

An analysis of the current framework for the exchange of taxpayer information, with special reference to the taxpayer in South Africa's constitutional rights to privacy and just administrative action

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ABSTRACT

Internationally, as well as in South Africa, legal reform aimed at increasing taxpayer information transparency has gained momentum over the past few years, especially in the light of the G20 led Base Erosion and Profit Shifting ('BEPS') Project. Ensuring that the fundamental rights of the taxpayer, guaranteed by the Constitution¹, remain protected amidst the hurried implementation of these reforms is of paramount importance and cannot be overlooked or deferred.

To a great extent, the question as to whether the current rules, regulations, and practices surrounding exchange of taxpayer information in South Africa would pass constitutional muster has, as yet, gone unasked and unanswered in academic literature.

This minor dissertation seeks to identify and analyse the constitutional questions raised by these existing rules and practices, with special reference to the constitutional rights of taxpayers in South Africa. Specifically, the current framework for both the automatic exchange of information and exchange upon request is considered in the context of two constitutional rights, namely the right to privacy and the right to just administrative action, with due recognition of the general limitation of rights provided for in the Constitution.

Importantly, this paper does not dispute the need for exchange of taxpayer information in principle, nor the desirability of effective tax administration. It is furthermore appreciated and acknowledged that a balance must be struck between the often competing interests of the South African Revenue Service ('SARS') as an administrator seeking to discharge its mandate in the most efficient manner possible, and the fundamental rights of the taxpayer.

The key finding arising from the research presented in this minor dissertation is that the constitutional rights of privacy and just administrative action of taxpayers enjoy limited and often no protection during the exchange of information process in South Africa. This is due to an underdeveloped legal framework and the current practices of the SARS that do not always respect the constitutional framework in the exchange of information process.

Although the SARS is enabled by legislation to exchange taxpayer information in accordance with South Africa's tax treaty obligations, the manner in which this is done and the protection afforded to the taxpayer during the exchange process is a separate matter. The SARS, in its actions, from whatever source it derives its authority, must stay within the bounds of the playing field as determined by the Constitution.

Following the analysis of the current protection afforded to taxpayers, as described above, this dissertation finally endeavors to provide recommendations where deficiencies in the current exchange of information framework are identified - be it through amendments to legislation or the conduct of the SARS in practice.

¹ Any reference in this document to "the Constitution" (or similar reference) refers to the Constitution of the Republic of South Africa (1996), including the Bill of Rights contained therein.

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CHAPTER 1: INTRODUCTION

1.1 Background and objectives of this paper

To a great extent, the question as to whether the current rules, regulations, and practices surrounding exchange of taxpayer information in South Africa would pass constitutional² muster has, as yet, gone unasked and unanswered in academic literature.

The South African government has repeatedly expressed and demonstrated its commitment to advancing the movement for greater transparency in the international tax arena – specifically in promoting the exchange of taxpayer information. This position was affirmed in the first interim report on base erosion and profit shifting ('BEPS') released by the Davis Tax Committee for public comment.³ The "[c]ompliant" rating assigned to South Africa in the combined first and second phase Global Forum Peer Reviews is indicative of South Africa's endeavours to ensure compliance with international best practice.⁴ South Africa's ever expanding network of tax treaties containing exchange of information mechanisms covers more than 90 jurisdictions.⁵

In South Africa, tax treaties are domesticated and become part of domestic tax legislation. In terms of this legislation, the competent authority, as part of the South African Revenue Service ('SARS'), enjoys broad authority and is granted extensive investigative powers. This includes the authority to gather information for the purpose sharing it with other States' competent authorities (in accordance with South Africa's treaty obligations).

Although the SARS has been afforded these powers by the relevant enabling legislation and is allowed a certain degree of discretion in the manner in which it conducts itself, all these powers remain subservient to the Constitution - which means that *"any law or conduct that is not in accordance with the Constitution, either for procedural or substantive reasons, will ... not have the force of law"*.⁶ The SARS, in its actions, from whatever source it derives its authority, must stay within the bounds of the playing field as determined by the Constitution.

² Any reference in this document to "the Constitution" (or similar reference) refers to the Constitution of the Republic of South Africa, 1996, including the Bill of Rights contained therein.

³ The Davis Tax Committee was called into being in 2013 by the then Minister of Finance and charged with *"assess[ing][South Africa's] tax policy framework and its role in supporting the objectives of inclusive growth, employment, development and fiscal sustainability"* – which includes evaluating the South African tax regime in the light of base erosion and profit shifting.

⁴ Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: South Africa 2013: Combined: Phase 1 +Phase 2, incorporating Phase 2 ratings, OECD Publishing, November 2013, p. 8, [cited 2016 Feb 14] available online from <<http://dx.doi.org/10.1787/9789264205901-en>>.

⁵ Ibid, p. 9.

⁶ Currie, I., and De Waal, J., *The Bill of Rights Handbook*, 6th edn. (Cape Town: Juta & Co. Ltd, 2014), p.9.

The cornerstone of the Constitution is the Bill of Rights, which enshrines the rights of all people in South Africa (both natural, and corporate), and applies also to persons who are not citizens. As such, the Bill of Rights is *“the principal source of substantive constraints on public power”*.⁷

The aim of this paper is to analyse, in light of existing South African constitutional law, both automatic exchange of information (‘EoIA’) and exchange upon request (‘EoIR’) in the context of two fundamental rights (as expressed in the Bill of Rights), namely the right to privacy⁸ and the right to just administrative action.⁹

In South Africa, constitutional rights and freedoms are not absolute.¹⁰ The Bill of Rights includes a general limitation provision by virtue of which any fundamental right may be restricted. Critically, however, this infringement may only be made in terms of law of general application to the extent that the limitation is *“reasonable and justifiable in an open and democratic society based on human dignity, equality, and freedom, taking into account all relevant factors”*.¹¹

The hurdle that must be cleared before lawfully limiting any of the fundamental rights is meant to be a high one.

The analysis will therefore also consider the questions raised by the limitation of rights clause in the context of the taxpayer’s right to privacy and just administrative action in the exchange of information (‘EoI’) process.

Internationally, as well as domestically in South Africa, projects aimed at increasing transparency in tax matters have gained momentum over the past few years, especially in the light of the G20 led BEPS project. Ensuring that the constitutionally guaranteed rights of the taxpayer remain protected amidst the hurried implementation of these reforms is of paramount importance and cannot be overlooked or deferred.

This paper hopes to take an initial step in identifying and analysing the constitutional questions South Africa currently faces in light of its existing treaty obligations to exchange taxpayer information. Where it is found that there are shortcomings in the manner or extent to which the taxpayer’s right to privacy and just administrative action have been effected (either in legislation or in the conduct of the SARS in practice), recommendations will be put forward on how these shortcomings may be addressed.

⁷ Ibid, p. 23.

⁸ Section 14 of the Constitution.

⁹ Section 33 of the Constitution.

¹⁰ Currie and De Waal, p. 150.

¹¹ Section 36 of the Constitution.

1.2 Research question and scope

This dissertation aims to identify and analyse the South African constitutional aspects raised by the protection currently afforded to taxpayers during the EoI process. The analysis will be confined to the protection of the taxpayer's fundamental rights to privacy and just administrative action.

1.3 Research method

In this paper, the research question is addressed and a conclusion is reached through an analysis of the relevant primary legislation, specifically the South African Constitution, the Income Tax Act No. 58 of 1962, the Tax Administration Act No. 28 of 2011, the Promotion of Administrative Justice Act No. 3 of 2001, the Protection of Personal Information Act No. 3 of 2013, as well as South African case law and the relevant statutory provisions. The analysis also draws on selected secondary sources, including foreign case law, EU law, various OECD¹² publications and model treaties and their commentaries, and publications by various South African and international researchers.

1.4 Structure of this paper

Chapter 2 of this paper sets out the current EoI landscape in South Africa, including the legal basis for EoI, as well as the protection currently afforded to taxpayers in practice.

Because the fundamental rights set out in the Bill of Rights are not absolute, but are subject to the general limitation provisions of section 36 of the Constitution, Chapter 3 provides further analysis of the limitation provision and its interaction with the rights contained in the Bill of Rights.

Following the introductory chapters, this paper is divided into two main chapters, namely Chapter 4: The Right to Privacy and Chapter 5: The Right to Just Administrative Action.

In both these chapters a short introduction is provided of the relevant fundamental right and the key principles established therein, including references to relevant pieces of enabling legislation and relevant case law. These principles are then applied to the current protection afforded to taxpayers in the EoI process in general – *i.e.* from the basic starting point that the SARS is distributing taxpayer information to foreign competent authorities. Questions raised as part of this analysis would apply to both EoIR and EoIA. Following this broad analysis, certain questions raised that are unique to either EoIA or EoIR will be addressed separately at the end of each chapter, where relevant.

The final chapter sets out conclusions drawn from the analysis in the preceding chapters as well as a number of recommendations to address the identified shortcomings.

¹² The Organisation for Economic Cooperation and Development (the 'OECD').

CHAPTER 2: EXCHANGE OF INFORMATION IN SOUTH AFRICA AND THE PROTECTION CURRENTLY AFFORDED TO TAXPAYERS IN PRACTICE

2.1 EoI in South Africa: the legal basis for the cross-border exchange of taxpayer information

2.1.1 General comments

South Africa has signed and ratified a number of multilateral and bilateral agreements containing EoI mechanisms, including the Convention on Multilateral Administrative Assistance in Tax Matters and Amending Protocol.¹³

In terms of bilateral agreements, most of South Africa's double tax treaties currently in force (currently over 90) contain some form of EoI article,¹⁴ with 13 tax information exchange agreements ('TIEA') currently in force.¹⁵

Section 231 of the Constitution, read with section 108 of the Income Tax Act¹⁶ ('ITA') provides that once a treaty entered into by the National Executive is approved by Parliament and published in the *Government Gazette*, the provisions of said treaty will have the same effect as if they were enacted in terms of the ITA. In other words, the provisions of the treaties are placed on level footing with domestic law.¹⁷

The majority of South Africa's treaties containing an EoI mechanism include wording similar to that of the OECD Model treaty. Depending on the age of the treaty (and the version of the OECD Model it is therefore based on), the treaty will enable the SARS to share taxpayer information with the competent authority of the treaty partner that is either 'necessary' (pre-2005 OECD Model treaties) or 'foreseeably relevant' for carrying out the provisions of the treaty or of the domestic laws of the two States.

The EoI clauses contained in the international agreements mentioned above form the legal basis for both EoIR and EoIA (with the exception of the TIEAs – which cater only for EoIR). Please refer to the section that follows for further detail regarding the specific mechanisms in place enabling EoIA, including 'FATCA', and the OECD EoIA instruments.

In South Africa, chapter 5 of the Tax Administration Act¹⁸ ('TAA') provides the SARS with far-reaching information gathering powers. The TAA also makes specific provision for EoI in pursuance of South Africa's treaty obligations in section 3(3):

¹³ According to the OECD's records, South Africa submitted its instruments of ratification on 21 November 2013, with the treaty entering into force on 1 March 2014.

¹⁴ Roeleveld, J. and West, C., "South Africa", in: International Fiscal Association, 2013 Copenhagen Congress, Cahiers De Droit Fiscal International, "Exchange of Information and Cross-Border Cooperation between Tax Authorities", Volume 98b, p. 687.

¹⁵ SARS, [cited 2016 Feb 14] available online from < <http://www.sars.gov.za/Legal/International-Treaties-Agreements/Pages/Document-Results.aspx>>.

¹⁶ Income Tax Act No. 58 of 1962.

¹⁷ Roeleveld and West, p. 687.

¹⁸ Tax Administration Act No. 28 of 2011.

“(3) If SARS, in accordance with an international agreement –

(a) received a request for, is obliged to exchange or wishes to spontaneously exchange information, SARS may disclose or obtain the information for transmission to the competent authority of the other country as if it were relevant material required for purposes of a tax Act and must treat the information obtained as taxpayer information.”

The SARS is therefore in principle empowered, by law, to gather, and then exchange taxpayer information internationally. The manner in which it does so, and how the taxpayers’ rights are protected in this process is, however, a separate matter entirely.

2.1.2 Specific considerations surrounding the legal basis for EoIA in South Africa

A brief background to the implementation of the United States (‘US’) Foreign Account Tax Compliance Act (‘FATCA’) and the OECD’s EoIA model instrument is provided below.

To implement the FATCA reporting framework in South Africa, the South African and US governments have entered into an inter-governmental agreement (‘IGA’). This IGA (as an ‘international agreement’ per the TAA) would require South African financial institutions to report specified information surrounding the accounts held by so-called ‘specified US persons’ or passive entities controlled by ‘specified US persons’ to the SARS on an annual basis. This information is then shared with the US by the SARS in accordance with Article 26 of the 1997 SA-US double tax treaty.¹⁹

The IGA entered into force in South Africa on 28 October 2014. The affected South African financial institutions were required to report the necessary financial information on its US account holders to the SARS in June 2015, with the SARS exchanging the information with the US Treasury by September 2015.

South Africa is also a so-called ‘early adopter’ of the OECD’s EoIA Model instrument.

The OECD’s EoIA Model instrument consists of a Competent Authority Agreement (‘CAA’) and Common Reporting Standard (‘CRS’), collectively referred to in this paper as the ‘OECD Standard’. The OECD Standard requires the bulk automatic exchange of taxpayer information between the signatories of the agreements.

This instrument is largely based on the FATCA IGA entered into between South Africa and the US and, accordingly, entails similar reporting requirements on the part of South African financial institutions and the SARS.

In order to identify accounts that should be reported to the SARS under either FATCA or the OECD Standard, financial institutions must carry out certain due diligence procedures to detect reportable accounts. These procedures would include a search of electronic records for the presence of at least one

¹⁹ The SA-US IGA is based on the Model 1 agreement. The Model 2 agreement, which would see the direct exchange of information with the US revenue authorities by the relevant foreign financial institutions, is not discussed further.

of a list of predefined indicia. The presence of one of the indicia would then serve as an indication that the account holder is a tax resident of another country. For example, these markers include instances where the account holder has a telephone number in the other State, and no telephone number in South Africa, and where the account holder has a mailing or residential address in the other State. The EoIA instruments do not provide for any tie-breaker test: the information must be shared with each jurisdiction for which an indicium has been identified.

As is the case with the FATCA IGA, the legal basis for exchange remains the EoI clause in the applicable double tax treaty (or the Convention on Multilateral Administrative Assistance in Tax Matters). A key difference between the FATCA IGA entered into with the US and the OECD Standard, however, is that the CRS provides for reciprocal exchange whereas the FATCA IGA entails a one-directional flow of information to the US.²⁰

In 2015, South Africa, in accordance with its commitments as an 'early adopter' of the OECD Standard, proposed and later enacted amendments to the TAA that enable and require South African financial institutions to report the necessary information in the prescribed form to the SARS for cross-border exchange,²¹ with the first exchange taking place in 2017. The financial institutions will be required to report information on all account holders irrespective of whether the country that the indicium points to is a treaty partner of South Africa or not.²² The SARS will then collate the information received from the financial institution and transmit the data to those countries with which the necessary treaties and agreements are in place.²³

In South Africa, the SARS, as well as National Treasury, have expressed their support of the movement towards greater tax transparency and the view that EoIA is an indispensable tool in achieving this. As stated in a briefing note addressing the adoption and implementation of the OECD Standard in South Africa released by the SARS²⁴, and echoed in the Explanatory Memorandum to the 2015 Tax Administration Laws Amendment Bill:²⁵

²⁰ During the International Fiscal Association ('IFA') 2015 Basel Congress, it was indicated that US domestic law will not allow for the US to participate in the automatic exchange of taxpayer information on a reciprocal basis. However, on 2 October 2015, the IRS released a statement (see IR-2015-111) in which it announced that the information exchange with certain, unspecified nations, will now be on a reciprocal basis. It is not clear whether South Africa is included in this group.

