100 | YEARS OF INCOME TAX

WITH A FOCUS ON SARS OVER THE LAST 20 YEARS

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ABBREVIATIONS AND ACRONYMS

BEPS	Base erosion and profit shifting
BCOCC	Border Control Operational Coordinating Committee
CCB	Customs Control Bill
CDB	Customs Duty Bill
CIPC	Companies and Intellectual Property Commission
CIT	Corporate income tax
CGT	Capital gains tax
Customs and Excise Act	Customs and Excise Act 91 of 1964
DWT	Dividend withholding tax
GAAR	General anti-avoidance rule
GST	General sales tax
G20	Group of Twenty
IMF	International Monetary Fund
Income Tax Act	Income Tax Act 58 of 1962
MTU	Mobile tax unit
OECD	Organisation for Economic Co-operation and Development
PAYE	Pay-As-You-Earn
PBO	Public benefit organisation
PIT	Personal income tax
SACU	South African Customs Union
STC	Secondary Tax on Companies
TA Act	Tax Administration Act 28 of 2011
TBVC	Transkei, Bophuthatswana, Venda and Ciskei
TCC	Tax Clearance Certificate
TCS	Tax compliance status
VAT	Value-added tax

PREFACE BY THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE

It is with great honour that I took up the position as the Commissioner for the South African Revenue Service (SARS) in the 100^{th} year of income tax in South Africa.

SARS' current target of almost R1 trillion would have seemed incredible in 1914 – when the total tax receipts was £482 000! In 1914 how astonishing it would have seemed to the approximately 5 000 taxpayers that in 2014 around four million taxpayers could file a tax return remotely, from any place and without the need for paper.

Over these 100 years, South Africa has evolved in a remarkable way. The country has seen its way through two world wars and has emerged as a constitutional democracy after an oppressive system marked as a pariah state, shackled by sanctions and fraught with internal conflict and prejudice.

SARS was created as a semi-autonomous organ of state in 1997, in the stages of the birth of democracy in our country. SARS has matured over the last 20 years to become a tax authority that is recognised for its professionalism and efficiency. The organisation reflects South Africa's progression, from a neglected and deteriorating institution, into an efficient administration that embodies Constitutional values and practices responsible administration.

The collective experience, effort and dedication of the thousands of SARS officials who make up SARS today have created a tax authority which is ready, willing and able to tackle the challenges that the next 100 years will present. Just as the country was affected by the Great Depression of the 1930s, the repercussions of the financial crises of 2007/8 have been felt in South Africa – although the sound financial regulatory framework shielded us from the full impact. The results of numerous recent studies and research suggest that global trade, electronic communications and transactions, coupled with increasingly sophisticated business practices, have contributed to enormous illicit outflows from South Africa as well as other developing countries. Tackling this is one visible challenge that exists in the immediate future. Supporting achievement of the New Growth Path and National Development Plan is another major immediate objective.

SARS responded to and supported the needs of a new democracy, and as the Commissioner, I am committed to ensure that SARS will continue to contribute what the country is entitled to expect of us.

Commissioner for the South African Revenue Service

This document was prepared as part of a conference held in Cape Town on 17 November 2014 to commemorate 100 years of income tax in South Africa. The challenge – in identifying a topic that would contribute meaningfully to the tribute of a century of income tax in South Africa – was deciding where to begin and where to end.

1994 was a profound time in the history of South Africa. The year marked the transition of South Africa to an open economy and democracy for all. The new economic and political dispensation created numerous demands on government administration, not least of which was the need for increased resources to improve the lives of all South Africans and to provide for government's developmental path.

In certain reviews conducted on other countries in transition, it has been noted that a comprehensive tax system and an effective tax administration play a central role in transitional economies. It has even been said that this is "one of the most complex and serious macroeconomic problems that transition countries are faced with"[1]. Tax reform is a fundamental component in the progression of transitional countries, and cannot be achieved without both good tax policy and an effective tax administration. Tax policy and tax administration are therefore closely intertwined.

Tax is woven into the fabric of civil society. In essence the implicit social contract – between the state and those who use a country's resources as a resident or as a trader – provides the moral and legal justification for paying and enforcing payment of taxes. The elements that make up this social contract between the state and people of South Africa changed dramatically in 1994.

It is therefore considered to be sufficiently important to concentrate on tax law and the tax administration between the period between 1994 and 2014. The Austrian-American economist Joseph Schumpeter said[2]:

> *The spirit of a people, its cultural level, its social structure, the deeds its policy may prepare all this and more is written in its fiscal history. He who knows how to listen to its message here discerns the thunder of world history more clearly than anywhere else.*

Chapter 1 touches briefly on the years before 1994 and provides a baseline of both tax legislation and the structure of the revenue and customs authority, against which the reform process can be compared. This Chapter provides the historical context to the establishment of SARS as a semi-autonomous authority which is the subject of Chapter 2.

Semi-autonomy allows greater flexibility over the management of resources and personnel and Chapter 3 deals with these aspects of transformation. Chapter 4 continues the theme of transformation, but focuses on the *Siyakha* programme which is the foundation of the current SARS. SARS' investment in automation and modernisation, which is discussed in Chapter 5, continues the SARS transformation theme. Chapter 6 explains how the modernisation and automation initiatives were implemented and how these have impacted on both SARS' operations and on the tax products managed by SARS.

After having followed the administrative transformation of SARS from inception to current modernisation, Chapter 7 explains the development of tax laws and policy over the period. This Chapter deals with various themes, from the alignment of tax policy and practice to constitutional principles, the amendments made to accommodate the integration of South Africa into the global community and the various incentives and provisions intended to generate economic growth and prosperity.

Chapter 8 focuses on the Tax Administration Act, 2011 which consolidates all tax-administrative provisions into a single piece of legislation. The tax court, tax board and the informal alternative dispute resolution process comprise the avenues available to taxpayers to resolve tax disputes and these are considered in Chapter 9. This Chapter also contains a brief review of certain cases that are considered to be watershed cases, many of which have stood the test of time. The discussion is by no means intended to be an exposition of the rich history of South African tax cases.

An overview of the last 20 years of taxation in South Africa would be incomplete without a review of the international environment. Chapter 10 therefore looks at the introduction of residence-based taxation in South Africa together with the growth in the network of international agreements and SARS' involvement in international bodies.

The establishment of SARS as a semi-autonomous body amalgamated the administration of both tax and customs and, although this document is focused on the history of taxation, a significant issue of transformation is the transformation of customs. This is discussed separately in Chapter 11.

Tax administrations are absorbed with the question of how to balance enforcing tax laws with the fair treatment of taxpayers. Chapter 12 discusses how SARS has used its resources to improve services provided to taxpayers, while Chapter 13 focuses on the measures intended to improve compliance levels.

SARS has used the benefits of its semi-autonomous status to become an effective tax and customs administration, and in Chapter 14 the benefits of SARS' transformation are discussed.

There is little doubt that tax has taken centre stage in 2014. This is evidenced by the Group of Twenty's (G20s) sustained focus on tax reform, the international response to the base erosion and profit shifting (BEPS) programme driven by the Organisation for Economic Co-operation and Development (OECD), developments in the exchange of information for tax purposes between countries and the international consensus around certain tax principles. Finally, Chapter 15 briefly sets out some of the major challenges SARS will face in the next few years.

CHAPTER 1

THE YEARS LEADING UP TO 1994

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This Chapter contains a brief discussion of the tax system that existed in the years before 1994 and sets out how the tax system and the revenue authority developed in the years before 1994.

1.1 Tax legislation in the years leading up to 1994

Before the Union of South Africa was established on 31 May 1910, the four administrative regions of the Cape Colony, Natal, Oranje Vrijstaat and the Zuid-Afrikaansche Republiek governed themselves and relied primarily on trade duties, indirect taxes and user fees for revenue.

Until 1914 there were no general income taxes. Revenue streams consisted of mining taxes, licence fees, stamp duties, transfer duties and similar levies. The Department of Customs and Excise and Posts and Telegraphs collected import duties, excise duties, postal fees and railways and harbour revenues. In 1914 the Income Tax Act was introduced and taxed profits and gains from a source in South Africa with effect from 20 July 1914. The Mining Tax Act of 1910 and the 1914 Income Tax Act were consolidated in 1917 under the Income Tax (Consolidation) Act and allowed Parliament to annually fix the rates of income tax.

The 1917 Income Tax Act was replaced in 1925, and in 1941 a new Income Tax Act was promulgated. During World War II an excess profit special levy and a special trade profits special levy were introduced and remained in force until 1947.

Donations tax was incorporated into the 1941 Income Tax Act in 1955 as a progressive duty that was levied on cumulative donations made after 23 March 1955. A flat rate of 15% was applied following the recommendations of the Margo Commission of Enquiry into the Tax Structure of the Republic of South Africa in 1988 and then increased to 25% in 1996 before the current level of 20% was applied from 2001.

A levy on wealth existed in one form or other in all administrations before 1910 and in 1922 the Death Duty Act 29 of 1922 was promulgated. This Act remained in force until it was replaced in 1955 by the Estate Duty Act 45 of 1955. Originally estate duty was levied at a progressive rate but, like donations tax, a flat rate was introduced in 1988.

It is said that transfer duty, which saw its beginnings in 1686, has the longest history of all taxes in South Africa. Transfer duty shifted to a “quitrent system” that evolved in different ways in the different administrations, but in 1910 transfer duty was consolidated at a fixed 2% (except for the Transvaal).

The current Income Tax Act 58 of 1962 was introduced in 1962 and was amended to include Pay-As-You-Earn (PAYE) in 1963. PAYE, together with provisional tax, eased the burden on taxpayers to pay large lump sums after the end of the tax year when they were assessed. These two mechanisms revolutionised the collection of taxes and, until today, assist taxpayers in spreading their tax payments over time. At the same time the provisional tax and PAYE systems improved government’s cash-flow and reduced the administrative burden to annually assess and collect taxes. The move to collect taxes periodically rather than annually was a challenge to administer and was not well-received by taxpayers.

In 1972 the Sixth Schedule to the Income Tax Act was introduced to include gains derived from certain insurance policies in gross income.

In 1978 a general sales tax (GST) on the sale to consumers of consumable and capital goods and services was introduced through the Sales Tax Act, 1978. GST was a cascading tax, in that it did not provide for the deduction of tax paid in earlier stages of the value chain. Economic factors rather than tax should determine business organisation, and one negative effect of GST was that it motivated traders to integrate their businesses vertically in order to avoid tax. GST also affected capital-intensive industries particularly and increased export prices. In an effort to address some of the challenges of GST, exemption certificates were used to allow tax-free purchases for resale by businesses. Exemption certificates were not well-regulated and the system was widely abused.

