Seychelles Revenue Commission

PUBLIC RULING - 2016-1

Subject Heading: Application of culpability penalties under section 44A of the Revenue Administration Act as amended by Act 4 of 2015.

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Any enquiry in relation to this Pubic Ruling can be addressed to the Seychelles Revenue Commission, PO Box 50, Maison Collet, Republic of Seychelles.

Preamble

1. This document is a ruling for the purposes of Section 44A of the *Revenue Administration Act 2009* (RAA). You can rely on the information presented in this document which provides the Revenue Commissioners view on the application of culpability penalties under section 44A of the Revenue Administration Act.

What this Ruling is about

2. The purpose of this public ruling is to provide clarity and transparency on the criteria looked at by the Seychelles Revenue Commission (SRC) in interpreting the concepts of “reasonable care”, “recklessness” and “intentional disregard” referred to under section 44A of the Revenue Administration Act 2009 dealing with imposition of additional tax.

3. However, the scope of this public ruling does not extend to the waiving of additional taxes and the conditions within which the waiving will be exercised.

Application of culpability penalties under section 44A of the Revenue Administration Act as amended by Act 4 of 2015.

Legislative Framework

4. Section 44A as recently incorporated under the Revenue Administration Act states as follows:

(1) Where a person-

(a) makes a statement to a revenue officer which is false or misleading and which results in revenue shortfall; or

(b) is assessed in accordance with section 9of this Act,

the person is liable to an amount of additional tax in accordance with subsection (2).

(2) The amount of additional tax referred to in subsection (1) shall be equal to-

(a) in the case of statement under subsection (1) (a) -

(i) 25% of the revenue shortfall where the statement being made by failure to take reasonable care to comply with revenue laws;

(ii) 50 % of the revenue shortfall where the statement being made with recklessness as to the operation of revenue laws; or

(iii) 75% of the revenue shortfall where the statement being made with intentional disregard of revenue laws

(b) in case of an assessment under subsection 1(b), 75% of the revenue liability.

Consideration of culpable behavior

The taxpayer's culpable behavior will be considered at the time the false and misleading statement is made. The taxpayer's behavior during the audit process should not have an impact on the application of penalties under section 44A of the Revenue Administration Act.

Ruling

Meaning of "a statement which is false or misleading in a material particular"

What is a statement?

5. A statement is anything disclosed to the Revenue Commissioner or to any revenue officer during the performance of his duties for a purpose connected with revenue law.

Has a statement been made?

6. A statement may be made orally or in writing or in any other way including electronically for a purposes connected with revenue law and may be made in correspondence, response to a request for information or for amendments or during an interview for audit purposes. A statement will also include entering information or amounts in tax returns, business activity statements, tax invoices and other documents prepared or given under revenue law.

7. However, a statement can also be materialised by an omission to make a statement where it is required to do so. A statement by omission can include situations where the person did not declare income earned or states that an event did not occur or that information requested does not exist.

Is the statement false or misleading in a material particular?

8. A statement is false if it is contrary to fact or wrong. The knowledge by the taxpayer of the statement being false or wrong does not matter. It may be false because of a mistake contained in the statement or because of something missing.

9. Example
   If assessable income is omitted from a tax return, that omission is taken to be a statement that the taxpayer did not derive the assessable income during the return period. Where a taxpayer's tax return includes a claim for a deduction to which the taxpayer is not entitled, the return contains a false or misleading statement.

10. A statement is also misleading if it creates a false impression.

11. <u>Example:</u>
    During an interview at the taxpayer's business premises, the taxpayer informs the SRC officers that the business did not lodge VAT returns for certain months because it did not trade during those months. It was later discovered that the business did trade during those months and was required to lodge VAT returns. The taxpayer's response to the SRC officers had created a false impression that business operations and trade had temporarily stopped. This situation was contrary to the later discovery and a false and misleading statement in a material particular has been made to the SRC officers.

12. A material particular is something that is likely to affect a decision regarding the calculation of a taxpayer liability or right for refund or credit.

Who is liable to penalties under section 44A of the amended Revenue Administration Act?

13. The taxpayer lodging the statement or on whose behalf the statement is lodged, is liable to the penalties.

14. The taxpayer will be liable to penalties for statements also made on its behalf by his agents or employees. For example, the taxpayer will be liable to penalties if their tax agent makes a false and misleading statement concerning the taxpayer's affairs. For corporate taxpayers; a company will also be liable to penalties resulting from statements made by an authorised employee, public officer or director.