²¹ Tax Administration Law Amendment Act No. 23 of 2015.

²² Memorandum on the Objects of the Tax Administration Laws Amendment Bill, 2015, par. 2.33, [cited 2016 Feb 14] available online from < <http://www.sars.gov.za/AllDocs/LegalDoelib/ExplMemo/LAPD-LPrep-EM-2015-02%20-%20Memorandum%20on%20the%20objects%20of%20TALA%20Bill%20of%20%202015.pdf>>.

²³ "Automatic exchange of information, what it is, how it works, benefits, what remains to be done", OECD, 2012, p. 9, [cite 2016 Feb 16] available online from < <http://www.oecd.org/tax/exchange-of-tax-information/automaticexchangeofinformationreport.htm>>.

²⁴ SARS, Briefing Note: Implementing the Common Reporting Standard in South Africa in terms of Regulations under The Tax Administration Act, 2011, [cited 2016 Feb 14] available online from < <http://www.sars.gov.za/AllDocs/LegalDoelib/Drafts/LAPD-LPrep-Draft-2015-62%20-%20Briefing%20Note%20on%20Common%20reporting%20standard%20TAA.pdf>>.

²⁵ Memorandum on the Objects of the Tax Administration Laws Amendment Bill, 2015, par. 2.33, [cited 2016 Feb 14] available online from < <http://www.sars.gov.za/AllDocs/LegalDoelib/ExplMemo/LAPD-LPrep-EM-2015-02%20-%20Memorandum%20on%20the%20objects%20of%20TALA%20Bill%20of%20%202015.pdf>>.

“Greater transparency and the automatic exchange of information between tax administrations is an important step forward in countering cross border tax evasion, aggressive tax avoidance and base erosion and profit shifting (BEPS) through, for example, transfer pricing arrangements”.

2.2 The current protection afforded to taxpayers during the EoIR and EoIA process in practice

In terms of EoIR, it is not the SARS’ practice to notify the relevant taxpayer upon receiving an information exchange request from another State. Taxpayers are not afforded the opportunity to make any representations during the exchange process, nor are they informed of the exchange after the fact.

Similarly, under FATCA (EoIA), the affected persons whose private financial information is transferred by the financial institutions to the SARS, and then on-sent to the US, are not informed of either transfer (not beforehand, nor after the fact), nor are they given the opportunity to object or make representations prior to the exchange.

Although not yet effective, it is expected that the rights afforded to taxpayers in practice under the OECD Standard in South Africa will be substantially similar to those under the FATCA IGA regime.

The EoI clauses of the various tax treaties also afford the taxpayer some protection. For example, the information to be exchanged is limited to that ‘necessary’ or ‘foreseeably relevant’ to the enforcement of the contracting States’ tax laws. The treaties would also typically contain provisions dealing with the confidentiality of the information exchanged. These measures are discussed in further detail in the chapters that follow.

CHAPTER 3: LIMITATION OF RIGHTS

Section 36 of the Constitution

“(1) The rights in the Bill of Rights may be limited only in terms of law of general application to the extent that the limitation is reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom, taking into account all relevant factors, including –

(a) the nature of the right;

(b) the importance of the purpose of the limitation;

(c) the nature and extent of the limitation;

(d) the relation between the limitation and its purpose; and

(e) less restrictive means to achieve the purpose.

(2) Except as provide in subsection (1) or in any other provision of the Constitution, no law may limit any right entrenched in the Bill of Rights”. [Emphasis added]

3.1 Introduction

The rights afforded to the taxpayer in the Bill of Rights are not absolute and are subject to the general limitation of rights provisions of section 36 of the Constitution. Consequently, should any of the taxpayer’s rights be restricted, the restriction will only be constitutional if the hurdles set in place by section 36 are cleared.

An analysis into the constitutional questions raised by the current rules and practices surrounding the protection of taxpayer rights in the EoI process in South Africa can therefore not merely address sections 14 (the right to privacy) and 33 (the right to just administrative action) of the Constitution in isolation, but should also extend to the questions raised by the general limitation provision.

Before proceeding with a discussion of the fundamental rights to privacy and just administrative action, this chapter considers the requirements that must be met before a limitation of the taxpayer’s rights can be determined to be lawful.

A look into the workings of the provisions of section 36, in the context of EoI, will be broken down into the following components:

- What is meant by a ‘law of general application?’
- What is meant by ‘reasonable and justifiable’ (in the light of the ‘relevant factors’ listed in section 36)?

3.2 The general limitation provision in the context of the protection of taxpayer rights in EoI

3.2.1 The limitation of rights in terms of a 'law of general application'

In order for a limitation of any of the taxpayer's fundamental rights to be considered to be constitutional, that limitation must have been done in accordance with a law of general application.

It would appear as though the term 'law' would include all forms of legislation (delegated or original), as well as common law and customary law.²⁶ Importantly, however, the public policy or practice of an organ of State, such as the SARS, will not qualify as 'law'.²⁷ Also, administrative action taken under the authority of law does not in itself qualify as a law of general application.²⁸

The 'law' must also be general in its application. That is to say, it must apply equally to all, impersonally, and must be clear, accessible, and precise enough to allow all those affected to understand their rights and obligations. The 'law of general application' requirement therefore guards against arbitrary action against individuals or groups. Ackerman J in the *S v Makwanyane* case held that: "*Without such a rational justifying mechanism, unequal treatment must follow*".²⁹

An empowering provision will not be considered to be of 'general application' if it merely grants an administrator wide discretionary powers.³⁰ Legislation conferring discretionary powers on administrative officials (such as the SARS) must also include constraints and guidelines on the proper exercise of this power.³¹ In the *Dawood* case (in the context of the broad discretionary powers afforded to immigration officials by the Aliens Control Act 96 of 1991), the court ruled as follows:³²

"It is an important principle of the rule of law that rules be stated in a clear and accessible manner. It is because of this principle that section 36 requires that limitations of rights may be justifiable only if they are authorized by a law of general application. Moreover, if broad discretionary powers contain no express constraints, those who are affected by the exercise of the broad discretionary powers will not know what is relevant to the exercise of those powers or in what circumstances they are entitled to seek relief from an adverse decision. In the absence of any clear statement to that effect in the legislation, it would not be obvious to a potential applicant that the exercise of the discretion conferred upon the immigration officials ... by [the Aliens Control Act] is constrained by the provisions of the Bill of Rights, and in particular, what factors are relevant to the decision to refuse to grant or extend a temporary permit. If rights are to be infringed without redress, the very purposes of the Constitution are defeated."

²⁶ Currie and De Waal, p. 156.

²⁷ See *Hoffmann v South African Airways* 2001 (1) SA 1 (CC), para. 41.

²⁸ Currie and De Waal, p. 161.

²⁹ *S v Makwanyane* 1995 (3) SA 391 (CC), para. 156.

³⁰ Currie and De Waal, p. 161.

³¹ *Ibid.*

³² *Dawood v Minister of Home Affairs* 2000 (3) SA 936 (CC), para. 47.

In order for a limitation of a person's fundamental rights to be in accordance with a law of general application, it cannot, therefore, be left simply to the administrative official to decide, without constraint, when and under what circumstances it would be justifiable to restrict that person's rights.

3.2.2 The 'reasonable and justifiable' limitation of rights

In essence, the requirement for a limitation to be reasonable and justifiable seeks to ensure that any law that restricts a fundamental right does so for reasons that would be acceptable in a free and fair democratic society. There must be a balance between the harm done by the restriction, and the benefits it is designed to achieve. This requirement for balance, or proportionality, was addressed in the *S v Makwanyane* case:³³

"The limitation of constitutional rights for a purpose that is reasonable and necessary in a democratic society involves the weighing up of competing values, and ultimately an assessment based on proportionality."

Section 36 includes a list of relevant factors that must be taken into account when determining whether the limitation was 'reasonable and justifiable' (*i.e.* whether there is a balance between the competing interests).

They are:³⁴

a) *The nature of the right.*

Not all fundamental rights are equal – some weigh more heavily than others.

b) *The importance of the limitation.*

In order for the limitation to be justifiable, it must serve a purpose that reasonable citizens will find compellingly important.

c) *The nature and extent of the limitation.*

The restriction of rights should not be more extensive than is warranted by the purpose that it seeks to achieve.³⁵

d) *The relation between the limitation and its purpose.*

There must be a causal link between the law, which restricts the rights, and the purpose it was designed to achieve. Importantly, unless this link is self-evident, appropriate evidence (such as statistical data)

³³ *S v Makwanyane* 1995 (3) SA 391 (CC), para. 104.

³⁴ Section 36 (1)(a)-(e) of the Constitution.

³⁵ Currie and De Waal, p.168.

must be presented to support the connection. A court cannot determine whether the limitation is reasonable or justifiable in the abstract.³⁶

e) *Less restrictive means to achieve the purpose.*

The law should not restrict a fundamental right more than is necessary to achieve its purpose. Therefore, if there is a less restrictive but equally effective measure available, that more balanced, or proportional approach will be preferred.

3.2.3 The lawful limitation of rights in the context of EoI

Any limitation of the taxpayer's rights during the EoI process will only be lawful should the criteria set out in section 36 of the Constitution be met.

The questions raised by the by the interaction between the limitation criteria and the right to privacy, and just administrative action in the context of EoI are analysed in further detail in Chapters 4 and 5, respectively.

3.3 Summary remarks

Critically, when determining whether the limitation of a person's fundamental rights is reasonable and justified (and therefore lawful) it must be understood that the hurdles put in place by section 36 for the lawful limitation of fundamental rights are necessarily high.

As perhaps best captured by Currie and De Waal:³⁷

"It must be emphasized that the existence of a general limitation section does not mean that the rights in the Bill of Rights can be limited for any reason. It is not simply a question of determining whether the benefits outweigh the cost to the right-holder. If the rights can be overridden simply on the basis that the general welfare will be served by the restriction then there is little purpose in the constitutional entrenchment of rights. The reasons for limiting a right need to be exceptionally strong. The South African Constitution permits the limitation of rights by law but requires the limitation to be justifiable. This means that the limitation must meet a purpose that most people would regard as compellingly important. But, however important the purpose of the limitation, restrictions on rights will not be justifiable unless there is good reason for thinking that the restriction would achieve that purpose it is designed to achieve, and that there is no other 'realistically available' way in which the purpose can be achieved without restricting right".

In the chapters that follow, the taxpayer's rights to privacy and just administrative action in the EoI process are analysed in light of this general limitation clause.

³⁶ Currie and De Waal, p.154.

³⁷ Currie and De Waal, p.152.

CHAPTER 4: THE RIGHT TO PRIVACY

Section 14 of the Constitution

“(1) Everyone has the right to privacy, which includes the right not to have –

a) their person or home searched;

b) their property searched;

c) their possessions seized; or

d) the privacy of their communications infringed.”

4.1 Introduction

Section 14 of the Constitution guarantees the right to privacy. The section contains two parts, namely a general right to privacy, and a specific list of prohibited infringements. Note that that the specific list of infringements forms part of the general right to privacy and does not limit or confine the general right to privacy to these specific examples.³⁸

In the context of taxation, the constitutional right to privacy is currently given effect to primarily in the TAA. In the context of EoI, the relevant international agreements themselves also contain provisions speaking to the confidentiality of the information exchanged. The questions raised by the protection afforded to taxpayers in practice, when viewed in the light of the provisions of section 14 of the Constitution (as given effect to in the TAA and international agreements), will be analyzed in further detail in the sections that follow.

Further to this, in 2013, Parliament enacted legislation specifically aimed at giving effect to the constitutionally guaranteed right to privacy, namely the Protection of Personal Information (‘POPI’) Act.³⁹ Although most sections of the POPI Act are not yet effective,⁴⁰ its provisions do raise a number of questions regarding EoI and the protection currently enjoyed by taxpayers in South Africa – questions that will become of great relevance once the provisions of the POPI Act become effective. The details of this piece of legislation and its interaction with EoI is therefore discussed in further detail in a separate section to this Chapter.

In terms of the taxpayers’ right to privacy, a useful starting point to the analysis would be a comparison of the protection afforded to taxpayers and their private information within the borders of the Republic (*i.e.* in a purely domestic context), with the protection enjoyed once the information crosses the country’s borders. Should there be any differences, the analysis will consider whether this amounts to a limitation of the taxpayer’s rights, and whether this limitation could be said to be ‘reasonable and justifiable’ and in

³⁸ Currie and De Waal, p.295.

³⁹ Protection of Personal Information Act No. 3 of 2013.

⁴⁰ As at 25 February 2016.

terms of 'a law of general application'. The comparison is based on the assumption that exchange of taxpayer information in a purely domestic setting meets with constitutional principles. It is beyond the scope of this paper to investigate the validity of this assumption, although it may be self-evident from the analysis that will follow.

4.2 The taxpayer's constitutional right to privacy in a domestic context, as given effect to by the TAA and international agreements

4.2.1 The taxpayer's right to privacy in a domestic context

4.2.1.1 The limitation of the taxpayer's right to privacy when disclosing information to the SARS

In South Africa, the taxpayer is obliged, by law, to submit an income tax return to the Commissioner. Given the very nature of income tax (a tax not purely based on some external manifestation of the taxpayer's wealth, such as land ownership or social class), this return will necessarily contain certain personal details of the taxpayer; details that he or she would arguably not voluntarily disclose, if given the choice.

By requiring taxpayers to disclose this information to the SARS, their right to privacy is infringed.⁴¹

In order to determine whether this infringement is lawful, the question therefore becomes whether this breach is justified and reasonable in a fair and open democratic society (as is required by section 36 of the Constitution).

The State is obliged to provide its citizens with certain services; services which are funded by taxes collected. In order for the SARS to carry out its mandate as the nation's revenue collections agency, it requires access to certain personal details of the taxpayer to ensure that the amount of income tax lawfully due has been paid. There is arguably no less intrusive way to do this other than to require the taxpayer to disclose certain facts to the SARS and to grant the SARS investigative powers where there is a concern that the information provided by the taxpayer is inaccurate or incomplete.

Moreover, once the SARS receives this private information from the taxpayer, it is subject to strict secrecy provisions. Chapter 6 of the TAA obliges the SARS to maintain the confidentiality of the taxpayer information with which it has been supplied.

This duty imposed on the SARS to preserve the secrecy of taxpayer information is a significant factor in ensuring that the limitation of the taxpayer's right to privacy is not excessive, bringing a sense of proportionality to the violation.

It is therefore commonly accepted, internationally, that it is a reasonable and justifiable limitation of the taxpayer's right to privacy (and, accordingly, is lawful in a South African context).

⁴¹ Croome, B., *Taxpayers' Rights in South Africa*, 1st edn. (Cape Town: Juta & Co. Ltd, 2010), p. 125.

4.2.1.2 The protection currently afforded to taxpayers in South Africa in terms of their right to privacy

As mentioned previously, a key contributing factor to the reasonableness of the intrusion on the taxpayer's right to privacy is the strict secrecy provisions that the SARS must adhere to in respect of the information supplied by the taxpayer.