In 1984 the Seventh Schedule to the Income Tax Act was introduced to identify non-cash employment benefits and advantages that were to be included in remuneration and to provide a method for their valuation. The legislative changes followed recommendations made by various committees and commissions, but to soften the impact, parts were phased in over time. As is discussed later, a consistent theme of tax policy over the years has been to match the value of fringe benefits to an equivalent cash value.

In mid-1987 the report of the Margo Commission[3] was published. This report recommended that the growth of the economy would be hampered if business decisions were based on the tax consequences of transactions and not on business and trade considerations. The Commission made far-reaching recommendations aimed at simplifying the tax system and promoting neutrality. These recommendations included minimising the available tax concessions which complicated the tax system and frustrated organic economic growth, addressing foreign exchange gains and losses, and considering the introduction of a "comprehensive business tax" on value added by business activity on an origin basis.

In 1991 GST was replaced by the consumption and invoice-based system of VAT. The introduction of the Value-Added Tax Act 89 of 1991 brought South Africa in line with many other countries and broadened the base of tax contributors. Although the conversion from GST to VAT was initially burdensome, the benefits to both traders and the *fiscus* outweighed the increased compliance costs and the administrative burden required to regulate the system.

Before 1994, there were independent tax administrations in the broader South Africa, each administering different tax laws. Separate tax administrations and tax laws had developed in Transkei, Bophuthatswana, Venda and Ciskei (the TBVC states). Working Group Four of the Convention for a Democratic South Africa (CODESA) was established to investigate and make recommendations concerning, amongst others, integrating the TBVC states into the Republic of South Africa[4]. It was recognised that separate but parallel administrations and laws existed; and Working Group Four was tasked to address the "harmonisation of legislation and taxation". The Working Group's recommendation made during 1992[5] was:

> *3.2.2.3 Working group 4 is unanimous that there should be harmonisation of the taxation regime. The tax system of the TBVC states should be brought in line with the applicable tax laws in the RSA. This process should apply to all forms of tax structures e.g. company tax, personal tax etc. The question of tax concessions may be considered in relation to regional development issues.*

The following extract, which is a response by the South African Communist Party[6] on the issue, illustrates the complexities involved in integrating the different systems and administrations with South Africa's:

SOUTH AFRICAN COMMUNIST PARTY COMMENTS

2. A multi-lateral commission to be set up by CODESA 2 to consider a plan for the harmonisation of taxation and regulation environments. This Commission to consist of representatives of the tax authorities of the TBVC states and to include representatives from organisations who would not have automatic representation - Democratic Party, ANC, etc.

3. The process of harmonisation could be implemented incrementally and the revenue would accrue to the TBVC administrations. A date would have to be established on which agreements on taxation, etc. between businesses and TBVC governments would terminate. This would presumably be the date of dissolution of the "independent" status of the TBVC administrations and the effective date of reincorporation into the central South African state.

Figure 1: Extract from the South African Communist Party's response

1.2 The revenue authority in the early years

Before 1910 the tax administration was headed by an Inspector of Revenue which was a branch of Treasury. The consolidated revenue fund was formed by the Union of South Africa Act, 1909, into which revenue receipts had to be paid. There was an exception for revenue that was raised from the administration of railways, ports and harbours – these funds were paid to the railway and harbour fund.

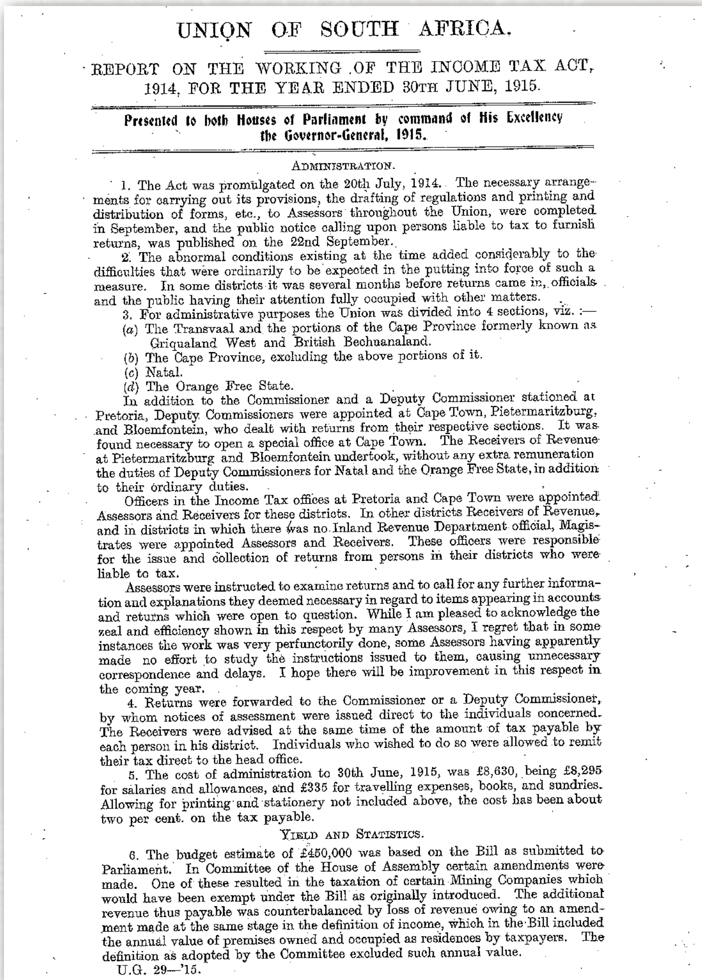
With the unification of South Africa in 1910 two separate Departments – of Inland Revenue and of Customs – were established and headed by separate Commissioners.

The separation of the administration of tax and customs and excise continued as a feature of the revenue authority until SARS was established in 1997.

In 1914, with the introduction of the Income Tax Act, a Commissioner of Income Tax was appointed alongside the Commissioner of Inland Revenue, and this continued until 1917 when the two administrations were amalgamated and a Commissioner of Taxes was established as the head of the Department of Inland Revenue.

When income tax was first introduced in 1914 it was estimated that there were approximately 5 000 individual taxpayers who were categorised as well-off, very well-off and, if a person's annual income exceeded £5 000, as rich. In terms of the first Income Tax Act around 5 742 assessments for the total value of £482 000 were issued.

The Commissioner of Taxes reported to both Houses of Parliament that the cost of collection was approximately 2% of the tax payable and that approximately 98% of the assessed amounts were paid[7].



UNION OF SOUTH AFRICA.

REPORT ON THE WORKING OF THE INCOME TAX ACT, 1914, FOR THE YEAR ENDED 30TH JUNE, 1915.

Presented to both Houses of Parliament by command of His Excellency the Governor-General, 1915.

ADMINISTRATION.

1. The Act was promulgated on the 20th July, 1914. The necessary arrangements for carrying out its provisions, the drafting of regulations and printing and distribution of forms, etc., to Assessors throughout the Union, were completed in September, and the public notice calling upon persons liable to tax to furnish returns, was published on the 22nd September.

2. The abnormal conditions existing at the time added considerably to the difficulties that were ordinarily to be expected in the putting into force of such a measure. In some districts it was several months before returns came in, officials and the public having their attention fully occupied with other matters.

3. For administrative purposes the Union was divided into 4 sections, viz. :—

(*a*) The Transvaal and the portions of the Cape Province formerly known as Griqualand West and British Bechuanaland.

(*b*) The Cape Province, excluding the above portions of it.

(*c*) Natal.

(*d*) The Orange Free State.

In addition to the Commissioner and a Deputy Commissioner stationed at Pretoria, Deputy Commissioners were appointed at Cape Town, Pietermaritzburg, and Bloemfontein, who dealt with returns from their respective sections. It was found necessary to open a special office at Cape Town. The Receivers of Revenue at Pietermaritzburg and Bloemfontein undertook, without any extra remuneration the duties of Deputy Commissioners for Natal and the Orange Free State, in addition to their ordinary duties.

Officers in the Income Tax offices at Pretoria and Cape Town were appointed Assessors and Receivers for these districts. In other districts Receivers of Revenue, and in districts in which there was no Inland Revenue Department official, Magistrates were appointed Assessors and Receivers. These officers were responsible for the issue and collection of returns from persons in their districts who were liable to tax.

Assessors were instructed to examine returns and to call for any further information and explanations they deemed necessary in regard to items appearing in accounts and returns which were open to question. While I am pleased to acknowledge the zeal and efficiency shown in this respect by many Assessors, I regret that in some instances the work was very perfunctorily done, some Assessors having apparently made no effort to study the instructions issued to them, causing unnecessary correspondence and delays. I hope there will be improvement in this respect in the coming year.

4. Returns were forwarded to the Commissioner or a Deputy Commissioner, by whom notices of assessment were issued direct to the individuals concerned. The Receivers were advised at the same time of the amount of tax payable by each person in his district. Individuals who wished to do so were allowed to remit their tax direct to the head office.

5. The cost of administration to 30th June, 1915, was £8,630, being £8,295 for salaries and allowances, and £335 for travelling expenses, books, and sundries. Allowing for printing and stationery not included above, the cost has been about two per cent. on the tax payable.

YIELD AND STATISTICS.

6. The budget estimate of £450,000 was based on the Bill as submitted to Parliament. In Committee of the House of Assembly certain amendments were made. One of these resulted in the taxation of certain Mining Companies which would have been exempt under the Bill as originally introduced. The additional revenue thus payable was counterbalanced by loss of revenue owing to an amendment made at the same stage in the definition of income, which in the Bill included the annual value of premises owned and occupied as residences by taxpayers. The definition as adopted by the Committee excluded such annual value.

U.G. 29—'15.

Figure 2: Front cover of the report to both Houses of Parliament by the Commissioner of Taxes on the "Report on the Working of the Income Tax Act", dated 31 July 1915

Until 1980, the Department of Inland Revenue and the Department of Customs and Excise operated as independent departments with their own directors-general and budgets, and reported to the Minister of Finance. In 1980 government moved these two administrations into the Department of Finance as directorates, joining seven other directorates that included Public Finance, State Expenditure, Treasury, Financial Institutions and the State Tender Board.

The effect of this move was the downgrading of the Departments of Inland Revenue and Customs and Excise. A detrimental effect that this shift had on the operations of the administrations was that the direct control and management over resources was lost. The administration of resources then fell under the Department of Finance, which did the budgeting for the whole department. The appointment of personnel had always been a challenge because it was regulated by public service rules, which in effect, meant "one size fits all". Losing control of the human resources (HR) department made the downgrading worse. The loss of direct control of information technology, which is essential in the collection, management and recording of tax collections, was a further setback.

