

## 2025/26 Budget promises to clarify understatement penalties - but at whose expense?

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In the 2025/26 Budget Review, National Treasury commended SARS for the strides made over the past five years in rebuilding and modernising its systems by shifting to online services and automating many of its processes. Treasury further supported SARS in their efforts to focus on improved revenue collection in 2025/2026.

One of the (many) weapons in SARS' arsenal is the understatement penalty regime, which serves to encourage tax compliance by deterring tax evasion. These penalties apply across tax types and can range between 10% - 200% of the shortfall in tax, depending on the blameworthiness of a taxpayer's behaviour. The behaviour categories, ranging from least to most blameworthy, are:

- “substantial understatement” (a defined term based on the amount of tax involved);
- reasonable care not taken in completing return;
- no reasonable grounds for “tax position” taken;
- “impermissible avoidance arrangement” (pertaining to the anti-avoidance rules);
- gross negligence; and finally
- intentional tax evasion.

A “*bona fide* inadvertent error”, which is not a defined term, allows taxpayers to escape the imposition of any understatement penalties, regardless of the behaviour category involved (although categories such as intentional tax evasion and gross negligence would seem to be disqualified by implication).

SARS has traditionally taken an extremely narrow view of the term *bona fide* inadvertent error - perhaps understandably, given the power of the term. SARS has however in recent years not been able to successfully defend its narrow view in the highest courts, particularly where taxpayers relied on professional tax advice that “got it wrong”.

Seemingly in response to the defeat suffered by SARS in recent cases, Annexure C to the 2025/26 Budget proposes to clarify the term “*bona fide* inadvertent error” by explicitly linking the term with “substantial understatement” (i.e. the first of the behaviour categories). This will surely be an unhappy marriage since a “substantial understatement” is a precisely defined term based on the amount of tax involved, whereas the meaning of a “*bona fide* inadvertent error” is open to interpretation.

It is unclear how linking the two terms will address the uncertainty inherent in the one. One can speculate that given the focus on improved revenue collection, the circumstances under which taxpayers will in future be allowed to rely on a *bona fide* inadvertent error are bound to become more restricted. It would be regrettable if this comes at the expense of taxpayers who committed a *bona fide* inadvertent error by relying on professional tax advice that “got it wrong”.