Any erosion of this duty and obligation on the part of the SARS would be counterproductive to its core function as tax collector. Croome summarizes this principle as follows: ⁴²

"The underlying rationale of the secrecy provision in the Income Tax Act is to encourage taxpayers to make full and proper disclosure of their income to the Commissioner. The thinking is that the taxpayers would be uncomfortable about making full and proper disclosure of their personal financial affairs to the Commissioner if they knew that such information could readily be made available to third parties without good reason."

This view is in line with the judgement by Feetham JP in the *Silver v Silver* case: ⁴³

"For the purpose of the administration of the Income Tax Act, it is necessary that the fullest information should be available to the Department of Inland Revenue. If that information is to be obtained, there must be some guarantee as to the secrecy."

This obligation under the TAA to maintain the confidentiality of taxpayer information is, however, subject to certain limitations and exceptions.

'Taxpayer information' is widely defined in the TAA as being any information provided by a taxpayer or information obtained by SARS in respect of the taxpayer, including biometric information. ⁴⁴

The Commissioner is allowed, expressly by chapter 6 of the TAA, to disclose certain taxpayer information to specified third parties, such as the Statistician-General, the Governor of the South African Reserve Bank, and the Financial Services Board. ⁴⁵

The Commissioner may also disclose the confidential taxpayer information in his possession to the South African Police Service and National Prosecuting Agency ('NPA') if such information relates to a tax offence. ⁴⁶

⁴² Croome, p. 156.

⁴³ *Silver v Silver* 1937 NPD 129, paras. 134-135.

⁴⁴ TAA section 67(b).

⁴⁵ TAA section 70.

⁴⁶ TAA section 69(2)(a).

A 'tax offence' is defined as:⁴⁷

"an offence in terms of a tax Act or any other offence involving –

- a) fraud on SARS or on a SARS official to the administration of a tax Act; or*
- b) theft of moneys due or paid to SARS for the benefit of the National Revenue Fund."*

A 'tax Act', as defined, includes only South African tax legislation.

In other cases, *i.e.* those not relating to South African tax offences (including other criminal matters), such a disclosure may only be made provided that an order to do so has been granted by a judge in chambers following an *ex parte* application.⁴⁸

It remains difficult to balance the needs of the State in administering its tax laws, and the taxpayer's right to privacy. However, the fact that the approval of a judge in chambers is required before any confidential taxpayer information is disclosed to the NPA (in cases other than those involving South African tax offences) forms a significant component to the equilibrium struck between these competing interests. The judicial oversight places restraints on the SARS' authority and discretion in how it deals with taxpayer information, providing a degree of certainty to the taxpayer that the information shared with the SARS will not be arbitrarily disclosed to third parties within South Africa, based solely on the discretion of an administrative official.

In essence, the rules and regulations surrounding the safeguarding of taxpayer confidential information within the borders of South Africa, as spelled out in chapter 6 of the TAA, ensure that the authority and discretion afforded to the SARS are appropriately reigned in, and the violation of the taxpayer's rights are reasonable, and not excessive.

4.2.2 The taxpayer's right to privacy in South Africa in the context of EoI

4.2.2.1 The exchange of taxpayer information by the SARS and the TAA secrecy rules

Section 108 of the ITA read with section 231 of the Constitution authorizes the Executive to enter into treaties for the avoidance of double taxation with foreign governments. Once these agreements have been approved by Parliament and published in the *Gazette* they have the same effect as if they were enacted in the ITA.

Specifically, section 108(5) of the ITA provides for the relaxing of the secrecy provisions surrounding taxpayer information in the context of South Africa's obligations per its treaty network:⁴⁹

⁴⁷ TAA section 1.

⁴⁸ Klue, S., Arendse, JA., and Williams, RC., *Silke on tax administration*, 1st edn (LexisNexis, 2015), at § 3.16, and TAA section 71.

⁴⁹ ITA section 108(5).

“The duty imposed by any law to preserve secrecy with regards to such tax shall not prevent the disclosure to any authorized officer of the... [other contracting State], of the facts, knowledge of which is necessary to enable it to be determined whether immunity, exemption or relief ought to be given or which it is necessary to disclose in order to render or receive assistance in accordance with the [treaty]”.

It is interesting to note that the wording of this particular provision of the ITA has not changed significantly over the past 40 years (with the coming into force of the 1996 Constitution having no effect).⁵⁰

Section 69(2)(b) of the TAA allows for the confidentiality provisions contained in chapter 6 of the TAA to be overridden by the provisions of other Acts (such as section 108(5) of the ITA).

Depending on the wording of the relevant treaty, the secrecy provisions of the TAA would therefore not prevent the SARS from exchanging tax information with its treaty partner where that information is ‘necessary’ or ‘foreseeably relevant’ for carrying out the provisions of the treaty or the domestic laws of either of the two States.

Importantly, although section 108(5) of the ITA would not permit the exchange of information to be refused solely on the basis of any domestic secrecy provision (such as bank secrecy rules and regulations) it should be borne in mind that the ITA cannot go so far as to unjustly or unreasonably limit the constitutional rights of the taxpayer. In other words, section 108(5) does not absolve the SARS from its duty to operate within the bounds of the Constitution.

As stated previously, although the SARS is empowered by law to exchange taxpayer information, it remains bound by the Constitution in the manner in which it does so and the protection afforded to taxpayers during the process.

4.2.2.2 In the context of their right to privacy, the protection currently afforded to taxpayers in South Africa in the EoI process

Tax treaties typically include wording that requires the contracting State receiving the information to ensure that the information received is treated in the same manner as information obtained under its own domestic legislation would be. In other words the secrecy provisions of the receiving State will apply, as opposed to those of the State supplying the information.

What procedures the SARS would perform to confirm the scope of the secrecy provisions of the receiving State, or the degree of confidentiality that the information will be afforded, in practice, is not clear. No information is publically available to provide insight as to whether at all, or to what extent, the protection afforded by the receiving State is compared or weighed against the protection afforded under South

⁵⁰ The last (minor) updates to the wording of section 108(5) were made in 1978 and 1997.

African law during the treaty negotiation process, nor is it known with any certainty whether the appraisal is performed before the information is later shared. There is currently no provision in the ITA or TAA that would oblige the SARS to carry out any such procedures before sharing the information.⁵¹

The OECD Peer Review report on South Africa merely states that “[w]hen a request is forwarded to a local revenue office, the confidentiality of the information is emphasized to ensure maximum awareness of the issue”.⁵²

As stated previously in Chapter 2, currently in South Africa, the ITA and TAA in effect places the decision to share taxpayer information purely at the discretion of the SARS.

The legal protection that must be afforded to taxpayers or the specific procedures that must be adhered to by the SARS in the disclosure of taxpayer information to foreign governments is not specifically dealt with in the TAA. Other possible exceptions (in a purely domestic setting) to the strict secrecy rules are spelled out in the TAA. No further specific rules or checks and balances are expressed in the TAA to constrain the SARS’ discretion in this regard. For example, no further guidance or restrictions are placed on the SARS when determining whether the information to be exchanged is ‘necessary’ or ‘foreseeably relevant’ for the enforcement of the contracting States’ tax laws.

It would appear, therefore, as though the protection afforded to taxpayers in South Africa in relation to exchanges with foreign revenue authorities is similar (but not identical) to that afforded to taxpayers when the SARS shares information with the NPA relating to domestic tax offences. In other words, the disclosure is made at the sole discretion of the SARS, with no need to obtain a ruling from a judge in chambers beforehand. These two instances are, however, clearly not comparable: the one (the sharing of information with the NPA) deals with criminality, and the other with investigation only.

It should be noted that specific rules and regulations are in place in the TAA surrounding the sharing of taxpayer information with the NPA. Section 43 of the TAA provides that before a criminal investigation can be pursued, the matter must first be referred to a senior SARS official who must make the final decision whether this course of action would be warranted. This oversight by a senior SARS official is not currently required by either the TAA or ITA in the EoI process.

It must be borne in mind that from a constitutional perspective, as discussed in Chapter 3, in order for a restriction of a person’s fundamental rights to be lawful, that limitation must have been done in accordance with a ‘law of general application’ (as required by section 36 of the Constitution). This will not be the case when the rights in question are limited in terms of an enabling provision granting an administrator wide, unconstrained discretionary powers. Should the taxpayer’s right to privacy be limited or restricted during the EoI process, the question arises whether the discretion afforded to the

⁵¹ Refer, however, to the discussion surrounding the POPI Act in a separate section to this chapter.

⁵² Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: South Africa 2013: Combined: Phase 1 +Phase 2, incorporating Phase 2 ratings, OECD Publishing, November 213, p. 73, [cited 2016 Feb 14] available online from <<http://dx.doi.org/10.1787/9789264205901-en>>.

SARS in determining when and how information is to be shared with the foreign country's competent authority is so broad and unconstrained by the TAA and ITA that it falls beyond the legal norm (*i.e.* a limitation 'in terms of a law of general application'). Should this be the case, the limitation would not be lawful.

4.3 The relaxation of the secrecy rules and the erosion of the reasonableness and proportionality of the violation of the taxpayer's right to privacy

As discussed previously, when taxpayers are obliged to disclose their private information to the SARS by way of assessment, their right to privacy is violated. This limitation, is, however, done in terms of a law of general application (namely the TAA), and is accepted to be reasonable and justifiable. The infringement of the taxpayer's right is therefore not unconstitutional.

The obligation on the part of the SARS to treat any taxpayer information it receives as strictly confidential (as per the secrecy provisions of chapter 6 of the TAA) is one measure that ensures that the violation of the taxpayer's right is not excessive – *i.e.* that there is proportionality between the harm done, and the purpose it sought to achieve.

The question therefore arises whether the current lack of protection afforded to taxpayers in the EoI process could be said to erode this proportionality to the point where the hurdles put in place by section 36 of the Constitution, namely the 'reasonable' and 'justifiable' criterion, are no longer cleared.

The question is complex, and one would be confronted with various arguments leaning one way or the other. For example, one would first have to agree on the weight this guarantee of confidentiality carries in the proportionality equation. Then it would have to be considered whether the confidentiality guarantee is at all affected by the transfer of the information, and if so, to what extent (given the confidentiality requirements included in the tax treaties).

In the context of the right to privacy, it can be argued that it would be fair for the protection afforded to taxpayers during the sharing of information with foreign governments to be on par with those surrounding information sharing during domestic investigations into tax offences.

The arguments in favour of this view would include the fact that, as is the case with South African tax investigations, the sharing of taxpayer information across borders is also part of a larger investigation, with no assessment having been issued. Moreover, the tax treaty would require the receiving competent authority to maintain the secrecy of the taxpayer information as it would had it obtained the information under its own domestic legislation. The maintenance of secrecy by the receiving authority is comparable with the requirements placed on the NPA to maintain the confidentiality of the information it receives (subject, naturally, to various other provisions governing the NPA and its conduct).

Domestically, further support for the above position might be drawn from judgements such as that in the *Mistry* case,⁵³ where a member of the public provided information to the Interim National Medical and Dental Council of South Africa ('the Council') about a possible violation of the law by the applicant, a medical doctor. The Council's officials communicated this information to an official of the Department of Health who had a statutory responsibility for carrying out investigations into allegations of this sort. The applicant objected to this disclosure on the basis that violated his right to privacy. Importantly, all the officials involved were subject to the requirement of confidentiality. The court, in this instance, found no violation of the applicant's right to privacy.

It is submitted, however, that there are certain key shortcomings to the argument set out above.

When the SARS shares the taxpayer information with the NPA, it does so in order to facilitate the prosecution of a domestic tax offence. The EoI process, on the other hand, is not necessarily undertaken as part of the investigation or prosecution of a tax offence. This is especially true in the case of EoIA (a point which is elaborated upon in a later section to this chapter). The purpose of a prosecution and the processes surrounding it is quite dissimilar from that of other investigations. Consequently, when analysing the balance struck between the harm done and the purpose achieved by the limitation, it would not be appropriate to equate the sharing of information with the NPA as part of a criminal investigation, with the disclosure of information to a foreign competent authority for investigative purposes.

In terms of the receiving State's treaty obligation to maintain the secrecy of the data obtained, it should be kept in mind that when taxpayers share private information with the SARS, their constitutional right to privacy is restricted. The restriction is deemed to be fair and justifiable in fair and open democratic society partly because of the fact that the information will be kept confidential by the SARS. The SARS' duty to maintain the confidentiality of the taxpayer information does not mean that the taxpayer's right to privacy has not been violated.

Baker & Groenhagen draws the following distinction between confidentiality and privacy:⁵⁴

"Confidentiality relates to the handling of information which has been supplied to the revenue authority and which should not be passed on to any other person in breach of that confidence: privacy relates to the right of an individual not to suffer any intrusion into his private or business life, his home or business premises unless that intrusion is necessary and is expressly authorized by law.... It goes without saying that any interference with a taxpayer's right to privacy must be in accordance with the law and should not be disproportionate to the context of the investigation."

⁵³ *Mistry v Interim National Medical and Dental Council of South Africa* 1998 (4) SA 1127 (CC), para. 51.

⁵⁴ Baker, P and Groenhagen, AM, *The protection of taxpayers' rights – an international codification*, European Policy Forum (London, 2001), pp. 47-48.

The question is therefore whether the duty of the receiving government to maintain the secrecy of the taxpayer information (as per the treaty) is weighty enough to bring a sufficient degree of balance to the proportionality equation.

In analysing this question, it is important to note that the tax treaty does not require the receiving government to uphold the South African Constitution and the protection afforded by the underlying legislation (such as chapter 6 of the TAA), but rather requires the State to treat the information as it would had it received it from its own domestic sources.

The level of protection afforded to the taxpayer could therefore vary considerably from that enjoyed under South African law.

Once the taxpayer information leaves South Africa and is placed in the hands of the foreign revenue authority, any breaches in the confidentiality of that information is no longer under the jurisdiction of the South African legal system. The taxpayer does not have any recourse against the foreign government in a South African court (compared to the recourse it would have against the NPA should the violation occur under their watch).

This is a further differentiating factor between the sharing of information between the SARS and the NPA in the investigation of domestic tax offences, and the sharing of information between the SARS and a foreign government. Both the SARS and the NPA are subject to South African legislation and are answerable to the South African courts should they violate any South African law. The foreign government the SARS is sharing confidential taxpayer information with, is not.

As Croome concludes:⁵⁵

“A taxpayer should not be prejudiced such that information that would be protected in their home country is made known to another revenue authority which does not have similar privacy provisions as in his or her home State. That would constitute an undue violation of the taxpayer’s right to privacy and the taxpayer would in such a case have no remedy, because the violation is taking place in a foreign country.”

It is submitted that one of the most troubling questions from a South African constitutional perspective arises as a result of the unequal degree of protection afforded by the receiving and requesting States, together with the limited remedies for a taxpayer in South Africa.

Additional factors to consider when determining the reasonability of the violation would entail analysing the relation between the limitation, and its purpose. Can it be said that this limitation of the taxpayer’s right to privacy is causally linked with the purpose it pursues? What evidence might one produce to substantiate this claim? This question is considered separately under the sections below.

⁵⁵ Croome p. 168.

In assessing the reasonableness of the violation, it must also be asked whether there are less restrictive means to achieve the desired purpose.