Another development that affected Inland Revenue and Customs and Excise was the announcement by government in 1996/7 that civil servants were entitled to take voluntary retirement. This offer was particularly beneficial to persons with long service and about 1 600 employees left the directorates of Inland Revenue and Customs and Excise on voluntary retirement. This compounded the existing shortage of skilled personnel that Inland Revenue and Customs and Excise had suffered for years.

1.3 Background to structural changes in revenue administration

The position continued to deteriorate in both Inland Revenue and Customs and Excise, and was confirmed by subsequent investigations by two commissions of inquiry and the International Monetary Fund (IMF).

The Margo Commission's report in 1987 recommended that the status of the two tax collecting departments should be restored, the shortage of staff be rectified and adequate resources be provided. The White Paper[8] on the report accepted the recommendation, but it was not implemented.

Between 1989/90 and 1992/3 the ratio of taxation to gross domestic product had declined from 23.6% to 21.9%. At the time it was considered that the downward movement of the ratio was due to the downturn in economic activity but also reflected the inefficiency in tax collection.

It was recognised that there was a need to restructure government finance and in 1994 it was announced that the Financial and Fiscal Commission would play an important advisory role in regard to government's financial requirements. Steps were taken to usher in institutional changes that were needed to promote growth, increase employment opportunities, relieve poverty and change the pattern of income distribution.

In the 1994 Budget Speech the Minister of Finance announced the appointment of the Katz Commission of Inquiry into Certain Aspects of the Tax Structure to investigate the tax system and to assess improvements.

The interim report of the Commission reflected a much greater sense of urgency[9]:

> *This Commission is of the view that the problem is much deeper and more serious than simply the status of the office of the Commissioner; it is the entire organisational structure of Inland Revenue that is at issue. Major structural issues require to be addressed.*

The Commission's recommendation was that the revenue authority no longer be under the control of the Public Service Commission and be given administrative autonomy in order to be able to compete with the private sector.

In 1994 the IMF also analysed the customs administration in South Africa and found that there was almost no control over customs revenue and trade activities across borders. There was also widespread frustration within both the trading community and the customs administration about the lack of control and monitoring of trade flows.

After 1994, an additional strain was experienced by the revenue administration because the separate tax administrations of Transkei, Bophuthatswana, Venda and Ciskei, as well as those of the self-governing territories of Gazankulu, Kangwane, Kwandebele, Kwazulu, Lebowa and Qwaqua had to be absorbed into the South African Inland Revenue Department. The demand was not only on functional absorption but involved harmonising different taxes, different tax rates and the equal tax treatment of all persons. The process proved challenging and alignment was phased in over a period.

1.4 The Standing Committee on Finance

In 1993 the directorates of Inland Revenue and Customs and Excise appeared before the Standing Committee on Finance to give account of how the administrations had operated. The meeting was held in public and with absolute transparency. It was explained to the Committee the state that the administrations were in, that not all the tax that should be collected was being collected and that the control of trade activities across borders was not satisfactory.

The administrations suggested that if resources and support were given to them, additional revenue could be collected from the increased efficiency in collections, without incurring debt or the imposition of new taxes or increasing the rates of tax.

As a result of the support and efforts of the Committee and the Executive, including the Minister of Finance, change began to happen and broader support for a semi-autonomous revenue authority gained momentum.

LEGISLATION

Pre-1910 administrative regions relied on dispersed charges such as trade duties, indirect taxes, user fees, licence fees & stamp duties

- **1910** – Consolidated Revenue Fund established
- **1914** – Income Tax Act
- **1917** – Income Tax (Consolidation) Act – incorporating mining taxes
- **1922** – Death Duty Act
- **1925** – New Income Tax Act
- **1941**
  - World War II – Excess Profit Special Levy
  - Special Trade Profits Levy
  - Donations Tax incorporated
- **1962** – Current Income Tax Act
- **1963** – PAYE & Provisional Tax introduced
- **1972** – Sixth Schedule – Gains on certain insurance policies
- **1978** – Sales Tax Act
- **1984** – Seventh Schedule introduced
- **1991** – Value-Added Tax Act

REVENUE ADMINISTRATION

- **1909** – Inspector of Taxes under Treasury
- **1910** – Commissioner of Inland Revenue & Commissioner of Customs
- **1914**
  - Commissioner of Inland Revenue & Commissioner of Income Tax
  - About 5 000 taxpayers – collection of about £482 000
- **1917** – Commissioner of Taxes – consolidation of two Revenue Commissioners
- **1980** – Inland Revenue & Customs moved to National Treasury as departments
- **1987** – Margo Commission Report published
- **1990** – Trend towards semi-autonomy
- **1993** – Revenue & Customs appear before Standing Committee
- **1994**
  - Budget Speech Announcement of Commission
  - Katz Commission 1st Interim Report
  - IMF Report on structure

CHAPTER 2

ADMINISTRATIVE AUTONOMY

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This Chapter explains how SARS was established as an entity within government but with a degree of administrative autonomy required to improve efficiency.

2.1 Introduction

Semi– or administrative autonomy allows the authority to focus on its mandate, allows managerial functions to be performed in a business-like manner and gives the revenue authority greater control over its resources. An administratively autonomous revenue authority therefore has the benefit of greater flexibility and the ability to respond quickly to a changing environment.

2.2 Approval of administrative autonomy

During 1995 a memorandum on "Reforming the Inland Revenue and Customs & Excise Functions of the SA Government" was prepared by Inland Revenue and Customs and Excise. It set out the proposed plan for the autonomy of SARS outside the public service and the new entity's business plan.

It is interesting to note that some other revenue authorities within Africa were also moving towards autonomy. A working paper issued in 2011 by the IMF "Revenue Administration Reforms in Anglophone Africa Since the Early 1990s" remarked that the emergence of semi-autonomous revenue authorities was a distinguishing feature in Anglophone Africa during the 1990s:

> *Leading the RA (revenue authority) trend, Ghana established separate semiautonomous revenue services for tax and Customs administration in the mid-1980s that were loosely brought under the auspices of an RA governing board (RAGB) in 1998, followed by Nigeria's creation of separate revenue services for Customs (NCS) and tax administration (Federal Inland Revenue Service (FIRS)) in the early 1990s. However, in 1991, Uganda established the first incarnation of the model that became widely emulated over the next two decades …*

These initiatives had been studied and were detailed in the report to Cabinet. Further information on the operation of autonomous revenue authorities had been provided by an IMF Mission.

In another paper by the IMF, "Revenue Administration: Autonomy and the Revenue Authority Model", it is explained that as revenue authorities worldwide have some of the most pervasive powers seen in statute, it is not possible for a revenue authority to function wholly outside of government[10].

Along a continuum of autonomy, revenue authorities have more autonomy than a department but less autonomy than a state-owned enterprise, and the IMF located SARS within the semi-autonomous continuum of revenue authorities.

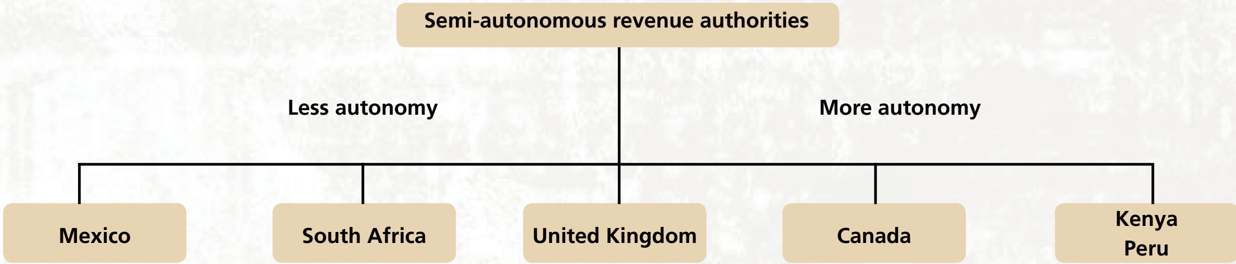

Figure 4: Relative autonomy extracted from the IMF paper

On 18 October 1995, Cabinet approved a two-step approach to the autonomy of SARS. The first step was that the directorates of Inland Revenue and Customs and Excise would be moved out of the Department of Finance to a new government department called the South African Revenue Service (SARS). All the government laws and regulations and policies applying to the old government department would apply to the new government department and personnel. When the autonomous SARS outside the public service had been created, the personnel would, as a second step, be transferred to the new entity, also initially subject to all the same rules and regulations. Only when the personnel were transferred to the new semi-autonomous SARS could the rules and regulations relating to personnel be changed.

Cabinet's approval of SARS' semi-autonomy was addressed in the 1996 Budget Speech, and the 1996 Budget Review underscored the ambitious reform programme that was expected of the new revenue authority.

> The situation in the revenue collection and control functions of Inland Revenue and Customs and Excise have deteriorated to such an extent over the past few years that a substantial investment in management, the development of professional skills and upgrading of information systems is required. The enormity of the task of reforming these functions must therefore not be underestimated.

2.3 Autonomy becomes law – the South African Revenue Service Act, 1997

In October 1997, 18 months after the initial transfer on 1 April 1996 of personnel to SARS as a government department, SARS was formally established as an organ of state within the public administration, but as an institution outside the public service. Achieving autonomy would not have been possible without the broad support of Cabinet and the Executive including the then Minister of Finance and Deputy Minister of Finance.

The South African Revenue Service Act 34 of 1997 or the SARS Act, as it is referred to, was promulgated on 5 September 1997 in *Government Gazette* No.18257.

REPUBLIC OF SOUTH AFRICA

GOVERNMENT GAZETTE

STAATSKOERANT

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No. 18257

OFFICE OF THE PRESIDENT

No. 1165. 5 September 1997

It is hereby notified that the President has assented to the following Act which is hereby published for general information:—

No. 34 of 1997: South African Revenue Service Act, 1997.

KANTOOR VAN DIE PRESIDENT

No. 1165. 5 September 1997

Hierby word bekend gemaak dat die President sy goedkeuring geheg het aan die onderstaande Wet wat hierby ter algemene inligting gepubliseer word:—

No. 34 van 1997: Wet op die Suid-Afrikaanse Inkomstediens, 1997.

Figure 5: Front page of *Government Gazette* No. 18257 of 5 September 1997 promulgating the South African Revenue Service Act 34 of 1997

The SARS Act prescribes SARS' functions, objectives and powers, determines the appointment and duties of the Commissioner for SARS and sets out the financial standards for SARS. Under this Act, SARS must advise the Minister of Finance on all matters relating to revenue and the functions that the Minister must perform in relation to revenue. SARS must also advise the Minister of Trade and Industry on matters concerning the control over the import, export, manufacture, movement, storage or use of certain goods. SARS has to report annually to Parliament and is subject to annual audit by the Auditor-General in order to ensure accountability.