Meaning of "revenue shortfall"

15. As stated in the law, revenue shortfall means the amount by which the revenue liability of the person is less than it would have been if the statement was not false or misleading OR an amount the Revenue Commissioner must pay or credit the person with that is more than it would have been if the statement was not false or misleading.

Meaning of "reasonable care"

What is "reasonable care"?

16. There is no established definition of "reasonable care" but considered in the context of a taxpayer making a false or misleading statement, this means that the taxpayer did not give **appropriate attention** to complying with the obligations imposed under a revenue law.

17. The reasonable care test requires a taxpayer to take the same care in fulfilling its tax obligations that could be expected of a **reasonable person in the same position**. This means that even though the standard of care is measured objectively, it takes into consideration the particular circumstances of the taxpayer, including knowledge, education, experience and skill. A reasonable and genuine attempt to comply with revenue law requirements given a taxpayer's particular circumstances would usually be sufficient to pass the test.

Importance of individual circumstances in the "reasonable care" test

18. The taxpayer's individual circumstances and the actions they undertook are the determining factors of the reasonable care test. The test shall take into account all the relevant acts or omissions leading to false

or misleading statement. The liability to penalty will only arise where the conduct of the taxpayer falls short of the standard of care expected of a reasonable person in the same circumstances.

18. The SRC will focus on identifying what ought to have been done or ought not to have been done to avoid the risk of making a statement that is false or misleading. The elements looked at in determining whether the appropriate standard of care required has been applied include:

    - The personal circumstances (such as the age, health and background);
    - Level of knowledge, education, experience and skills; and
    - Understanding of revenue laws.

(1) The personal circumstances (such as the age, health and background)

19. SRC will look at the age, the mental health, or physical incapacity that may adversely impact on the care taken by the person.

20. The SRC will not be satisfied with claims that a business was too busy to devote time for tax compliance, this will be the case even in situations where evidence showed the person responsible were overwhelmed with other obligations (such as family commitments or was short staffed).

    Example 1:

    A sole trader was hospitalised and unable to attend to his business for a period of time leading to errors in the business tax return. The 'reasonable care test' requires a taxpayer to make a reasonable and genuine attempt to comply with obligations imposed under a taxation law. The effort required is one commensurate with the taxpayer's circumstances. In practice, this means that all actions leading up to the making of the statement should be taken into account, including whether a tax agent or other person was engaged to act in the sole trader's capacity during this time.

    The SRC will be satisfied that subject to the taxpayer's circumstances and having made a genuine attempt that in the same situation, a reasonable person would not have done better and the test is fulfilled.

    Example 2:

    A taxpayer claimed mistakes made in its VAT returns were due to his accountant having quit during a peak period. The SRC will not be satisfied that the taxpayer has taken reasonable care in ensuring the VAT returns lodged were correct.

(2) Level of knowledge, education, experience and skills

21. The taxpayer's knowledge, education, experience and skills will also be examined; a professional person with tax knowledge will be subject to a higher standard of care. For a business, the knowledge and experience of the persons managing the business would be used as the point of reference.

    Example:

    A company managed by a director failed to exclude the director's personal use (private) items from its allowable deduction.It is expected that the director should exercise the care that a reasonable, ordinary person would exercise in the same circumstances to fulfil their tax obligations.The position of director requires a level of skill, knowledge and due diligence in running the company and he ought to have known that his private expenses are not deductible for business tax purposes. The company would not satisfy the reasonable care test.

22. In undertaking the determination of the level of care to be expected for tax and accounting professionals, the SRC will look at factors such as the size, resourcing, degree of specialization and the client base of the practitioner. For businesses, the SRC will look to factors such as the nature and size of the business together with other relevant circumstances.

(3) Understanding of revenue laws

23. Factors such as the complexity of the law and whether recent amendments have been made to the relevant law will be considered in determining the standard of care that is reasonable in the given circumstances.