Specifically in the context of EoIR, alternative, less restrictive measures might include requiring the SARS to make an *ex parte* application to a judge in chambers before sharing the information (which would be similar to the rights currently afforded to South African taxpayers in instances where information is shared with the NPA in cases other than South African tax offence investigations).

Another alternative, applicable to both EoIR and EoIA, might be to provide the taxpayer with prior notice of the intended exchange, as well as affording them the opportunity to lodge an objection should they feel that their rights will be unreasonably compromised should the information be shared.

Others would, however, oppose the view that these alternative procedures will be able to meet the same objectives as the current process. This is discussed in more detail in Chapter 5 of this paper.

The argument that the exchange of information is in reality, similar to a domestic tax offence investigation, becomes particularly strained in the context of EoIA given the very nature of EoIA, where the exchange is triggered automatically where certain fixed, predetermined criteria are met.

The question of whether the extent of the restriction of the taxpayer's right to privacy is justified therefore becomes even more compelling.

Both FATCA and the OECD Standard stipulate various indicia which, if identified by the financial institution, would trigger an automatic exchange of that taxpayer's information with that country. These indicia include having a mailing address or a telephone number in the reportable jurisdiction. The net is therefore cast quite widely – raising questions surrounding the necessity and proportionality of the exchange.

Please refer to the separate discussion in this Chapter (dealing with the POPI Act) for further discussion and analysis of the safeguards currently contained in the various EoIA instruments, and the questions asked in a global stage regarding the necessity and proportionality of both FATCA, and the OECD Standard.

4.4 The POPI Act and the current protection enjoyed by taxpayers during the EoI process

4.4.1 The practical protection extended to data subjects by the POPI Act

The POPI Act was first tabled in the South African parliament in 2009, and enacted in November 2013. Note that although enacted, almost all of the provisions of the Act are not yet effective – including those sections creating compliance obligations.⁵⁶ The reason for the delay in bringing the provisions into effect

⁵⁶ As at 25 February 2016.

is to afford affected parties the opportunity to put the necessary processes and safeguards in place to ensure their compliance with the Act, once effective.

Given the interplay between EoI and the taxpayers' fundamental right to privacy, however, one would be remiss not to consider the potential implications of the POPI Act on the processing of taxpayer information in South Africa. In particular, the interaction between the POPI Act and the current bilateral and multilateral exchange instruments should be analysed, along with the questions this raises regarding the manner in which the taxpayers' constitutional rights are given effect in practice by the relevant parties responsible for processing the taxpayer information during the exchange process.

The POPI Act, hailed by some as "*the most comprehensive piece of privacy legislation in the world*"⁵⁷ when first introduced, was enacted:⁵⁸

"to give effect to the constitutional right to privacy, by safeguarding personal information when processed by a responsible party, subject to justifiable limitations that are aimed at balancing the right to privacy against other rights ... and protecting important interests, including the free flow of information within the Republic and across international borders".

The Act therefore has as its foundation section 14 of the Bill of Rights, read with the general limitation provision, section 36.

The Act goes further to state that the purpose of the legislation is also to:⁵⁹

"regulate the manner in which personal information may be processed, by establishing conditions, in harmony with international standards that prescribe the minimum threshold requirements for the lawful processing of information".

In developing the POPI Act, the South African Law Reform Commission took into consideration the approaches adopted internationally, including those by the European Union ('EU'). This alignment with international best practice was emphasised during the parliamentary debates on the Bill.⁶⁰ It is therefore not surprising to find many similarities between the POPI Act and the EU Data Protection Directive.⁶¹

Although a detailed discussion of the POPI Act falls beyond the scope of this paper, the Act, at its core, sets out the conditions under which the data subject's personal information may be collected, as well as manner in which the data may be processed thereafter. It should be noted that the Act defines the 'processing' of information very broadly to include any operation or activity, automatic or otherwise,

⁵⁷ PwC, "The protection of personal information bill: The journey to implementation", November 2011, p. 1, [cited 2016 Feb 14] available online from < <https://www.pwc.co.za/en/assets/pdf/popi-white-paper-2011.pdf>>.

⁵⁸ POPI Act section 2(a).

⁵⁹ POPI Act section 2(b).

⁶⁰ See, for example, the minutes of the second reading debate of the Protection of Personal Information Bill in the National Assembly, 10 September 2012, [cited 2016 Feb 14] available online from <<https://pmg.org.za/hansard/18275/>>.

⁶¹ Directive 95/46/EU.

concerning personal information, including the collection, storage, use and transmission or distribution of the information.⁶²

The POPI Act, *inter alia*, affords data subjects the right to have their personal information processed in a lawful manner, including the right to be notified that their personal information is being collected,⁶³ to request the correction or deletion of their personal information held by others,⁶⁴ and to object, on reasonable grounds, to the processing of their information.⁶⁵

More specifically, the POPI Act stipulates the circumstances under which the data may be processed, which include where the data subjects have given their consent to the processing, or where the processing complies with an obligation imposed on the 'responsible party' (*i.e.* the party which determines the purpose of and means for the processing of the data) by law.⁶⁶ The POPI Act further requires that where personal information is collected, it must be done so for a specific, explicitly defined and lawful purpose, and that any further processing must be done in accordance or compatible with this purpose.⁶⁷ The responsible party must also to take steps to ensure that the data is complete, accurate, not misleading and updated where necessary.⁶⁸

The Act gives effect to the fundamental principle of proportionality, stipulating that personal information may only be processed if, given the purpose for which it is processed, it is adequate, relevant and not excessive.⁶⁹ It further places limitations on the retention of records for any period longer than is necessary for achieving the purpose for which it was gathered.⁷⁰

Beyond the requirements surrounding the processing of personal information, the POPI Act requires that the data subjects must, *inter alia*, be informed (notified) that their personal information is being collected, the purpose for which it is being collected, the details of any law authorising the collection of their personal information, and where applicable, the responsible party's intention to transfer the information to a third country,⁷¹ including the level of protection afforded to the information by that third country.⁷²

The duty to notify the data subject is also in keeping with the other obligations imposed on the responsible party by the Act. For example, the duty to take steps to ensure that the data being processed

⁶² POPI Act section 1, definition of 'processing'.

⁶³ POPI Act section 5(1)(a)(i).

⁶⁴ POPI Act section 5(1)(c).

⁶⁵ POPI Act section 5(1)(d).

⁶⁶ POPI Act section 11(1).

⁶⁷ POPI Act sections 13 and 15.

⁶⁸ POPI Act section 16.

⁶⁹ POPI Act section 10.

⁷⁰ POPI Act section 14.

⁷¹ Note that the term 'third country' is not defined in the POPI Act. It can be speculated that perhaps this term was taken directly from the EU Data Protection Directive, where it would refer to non-EU Member States. It is submitted that in the context of the POPI Act, it refers to all countries other than South Africa.

⁷² POPI Act section 18.

is accurate and complete could in itself be argued to presuppose the need for the data subject to be notified of the processing and afforded the opportunity to correct the information, where needed.

The POPI Act also contains provisions specifically regulating the transfer of personal information across national borders.⁷³ Personal information of the data subject may only be transferred to parties outside of South Africa if the receiving party is subject to substantially similar privacy rules as those prescribed by the POPI Act – including those surrounding the further processing of the information after having received it.⁷⁴

As previously mentioned, the POPI Act does allow for reasonable limitations to the data subject's right to privacy under certain, specified, circumstances.

For example, the POPI Act does not apply to the processing of information by or on behalf of a public body for the purpose of investigating offences,⁷⁵ including the prevention or detection of unlawful activities and the combating of money laundering activities. Note that the term 'money laundering' is broadly defined under South African law, and would include transactions that involve the proceeds of tax offences.⁷⁶

Other exclusions restrict the data subject's right to be informed. In this regard, the POPI Act specifies that no notification is required in instances where this is necessary to avoid prejudice to the maintenance of the law by any public body; to comply with an obligation imposed by the law; or to enforce legislation concerning the collection of tax revenue.⁷⁷

Note that these limitations are in line with those contained in Article 13 of the EU Data Protection Directive, which affords the Member States the right to include certain restrictions on the Directive's provisions in their domestic legislation, where necessary (taxation matters are specifically listed as an example of when a restriction might be justified).

4.4.2 The POPI Act and the current EoI framework

Firstly, in order to establish whether EoI would be subject to the POPI Act, it should be considered whether the processing of information as part of the EoI process would form part of an investigation into an 'offence' (in which case the Act would not apply).

Section 6(1)(c) of the POPI Act determines:

⁷³ POPI Act section 72.

⁷⁴ Note that the POPI Act also allows for the transfer of the data should the data subject consent to the transfer, or should the transfer part of the performance of a contract that the data subject is party to. As these two scenarios are arguably not applicable in the context of EoI, it will not be discussed further.

⁷⁵ POPI Act section 6(1)(c).

⁷⁶ Public Accountant's and Auditor's Board, "Money laundering and control: a guide for registered accountants and auditors", June 2003, p. 8.

⁷⁷ POPI Act section 18(4).

“This Act does not apply to the processing of personal information by or on behalf of a public body - the purpose of which is the prevention, detection, including assistance in the identification of the proceeds of unlawful activities and the combating of money laundering activities, investigation or proof of offences ..., to the extent that adequate safeguards have been established in legislation for the protection of such personal information;”

The question is therefore twofold: is the EoI information gathering process undertaken by the SARS done so to detect, or as part of an investigation into an ‘offence’; and if so, have adequate safeguards been established in legislation for the protection of the information in question?

As to the first question, it is submitted that the information gathered under the EoI process is not necessarily done with the express purpose of detecting or investigating an offence. For example, this would not be the case in instances where the information is gathered as part of an ordinary audit conducted by the revenue authorities, given that the purpose of an audit is to confirm compliance with the relevant tax legislation (*i.e.* not targeting tax offences, *per se*). This would be of particular relevance in the EoIA process, where the exchange is not done in pursuance of a specific inquiry into the taxpayer’s affairs, but is triggered by predetermined and presumptive criteria.

The scope of the word ‘offence’, as contained in the POPI Act, must also be considered.

Section 3(3) of the TAA allows the SARS to “*obtain the information for transmission ... as if it were relevant material required for the purposes of a tax Act*” (*i.e.* as the SARS would gather the information in the context of its own, domestic information gathering procedures). It is submitted, however, that section 3(3) of the TAA does not, on the wording of the provision, extend the meaning of the term ‘offence’ to other pieces of legislation such as the POPI Act. The term ‘offence’ is not defined in the POPI Act, and the Act does not include any deeming provision that would expressly include foreign offences (*i.e.* actions that would be seen to be offences under the laws of another State) within the scope of the term for the purposes of the POPI Act. It is therefore submitted that a foreign tax offence does not constitute an ‘offence’ for the purposes of the POPI Act.

Lastly, even should the first two questions be answered in the affirmative (about which there is considerable doubt), it would remain to be proved that adequate protection of the taxpayer’s right to privacy is contained in other legislation such as the ITA and TAA. This question is unpacked in further detail throughout this Chapter. In short, based on the analysis performed, it is not evident that the relevant provisions currently contained in the ITA and TAA alone are sufficiently robust to truly give effect to the taxpayer’s constitutional right to privacy in the EoI process.

With the arguments presented above in mind, the discussion therefore proceeds on the basis that the exception to the POPI Act contained in section 6(c) does not apply to the EoI process.

Accordingly, as a next step, it should be considered whether there is any justification to restrict the data subject's right to be notified that their information is being processed.⁷⁸

Could it be argued that the notification would prejudice the maintenance of any law⁷⁹ – *i.e.* defeating the purpose of the EoI process? It could be contended that providing the affected taxpayer with prior notice of the exchange would merely 'tip off' the suspected offender, allowing them to delay and frustrate the investigation into their tax affairs.

Please refer to the discussion that follows in Chapter 5 regarding the right to administrative justice for a more detailed discussion in this regard. In short, there are many questions that cast doubt on the validity of the 'tip off' defence as a justification for the blanket denial of the right to be notified.

Specifically, in the context of the EoIA, there is an argument that the sheer volume of persons affected would make notification impractical. This contention might, however, fail to convince in an age where, in South Africa at least, it is common practice for account holders to be notified by the relevant financial institution via text message or email should there be any transaction processed to their accounts. It is therefore difficult to understand how the same technology cannot be employed to notify data subjects that their personal information is being collected and transferred in accordance with the relevant treaty and TAA (especially given that this technology is also already being used by the SARS to keep taxpayers informed of the status of their income tax returns filed via the SARS' online electronic filing system).

Could it then be said that the right to notification is restricted in order to comply with an obligation under the provisions of any law (including those governing the collection of revenue)?⁸⁰

In both EoIR and EoIA it is submitted that no Act (not the POPI Act, ITA or TAA) specifically prohibits the SARS from informing any taxpayer of the pending exchange of his or her personal information.

It should be noted, however, that it would not be necessary to obtain the data subjects' consent to process their data, given that the processing is done by virtue of the obligations imposed on the responsible party by a law (namely the relevant international agreement, TIEA, and TAA). Again, it must be emphasised that although the EoI is permitted by law, the manner in which this is done and the protection afforded to the taxpayer during the exchange process is a separate matter.

It is clear, therefore, that once effective, the detailed POPI Act will have a significant impact on the manner in which data is processed in South Africa and the specific protection that must be afforded to the data subject during the process. The parties within South Africa responsible for the processing of taxpayer information will be not be excluded from the ambit of the POPI Act as it currently reads.

⁷⁸ POPI Act section 18(4).

⁷⁹ POPI Act section 18(4)(c)(i).

⁸⁰ POPI Act section 18(4)(c)(ii).

It should be borne in mind, however, that the POPI Act has been enacted to provide the detailed procedures designed to give effect to the rights already granted to taxpayers by the Constitution. Arguably, therefore, these safeguards should have already be in place in practice.

In the context of EoI, the POPI Act provisions of particular importance will be those surrounding the circumstances under which the data subject's information may be processed, the conditions and safeguards which must be in place before the data is transferred across national borders, as well as the transparency of the EoI process (*i.e.* the notification of the taxpayer concerned).

For example, as mentioned, currently, most of the existing double tax treaties stipulate that the data protection and confidentiality rules of the receiving State will be applied to the data exchanged. This would be at odds with the relevant provision in the POPI Act which prohibits the cross-border transfer of information where the receiving State does not uphold substantially similar data protection rules as in South Africa.⁸¹ Many of South Africa's double tax treaties go further to stipulate the EoI is not required where this would be at odds with the supplying State's domestic laws and administrative practices (see for example the SA-US 1997 treaty to which the FATCA IGA is tethered⁸²). The implication of these provisions is that they would preclude EoI in instances where the SARS fails to definitively establish that the data protection standards in place in the receiving State are sufficiently robust.

Furthermore, the POPI Act prohibits the processing of data for a purpose that is not relevant, adequate or that would be considered excessive.⁸³ In the case of EoIA (where a large range of indicators regarding a taxpayer's potential taxable presence in a country automatically triggers an exchange) the bulk and somewhat indiscriminate exchange of vast amounts of personal information may be excessive (and potentially irrelevant).

The impact of section 108(5) of the ITA will also need to be considered (section 108(5) stating that the exchange shall not be prevented by any secrecy provision contained in any law). As stated previously in this chapter, section 108(5) of the ITA does allow for the deviation from secrecy provisions prescribed in any law (which would include the POPI Act), however, this does not equate to a blanket authority being granted to all those involved in the EoI process to disregard the constitutional rights of the taxpayer. For any violation to be lawful, it must still be proven to be reasonable, justifiable and in terms of a law of general application.