Initially the SARS Act established a SARS Advisory Board to advise the Commissioner and the Minister of Finance on various issues including the management of SARS, improving revenue collection, employees' terms and conditions and SARS' budget. A former Chief Justice of South Africa acted as the Chairperson of the SARS Advisory Board until 2001. In 2002 the SARS Act was amended to substitute the Advisory Board with specialist advisory committees. The members are appointed by the Minister of Finance and advise the Commissioner and the Minister on asset management, HR and IT.

One of the consequences of becoming a semi-autonomous body was that all internal policies such as HR and finance had to be reviewed and a lot of HR and finance development work had to be done.

CHAPTER 3

CONSOLIDATION UNDER SARS AUTONOMY

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CONSOLIDATION UNDER SARS AUTONOMY

The transition from a department to a semi-autonomous body was a radical, but essential, step that allowed SARS a certain amount of freedom to transform the revenue authority from subdued divisional directorates into an efficient, professional and effective semi-autonomous authority. This transition had to be closely managed to balance stability and foster support for the changes about to happen. This Chapter deals with the initial transformation stage from directorates to SARS.

3.1 Introduction

In June 1998 the SARS Transformation Programme was launched. The programme was launched through a live broadcast involving the then Minister of Finance, the then Deputy Minister of Finance, SARS Advisory Board members and Executive Committee members.

The message was clear: Change was necessary and would have an immediate impact on all aspects of the organisation and result in positive deliverables. The process was compared to that of a caterpillar changing into a butterfly. About 400 people attended the launch and it was broadcasted to approximately 6 000 SARS employees around the country.

A National Management Forum (NMF) was introduced to take place on an annual basis. The top 200 to 300 managers were invited for two to three days during which the priorities for the year were made known and discussed. They were encouraged to participate to ensure that plans were acceptable and could be implemented, and that potential problems were identified in advance. The NMF continues to be held annually and is important for getting the buy-in of middle and top management relating to the strategic vision of the organisation and the deliverables they have to commit to.

A golden thread which informed the transformation at SARS was that working for SARS was working for the greater good of the country. This “higher purpose” related to making a contribution to the economic and social development of the country through collecting the revenue needed by government to meet its policy and delivery priorities. In 2003 a manual, *What it means to be a SARSafrican*, was produced, showing SARS employees how they fitted into the organisation and SARS’ role in the government and the economy of South Africa.

SARS introduced a policy that no gifts may be accepted by employees and a zero-tolerance to corruption was adopted and communicated. A telephone hotline system, called the Suspicious Activity Reporting System, was set up to report suspicious activities. Those allegations SARS would then investigate. This system is still in place today and is supplemented with an on-line facility to report suspicious activities to SARS.

The transformation allowed people to think more creatively about revenue collection and one of the earliest examples of this was when, on the demutualisation of two of the country’s biggest insurers, shares were given to shareholders. A regional manager of SARS noticed that a number of people who owed money to SARS were eligible to receive free shares under the demutualisation programme. SARS obtained the necessary court order instructing that shares that had been issued to indebted taxpayers were to be withheld from the shareholders until the outstanding tax was paid. This activism planted the seed for what was to become an increasingly assertive enforcement programme at SARS.

In October 1998 SARS moved its head office from the Vermeulen Street and Paul Kruger Street buildings in the Pretoria city centre to new premises in the suburb of Nieuw Muckleneuk, thereby drastically improving the work environment. There were many reasons for this move, which included promoting integration of the administration of tax and customs.

The move to a modern building underscored SARS' semi-autonomous status and contributed towards boosting staff morale.

Figure 6: Entrance to Lehae La SARS

The New Income Tax System (NITS) was developed for implementation in 1999, and its implementation (initially in the Benoni office) was the beginning of SARS' extensive automation programme. The system's main objectives were to increase on-line business functionality, enhance productivity and create a more stable income tax system by reducing human intervention and improving data integrity.

The year 1999 proved to be a watershed year for SARS, when all offices gained internet access, SARSBANK was implemented (which computerised all SARS' cash office functions), employees' tax certificates could be submitted electronically and SARS developed the capability of interfacing electronically with other institutions.

3.2 Governance structure

A conscious decision was made in 1999 to centralise decision-making and dismantle the regional structures. The rationale behind this was that inconsistent practices were developing amongst the regions. Taxpayers were also beginning to notice the variances in practice and sometimes shifted their place of registration to a region that was compatible with their needs. The centralisation of management was therefore needed to administer the tax Acts consistently throughout the country. The dismantling of the regional structures also heralded a flatter structure and a move to teamwork.

3.3. Human resources – foundational changes

Officials employed in the directorates of Inland Revenue and Customs and Excise were transferred to SARS, their rights entrenched in the SARS Act, and the HR policies applicable to civil servants were gradually replaced. Drafting and adopting new policies and practices was a major task. Over a four-year period far-reaching changes were made at SARS. The grading system was changed, the organisational structure was flattened and a new remuneration policy and performance-based rewards system were introduced.

The transformation process was not devoid of challenges. One concern was that, because of the size of Customs and Excise, it would lose its identity when integrated with Inland Revenue. Another concern was that as a result of the modernisation of SARS, people's jobs would be replaced by computers.

Managing organisational change became an important priority and SARS' internal communications division featured strongly in the change strategy. Many opportunities were given to staff members to engage with top management and to voice their concerns during several "road shows" around the country. There was a concerted effort to persuade people that those persons who bought into the vision, and who performed, would be welcomed in the transformed SARS. They were offered employment security, but not job security.

Central to the drive to get people on board was a strategic partnership with organised labour as around 85% of employees belonged to unions. Meetings were initiated with the unions to share the vision of transformation and the principles that would underpin it. After months of negotiations a collective agreement of critical importance was reached. The unions were part of the road shows to "sell" the transformation plans to employees and shared the platform with SARS management. This did not mean there was no conflict, but the communication channels remained open.

A performance-based reward system was proposed, but first employees had to be convinced that it would be to their benefit to leave behind the temporary bonus system that had been introduced earlier. Global specialists in job grading were called in for a more scientific approach towards bonuses, salary scales and placing people at the right levels. The grading system that was adopted evaluated jobs according to the level of difficulty or complexity, and replaced the civil service approach of pay increases based on tenure with promotion that was based on performance and competence. In 2001 the performance-based reward system was introduced and subsequently has been refined to better measure individual-based performance.

The changes to the remuneration system became more closely aligned to the market, making it easier to attract skilled personnel. Improving remuneration was important, but the message that was communicated was that a SARS position was not just about salary. It is considered that SARS is today a preferred employer because of the organisational structure, the purposefulness and the reward for skill.

3.4 Employment equity

Part of the new HR policies was to adopt an employment equity plan to give preference to previously disadvantaged groups. However, there was no intention to alienate long-serving employees who held value because they had acquired skills and experience over the years. Retaining the commitment of experienced staff, while also opening up opportunities for SARS to achieve employment equity, required a balancing act. Experienced employees were identified and recognised as functional experts and reassured of their future in SARS. These employees were acknowledged as specialists who could share their technical knowledge. In addition, this opened up space for persons with managerial skills from within and outside SARS to perform these functions.

Below is a graphical illustration of the growth in the equity of the workforce that has been achieved since the transformation was launched in 1998.

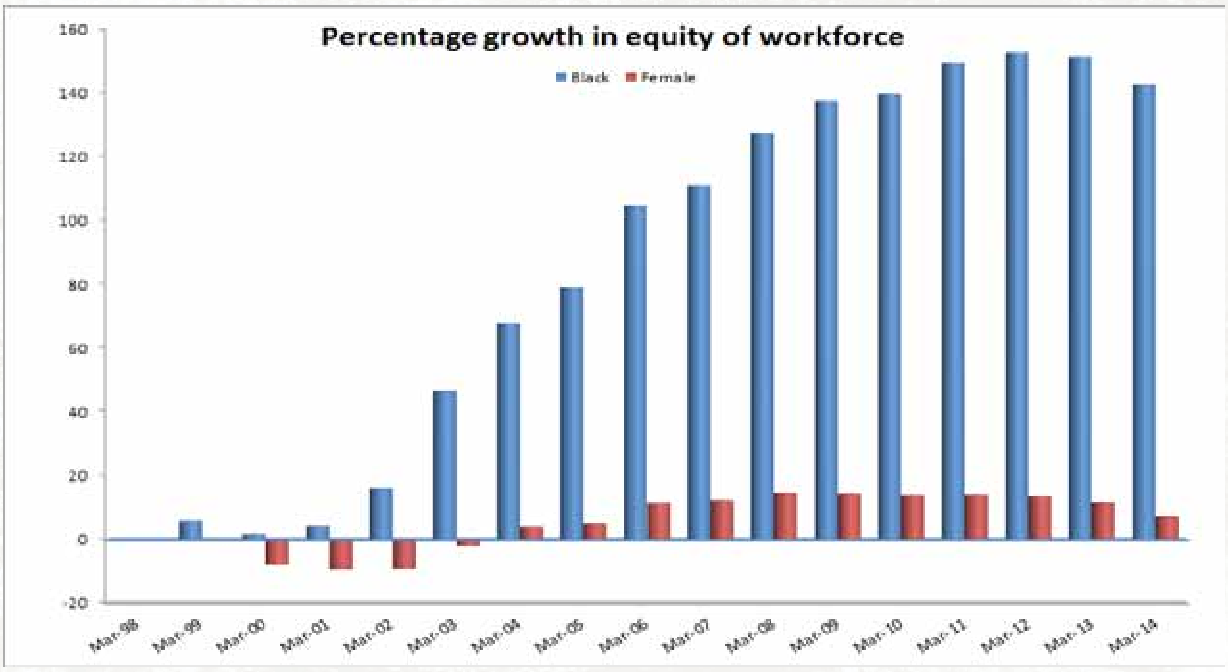

Figure 7: Growth in equity of the SARS workforce between 1998 and 2014

The graph below reflects the equity in the workforce between 2009/10 and 2013/14.

