose taxpayer information to debt collectors. The debt collection agencies have been sworn to secrecy and face potential criminal charges if they violate their oath.

Finally, SARS is paying a percentage of the recoveries to the collection agencies. It is not public knowledge what the percentage will be, but it is estimated that it will cost SARS about R1.5 billion to collect R15 billion of outstanding tax. This estimated 10% cost seems high when taking into account the above-mentioned factors.

The process

SARS has begun this process by appointing three debt collection agencies to collect the outstanding amount of R15 billion. The agencies are required to contact relevant taxpayers stating:

- That their tax debt has been handed over to the agency,
- The amount owed and any outstanding tax returns.

Thereafter, the agency will commence with the collection process.

If you are contacted, here's what to do

- **Speak to your accountants** – they are well qualified to give professional advice.

- **Beware of scams!** There are already many scams relating to SARS and this will definitely attract the scammers. Make sure callers are genuine – for example, they should know your tax number and the amount you owe. You can easily verify this on your eFiling account, also check the collectors are genuine by phoning the SARS Contact Centre at 0800 00 7277 (0800 00 SARS). Most importantly, whatever you do check the account you are paying into is a genuine SARS account.

YOUR TAX DEADLINES FOR SEPTEMBER

23 September is the due date for manual and postal income tax submissions.

Don't forget these other important deadlines for the 2015/2016 tax year:

- 25 November 2016 – eFiling for non-provisional taxpayers. If you plan to submit from a SARS' office this is also the due date for filing (non-provisional taxpayers),

- 31 January 2017 – provisional taxpayers via eFiling.

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