Given that the POPI Act has its foundations in the EU Data Protection Directive, the questions raised regarding the potential impact of the POPI Act on the EoI processes in South Africa should also be viewed in the light of recent developments in Europe. Please refer to the section that follows for further discussion.

⁸¹ POPI Act section 72.

⁸² It is interesting to note that following a recent decision by the Court of Justice of the European Union, the European Commission no longer recognises the US as providing an adequate level of data protection as would be required by Article 25 the EU Data Protection Directive (which deals with the cross-border transfer of data). See Case C-362/14.

⁸³ POPI Act section 10.

4.4.3 Recent developments in the EU in the field of EoIA

Given that the privacy provisions contained in the POPI Act and the various EoI mechanisms are not unique to South Africa, it comes as no surprise that the questions highlighted in the previous section have also been raised on a global stage.

It is not disputed that one should apply a healthy dose of caution when attempting to interpret the interaction of South African domestic legislation with its treaty obligations in the light of international developments and foreign case law in the field. In this specific instance, however, it is argued that as the South African treaties, as well as the POPI Act have their foundation in international instruments, much can be gained from an analysis of the developments beyond South Africa's borders. Arguably, even more so in the case of the POPI Act and the EoIA instruments, given that one of the intended purposes of the Act is to bring South Africa's domestic standards in line with those applied internationally.

In two 2012 letters to the European Commission's Director General of Taxation and Customs Union, the Article 29 Data Protection Working Party⁸⁴ raises serious concerns regarding the compatibility of certain obligations under FATCA (and the accompanying IGAs), and the EU Data Protection Directive.⁸⁵

Amongst other concerns, the Working Party questions the necessity of the FATCA for Europe. Although it could potentially be argued to be necessary and justified from a US perspective (given that it will grant the Internal Revenue Service ('IRS') access to information they deem necessary to administer their tax laws), it is less clear whether it is equally necessary from the supplying State's perspective – especially given the non-reciprocal nature of the agreement.

In determining whether there is a 'necessity' for the processing of the taxpayers' data, the Working Party goes further to say that:⁸⁶

"This requires ensuring that there is a lawful basis for the processing through careful assessment of how FATCA's goals balance with that of the EU's fundamental right enshrined in Article 8 of the Charter of Fundamental Rights – the right to a private and family life, i.e. by demonstrating necessity by proving that the required data are the minimum necessary in relation to the purpose. A bulk transfer and the screening of all data is not the best way to achieve such a goal. Therefore more selective, less broad measures should be considered in order to respect the privacy of law-abiding citizens, particularly; an examination of alternative, less privacy-intrusive means must be carried out to demonstrate FATCA's necessity.

⁸⁴ An independent European advisory body on data protection and privacy.

⁸⁵ See [cited 2016 Feb 10] <http://ec.europa.eu/justice/data-protection/article-29/documentation/other-document/files/2012/20120621_letter_to_taxud_fatca_en.pdf> and <http://ec.europa.eu/justice/data-protection/article-29/documentation/other-document/files/2012/20120621_letter_to_taxud_fatca_en.pdf>.

⁸⁶ Article 29 Data Protection Working Party, Letter to the Director General of Taxation and Customs Union of the European Commission, 21 June 2012, para. 8.3-8.4, [cited 2016 Feb 10] available online from <http://ec.europa.eu/justice/data-protection/article-29/documentation/other-document/files/2012/20120621_letter_to_taxud_fatca_en.pdf>.

[The Working Party] respects the legitimate goal of the US government to ensure tax compliance, but stresses that it must be done in accordance with the Directive, respect for Article 8 of the Charter of Fundamental Rights and Convention for the protection of individuals with regard to automatic processing of personal data (Convention 108). However in the absence of a lawful basis to legitimise the processing required, [the Working Party] does not see how compliance of FATCA and the Directive could be simultaneously achieved.”

On the basis that there will be no reciprocal transfer of data from the US to South Africa, could the argument be made that a unilateral decision taken in a foreign country (the US), in pursuance of their own domestic interests, necessitates the bulk transfer of taxpayer information and the resultant violation of taxpayer rights in South Africa?

The Working Party goes further to raise questions surrounding the proportionality of the processing of the data.⁸⁷ Can it be said that the personal information requested to be shared under FATCA is proportional to its goal? Could this goal not be achieved through less restrictive means?

The Working Party also warns the relevant role players (namely the financial institutions and the competent authorities) that they would still be required to comply with the parameters set out in the Data Protection Directive when processing the taxpayers' data under FATCA, including the obligations of transparency, and keeping the data subject informed of what is happening to their personal information.⁸⁸

Similarly, in a South African context, should it be accepted that the EoI information gathering and exchange process does not fall within any of the exceptions to the POPI Act, the SARS and the relevant financial institutions would have to comply with the POPI Act when processing the taxpayer's data per the FATCA IGA. Specifically, when processing the relevant taxpayer's information, it would have to be evaluated whether the processing, and extent thereof is justified given the purpose thereof.

Following their work done in relation to the interaction between the EU Data Protection Directive and FATCA, the Working Party also published a number of letters and reports dealing with the implementation of the OECD Standard in Europe.

As is the case with the FATCA IGA, the protection afforded to taxpayers under the OECD Standard will also be those contained in the underlying bilateral or multilateral tax treaty. Typically, these treaties will also stipulate that the confidentiality rules of the receiving State will be applied to the data exchange. In recognition of the potential conflict this might create with existing data protection laws across the globe, the OECD Standard, does, however, contain specific provisions relating to the confidentiality of taxpayer information exchanged.

⁸⁷ Ibid, para. 9.

⁸⁸ Ibid, para. 12.5.

Section 5, paragraph 1 of the Model CAA reads as follows:

“All information exchanged is subject to the confidentiality rules and other safeguards provided for in the [Convention]/[Instrument], including the provisions limiting the use of the information exchanged and, to the extent needed to ensure the necessary level of protection of personal data, in accordance with the safeguards which may be specified by the supplying Competent Authority as required under its domestic law.”

The OECD Standard therefore creates the scope for the county supplying the information to stipulate the data security safeguards which must be maintained in the receiving country in relation to the data supplied.

The Commentary to paragraph 1 of section 5 reads as follows:⁸⁹

“Many jurisdictions have specific rules on the protection of personal data which apply to taxpayer information. For example, special data protection rules apply to information exchanges by EU Member States (whether the exchange is made to another EU Member State or a third jurisdiction). These rules include, inter alia, the data subject’s right to information, access, correction, redress, and the existence of an oversight mechanism to protect the data subject’s rights. Paragraph 1 of Section 5 provides that the supplying Competent Authority may, to the extent needed to ensure the necessary level of protection of personal data, specify in the Competent Authority Agreement the particular safeguards that must be respected, as required under its domestic law. The Competent Authority receiving the information must ensure the practical implementation and observance of any safeguarding specified. The Competent Authority receiving the information shall treat the information in compliance not only with its own domestic law, but also with additional safeguards that may be required to ensure data protection under the domestic law of the supplying Competent Authority.”

To ensure that the requirements of the POPI Act surrounding the cross-border transfer of information are met, South Africa should specify in its CAAs that safeguards substantially similar to those provided for in the POPI Act are maintained in the receiving State.

In the EU, the European Commission in December 2014 adopted Council Directive 2014/107/EU (which amended the Directive 2011/16/EU on Administrative Cooperation in the Field of Taxation). The Directive, as amended, aims to extend mandatory EoIA across EU Member States in accordance with the OECD Standard. Importantly, the amendments to the Directive specifically include provisions which make it clear that the Data Protection Directive must be adhered to when taxpayer information is processed during the EoIA process.⁹⁰ Specifically, the amendments obliges each Member State to ensure that the affected data subjects are informed of the fact that their personal information is to be collected and

⁸⁹ OECD Model Competent Authority Agreement Commentary to section 5, par. 4.

⁹⁰ Council Directive 2014/107/EU, par. 5(b) of Art. 1.

transferred internationally, and that they are provided with the necessary information in sufficient time to enable them to exercise their data protection rights before the information is exchanged.

In a statement released on 4 February 2015,⁹¹ the Working Party again raised serious concerns regarding the compatibility of the amended Directive 2011/16/EU and the OECD Standard with the EU Data Protection Directive.

Concerns were once again raised regarding whether the mass collection and transfer of data could be said to meet the fundamental principles of purpose and necessity. Following a recent decision by the Court of Justice of the European Union in the *Digital Rights Ireland* case⁹² invalidating the Data Retention Directive (Directive 2006/24/EU) on similar grounds, the Working Party warns that:⁹³

“in order not to violate the proportionality principle, it is necessary to demonstrably prove the necessity of the foreseen processing and that the required data are the minimum necessary for attaining the stated purpose and thus avoid, an indiscriminate, massive collection and transfer.”

This concern was echoed in the European Data Protection Supervisor’s opinion dealing with the agreement entered into between the EU and Switzerland on the automatic exchange of tax information⁹⁴ (which is based on the OECD Standard).

In relation to the proportionality of the data collection and transfer under the agreement, the Opinion states the following:⁹⁵

“The relationship between legitimate public policy goals and protection of personal data has been addressed by the European Court of Justice in its Digital Rights Ireland judgment. In fact, based on the Court judgment annulling Directive No 2006/24/EC (Data Retention Directive applied to persons for whom there was no evidence capable of suggesting that their conduct might have a link, even an indirect or remote one with criminal activity), measures introducing massive and indiscriminate collection of data are deemed not to be proportionate, if they fail to narrow down the types of persons who can be targeted as individuals suspected of a crime.

Therefore, we consider that the Agreement should have included provisions and criteria that explicitly link the reporting of personal data concerning financial accounts to possible tax evasion

⁹¹ Article 29 Data Protection Working Party, Statement of the WP29 on automatic inter-State exchanges of personal data for tax purposes, 4 February 2015, [cited 2016 Feb 10] available online from <http://ec.europa.eu/justice/data-protection/article-29/documentation/opinion-recommendation/index_en.htm>.

⁹² Cases C-293/12 and C-594/12.

⁹³ Article 29 Data Protection Working Party, Statement of the WP29 on automatic inter-State exchanges of personal data for tax purposes, 4 February 2015, p. 3, [cited 2016 Feb 10] available online from <http://ec.europa.eu/justice/data-protection/article-29/documentation/opinion-recommendation/index_en.htm>.

⁹⁴ European Data Protection Supervisor, Opinion 2/2015, Opinion of the EDPS on the EU-Switzerland agreement on the automatic exchange of tax information, 8 July 2015, [cited 2016 Feb 10] available online at <https://secure.edps.europa.eu/EDPSWEB/webdav/site/mySite/shared/Documents/Consultation/Opinions/2015/15-07-08_EU_Switzerland_EN.pdf>.

⁹⁵ *Ibid*, at para. 13-14.

and that exempt low-risk accounts from reporting. In this respect, such criteria should be applicable ex ante to determine which accounts (and which information) would need to be reported. Only at that stage -once the relevance (or irrelevance) of the reporting for the purpose of countering tax evasion has been established- the electronic search might help determining the residence of the account holder.”

Given that the ‘necessity’ and ‘proportionality’ criterion of the Data Protection Directive are echoed not only in the POPI Act, but also in section 36 of the South African Constitution, it is certainly fair to argue that the concerns and recommendations raised by the Working Party and Data Protection Supervisor warrant further investigation in South Africa as well.

Interestingly, it should be noted that although modelled on the EU Directives dealing with the automatic exchange of tax information, this EU-Switzerland agreement does not include all the amendments contained in Directive 2014/107/EU – specifically those dealing with the notification of the data subject. The Data Protection Supervisor duly included the following recommendation: ⁹⁶

“the Agreement should have specified that information on data transfers should be provided to the data subject with a reasonable delay before the actual exchange of the data takes place (so that the individual concerned gets time to defend himself if relevant). The information provided should at the minimum inform the data subjects of the fact that their personal data will be sent to a competent authority for the purpose of fighting tax evasion, include a list of the category of data sent and the contact of the controller in their country of residence and inform them of their right to object and their right of redress.”

Given the similarities between the relevant EU directive and agreements and South African legal framework in this regard, it is submitted that this obligation to notify the data subject will be equally applicable in South Africa.

4.5 Summary remarks

The key questions that arise from an analysis of the current protection of the taxpayer’s right to privacy centre around whether that right is violated during the EoI process, and to what extent that violation erodes the proportionality of the limitation.

In dissecting these questions the difference between ‘confidentiality’ and ‘privacy’ should be borne in mind. The obligation on the part of the competent authorities to maintain the confidentiality of exchanged information does not necessarily mean that no violation of the taxpayer’s privacy has occurred.

In a purely domestic context, the SARS must operate within strict secrecy provisions spelled out in the TAA. This plays a critical role in bringing balance to the harm done by the intrusion into the private lives of the taxpayers when they disclose their information to the SARS, and the purpose of the restriction. In

⁹⁶ Ibid, at para. 21.

the context of EoI, however, these secrecy provisions are watered down in South Africa, with the taxpayer information being transferred to foreign competent authorities purely at the discretion of the SARS without any participation by the affected taxpayers.

This raises concerns surrounding whether the imposition on the taxpayer's constitutionally guaranteed right to privacy is 'reasonable' and 'justifiable' and in accordance with a 'law of general application', as required by section 36 of the Constitution.

Specifically, the discretion afforded to the SARS in the EoI process is effectively unrestrained by the provisions of the ITA and TAA (with the POPI Act not yet being effective), indicating that the SARS' limitation of the taxpayer's right to privacy is not performed in accordance with a 'law of general application'.

Questions are also raised regarding the reasonableness and proportionality of said limitation.

When the taxpayer's information is transferred to the foreign tax authority, it is not clear to what extent (or whether at all) the SARS ensures that the receiving State will uphold substantially similar confidentiality safeguards in relation to the exchanged information.

This current lack of protection afforded to taxpayers during the EoI process in practice significantly erodes the proportionality between the harm done and the purpose of the exercise potentially to the point where the hurdles put in place by section 36 of the Constitution, namely the 'reasonable' and 'justifiable' criterion, are no longer cleared.

This is of particular relevance in the context of EoIA, where the exchange of information is triggered purely by the taxpayer having met any one of a set of broad presumptive criteria. Serious misgivings have also been voiced on a global stage (in the EU in particular) regarding the necessity and proportionality of the current EoIA framework (as set out in the OECD Standard and FATCA IGAs). It is submitted that these concerns are of relevance in South Africa as well, and will become of even greater importance once the provisions of the POPI Act become effective (given the alignment of the POPI Act with the EU Data Protection Directive).

The impact of the coming into effect of the POPI Act on the protection afforded to taxpayers in both the EoIA and EoIR process will be significant. This is because the EoI process will be subject to the provisions of the POPI Act and will not fall within the exemptions to the Act. Further investigation into the procedures and safeguards to be put into practice by both the SARS and the relevant financial institutions (in the context of EoIA) to ensure POPI Act compliance, is warranted.