24. If a taxpayer is uncertain about the correct interpretation to be given, reasonable care requires the taxpayer to make appropriate enquiries to arrive at the correct interpretation of his/her tax obligations. This includes contacting the SRC, consulting any official publications made on the subject (being in the newspaper or on TV or consulting any official SRC website) or seeking advice from a tax agent. The SRC will be satisfied that reasonable care has been taken by a taxpayer where it can be shown a genuine effort has been made, commensurate with the taxpayer's ability to research and support the position taken.

25. What should be understood by "genuine effort" is where a taxpayer can show they are engaged in the tax system by actively attempting to comply with their tax obligations. A key indicator is whether the taxpayer is making reasonable attempts to effectively manage the risks associated with their tax position and displays this approach in their reporting to the SRC.

26. However, an interpretative position which deemed frivolous will be interpreted as falling short of the standard of care required because it will demonstrate that the taxpayer has made little efforts to exercise sound judgment.

27. Sometimes a taxpayer will rely on information provided by a third party. Whether this is sufficient to satisfy taking reasonable care will depend on examination of the facts and the taxpayer's circumstances.

<u>Example 1:</u>
A taxpayer relying on the advice given by a student in law to ascertain the legality of a claim for input tax credits that were incurred for construction of residential dwellings under VAT will be assessed as having not complied with the expected standard. Indeed, an ordinary person in the same position would have asked SRC views which would have then informed the taxpayer that construction of residential dwelling being an exempt supply, no input tax can be claimed.

<u>Example 2:</u>
A taxpayer reports on his business tax return information extracted from his financial statements prepared by a firm of accountants. The financial statements contained some mistakes. A taxpayer who relies on information prepared by an expert will generally have taken reasonable care unless they should reasonably have known that the information was incorrect.

<u>Example 3:</u>
A taxpayer receives a tax invoice from a supplier which shows that VAT was not charged on a taxable supply of goods. The taxpayer cannot reasonably rely on the accuracy of the tax invoice, knowing that the supply of goods should be subject to the VAT.

(4) The class of persons concerned

SRC will look at the level of complexity of the tax affairs of the entity depending on the group or class of taxpayers it belongs to. The more complex the transactions entered into by the taxpayer are, the more onerous the tax obligations are and therefore the higher expectations of reasonable care.

28. *(5) Using a tax agent*

29. To use the services of a tax agent or other accounting professional does not discharge the taxpayer from taking reasonable care in ensuring that the tax agent is provided with all facts and elements necessary to the tax agent for them to perform their job correctly.

Example 1:

A taxpayer who did not draw the attention of his tax agent on interest income being derived recently will be considered as not satisfying the test of reasonable care.

(7) Whether the taxpayer has in place appropriate record-keeping system and other procedures ensuring that the income and expenditure is properly recorded.

30. The reasonable care standard does not require any entity to guard against every conceivable shortfall amount. If a taxpayer's accounting systems and internal controls are appropriately designed and monitored to ensure that the likelihood of error is reduced to an acceptable level, this will be consistent with taking reasonable care. Some examples of practices that will satisfy SRC appropriate procedures are in place include where the taxpayer undertakes regular internal audits, sample checks, provides adequate training to staff and have instruction manuals at the staff disposal to ensure accurate data reporting.

31. As not all businesses are the same, factors such as the size and nature of the business will be taken into consideration in determining what is sufficient in any given case.

Example 1:

An employee of a large business makes a mistake of Sr100,000 in transferring figures from the accounts to the VAT return. The accounting system of the business does not have any checks and safeguards against errors. The reasonable care test is not satisfied.

Example 2:

A sole-trader who owns and runs a Patisserie attempts to record all sales in a cashbook but he sometimes forgets to record some sales due to long working hours. He completes and lodges his own tax return. An SRC audit of the tax return reveals the false and misleading statement of incorrect sales revenue leading to a revenue shortfall. By failing to record sales carefully and not having proper controls in place, the sole trader has not taken reasonable care.

Example 3:

A small business operates electronic point of sale equipment, but poorly trained cashiers often forget to use the system properly. The owner tries to account for sales not shown in the point of sale equipment but an audit shows the business did not report all its sales for the year. Even though the taxpayer tried to account for unrecorded sales, he failed to take reasonable care to ensure the business records are properly maintained.

(8) The size of the shortfall amount

32. Where a false or misleading statement results in a shortfall, the size of the shortfall or percentage of the shortfall to the overall tax payable will indicate magnitude of the risk involved in making the statement. In cases involving a higher amount of tax or a large percentage of the overall tax payable the taxpayer must exercise a higher standard of care because the consequences of an error are greater.