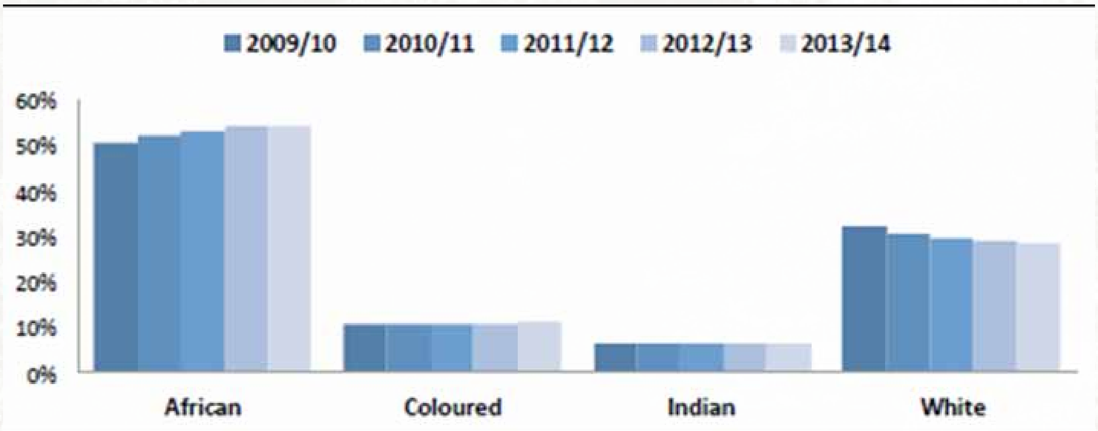

Figure 8: Equity in the workforce between 2009/10 and 2013/14

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CHAPTER 4
SIYAKHA

CHAPTER 4
SIYAKHA

The initial transitioning from a department to a semi-autonomous SARS was a success. By the end of 1999 SARS housed both tax and customs functions and HR had substantially stabilised. SARS had also met, and exceeded, budget targets. SARS then embarked on a radical reorganisation to further realise the benefits of semi-autonomy. This Chapter explains this next step in SARS' transformation.

4.1 Introduction

The year 2000 was pivotal in SARS' transformation. It was foreseen that there were huge opportunities for positive change by significantly reducing the tax gap through improved services and increased enforcement.

The objective was to radically transform the authority into a modern revenue authority that epitomised efficiency, effectiveness and responsiveness and to engender a professional, ethical and service-oriented workforce. SARS aimed to create a service culture that focused on the needs of the taxpayer, based on the principle that good service would facilitate tax compliance.

International trends in tax administration showed that there were benefits in concentrating the processing, enforcement, and service functions into specific centres. This would make best use of scarce resources and skills (such as in audit functions), gain economies of scale and develop a more integrated view of individual taxpayers.

SARS, therefore, embarked on a formal programme to re-engineer and restructure the entire organisation – a programme called *Siyakha* which is an isiZulu word that means "We are building".

4.2 The *Siyakha* focus areas

The *Siyakha* transformation programme focused on certain core problems that had been identified from in-depth research.

4.2.1 Inefficient organisational structures

Although a number of changes had been introduced into the structure, it was still bureaucratic, with many layers of management and narrow spans of control.

The way SARS was run was determined by function rather than the process and there was still a lack of uniformity across branch offices. Other shortcomings included inadequate attention being given to the service offered to taxpayers and inadequate integration of the operations of customs and revenue, which meant that activities were often duplicated.

4.2.2 Inefficiency in core business processes

It was identified that duplication of processes was wide-spread. For instance duplication of processes occurred across tax types and in respect of the registration, assessment, collection and audit functions. Furthermore, these functions were performed at each of the then 42 revenue offices, thereby compounding the duplication of processes.

Apart from the inefficiency of duplicated processing, the fragmentation of processing did not support uniformity and allowed regional peculiarities to develop.

4.2.3 Human Resource weaknesses

Despite the significant progress that had been made on this front, there were still problems relating to staff retention, especially in key functions such as audit. In addition, training was not sufficient to address the key skill shortages and staff morale was low.

4.3 *Siyakha* roll-out

The broad strategy of SARS with this project was to be a non-technology change. This meant that even though there would be adaptions to some existing legacy systems, the focus would not be on technological investment. The programme was about processes, people, changing the service approach and ultimately changing the enforcement approach.

After a detailed planning phase, SARS launched the pilot phase on 1 October 2001 in KwaZulu-Natal.

The processing, taxpayer service, customs and compliance functions were separated. The physical infrastructure, in which these areas were located, was complemented by re-engineering of internal processes and the deployment of employees to more appropriate locations.

The creation of a service centre and points of presence demonstrated SARS' focus on a customer-centricity.

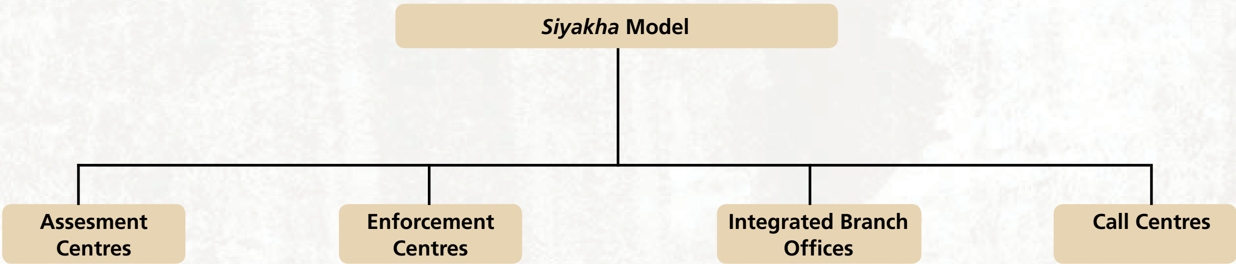

Figure 9: Diagrammatic representation of *Siyakha* model

4.4 Enterprise-wide transformation

It was envisaged that the transformation would be rolled out to the Western Cape and Gauteng. However, this decision was to be informed by information gathered from the monitoring of the pilot roll-out.

From the pilot project, SARS gained a better understanding of what was needed. It was identified that fragmentation between centres existed in the model, that there were skills gaps and that there was a greater need to improve services to taxpayers. The initial scope of *Siyakha* was then expanded to a technology-enabled, enterprise-wide transformation programme.

The enhanced *Siyakha* programme was rolled out in 2003 in the Western Cape and in Gauteng.

4.5 Results of the *Siyakha* transformation

The programme took six years from the time design began until completion, and influenced the modernisation programmes which started in 2007.

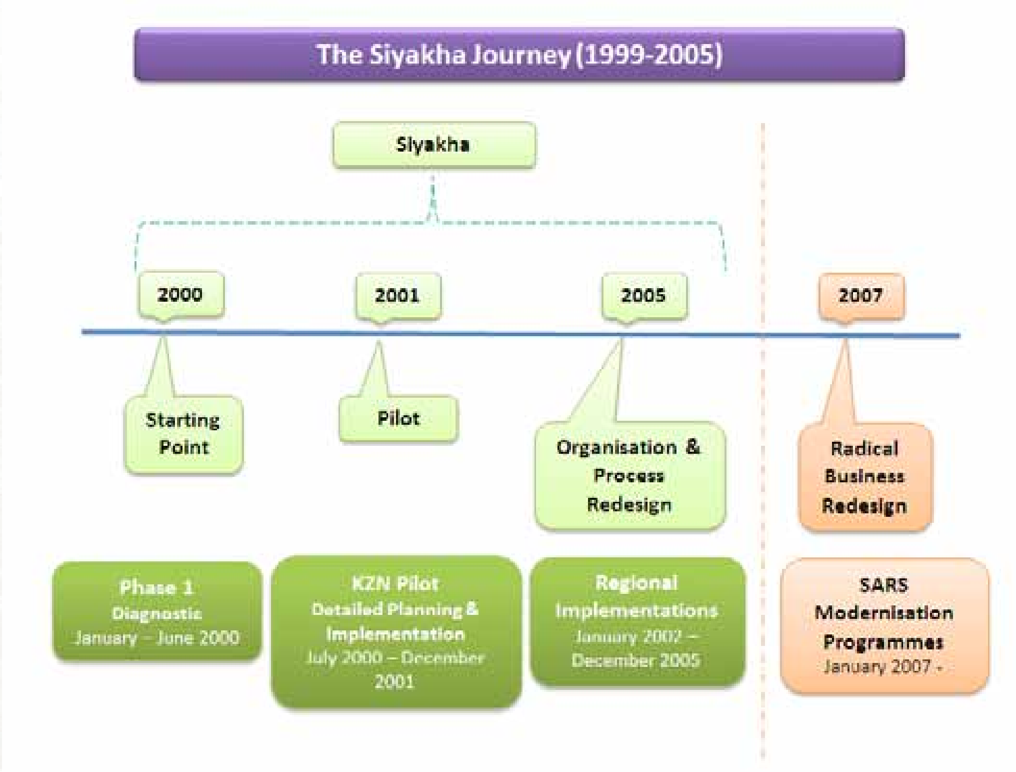

Figure 10: The *Siyakha* Journey (2000-2005) and start of the modernisation programmes

As a consequence of *Siyakha*, SARS established four large scale tax processing centres; two in Gauteng and one each in Cape Town and Durban. The centres focused on assessing taxpayers' returns, registering new taxpayers and maintaining taxpayers' files. SARS improved operational efficiency by standardising processes and grouping the functions into these four processing centres.

Additionally, 10 compliance (or enforcement) centres were established to concentrate specifically on audit, collections and criminal investigations. These centres were located in Pretoria, Alberton, Port Elizabeth, East London, Bloemfontein, Bellville, Polokwane, Nelspruit, Rustenburg and Durban.

SARS designed 42 service centres (most of them in established locations). Their functions were to focus on meeting the needs of taxpayers and to provide places where taxpayers' queries could be addressed, either in person, by telephone or through correspondence. These centres also focused on taxpayer education. Call centres were set up to handle enquiries in respect of both tax and customs matters, with extended operating hours.

Figure 11: SARS Call Centre

Siyakha brought about a few new concepts in customs administration, such as the co-location of customs and revenue, the creation of audit capacity and making the transit process more efficient.

In addition, all customs offices were restructured. SARS put in place new management teams, established risk profiling teams and an anti-smuggling unit.

The initial transformation of the revenue authority from a department to an administratively autonomous body is still considered to be the most ambitious transformation in SARS' history. As is discussed later, SARS has consistently kept the cost of collection within international norms, however during the implementation of *Siyakha* there was a necessary increase in spending.

As is discussed in 14.1 the international benchmark is around 1% of revenue collections with USA at a low of 0.6 % and Germany at a high of 1.5%.

The graph below illustrates SARS' cost to tax revenue ratio.