In summary, the following recommendations are put forward to address the shortcomings identified by the analysis performed in this Chapter:

- Legislation should be developed to circumscribe the discretionary powers currently afforded to the SARS in the EoI process. Specifically, the antiquated section 108(5) of the ITA (empowering the SARS

to deviate from the TAA chapter 6 secrecy provisions) should be amended to take into account the coming into effect of the 1996 Constitution. Furthermore, guidance should be provided in legislation as to what would constitute 'necessary' or 'foreseeably relevant' information in the context of the tax treaties' EoI clauses.

- The above-mentioned new legislation should give effect to the POPI Act by providing detailed rules as to how the taxpayer's constitutionally guaranteed right to privacy is to be protected in practice during the EoI process. This would include the prior notification of the affected taxpayer by the SARS. Safeguards that must be in place before the information can be transmitted to foreign governments must also be stipulated.
- Finally, also in the context of EoIA, the SARS should exercise its right under section 5 of the OECD Standard's CAA to insist that the receiving State's data security standards are similar to that of South Africa's before the information is exchanged.

CHAPTER 5: THE RIGHT TO JUST ADMINISTRATIVE ACTION

Section 33 of the Constitution

(1) Everyone has the right to just administrative action that is lawful, reasonable and procedurally fair.

(2) Everyone whose rights have been adversely affected by administrative action has the right to be given written reasons.

(3) National legislation must be enacted to give effect to these rights, and must –

(a) provide for the review of administrative action by a court or, where appropriate, an independent and impartial tribunal;

(b) impose a duty on the State to give effect to the rights in subsection (1) and (2); and

(c) promote an efficient administration.

5.1 Introduction

Internationally, it is rare to find the right to administrative justice codified in a bill of rights.⁹⁷ This inclusion of the fundamental principles of administrative law in the South African Bill of Rights must be viewed in the context of South Africa's political history, which was for a long period characterised by the abuse of government power and executive autocracy.⁹⁸ The Constitution therefore protects the review of administrative power against legislative and executive interference and provides relief for those affected by unlawful administration.⁹⁹

Hoexter summarises the position as follows:¹⁰⁰

“Thus the legislature can no longer simply authorise the administration to depart from the fundamental principles of administrative justice that have been guaranteed in the Constitution. Any such authorisation would have to be justified under the limitation clause, section 36, in order to be constitutionally acceptable”.

Section 33(3) of the Constitution requires “*legislation to be enacted to give effect to these rights*”.

Accordingly, the Promotion of Administrative Justice Act¹⁰¹ (‘PAJA’) was enacted for this express purpose.

⁹⁷ Croome, p. 204.

⁹⁸ Hoexter, C., “Just Administrative Action”, in: *The Bill of Rights Handbook*, 6th edn. (Cape Town: Juta & Co. Ltd, 2014), p. 644.

⁹⁹ *Ibid*, p. 645.

¹⁰⁰ *Ibid*, p. 646.

¹⁰¹ Promotion of Administrative Justice Act No 3 of 2001.

This chapter will analyse the questions raised by the current protection afforded to taxpayers in the EoI process in the light of the constitutional right to just administrative action, as given effect to by the PAJA.

5.2 The Promotion of Administrative Justice Act and EoI

Should EoI amount to 'administrative action' as defined in the PAJA, the protection afforded to the taxpayer in the process will be subject to the provisions and requirements of the PAJA.

Importantly, therefore, it must be established whether the PAJA applies to the EoI process.

5.2.1 EoI and 'administrative action' under the PAJA

The PAJA defines 'administrative action' in section 1 as:

"any decision taken, or any failure to take a decision, by –

a) An organ of State when –

i) exercising a power in terms of the Constitution or a provincial constitution; or

ii) exercising a public power or performing a public function in terms of any legislation;..."

Section 2 of the South African Revenue Services Act¹⁰² provides as follows:

"The South African Revenue Services is hereby established as an organ of State within the public administration but as an institution outside the public service".

As an organ of State, the PAJA applies to the decisions of the Commissioner and his officials.¹⁰³

When it comes to determining whether an action taken by an organ of State, such as the SARS, is administrative action for the purposes of the PAJA, there is a degree of interplay between the various definitions contained in the Act. Hoexter summarises the effective result of the interrelation of definitions as follows:¹⁰⁴

"In summary, an action will qualify as administrative action under the PAJA if it is:

- 1. A decision*
- 2. By an organ of State (...)*
- 3. When exercising a public power or performing a public function*
- 4. In terms of any legislation (or in terms of an empowering provision)*

¹⁰² South African Revenue Services Act No. 34 of 1997.

¹⁰³ Croome, p. 209.

¹⁰⁴ Hoexter, C., "Just Administrative Action", in: The Bill of Rights Handbook, 6th edn. (Cape Town: Juta & Co. Ltd, 2014), p. 656.

5. *That adversely affects rights*
6. *That has direct, external legal effect*
7. *And, that is not specifically excluded by the list of exclusions in subparas (aa) to (ii) of the definition of administrative action”*

5.2.1.1 EoI, as a ‘decision’ envisaged by the PAJA

A ‘decision’ is defined in section 1 of the PAJA as:

“Any decision of an administrative nature made, proposed to be made, or required to be made, as the case may be, under an empowering provision,... and a reference to a failure to make a decision must be construed accordingly.”

For the purposes of the PAJA, the term ‘decision’ encompasses both the making of a decision of an administrative nature, as well as the failure to make such a decision.

It would be useful to firstly determine whether there has been any failure to make a decision on the part of the SARS when exchanging information. This question would be of particular relevance in the context of EoIA, where the exchange is based on a set of objective, presumptive criteria. The process therefore does not require application of mind by a decision maker in each instance where information is harvested by financial institutions and passed automatically to a competent authority of another State by the SARS.

According to Hoexter, a ‘decision’ would usually, but not inevitably, encompass certain features, including the gathering of information, an evaluative process, reaching a conclusion and an exercise of power based on the conclusion.¹⁰⁵

Given Hoexter’s description of what a ‘decision’ entails for purposes of PAJA, it could be argued that the EoIA process in particular is so rigidly automated that it erodes the decisiveness or determinative nature of a revenue official’s involvement in the process.

In South Africa, at present, the only functions known, with reasonable certainty, to be performed by a SARS official during the EoIA process include: collating the information received from the various financial institutions; determining whether the foreign country identified by the various indicia is a treaty partner of South Africa; and handling the actual transmittal of the data to the foreign competent authority.¹⁰⁶

¹⁰⁵ Ibid, p. 657.

¹⁰⁶ “Automatic exchange of information, what it is, how it works, benefits, what remains to be done”, OECD, 2012, p. 9, [cite 2016 Feb 16] available online from < <http://www.oecd.org/tax/exchange-of-tax-information/automaticexchangeofinformationreport.htm>> and Memorandum on the Objects of the Tax Administration Laws Amendment Bill, 2015, par. 2.33, [cite 2016 Feb 14] available online from < <http://www.sars.gov.za/AllDocs/LegalDoclib/ExplMemo/LAPD-LPrep-EM-2015-02%20-%20Memorandum%20on%20the%20objects%20of%20TALA%20Bill%20of%20%202015.pdf>>.

Beyond the actions listed above, it is not publically known what other tasks and procedures the SARS will undertake before exchanging the information in bulk with the relevant receiving States. For example, it is not known whether a SARS official will conduct any procedures to independently test the accuracy of the financial information to be shared or the accuracy of the indicia identified by the relevant financial institutions.

Should the SARS' role in the EoIA process be limited to the menial procedural tasks listed previously, there would be a failure on the part of the SARS officials to apply their minds to the substance of the information to be exchanged and, for example, whether this information is necessary or foreseeably relevant to the enforcement of the contracting State's tax laws. Expressed in terms of Hoexter's definition, the SARS' EoIA procedures will lack an evaluative process, and the subsequent reaching of a conclusion, and could therefore be argued to amount to a 'failure to make a decision'.

Although it is also not clear what the extent of the SARS' evaluative process is under EoIR, it would be fair to assume that given the difference in the very nature of the two exchange mechanisms and the volume of data involved, these processes would likely be more robust under EoIR than under EoIA.

Should it be accepted that, under EoIR there is no 'failure to make a decision' on the part of the SARS, it remains to be considered whether the SARS makes a 'decision' as envisaged by the PAJA, when exchanging taxpayer information upon request.

Accordingly, it must firstly be considered whether the decision to share the information would be of an 'administrative nature'.

In this respect, commentators have warned against taking too narrow a view of what is meant by the phrase 'of an administrative nature', given that the PAJA is intended to give effect to the constitutional right to administrative action (which has been held to apply to conduct connected to the daily business of government, that includes the making of delegated legislation, adjudication processes and administration).¹⁰⁷

Croome provides a list of decisions made by the SARS that would be of an administrative nature (and hence constitute 'administrative action' under the PAJA). Included in this list is the decision on whether to conduct an audit into the affairs of the taxpayer.¹⁰⁸

It is submitted that the decision to share information across national borders also falls within the ambit of the PAJA definition of a 'decision', since it involves the administration of South Africa's information exchange obligations under tax treaties. The aim of the treaty clauses being to assist in the audits of taxpayer compliance with the tax laws of the countries that are party to the treaty.

¹⁰⁷ Ibid, p. 658.

¹⁰⁸ Croome, p. 211.

Secondly, the PAJA definition of a ‘decision’ requires that the decision is made under an ‘empowering provision’, and in accordance with ‘any legislation’.

‘Empowering provision’ is widely defined in section 1 of the PAJA, and includes a law, a rule of common law, customary law, an agreement, instrument, or other document in terms of which an administrative action was taken.

A provision of the TAA, such as section 3 that allows for the exchange of taxpayer information in accordance with South Africa’s treaty obligations, would certainly fall within this definition. So too, arguably, might the treaty itself fall within this definition because once approved by Parliament and *Gazetted*, the provisions of the treaty have the same standing as if it had been enacted in the ITA.¹⁰⁹

In the context of EoIR, the SARS therefore does make a ‘decision’, when sharing the taxpayer information as requested. In terms of EoIA, the SARS’ failure to vet or otherwise subject the relevant data to some form of evaluative process to assess the accuracy or foreseeable relevance of the information would amount to a ‘failure to make a decision’.

Both EoIA and EoIR would therefore fall within the meaning of ‘decision’ for the purposes of administrative action under the PAJA. Any reference to ‘decision’ in the discussion that follows should be read in this context.

5.2.1.2 The decision to exchange taxpayer information and the adverse, direct, external legal effect on the taxpayer’s rights

The inclusion of the requirement for the decision to adversely affect the rights of the taxpayer, with direct, external legal effect, could be the most complex aspect to apply in the context of EoI.

Indeed, generally speaking and beyond its implications in the context of exchange of information, the inclusion of the requirement (in its current form and wording) has muddied the waters somewhat in interpreting what exactly is meant by ‘administrative action’ under the PAJA.¹¹⁰

The two key elements of the requirement which are likely to have the most determinative effect on any discussion surrounding administrative action in the context of EoI will be unpacked and addressed separately below.

5.2.1.2.1 The ‘adverse’ effect on the taxpayer’s ‘rights’

Firstly, when taxpayer information is exchanged, how could the taxpayer’s ‘rights’ be ‘affected’ adversely?

As to what is meant by ‘rights’, several judgements have turned on adopting a less strict interpretation of the word.

¹⁰⁹ ITA section 108.

¹¹⁰ See Hoexter, C, *Administrative Law in South Africa*, 1st ed (Cape Town: Juta & Co Ltd, 2007), pp. 199 - 209.

In the *Transnet* case,¹¹¹ for example, ‘rights’ were construed to include the applicant’s fundamental right to administrative action. In this case, the court held that the applicant’s right to fair administrative action would be adversely affected if they were not given reasons for the failure to have been awarded a tender (as opposed to trying to determine whether the applicant had a right to be awarded the tender or not). The reasoning being that without being given reasons for the failure, the applicant will have no way of knowing whether their right to just administrative action had been violated.

In the *Bullock* case,¹¹² Cloete JA suggested that ‘rights’ in this context should not be restricted to those enforceable in a court of law (albeit that the judgement was delivered in the context of the interim Constitution).

Similarly, support for a more liberal interpretation to the phrase ‘adversely affects the right of any person’ can also be found in Nugent JA’s judgement in the *Grey’s Marine* case:¹¹³

“While PAJA’s definition purports to restrict administrative action to decisions that, as a fact, ‘adversely affect the rights of any person’, I do not think that literal meaning could have been intended. For administrative action to be characterised by its effect in particular cases (either beneficial or adverse) seems to me to be paradoxical and also finds no support from the construction that has until now been placed in s 33 of the Constitution... The qualification, particularly when seen in conjunction with the requirement that it must have a ‘direct and external legal effect’, was probably intended rather to convey that administrative action is action that has the capacity to affect legal rights, the two qualifications in tandem serving to emphasise that administrative action impacts directly and immediately on individuals.”

Under this interpretation credence is given to an action’s mere *capacity* to impact someone’s ‘rights’. Should one therefore determine that the taxpayer’s right to, for example, privacy, has been impacted or affected during the EoI process,¹¹⁴ it will certainly be reasonable to conclude that the taxpayer’s rights have been ‘adversely’ affected for the purposes of the PAJA. To otherwise deny that the PAJA applies would mean that the remedies afforded under PAJA (e.g. the right to be notified, to make representations or to be given reasons for deciding to exchange information) would not be available to taxpayers. This would be an illogical outcome given that these remedies are the ultimate and practical realisation of the right to just administrative action.

5.2.1.2.2 The direct, external legal effect of the EoI decision

Secondly, should one be able to establish that the taxpayer’s rights have been adversely affected, it remains to be determined whether this has been done with ‘direct’ ‘external’ legal effect.

¹¹¹ *Transnet Ltd v Goodman Brothers (Pty) Ltd* 2001 (1) SA 853 (SCA), paras. 11-12.

¹¹² *Bullock NO v Provincial Government, North West Province* 2004, (5) SA 262 (SCA), para. 19.

¹¹³ *Grey’s Marine Hout Bay (Pty) Ltd v Minister of Public Works* 2005 (6) SA 313 (SCA), para. 23.

¹¹⁴ As discussed separately in Chapter 4.

The requirement, which has its origins in German law,¹¹⁵ seems to add an additional distinct hurdle to be cleared, namely that the decision must be conclusive or final. This requirement for the decision to be 'ripe' would seemingly ensure that only once final, and no longer subject to change, will it fall within the ambit of 'administrative action'.

An argument could be made that this insistence on finality could be interpreted so as to exclude all preliminary decisions from 'administrative action'. This interpretation of the requirement would arguably be in line with the German law which inspired the phrase.

Hoexter, citing Pfaff and Schneider, provides the following guidance as to the original German interpretation of the phrase:¹¹⁶

"If, for example, a decision requires several steps to be taken by different authorities, only the last of which is directed at the citizen, all previous steps taken within the sphere of public administration lack direct effect, and only the last decision may be taken to court for review....Therefore, all the preparatory decisions are in principle not reviewable by the administrative courts."

This interpretation would therefore see preliminary decisions falling short of the scope of 'administrative action' under the PAJA.

Given that some have argued that EoI merely forms part of an investigative process, this interpretation could have a significant impact as to whether the provisions of the PAJA would apply to the EoI process.¹¹⁷ In other words, on this view the exchange is merely part of the process leading up to a final decision and does not involve the final decision itself. The argument being that only once the information is used to make a decision to, for example, issue an additional assessment, are the taxpayer's rights affected with direct, external legal effect. All other decisions leading up to this (such as sharing the information with the requesting State) are merely preparatory to the final decision and therefore do not have a direct external effect on the taxpayer.