    Example:
    A taxpayer with a turnover of over Sr 10 million has in place a payment approval system which processes every expense payment of over Sr 100. Payments less than Sr 100 are processed by hand with a less stringent approval system. During an audit, the auditor found a small number of deductions erroneously claimed at Sr 90. The SRC would consider the taxpayer had taken reasonable care in maintaining its payment systems.

Meaning of recklessness as to the operation of a revenue law

33. "Recklessness" means a conduct that is more culpable than a failure to take reasonable care but less culpable than an intentional disregard of a taxation law. "**Recklessness goes beyond inadvertence and is gross carelessness.** As opposed to the failure to take reasonable care, which applies to someone who falls short of standard, a taxpayer being reckless is a taxpayer who **falls significantly short of standard**.

34. In order to ascertain that a taxpayer has been reckless, there must be the presence of conduct that falls significantly short of standard of a reasonable person in the same position.

35. The intention of the taxpayer will not be taken into account for the determination of recklessness. The test for establishing whether a taxpayer has taken reasonable care fulfilling its tax obligations will be the same for recklessness; however, the degree to which the conduct of the taxpayer falls below the standard required from a reasonable ordinary person is the key.

36. The SRC will look at how a reasonable person in a similar situation would have acted and whether the behaviors exhibited by the taxpayer show a gross indifference to the application of revenue laws.

37. Like for the reasonable care test, each case has to be viewed on its own particular facts and special circumstances.

    Example 1:
    A taxpayer is informed by his tax agent that an amount cannot be claimed as a deduction in its business tax return. The taxpayer nevertheless instructed the tax agent to include the amount as a deduction in

the return. In making the statement, the taxpayer showed a reckless disregard for the correct application of revenue law when a tax professional had previously informed him his decision may not be correct.

Example 2:
The manager and staff of a busy stationary company "Seytionary Pty Ltd" are too busy to carry out a stock take at year's end. Instead, they estimate the value of the stock and record that figure in the accounts. An SRC audit of Seytionary's tax return reveals the estimate causes a revenue shortfall and is thus a false and misleading statement.

The Stationary company has shown a disregard or indifference toward the foreseeable consequences of their actions or inactions and would be considered reckless.

Meaning of intentional disregard of a revenue law

38. The additional tax applied for intentional disregard of the revenue law is the highest imposed under section 44A of the Revenue Administration Act.

39. Unlike the objective test which applies to determine whether there has been a lack of reasonable care or recklessness, the test for intentional disregard is purely subjective in nature. The actual intention of the taxpayer is the critical element.

40. Intentional disregard means that there must be actual knowledge that the statement made is false. The taxpayer must know the correct interpretation of the revenue law and intentionally decide to ignore it.

41. In order to prove the intentional element, dishonesty has to be demonstrated. Evidence must be found through direct evidence and analysis of all surrounding circumstances.

Example 1:
A taxpayer was audited and upon its completion was advised by the SRC that they had incorrectly applied the revenue law and particular deductions claimed were disallowed. The SRC subsequently reviewed the taxpayer's tax affairs a year later to find that the taxpayer continued to claim the same deductions contrary to the law. The taxpayer has acted with intentional disregard.

Example 2:
A business owner claimed several hotel stays as deductions for his business. During an audit when questioned he advised that these expenses were incurred on business travel to meet clients and garner business. Subsequent information was obtained that contradicted his statement, and confirmed that

the hotel stays were for him and his family with no business use at all. The taxpayer has acted with intentional disregard.

Date of effect

42. This ruling applies from the 08th July 2015, date of entry into force of the Revenue Administration Act as amended by Act 4 of 2015. This penalty regime will apply in relation to:
    - Business tax for the 2015 and later tax years
    - Other taxes covered under the Revenue Administration Act 2009 (RAA 2009) whereby lodgement/declaration has to be made on a monthly basis; from 8 July 2015 going forward.

    Note: Assessments raised under section 9 of the RAA 2009 for earlier years for business and other taxes will be subject to section 44 A (2) (b) penalty of 75% from 8 July 2015.

Any enquiry in relation to this Public Ruling can be addressed to the Seychelles Revenue Commission, P.O Box 50, Maison Collet, Republic of Seychelles.