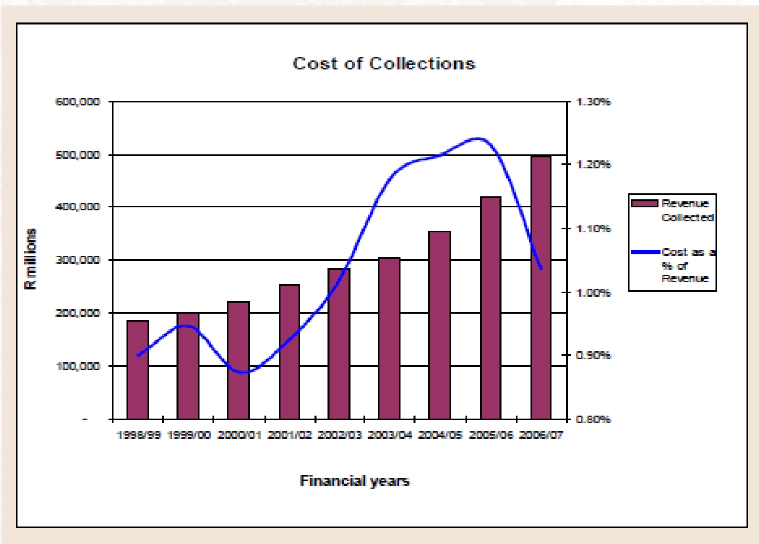

Figure 12: The cost of collections from 1999 to 2007

CHAPTER 5
MODERNISATION

CHAPTER 5
MODERNISATION

This Chapter explains the key concepts involved in SARS' modernisation programme.

5.1 Overview of modernisation

The SARS modernisation programme has its roots in the early years of the new millennium. It applies advanced technology and systems to enable the organisation to process increasing transaction volumes, contain costs and operate an innovative business model that incorporates sophisticated risk-management and the promotion of voluntary tax and customs compliance.

The modernisation programme is intended to deliver extensive performance improvements to all aspects of SARS' operations. The automation of a wide range of processes and activities has enabled SARS to transfer many employees from tasks that added less value to the organisation to more complex and rewarding work. It has also significantly improved the quality of service to taxpayers and traders.

Since the modernisation programme was launched in 2007, tax and customs revenue collected by SARS has increased from R321 billion to R900 billion and the number of registered taxpayers, traders and other persons have grown from 8.24 million to more than 20 million.

Compliance with tax and customs legislation has also improved dramatically. Efficiency of international trade has been enhanced by introducing advanced customs facilities such as the screening of goods using risk analysis and the electronic clearing of import and export declarations.

The modernisation programme has been implemented incrementally so that newly introduced capabilities could be leveraged across SARS to improve processes, systems and client service and to ensure high levels of efficiency and cost-savings.

The highly automated electronic processes and systems introduced have also enabled the organisation to change its fundamental business philosophy. SARS has developed its role from a tax and customs "gate-keeper" towards a risk management function that optimises resource allocation.

SARS uses sophisticated risk management systems, coupled with information sourced from third parties, to detect potential non-compliance. The incorporation of sophisticated "risk engines", which identify anomalies in taxpayer information, has so far yielded substantial tax adjustments. This enhanced ability to detect non-compliance has in itself improved taxpayers' attitude towards voluntary compliance.

SARS has substantially improved the service it provides to its clients to ensure closer co-operation with taxpayers, employers and traders. The modernisation programme has enabled the organisation to simplify the process of submitting tax and customs returns, reduce its response times, improve client support, extend its presence in communities throughout the country and introduce a variety of innovative services. These advances have been achieved by building an "electronic platform" that supports SARS' service personnel (by providing them with accurate and timeous information) and enables clients to interact with the organisation remotely by using the SARS eFiling service.

The development and promotion of eFiling as an online electronic channel was an integral component of the modernisation strategy. In July 2001 the electronic submission of tax returns (eFiling) was introduced and was extended to VAT, PAYE and income tax in 2003.

5.2 Key developments in the modernisation programme

SARS' operations, which were dependent on extensive manual processes and aged computer systems, were unable to handle the growth in the number of taxpayers and traders and the increasing volume of documents that needed to be processed. These legacy operations could not support SARS changing and increasingly sophisticated business requirements.

In response to the rapidly increasing and swiftly changing environment SARS outlined its Vision 2010 strategy document in 2004. A key component of this vision was a modernisation programme.

The programme involved applying advanced technology and systems to:

- Process increasing transaction volumes
- Improve service to taxpayers and traders
- Incorporate sophisticated risk-management capability
- Promote voluntary compliance and complementing enforcement capability
- Achieve cost efficiency
- Deliver a sustainable solution for future development

The central theme of the programme was "streamlining the middle" – which would reduce the amount of human effort needed to administer certain transactions and free-up these people to focus on compliance or service. It was intended that the modernisation of these transactions would improve the ease with which taxpayers and traders could comply with their obligations.

The figure below is a graphical representation of "streamlining the middle".

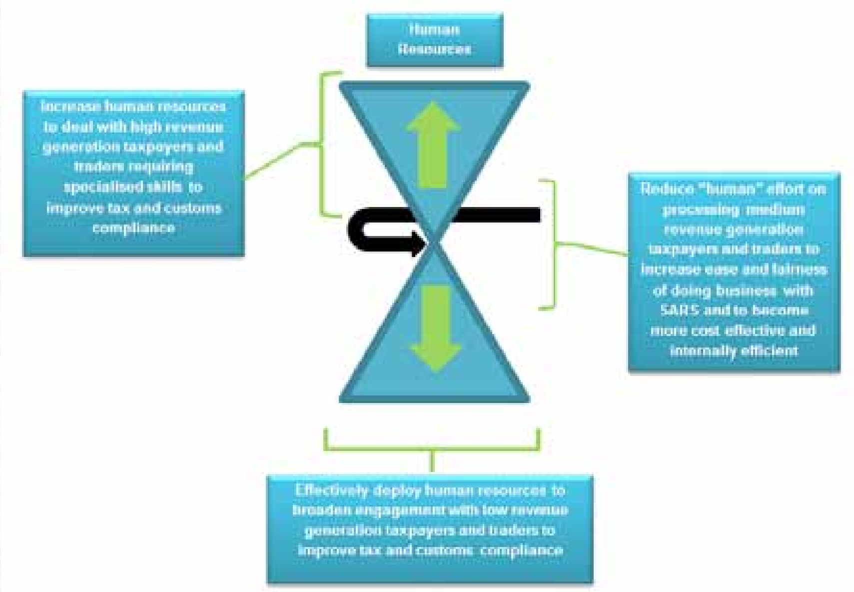

Figure 13: "Streamlining the middle"

SARS' strategy was to implement the modernisation programme in three phases. The initial phase was to create capacity, design the programme in detail and prepare the organisation for modernisation. During the next phase SARS would implement the new business model throughout the organisation. The final phase was the delivery of world-class technology-driven services to support the new business model.

SARS called for tenders late in 2005 for the provision of technology, services and skills to assist with the implementation of the modernisation programme. The contract was awarded to a consortium of information technology service providers towards the end of 2006 and the formal implementation began early in 2007.

Over the years SARS had been able to increase the number of registered eFiling users from about half a million at the end of 2006 to just over 6.8 million at the end of March 2013. This is more than a 12-fold increase.

In 2006 the vast majority of taxpayers (97%) still filed their returns manually and only approximately 120 000 individual tax returns were filed electronically. A new two-page individual tax return was introduced in 2007, which together with other improvements, led to the electronic submission of returns by close to a million people in 2007. eFiling has transformed the way SARS and taxpayers conduct business, and during the 2014 year of assessment, less than 1% of returns were filed manually. Collectively, the number of returns received during 2013/14 was 23.6 million with 96% received electronically. Although administrative penalties for non-filing has played a role in compliance levels, the improvements to the electronic filing process, which include the generation of bespoke returns, pre population and third party validations, have made filing easier and have improved compliance levels too.

The table below compares the number of returns and payments done electronically in 2006 and 2013.

	2006		2013	
Personal Income Tax				
Number of Returns filed Electronically	120K		6.7Mil	
eFiling	120K	3%	3.8Mil	57%
Branch Interface	0%		2.9Mil	43%
% Electronic Returns Received	3%		99.90%	
Number Manual Returns Received	4Mil		34 842	
Average Assessing Turnaround Times	180 days		3 days	
Average refund turnaround times 85% within 24hrs Depending on Bank Processing				
VAT				
Number of Payments Received				
Electronic	400K		2.06Mil	
Manual Payments via Branch	1.71Mil		52K	
%Growth in Electronic Payments Received				327%
Number of Returns Received				
Electronic	700K		2.6Mil	
Manual	2.9Mil		137K	
%Growth in Electronic Returns Received				287%
% Refunds processed within 48 hours	3%		56.30%	

	2006	2013
Company Income Tax		
Number of Returns Filed	672K	914K
Electronic	909K	882K
Manual	671K	32K
%Electronic Returns Received	0.14%	96.50%
Average Assessing Turnaround Times	68 days	0.47 day
PAYE		
Number of IRP5's Returns Filed	11.1Mil	30.6Mil
Electronic	10.2Mil	25.9Mil
Manual	0.9Mil	4.7Mil
% Growth		176%
Number of EMP501's Recons submitted	55 800	577 436
Electronic	0	544 070
Manual	55 800	33 366
%Electronic submissions	0%	94.40%
% Growth		935%
Rand Value of PAYE	R133.8bn	

Table 1: Comparative table: Returns and payments made in 2006 and 2013

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CHAPTER 6
IMPLEMENTATION OF THE MODERNISATION PROGRAMME

CHAPTER 6
IMPLEMENTATION OF THE MODERNISATION PROGRAMME

Given the size and scope of the modernisation agenda, it was decided that the implementation would be phased in over seven years, and that delivery would be carefully staged over that period. During 2007/2008, it was decided to focus on the most critical areas and this led to a focus on the following four programmes:

- Risk and Tax Operations – Enhancing core operations, building sustainable processing capabilities and developing an integrated risk management and enforcement system.
- Service – Improving customer service, outreach and education.
- Customs – Modernising the infrastructure and strengthening border control.
- Support initiatives – Reinforcing core support systems.

This Chapter describes the significant progress towards the modernisation objectives.

6.1 Personal income tax (PIT) – 2007-2013

SARS began implementation by overhauling its employees' tax administration systems and processes.

Before modernisation, SARS printed and posted lengthy PIT tax returns to around four million registered taxpayers every year. The shortest of these forms consisted of 12 pages. Taxpayers were then required to complete these forms and submit them to SARS together with supporting documents such as IRP5 certificates, records of interest and other income, retirement annuity certificates, travel logbooks, invoices that support expense claims and proof of medical expenses.