Internationally, this view appears to be held by many countries¹¹⁸ and is supported by a recent decision of the Court of Justice of the European Union in the *Sabou* case.¹¹⁹

¹¹⁵ German Federal Law of Administrative Procedure of 1976 (*Verwaltungsverfahrensgesetz*).

¹¹⁶ Hoexter, C, Administrative Law in South Africa, 1st ed (Cape Town: Juta & Co Ltd, 2007), p. 205.

¹¹⁷ Baker, P. and Pistone, P., "General Report", in: International Fiscal Association, 2015 Basel Congress, Cahiers De Droit Fiscal International, "The Practical Protection of Taxpayers' Fundamental Rights", Volume 100b, p. 61, and Case C-267/12.

¹¹⁸ Baker, P. and Pistone, P., "General Report", in: International Fiscal Association, 2015 Basel Congress, Cahiers De Droit Fiscal International, "The Practical Protection of Taxpayers' Fundamental Rights", Volume 100b, p. 61.

¹¹⁹ Case C-267/12 (note, however, that this decision has come under scrutiny, with many believing that the principle on which it is based is flawed. See, for example, Baker and Pistone, p. 61).

In South Africa, the courts have in the past found that a mere investigation on its own would not typically qualify as having a direct external effect.¹²⁰

Importantly, however, although the South African legislation has its roots in the German law, the local interpretation of the phrase will be the key determining factor. In the *New Clicks* case it was held that:¹²¹

“transplanting provisions...into our legal and constitutional framework may produce results different from those obtained in the countries from which they have been taken”.

Hoexter, in criticism of the German interpretation (as employed in South African common law in the past), further notes that:¹²²

“This reasoning has since been subjected to vigorous reappraisal by the Supreme Court of Appeal, and our courts have recognised that preliminary or intermediate decisions can have significant and even devastating effects on individuals^[123]. It may make practical sense to place some limits on the reviewability of preliminary action but...it would be a great pity if the term ‘direct’ were to be read as flatly contradicting this jurisprudence or as rendering preliminary decision-making entirely unreviewable.”

Other indications that would point to strict adherence to the German interpretation being somewhat misplaced in a South Africa would be the fact that the PAJA definition of ‘decision’ still makes specific reference to decisions *“proposed to be made”*, which indicates that the preparatory stages of the decision making process are not meant to be automatically excluded from ‘administrative action’.

Moreover, as discussed in further detail later in this chapter, sections 3 and 4 of the PAJA set out specific procedures to be followed before decisions are made. This too indicates that the PAJA was not merely enacted to enable the review administrative decisions after the fact.

In the *Digital* case, the Supreme Court of Appeal (‘SCA’) quoted Lawrence Baxter on determining what is meant by ‘ripeness’ and held as follows:¹²⁴

“the appropriate criterion by which the ripeness of the action in question is to be measured is whether prejudice has already resulted, or is inevitable, irrespective of whether the action is complete or not.”

This interpretation is more appropriate considering what the aims are of entrenched constitutional rights, namely to give practical effect by advancing remedies to prevent prejudice. The SCA’s approach in

¹²⁰ Hoexter, C., “Just Administrative Action”, in: *The Bill of Rights Handbook*, 6th edn. (Cape Town: Juta & Co. Ltd, 2014), p. 665.

¹²¹ *Minister of Health v New Clicks South Africa (Pty) Ltd* 2006 (2) SA 311 (CC), para. 142.

¹²² Hoexter, C, *Administrative Law in South Africa*, 1st edn (Cape Town: Juta & Co Ltd, 2007), p. 206.

¹²³ Hoexter cites *Du Preez v Truth and Reconciliation Commission* 1997 (3) SA 204 (A) and *Director: Mineral Development, Gauteng Region v Save the Vaal Environment* 1999 (2) SA 709 (SCA).

¹²⁴ *Chairman, State Tender Board v Digital Voice Processing* 2012 (2) SA 16 (SCA), para. 17.

the *Digital* case unties the Gordian knot between the one view that exchange of information is an intermediary step in a larger investigation, and the other that it is the final step in a process unto itself. If one applies the SCA's approach to the issue of 'ripeness' to EoI in a South African context, then the following question arises: Are the taxpayer's rights affected, or is it inevitable that they will be affected, when a 'decision' is taken to share confidential information with foreign revenue authorities?

If one accepts that rights are affected, then the 'direct external legal effect' hurdle is cleared. For example, as far as the taxpayer's right to privacy is concerned, decisions or failures to decide upon EoI does have an adverse effect, as was discussed in Chapter 4.

In summary, for the reasons set out above, it appears reasonably certain EoI constitutes administrative action for the purposes of the PAJA.

5.2.2 The protection that must be afforded to the taxpayer under the PAJA

Section 3 of the PAJA provides the basis for the obligations imposed by PAJA on the State and the protection thereby afforded to the subjects of the administrative action. It determines that:

"Administrative action which materially and adversely affects the rights or legitimate expectations of any person must be procedurally fair."

Interestingly, with the inclusion of the reference to the 'legitimate expectations' of the person, the language of section 3 is much broader than that of the definition of 'administrative action' in section 1. Section 3 seemingly extends the requirement for procedural fairness beyond the section 1 definition.¹²⁵ Although much has been made of this apparent contradiction between the section 1 and section 3 definitions of 'administrative action',¹²⁶ suffice to say that if the narrower section 1 definition is met, so too is that of section 3.

Section 3 goes on to determine that:

"(2)(a) A fair administrative procedure depends on the circumstances of each case.

(b) In order to give effect to the right to procedurally fair administrative action, an administrator, subject to subsection (4), must give a person referred to in subsection (1) –

(i) adequate notice of the nature and purpose of the proposed administrative action;

(ii) a reasonable opportunity to make representations;

(iii) a clear statement of the administrative action;

¹²⁵ Klue, Arendse and Williams, at § 3.26.

¹²⁶ As Hoexter refers to it: "a perverse piece of drafting that gives rise to a mind-boggling contradiction between ss 1 and 3". See Hoexter, C, *Administrative Law in South Africa*, 1st ed (Cape Town: Juta & Co Ltd, 2007), p. 199.

(iv) adequate notice of any right of review or internal appeal, where applicable; and

(v) adequate notice of the right to request reasons on terms of section 5.

(3) ...

(4)(a) If it is reasonable and justifiable in the circumstances, an administrator may depart from the requirements referred to in subsection (2).

(b) ...

(5) Where an administrator is empowered by any empowering provision to follow a procedure which is fair, but different from the provisions of subsection (2), the administrator may act in accordance with that different procedure.”

Except for situations where sections 3(4) and 3(5) are applicable, in order for the administrative action to be procedurally fair under the PAJA, the taxpayer must be given adequate notice of the proposed administrative action, the nature and purpose thereof, and be afforded a reasonable opportunity to make representations.

Quoting Hoexter, the Constitutional Court in the *Joseph* case held that:¹²⁷

“Procedural fairness ... is concerned with giving people an opportunity to participate in the decisions that will affect them, and – crucially – a chance of influencing the outcome of those decisions. Such participation is a safeguard that not only respect for the dignity and worth of the participants, but is also likely to improve the quality and rationality of administrative decision-making and to enhance its legitimacy.”

As mentioned in Chapter 2, currently taxpayers are not provided with any notice when (i) the SARS has received a request to exchange their confidential information (in the context of EoIR), (ii) a decision is taken by SARS to adhere to the request and share the requested (or other) information, nor (iii) are taxpayers informed once the information has been shared. Taxpayers are also not afforded the opportunity to make any representations during any stage of the decision making process or to otherwise participate in the EoI process, for example, to verify, update, or correct information that will be exchanged.

The current practice of the SARS in the EoI process therefore does not comply with the provisions of section 3(2) of the PAJA in all material aspects.

It therefore remains to be asked whether the current SARS practice is ‘fair and justifiable’ for purposes of the carve-out under section 3(4) or (5) of the PAJA?

¹²⁷ *Joseph v City of Johannesburg* 2010 (4) SA 55 (CC) at 71C, para. 42.

Section 3(5) allows for the use of other procedures (mandated by another empowering provision) provided that said procedures are still 'fair'.

Section 3(4) of the PAJA lists factors that must be taken into account when determining whether the departure from the section 3(2) notice procedure can be justified. The factors include (but are not limited to):

- i. the objects of the empowering provision;*
- ii. the nature and purpose of, and the need to take, the administrative action;*
- iii. the likely effect of the administrative action;*
- iv. the urgency of taking the administrative action or the urgency of the matter; and*
- v. the need to promote an efficient administration and good governance."*

This requirement for the alternative procedures to be 'fair and justifiable' can be read in the context of section 33 of the Constitution, which calls for administrative action that is 'lawful, reasonable and procedurally fair'. The wording of section 33 of the Constitution echoes section 36's requirement for any limitation of a fundamental right to be 'reasonable and justifiable'. It would be hard to imagine an instance where administrative action that is not 'fair and justifiable', will be deemed to clear the 'reasonable and justifiable' requirement of the general limitation clause. It is therefore not surprising to note the similarities between the factors mentioned above (section 3(4) of PAJA), and those listed in section 36 of the Constitution.

On the basis that the cross-border exchange of taxpayer information is 'administrative action', the question arises whether the SARS' practice is reasonable and justifiable, in the context of administrative justice, as far as it deviates from the 'standard' PAJA section 3(2) notice process.

5.2.2.1 The reasonableness and justifiability of current SARS practice in the EoI process

Firstly, in answer to the issue under this heading, it should be considered what the purpose of the administrative action by the SARS is.

It would not be sufficient to state that the purpose of sharing the taxpayer information is to comply with tax treaty obligations.

Using the preamble of most of South Africa's double tax treaties as guide, the purpose of information exchange could be to aid in the avoidance of double taxation and prevention of fiscal evasion. Information is exchanged under TIEAs in order to assist in the administration and enforcement of the contracting State's domestic laws.

Secondly, it must be considered whether there is a causal link between the administrative action, and the purpose it aims to achieve.¹²⁸

To this question some might answer that it is reasonable not to provide the taxpayer with upfront notice of the exchange given that this may effectively ‘tip off’ tax evaders.¹²⁹ In other words, notice of an impending exchange may provide potential evaders with the opportunity to appeal the process as a delaying tactic in order to afford them time to transfer the assets in question to another jurisdiction or destroy incriminating evidence.¹³⁰ Proponents of this argument might point to other instances in South African law where the SARS is permitted to act without providing the taxpayer with prior notice or the opportunity to make representations. Instances such as this include cases where the Commissioner is entitled to appoint an agent to collect a tax debt due. See for example the judgement delivered in the *Contract Support Services* case:¹³¹

“I agree with the submission made ... that not all administrative acts require the application of the audi alteram partem rule before they are given effect to... Where prior notice and a hearing would render the proposed act nugatory, no such prior notice or hearing is required.”

Similarly, when conducting search and seizure procedures under Part D of the TAA, the SARS is also not required to provide the taxpayer with prior notice. Importantly, however, before conducting the raid, the SARS must apply (*ex parte*) to a judge for a warrant to authorise the action. This is common practice internationally, and is accepted as reasonable and fair administrative action under the circumstances (given that providing the particular taxpayer with prior notice would defeat the purpose of the exercise).

There are, however, a number of shortcomings in this type of reasoning in the context of EoI.

It is a fundamental principle of administrative justice that the fairness of the administrative procedure will depend on the circumstances of each case. Fair procedural action by its nature requires the decision maker to apply their mind to the circumstances of each case, which reduces the scope for generalisation.

As a result, broadly speaking, the SARS would therefore not be justified in assuming that each taxpayer whose information is to be exchanged is likely to be a tax evader who will abuse any notification procedure in order to undermine an investigation into his or her tax affairs. It is submitted that the failure by SARS to comply with section 3(2) of the PAJA in all instances of information exchange will result in a presumption of guilt to tax evasion that cannot be justified. It is inconceivable that the SARS would be able to procure evidence to substantiate such a blanket claim.

¹²⁸ Section 36(1)(e) of the Constitution.

¹²⁹ Oguttu, A.W., A Critique on the Effectiveness of “Exchange of Information on Tax Matters” in Preventing Tax Avoidance and Evasion: A South African Perspective, 68 Bull. Intl. Taxn. 1 (2014), Journals IBFD.

¹³⁰ Ibid.

¹³¹ *Contract Support Services (Pty) Ltd and Others v C:SARS, and Others* 1999 (3) SA 11133 (W).

It is worth noting that in a purely domestic scenario, when conducting an investigation into the affairs of a taxpayer (in the context of an audit), the SARS must, under normal circumstances, notify the taxpayer of the impending administrative action and must provide the taxpayer with status reports throughout the process.¹³²

It is anomalous that the protection afforded to taxpayers in the context of a purely domestic investigation should differ so completely from that currently afforded to taxpayers, in practice, during the SARS' participation in EoI. Objectively, the 'tip off' risk is the same in both a domestic and international scenario (as assets may be dissipated in both instances).

Moreover, in both search and seizure procedures and the appointment of an agent to collect tax debts there are remedies available to the taxpayer should they believe that the administrative action taken was not fair (beyond the fact that notice was not provided). As expanded upon later in this section, such remedies might prove difficult to access in practice in the context of EoI. The fact that an application must first be brought before a judge before a search and seizure procedure is conducted also offers the taxpayer some form of protection that is currently absent in the EoI process in South Africa.

Having said this, however, the need for an effective administration must be borne in mind. Section 33(3)(c) of the Constitution requires legislation to be effected to promote efficient administration, which is why the fourth factor under section (3)(4) of the PAJA, namely the 'need to promote efficient administration and good governance', must be considered.

It could be argued that the notification process would place an unfair administrative burden on the SARS. For this argument to be successful, it would have to be shown that the detrimental impact on the ability to effectively administer the law is disproportionate to the harm done to the taxpayer under an alternative.

The conflicting interests between the efficiency of the administration versus the protection of the taxpayer's rights will boil down to the fundamental question of proportionality.

Hoexter comments in this regard as follows:¹³³

"Efficiency is, of course, an attractive and worthy goal because it promotes the speedy and cost-effective delivery of goods and services; but one must be wary of placing too much emphasis on it or treating it as an end in itself. There is always the possibility that speed and cost-effectiveness will be valued above correctness, producing the consequent danger of elevation of the means (efficiency) over ends (legislative goals)."

In terms of the affected person's rights following the taking of a decision, section 5 of the PAJA deals with the taxpayer's right to request written reasons from the administrators for the administrative action.

¹³² TAA chapter 5.

¹³³ Hoexter, C, Administrative Law in South Africa, 1st ed (Cape Town: Juta & Co Ltd, 2007), p. 217.

Section 6 deals with the judicial review of administrative action. Both these sections will be of relevance after the fact – i.e. after the decision has been made and the taxpayer’s rights have already been affected.

Section 5 would arguably allow taxpayers to request reasons from SARS for the decision to share their information with the other contracting State’s competent authority. If they were not made aware of the decision to begin with and are therefore not aware of it having happened, however, it would be practically impossible to call on this provision. Furthermore, informing the taxpayer of the decision to share their information after the fact seems to be little more than closing the stable door after the horse has bolted.

