ABC of tax authority’s thematic reviews (1) (2/35/20)

Under the Taxes and Duties Act and the State Revenue Service (“SRS”) Act, the tax authority has a wide range of tasks and responsibilities in tax administration. The SRS monitors the economic and financial activities conducted by all entities and individuals and enforces compliance with the tax laws. To fulfil its statutory responsibilities, the SRS carries out various control measures, from ones that can go unnoticed by the taxpayer until a certain moment to serious inspections requiring the taxpayer’s presence. This article explores thematic reviews as well as their substance, key aspects, and expected outcomes.

The substance and reasons

Section 1(17) of the Taxes and Duties Act defines a thematic review (“TR”) as a control measure the SRS conducts to verify a taxpayer’s compliance with certain rules, to examine certain accounting documents against the accounting information held by parties to the transaction, and to conduct other checks which do not lead to additional taxes being assessed.

The law defines the control measure and identifies its subject matter but does not prescribe how tax inspectors should proceed. Their conduct during a TR is based on their general rights and obligations. As part of the TR, the SRS monitors how the taxpayer complies with laws and regulations and keeps books, but the TR does not aim to determine whether the right amount of tax has been paid. According to the SRS, a TR is carried out to detect and prevent any commercial and financial irregularities and to ensure compliance with procedures for documenting and moving goods, procedures for recording revenues and expenses, and accounting and trading rules.

The SRS can start a TR for various reasons. It is possible that their computerised taxpayer risk analysis system has designated you as an entity subject to inspection because you have picked up a sufficient number of risk points that indicate a risk of tax evasion. An inspection can be caused by the company’s part in a chain of transactions if the SRS is checking all the parties to that chain. It is possible that the SRS has received a statement from an organisation or a complaint from an individual. You can guess the real reasons only from the items being inspected, the questions asked by tax inspectors, and other details.

The TR requires the taxpayer to mobilise their resources and make preparations. An easy-going attitude will lead to an unpleasant outcome. It is advisable to organise an internal audit on the subject matter of the TR before tax inspectors arrive. A taxpayer that has found mistakes in their business or accounting documentation when preparing for the beginning of a TR will be allowed to correct them, thereby reducing the scope of the TR and potential adverse consequences on its completion. For example, in one case, a taxpayer analysed the transactions to be examined by the SRS during a TR and decided to adjust the VAT returns and remove a few transactions. As a result, tax inspectors no longer had queries about those transactions and did not ask to see their documentation during the TR.

Irregularities can also be eliminated during a TR. In another TR, for example, tax inspectors found that supporting documents did not contain a particular accounting entry, but during the TR the taxpayer corrected the error and submitted documentary evidence of the required entry. This fact was later noted in the TR memorandum.

TI proceedings

The beginning of a TR and how the taxpayer is notified will depend on the reason why the SRS has decided to launch the TR. If the SRS wishes to catch the taxpayer off guard, the first step of the TR could be surveying the company or doing mystery shopping. In other cases, the SRS will send a TR notice informing the taxpayer of the date and place of the TR, as well as what accounting documents should be submitted.

The taxpayer can ask the SRS to postpone the start date of the TR if there is a good reason. For example, in one case, a TR was scheduled in summer, when the company's director and chief accountant were on leave, and the SRS were asked to allow for this because the presence of those persons is necessary during the TR, with attached documents confirming their absence. The beginning of the TR was postponed until two weeks later.

Most TRs take place at the company's registered office because that is (should be) the company's main centre housing its officers who can provide necessary explanations and its accounting documents. But this is not always possible. For example, if books are kept by an accounting service provider, the TR can also be held at their office because free access to the documentation is key. Some taxpayers might not even have an office because their business does not need one. In that case, it can be arranged for the TR to be held at another place, such as a lawyer's office or the SRS building. Tax inspectors usually agree to change the venue if the taxpayer explains why the registered office is not appropriate.

At the appointed time, tax inspectors will arrive at the agreed place (or the company's representatives will arrive at the SRS building) to start a TR.

During any meeting, tax inspectors will offer to make an audio recording of the interview and will ask the taxpayer's consent. In case of refusal, a statement will be drawn up, to be signed by the taxpayer or an authorised person. Taxpayers refuse to make an audio recording mostly for fear of accidentally providing evidence against themselves, for example, by giving inaccurate or erroneous explanations or by revealing too much. Tax inspectors recognise that in giving a true picture of the meeting, an audio recording also protects them against false complaints about irregularities or steps taken during the TR which the taxpayer claims to be unlawful.

(to be completed in our next Flash News)