This system was a frustration for SARS and taxpayers. It was complicated, time-consuming, error-prone and expensive. SARS had to store mountains of paper documents that required expensive and secure storage facilities. Access to information was also problematic. When SARS' personnel received a query from a taxpayer they had to request the documents containing the information to be couriered to them. This caused lengthy delays and sometimes resulted in taxpayer information being misplaced.

In addition to these inefficiencies, PIT and PAYE were tackled first because:

- These products affected more taxpayers and contributed more revenue than any of the other tax types.
- Almost 30% of SARS' employees were involved in administering these taxes, using mainly manual processes. Improving these systems would therefore affect a substantial number of people.
- As most PIT revenue is collected from employers through the PAYE system (with only around 20% of PIT income being collected through the submission of PIT returns) the risks inherent in modernisation programmes could be closely managed.

The radical and extensive overhaul of PIT included the following:

- Rationalising the amount of information needed for the standard PIT return.
- Prepopulating the PIT return with taxpayer information already held by SARS.
- Revamping the electronic eFiling service for the submission of PIT returns either by the internet or from terminals installed at SARS' branch offices.
- Installing high-volume document scanning systems that quickly and accurately converted paper-based information into an electronic digital format.
- Implementing sophisticated risk-management systems that effectively identified inaccuracies or discrepancies in information submitted to SARS.
- Allowing taxpayers to submit returns without providing supporting documents unless requested to by SARS.
- Introducing "Go green" initiatives such as automating all remaining manual income tax assessments, stopping the printing of taxpayer correspondence in favour of communication via the eFiling service or an email address, and using short messaging systems (SMSs) to notify taxpayers of assessment progress.

The modernisation of PIT was complemented through raising the threshold for the compulsory submission of PIT returns.

Within a year, the modernisation programme dramatically changed the way SARS administered PIT. However, it did not initially address the quality of the information submitted by taxpayers and employers.

6.2 Pay-As-You-Earn (PAYE) – 2008-2013

SARS moved swiftly to improve the accuracy of information supplied by employers. During 2008 the modernisation programme aggressively tackled inefficiencies and defects in the PAYE process. Improvements implemented by SARS included the following:

- The eFiling platform was extended to enable employers to electronically submit PAYE information directly to SARS. By using the e@syFile software provided by SARS, employers were able to submit a wide variety of PAYE information – such as IRP5 certificates, monthly and annual declarations and payment reconciliations – directly from their computer systems. This significantly improved the number of employers filing returns with SARS on time.
- Introducing bi-annual PAYE reconciliations for employers. This improved the accuracy of taxpayer information submitted by employers substantially.

Furthermore, changes that required employers to register all formally employed staff, not just those whose income was above the tax threshold, improved the volume and quality of information held by SARS.

Through these enhancements SARS could "pre-populate" many taxpayers' income tax forms with information it had received from employers. These taxpayers therefore no longer had to source such information from the IRP5 forms issued by their employers.

Improvements in the accuracy of PAYE information, initiated by the modernisation programme, ensured that the administration of PIT returns during the 2008 tax season avoided the pitfalls experienced the previous year. SARS has continued to refine and improve its processing of annual PIT returns and co-operation with taxpayers has steadily increased.

6.3 Value-added tax (VAT) – 2011-2014

Early in 2011, the modernisation programme began addressing VAT processes and systems. Specific attention was given to improving processing efficiency as well as risk management in order to stem VAT revenue "leakage" caused by vendors submitting inaccurate information to SARS. This has yielded remarkable results.

Improvements to VAT systems and processes include the following:

- An advanced risk management system was implemented. This system analyses VAT returns against the trader's history, the filing trends of similar entities and third party information. Returns identified as "high risk" are reviewed by SARS and, if necessary, investigated. This enables submissions identified as "low risk" to be processed quickly and for refunds to be paid promptly.
- The VAT screening process was re-engineered and this improved the effectiveness of interventions by matching case workloads to SARS' capacity.
- A VAT refund dashboard, on the SARS electronic platform service, was introduced, which enables vendors to view information about the status of their refunds. By using the eFiling internet service or a terminal at a SARS branch office, a vendor can discover why a refund has not been paid and what action is required to remedy the situation.
- The audit case workflow system that was introduced during the modernisation of PIT was leveraged to deliver similar capabilities for the auditing of VAT returns.

6.4 Corporate income tax (CIT) – 2011-2013

SARS began overhauling its CIT processes and systems in 2011. The modernisation programme used many of the enhancements applied to the administration of PIT and VAT to raise the efficiency of processing CIT.

A key component of the CIT modernisation was the alignment of CIT enforcement audits with the newly automated VAT and PIT processes. Integrated risk management systems automatically identify "high risk" CIT returns and enable SARS to interrogate such cases. Additional features of the CIT modernisation include:

- Dramatically simplified and "dynamic" electronic forms for income tax returns for companies (ITR14s).
- Registration forms that ensure verification of company demographics.
- Integrated risk management facilities that automatically identify "high risk" returns.
- Requests for returns are sent using the electronic eFiling service instead of the postal service.
- Forwarding financial statements, with taxpayer approval, to the Companies and Intellectual Property Commission (CIPC). To date approximately 60% of CIT taxpayers have granted SARS permission to forward their financial statements to CIPC.

6.5 Administrative penalties – 2009-2014

The late submission of large numbers of PIT returns was a major stumbling block in SARS' drive to improve performance and raise levels of compliance with tax legislation. For example, more than one million PIT returns were submitted to SARS after the deadline for the 2008 tax season.

In order to remedy the situation an administrative penalty regime was introduced in 2009 that imposed fixed-amount penalties on certain taxpayers with outstanding returns. Before penalties were imposed SARS publicised the new penalty regime widely and provided taxpayers the opportunity to avoid penalties and file any outstanding returns.

The modernisation programme supported this initiative through an automated process that imposed and collected administrative penalties. This system automatically generates monthly penalties and facilitates the collection of the penalties.

6.6 Dividends tax – 2011-2013

In 2011 government announced that secondary tax on companies (STC) would be phased out and replaced by a dividends tax. This shifted the liability for payment of tax on dividends from the companies that declared dividends to the taxpayers who received them.

The introduction of dividends tax required SARS to make extensive changes to its administrative systems and processes. Early in 2012 the modernisation programme addressed this requirement by implementing a new accounting system to manage payments by taxpayers and their agents, establishing a register to record beneficiaries of dividend payments and providing a facility on the eFiling service for the electronic submission of dividends tax returns.

The modernisation programme enhanced the administration of dividends tax later in 2012 by expanding the avenues through which taxpayers could submit their returns. By leveraging the extensive electronic platform SARS was able to provide taxpayers and their intermediaries with a comprehensive array of submission channels.

Dividends tax returns and supporting information can currently be submitted to SARS electronically using the e@syFile facility (first introduced for PAYE), direct network connections, the eFiling service or through a terminal at a SARS branch office.

6.7 Transfer duty – 2011-2014

The first phase of the modernisation of the administration of transfer duty began in 2011. This phase focused on implementing automated management systems to evaluate transfer duty declarations and identify applications for closer scrutiny.

The second phase involved the migration of transfer duty administration to an advanced processing platform and the introduction of an electronic submissions facility on the eFiling service. This facility incorporates an online transfer duty application form that improves the accuracy of information submitted to SARS and eliminates the need for supporting documents. This has dramatically improved processing turnaround times.

In January 2013, SARS introduced a new capability on eFiling for transfer duty to cater for the registration and deregistration of conveyancers and eAccount management. Conveyancers were able to voluntarily register for a transfer duty registration number through eFiling. The eAccount functionality enables the relocation of a credit to another debit and to request an interim statement of account.

Conveyancers were encouraged to register in order to enable a more effective method of facilitating transfer duty refunds. The next phase will include mandatory registration and compliance and the streamlining of processes for transfer duty submissions and refunds to registered conveyancers.

6.8 Automated risk engine

SARS implemented its first new-generation automated SARS risk engine during the 2007/08 financial year. The risk engine used information that was readily available, such as statistical data, to determine the accuracy of taxpayers' declarations.

The initial focus was on PIT returns and was enhanced through more sophisticated sets of rules.

The VAT and the CIT risk engines were both introduced during 2011/12. The introduction of these risk engines enabled SARS to correlate VAT, CIT, PAYE and customs declarations.

Further sets of rules were added to the risk engines before the 2013 filing season to improve the effectiveness of the systems.

6.9 Tax Clearance Certificates and Tax Compliance Status (2014)

Since the commencement of the TCC process there has been a steadily increasing volume of requests which topped 785 000 in the 2011/12 finacial year. These volumes placed a considerable administrative burden on SARS' branch network and its back-office facilities. The process was also burdensome for people applying for TCCs, and the mainly manual process used was vulnerable to fraud and corruption.

In order to address these issues SARS began implementing its Tax Compliance Status (TCS) system.

The first phase of the TCS system separated receiving TCC applications from the task of processing the applications. Branch personnel now receive TCC applications, but the processing of applications is conducted at a centralised SARS site. The initial phase of the TCS system also automated the assessment of TCC requests.

More than 75% of TCC applications are now automatically considered and responded to almost instantaneously. The process has reduced the workload at SARS' branches and has made applying for TCCs easier for taxpayers – even though taxpayers are still required to collect the TCC from a SARS branch.

The benefits of the complete TCS system are:

- Taxpayers can demonstrate their tax compliance without having to visit a SARS branch to apply for a TCC. Turnaround times for such confirmation will be cut from several days to just a few minutes.
- Taxpayers can monitor their tax status online and, if necessary, remedy non-compliance.
- SARS branch offices will be relieved of the administrative functions of responding to large (and growing) number of applications for TCCs.

- SARS' administrative personnel and IT systems will no longer have to process and issue the volumes of TCCs. This will substantially improve SARS productivity and, by eliminating paper certificates, reduce costs. The substitution of paper certificates with a secure electronic service will also substantially reduce opportunities for fraud.
- SARS' branch offices and contact centres will have to respond to far fewer tax clearance enquiries.
- The tax compliance status displayed by the TCS system will always be accurate and up-to-date. As the paper TCCs are valid for one year, the TCC remains "alive" even if a taxpayer fails to comply during this period. This will no longer be the case with the new TCS system.

6.10 Single registration

The single registration system was released into production on 10 May 2014. The legacy registration process with SARS requires a taxpayer, trader or vendor to register separately with SARS for each tax type and for the customs products. This results in duplication of information, time delays, and for SARS, administrative inefficiencies. The legacy registration process also hampers SARS' capability to manage risk and to counter fraud. SARS rolled out the single registration system to address these drawbacks.