This is also true, it is submitted, for the purposes of section 6’s judicial review. Once the information is shared – the damage is done, so to speak. The information could not practically be ‘unshared’. Where a judicial review or appeal reveals that there was a defect in SARS’ decision to share the information (either in the fairness or rationality of the procedures followed in making the decision itself, or in the accuracy of the information shared), this could form the basis of an application in the foreign jurisdiction for this information to be disregarded. The success of such an application is, however, by no means guaranteed.¹³⁴

The provisions of section 5 and 6 of the PAJA might provide the taxpayer with some relief. For example, where the information was illegally shared, the review process might pave the way for a claim for damages suffered. In practice, however, the risk remains that the taxpayer will be left bearing the consequences of unjust information exchange (without any real, practical remedy).

The *Aloe Vera* case¹³⁵ in the US is a good illustration of the injustice occasioned by unjust information exchange.

In the *Aloe Vera* case, the plaintiff, Aloe Vera of America Inc, sued the US government for USD 52 million following the leak of sensitive taxpayer information to the Japanese press. The information, shared as part of a dual tax investigation undertaken by the US and Japanese revenue authorities, was furthermore shown to have been inaccurate. The taxpayer was not given prior notification of the exchange, nor were they given the opportunity to make any representations during the process to dispute and correct the accuracy of the information. The court found in favour of the plaintiff, after determining that the US government shared information they knew to be inaccurate. The amount awarded, however, was a mere USD 1,000 in statutory damages, after the plaintiff failed to prove causality, *i.e.* that actual damage was incurred as a result of the unlawful EoI.

In South Africa there has been at least one instance where a taxpayer’s information was shared with the competent authority of the wrong country.¹³⁶ The taxpayer was not notified of the SARS’ proposed decision and was not allowed to make any representations in order to ensure that the information was

¹³⁴ See, for example, *Hua Wang Bank Berhad v Commissioner of Taxation* (No 7) [2013] FCA 1020.

¹³⁵ Case No VC-99-01794-PHX-JAT.

¹³⁶ Croome, pp.166-177.

correct, and shared with the correct country. Naturally, this caused difficulties for the taxpayer who then had to explain their affairs and position to the receiving State.

Internationally, there is no consensus as to what practical protection should be afforded to taxpayers during the exchange process. Some countries, such as South Africa, provide taxpayers with no notice whatsoever (either before, or after the exchange), whereas other countries, such as Germany, Ireland and Liechtenstein, require that the taxpayer must be notified prior to the exchange.¹³⁷

Proposed 'best practice' in this regard, as put forward by Baker and Pistone,¹³⁸ would be for both the supplying and receiving State to inform the taxpayer when EoI request is generated or received – with this right to notification being waived only when a reasoned request to do so is made by the receiving State in instances where the notification would prejudice the investigation.

It is therefore submitted that on the basis that EoI amounts to 'administrative action' subject to the PAJA, the taxpayer's right to procedural fairness can only be realised if the SARS principally adheres to the protection offered by section 3(2). As is evident of the discussion above, specific legislation may be required to regulate the circumstances under which SARS may deviate from the obligations under section 3(2), such as when a real risk exists that the investigation process may be prejudiced. As mentioned, precedent already exists in the parallel domestic scenario where an *ex parte* application must be brought before a High Court judge.

Moreover, as emphasised in Chapter 4 of this paper (in the context of the POPI Act's notification requirements), informing the taxpayer of the impending exchange and affording them the opportunity to correct any inaccurate information would improve the quality of the information shared and contribute to the efficacy of the process.

5.2.2.1.1 The reasonableness of the limitation, with specific reference to EoIR

Internationally, there have been questions raised surrounding the efficacy of EoIR in meeting its core objectives. Studies performed on the effectiveness of TIEAs (which only allow for exchange upon request) have indicated that they have little effect on the behaviour of tax evaders.¹³⁹ Many commentators have pointed out that there appears to be a lack of evidence to support the view that exchange of taxpayer information has had a meaningful impact on assisting in curbing tax evasion.¹⁴⁰

¹³⁷ Meinzer, M., The Creeping Futility of the Global Forum's Peer Reviews, Tax Justice Briefing (March 2012), Tax Justice Network, p. 16.

¹³⁸ Baker and Pistone, p. 80.

¹³⁹ Oguttu, p.11.

¹⁴⁰ Stewart, M., Transnational Tax Information Exchange Networks: Steps towards a Globalized, Legitimate Tax Administration, 4 World Tax J. (2012), Journals IBFD; also M. Meinzer, The Creeping Futility of the Global Forum's Peer Reviews, Tax Justice Briefing (March 2012), Tax Justice Network.

The doubt cast over the efficacy of EoIR in meeting the objective it was designed to achieve will raise questions as to whether the limitation of the taxpayer's rights can be justified (in the context of section 36 of the Constitution).

It must be noted however, that it has also been argued that the protection currently afforded to taxpayers, in combination with the other provisions currently in place surrounding EoIR (for example, the requirement that the information must be 'necessary' or 'foreseeably relevant' for the enforcement of the contracting States' tax laws) is the root cause of the disappointing results achieved thus far.¹⁴¹

5.2.2.1.2 The reasonableness of the limitation, with specific reference to EoIA

Some have argued that the obligation to notify the taxpayer prior to the exchange is of greater relevance under EoIR given that the issue of data security takes precedent in the context of EoIA.¹⁴² This argument is based on the sheer volume of information being processed and large number taxpayers affected as part of the EoIA process making it impractical to notify each taxpayer individually.¹⁴³ As mentioned earlier, care should be exercised not to over emphasise efficiency considerations when fundamental rights are at issue.

As stated in Chapter 4 in the context of the notification requirements contained in the POPI Act, this argument might be challenged in South Africa, where it is the norm for financial institutions to automatically notify accountholders via text message or email should any transaction be processed on their accounts. It should be possible to use this same, existing technology to notify the taxpayer of the impending exchange of their private information.

In the context of EoIA, it should also be considered whether the PAJA would impose any obligations on the financial institutions as well. The PAJA applies not only to administrative action carried out by organs of State, such as the SARS, but also by other persons "*exercising a public power or performing a public function*".¹⁴⁴ It should therefore be considered whether the financial institutions are also exercising a public power or performing a public function when participating in the EoIA process. This analysis is, however, beyond the scope of this paper.

5.3 Summary remarks

As required by section 33 of the Constitution, the PAJA was enacted to give effect to the fundamental right to just administrative action.

The 'standard procedure' prescribed by the Act would include the prior notification of the person whose rights are affected by the administrative action and affording them the opportunity to make

¹⁴¹ Ogutto, p. 10

¹⁴² Baker and Pistone, p. 59.

¹⁴³ Ibid, p. 64.

¹⁴⁴ PAJA section 1, definition of 'administrative action' par (b).

representations. Any deviation from this standard will only be considered lawful where it is shown to be just and fair under the circumstances.

The analysis performed in this chapter has shown that EoI falls within the scope of the PAJA because it meets the Act's definition of 'administrative action'. The SARS' processes and safeguards surrounding the EoI process would therefore need to comply with those prescribed by the Act. This is, however, not the case at present.

The detailed reasons supporting the aforementioned conclusion are as follows:

A key question in determining whether EoI would meet all the criterion of the PAJA definition is whether the 'decision' to share the information has a direct, external, legal effect on the taxpayer's rights.

The meaning of the term, 'decision', under the PAJA includes both the making of an administrative decision, as well as the failure to make such a decision. In applying this definition to EoI, it is necessary to differentiate between EoIA and EoIR.

Under EoIA, the exchange process is so rigidly automated that the procedures carried out by the SARS can be argued to be devoid of any real evaluative process. In other words, the relevant SARS official, as the 'decision maker', does not critically evaluate the information before them for accuracy, or foreseeable relevance, before executing the bulk exchange. The SARS' therefore fails to make a decision during the EoIA process.

This can be distinguished from EoIR. Under EoIR, the very nature of the mechanism requires a more determinative process on the part of the SARS, with the process and procedures undertaken by the SARS being comparable to those undertaken as part of a domestic tax audit. Here, the SARS does make an administrative decision when complying with a request to share taxpayer information.

Both EoIR and EoIA therefore amount to a PAJA 'decision'.

As to the so-called 'ripeness criterion' (*i.e.* whether the rights of the taxpayer have been affected with direct external legal effect), the South African courts have been clear in providing guidance as to how this requirement should be interpreted. In the *Digital* case,¹⁴⁵ the SCA's approach to making this determination is to not merely include actions where prejudice has already occurred, but also instances where prejudice is inevitable (regardless of whether the action is complete or not). In the context of EoI, where the taxpayer's right to privacy will necessarily be restricted (see Chapter 4), the meaning of 'direct, external legal affect' is broad enough to encompass the 'decision' (as defined by PAJA) to exchange taxpayer information.

¹⁴⁵ *Chairman, State Tender Board v Digital Voice Processing* 2012 (2) SA 16 (SCA), para. 17.

On this basis, the SARS has a legal obligation to comply with the provisions of the PAJA during the EoI process. Specifically, the SARS has a duty to comply with the notification procedures prescribed by the Act.

The SARS' current practice of universally denying taxpayers the right to notification is at odds with this obligation, and, it is submitted, cannot be argued to be to be fair and justifiable.

It is a fundamental principle of administrative justice that the fairness of the administrative procedure will depend on the circumstances of each case.

Given that the circumstances of each taxpayer, and therefore also circumstances surrounding each exchange will be different, the blanket denial of the right to be notified in every instance, without exception, cannot be justified.

It is submitted that the prior notification of the taxpayer should be the rule in the EoI process (both EoIR and EoIA). Any restriction of this notification process being the exception, made only when the specific circumstances of that exchange justifies the departure from this norm (for example, when a real risk exists that notifying the relevant taxpayer would prejudice that particular investigation).

To realise this in practice, it is recommended that legislation be enacted to regulate the circumstances under which the SARS may deviate from the 'standard' PAJA notification obligations (as set out in section 3(2) of the Act). In this respect, precedent already exists in the parallel domestic scenario where an *ex parte* application must be brought before a High Court judge in the context of a search and seizure operation.

CHAPTER 6: OVERALL SUMMARY REMARKS AND CONCLUSION

This minor dissertation identifies and analyses the constitutional considerations raised by the current protection afforded to taxpayers in South Africa during the EoI process. The analysis deals with both EoIA and EoIR, and is done with specific reference to the taxpayer's fundamental rights to privacy and just administrative action. Due recognition is given to the lawful limitation of these rights, as provided for in section 36 of the Constitution.

Currently in South Africa, taxpayers are not afforded the opportunity to participate in the EoI process. Taxpayers are not informed of the impending exchange of their private information, are not afforded the opportunity to review the information prior to the transfer, object to the exchange, or make any representations during the process. The affected taxpayer is also not informed of the exchange having taken place after the fact.

This paper by no means objects to the desirability or validity of the pursuit of effective tax administration. It is furthermore accepted that in the era of globalization and international mobility, achieving this purpose would require the cooperation of tax administrations across national borders. One such mechanism of cooperation being the exchange of taxpayer information between competent authorities.

Having said this, however, the research performed resulted in the identification of certain critical shortcomings in the current legal protection enjoyed by taxpayers in South Africa during the EoI process.

Specifically, the analysis identifies two fundamental deficiencies in the current EoI framework in South Africa, namely: inadequate measures to ensure that the confidentiality of taxpayer information is maintained during the exchange process; and the indiscriminate and categorical denial of the taxpayer's right to be notified of an exchange. These deficiencies are compounded by the limited remedies available to the taxpayer, in practice, once the information has been passed to a foreign State.

These shortcomings in the protection afforded to taxpayers arise as a result of a combination of factors, including deficiencies in legislation that does not adequately circumscribe the discretionary powers of the SARS, as well as a lack on the part of the SARS to adhere to those safeguards already provided for in South African law.

The extent of the resultant curtailment of the taxpayer's fundamental right to privacy and just administrative action profoundly erodes the proportionality and rationality of the limitation when weighed against the purpose it aims to achieve, namely the enforcement of tax laws.

Doubts surrounding the proportionality of the violation of the taxpayer's rights become particularly apparent in the context of EoIA, where the information exchange is triggered by a set of broad presumptive criteria (without any critical evaluation of the circumstances of each taxpayer affected). Given the number of taxpayers caught in the EoIA net, the rational link between the means of the process, and the ends it hopes to achieve, becomes frayed.

In light of the conclusions reached by the analysis performed for this dissertation, the following recommendations are proposed to address the various shortcomings identified:

- Legislation should be developed to circumscribe the discretionary powers afforded to the SARS in determining the circumstances and manner in which taxpayer information may be exchanged.
- In the context of safeguarding the confidentiality of the taxpayer's private information:
 - section 108(5) of the ITA, which permits the SARS to deviate from the standard confidentiality safeguards which would apply in a purely domestic context, should be amended to take into account the coming into effect of the 1996 Constitution; and
 - legislation, such as the POPI Act, must be given effect to ensure that before exchanging information with the other State, the SARS must ensure that the secrecy provisions in place in said State are similar to those enforced domestically (as is already provided for in the context of EoIA in the OECD Standard).
- In terms of the taxpayer's right to be notified, the SARS should adhere to the fundamental principles of administrative justice, as given effect to by the provisions of the PAJA. Accordingly, the SARS should, as standard practice, provide the taxpayer with prior notice of the pending exchange. The affected taxpayer should also be afforded the opportunity to make representations during the process, and request written reasons from the SARS for the administrative action taken. Any deviation from this standard should be done only in exceptional cases where a critical evaluation of the circumstances surrounding that particular taxpayer reveals compelling reasons to do so. To this effect, it is recommended that legislation be put in place to provide guidance as to under which circumstances such a deviation would be justified.

This minor dissertation furthermore highlights that South Africa is not unique in facing the challenges and shortcomings set out above. With the drive towards greater transparency being driven on an international stage by the G20, many other countries have also been left grappling with the same questions.

In this international context, Baker and Groenhagen rightly point out that:¹⁴⁶

"...as more information is exchanged between revenue authorities, it is increasingly anomalous that the taxpayer has no way of protecting the rights guaranteed in the instruments under which the information is exchanged."

This sentiment is echoed by commentators such as Pistone, who, along with Baker, have recently raised concerns regarding the one-sidedness of current developments in the EoI arena in favour of efficient administration – with little being done to ensure that the taxpayers' rights are adequately safeguarded.¹⁴⁷

In this regard, on the occasion of the 2015 Congress of the International Fiscal Association ('IFA'), it was announced that a monitoring group will be established within IFA. This Monitoring Group will measure

¹⁴⁶ Baker and Groenhagen, p. 22.

¹⁴⁷ Baker and Pistone, p. 58.

the effective protection of taxpayer rights across participating States (including South Africa) against certain identified minimum standards identified by Baker and Pistone in their General Report to the Congress.

As the work of the Monitoring Group progresses, one would hope that South Africa's enthusiasm for remaining at the forefront of international developments in tax law and administration extends to advances in the practical protection of taxpayers' rights.

The fervent efforts of the SARS to carry out its mandate as the nation's tax collector in the fullest and most efficient manner possible is indeed admirable, if not indispensable to the country as a whole. In doing so, however, the SARS must give effect to the rights of the taxpayer as enshrined in the Constitution of South Africa. In the context of EoI, this dissertation concludes that the taxpayer's fundamental rights to privacy and just administrative action cannot simply be sacrificed on the altar of administrative ease and efficiency, as it appears to currently be the case in practice. Where needed, legislation must be amended to rectify this, and so too must the conduct of the SARS in practice.

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