This programme is similar to the Financial Intelligence Centre Act (FICA) "Know Your Client" (KYC) programme undertaken by the Financial Intelligence Centre and the banks. The FICA (KYC) programme has been a long journey for the banks over many years – and it is anticipated that SARS' journey will be quicker but will still take a number of years.

Considering the scope of the project it was decided to split the project into phases to minimize the risks. The first phase of the project, which has gone live, involved the implementation of the underlying technology with only a few entities merged – branches are already taking the opportunity of face-to-face interaction with customers to merge records.

SARS identified two challenges in the early stages of the implementation. All companies have not kept the details of their appointed public officers current, and there is some confusion between the appointment of a representative (tax practitioner) and the appointment of a representative taxpayer (public officer).

Once these challenges have been resolved and updates have been made to registered details, SARS will begin merging the huge volumes of product accounts on an entity basis.

The single registration process will benefit registrants, who will have to provide certain key personal and demographic data only once. In addition, SARS staff, taxpayers, traders and vendors will have a single view providing a comprehensive picture of a taxpayer's relationship with SARS across all the tax types and customs products. It is anticipated that there will be improved compliance, more efficient debt equalisation and tighter security to guard against identity fraud.

As part of the project, SARS intends to validate taxpayers' data against the databases of the Department of Home Affairs (for individuals) and the CIPC (for companies) – thereby creating a single profile. This is one of the largest implementations SARS has undertaken with over 280 interfaces, 1 800 touch points and 20 million customer records to work through.

6.11 Other service initiatives

SARS introduced the Branch Queue Management System for the management of queues at branch offices which resulted in service and queuing improvements. An enhancement to the Branch Queue Management System was the introduction of the eFiling Mobile Application which uses mobile smart devices to issue tickets to queueing taxpayers. This use of mobile devices was pioneered by SARS.

The use of mobile devices has also been introduced at borders to assist in conducting physical inspections.

6.12 Support

The support programme focuses on improving core support systems in respect of SARS' administrative and internal environments. Administrative projects cover the areas of registration and revenue management which comprise payment processing, account management, debt and dispute management, and reporting. Internal projects focus on improving SARS' internal operating capabilities to better manage resources, such as its staff, buildings, assets and operating budget.

6.12.1 Account maintenance – 2009-2013

It is essential that SARS maintains accurate and up-to-date accounts. Enforcing payment is complicated if taxpayers are unaware of the status of their accounts with SARS. It is therefore important that taxpayers be aware of outstanding amounts.

It is especially challenging when taxpayers, such as large corporations, have multiple accounts with SARS and pay a variety of different taxes and duties. Errors in the allocation of payments for these taxes and duties, as a result of mistakes by taxpayers or sometimes SARS, can result in the levying of interest and administrative penalties. The modernisation programme implemented several initiatives designed to improve SARS' account maintenance and debt management systems.

These initiatives include the following:

- Using the eFiling service to provide taxpayers with an up-to-date statement of account. Taxpayers can use the eFiling internet service or visit a SARS branch office to review their payments, refunds, liabilities and penalties.
- A payment reference number system was introduced to curb errors and misallocations. VAT and PAYE forms are now printed with the required reference number to assist with the accurate allocation of payments.
- Automated financial systems were implemented that reconcile taxpayer payments and returns, and trigger follow-up procedures when non-compliance is detected.
- Introduction of capability that allows corporates to manage their accounts online.

The Account Verification System (AVS) was introduced to assist in validating data when a taxpayer requests a change of banking details. The AVS process is available to SARS for certain taxes and taxpayers.

6.12.2 Payments modernisation

In line with SARS' mandate and obligations as an organ of state, a decision was taken to mitigate the financial risk associated with payments made via debit orders. The initiative involved substituting debit order payments with credit push transactions by the five major banks. From the 2015 financial year payments by debit orders will not be accepted.

Debt equalisation involves applying a refund due to a taxpayer against a tax debt due by the same taxpayer. In 2014 SARS concluded a project whereby the debt equalisation journal transactions between VAT and income tax were automated. Previously, debt equalisation occurred when a refund stopper had been placed on an account. The improved process now accommodates equalisation of debt on refunds selected for debt equalisation irrespective whether a stopper had been placed on the account.

6.13 Service Manager functionality

A key component of this aspect of the modernisation programme was the development and implementation of the SARS Service Manager Business Automation System. Service Manager provides staff at SARS branch offices and contact centres with direct access to client information to enable them to quickly and efficiently respond to taxpayer queries. It comprises several highly innovative features, such as the following:

- Tracking all taxpayer interactions and queries.
- Instant access to taxpayer information, documents and returns.
- Branch office staff is able to capture taxpayer information and help clients use the SARS electronic platform to complete their PIT returns.
- Allows taxpayers to submit their PIT returns electronically at a SARS branch office and to sign the return electronically.
- Optimises the performance of SARS' staff by monitoring, evaluating and, where necessary, correcting their engagements with taxpayers.

CHAPTER 7
TAX POLICY DEVELOPMENT

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The development of tax policy involves designing a tax system that will generate sufficient funds to finance public expenditure within government's policies such as achieving equity, income and wealth redistribution, and growing employment opportunities. There is a close correlation between tax policy design, drafting tax legislation to express tax policy and the implementation of tax policy through the administration of tax legislation.

In many jurisdictions tax policy design is the function of treasury, implementation is the function of the revenue authority while drafting the legislation to give effect to policy falls between policy design and policy implementation.

SARS was responsible for drafting tax legislation in line with tax policy until around 2005 when National Treasury took the lead with SARS playing a supportive role. In addition to co-drafting legislation, SARS assists by ensuring the smooth passage of the Bills through the Parliamentary legislative process.

Tax policy, converting policy into law, converting the law into operational practice and the application of the law in practice are all interconnected, and it is therefore critical that a revenue authority is fully acquainted with the tax policy which informs the tax law. For this reason, capacity was created in SARS to facilitate alignment between these processes.

As part of a customer-oriented strategy SARS issues brochures and guides as well more formal interpretation notes and rulings to promote certainty in the application of legislation and to assist taxpayers and practitioners to comply with the law.

Figure 14: SARS brochures

The evolution of the tax system over the 20 years reviewed reflects the development of South Africa as a constitutional democracy and as an emerging economy.

Underlying tax reform over this period is a concerted effort to achieve greater equality, for instance, through lowering the effect of taxation on lower income earners, expanding the tax base and reducing opportunities to distort the tax burden.

As a developmental state, reform ranges from providing incentives for capital expenditure and certain industries, recognising the broader importance that public benefit organisations (PBOs) play in society and promoting small and medium-sized enterprises.

As an emerging economy South Africa's growing participation in the global economy has influenced tax policy. Global integration has exposed the economy to the impact of global events and some abusive practices, and tax law has evolved in response to these external events.

SARS' efficiency has given the legislature opportunities to boldly move to align the tax system with international norms, create a regime that strives to be internationally competitive, and protect the economy against abusive practices. This is demonstrated by the adoption of a residence-based tax system and the extensive network of international agreements, the introduction of dividends tax and numerous other enactments.

Protecting the environment has more recently emerged as an important tax policy initiative. Environmental taxes on coal-based electricity generation, plastic bags, incandescent light bulbs and motor vehicle carbon dioxide emissions have been introduced as well as allowing certain tax deductions to encourage the use of renewable resources, rehabilitation of the environment and improve energy efficiency.

In this Chapter the more important developments over the last 20 years are reviewed.

7.1 Reform of personal income tax (PIT)

In the early 1990s there were tax tables with 15 brackets for married men as well as separate rate structures for unmarried persons and for married women.

The recommendations in the Katz Commission's Third Interim Report on the relationship between income tax reform and income distribution reinforced the need for government to restructure the tax rate structure. This restructure involved reducing the gradation of the marginal rate schedule, reducing the number of brackets, raising the tax threshold and taking into account inflation induced bracket creep.

Initially four categories were anticipated for individuals, namely, for the low, low-middle, middle and high income groups.

From 1994 to 1998 the number of taxable income brackets was reduced from nine to only six and during the period from 2000 until 2002, the maximum marginal tax rate was reduced from 45 to 40%. The tax threshold, wich is based on the primary rebate, was increased per year from R10 714 in the 1995 tax year to R70 700 in the 2015 tax year. In addition to the secondary rebate for individuals 65 years of age and older, a tertiary rebate was introduced in 2007 for individuals 75 years and older.

The endeavour to improve horizontal and vertical equity and to improve the living standards of individuals in South Africa has been a consistent theme throughout the period. Another related and consistent theme throughout this period has been to compensate individuals for the effect of inflation – which would otherwise have pushed some individuals into higher tax brackets and reduced their purchasing power due to tax payable at a higher effective tax rate on annual taxable income.

One measure of the success of the initiatives is seen in the tax reductions given to individual taxpayers over the years. In the 20-year period from the 1995 Budget to the 2014 Budget, tax reductions of R155 billion in nominal terms were granted to individuals by way of adjustments to the personal tax rate structure.

The rationalisation of the number of taxable income brackets, coupled with the limitation of the deductions available to taxpayers who are employed, also reflects the intention to simplify tax for individuals and to simplify the administration of the PIT system.

In terms of the Constitution discrimination on the basis of gender and marital status is unconstitutional. As a consequence in 1995 the three rate tables that previously applied to married persons, married women and other persons were changed into a single rate structure of income tax which applied to all individuals irrespective of gender and marital status.

7.2 Corporate income tax (CIT)

Most reform measures around corporate taxes are aimed at removing tax-induced distortions, promoting competition, encouraging economic activity and growth of employment opportunities. In South Africa the reform of CIT also reflects the needs of a developmental state and an economy responding to increasing globalisation of trade.

In 1991 the first step in the long-term goal of reducing the rate of tax on companies (company rate) was implemented when the rate was reduced from 50% to 48%. In 1993 the company rate was drastically reduced from 48% to 40% and a tax of 15% on distributed profits via dividends distributed from 17 March 1993 was introduced (known as STC). Further significant reductions in the company rate were made in 1994 and 1999. In 1994 the company rate was reduced from 40% to 35% and a corresponding increase in STC was made from 15% to 25%. In 1999 the company tax rate was reduced from 35% to 30%.

STC was used to absorb the effects of the reduction of the company rate. STC rate remained at a constant 25% from 1994 until 1996, while during the same period the income tax rate on companies was reduced from 48% to 35%. By 1996 the impact had been absorbed and the STC rate was reduced to 12.5%.

The graph below illustrates the movement in the company rate from 1980 to 2014:

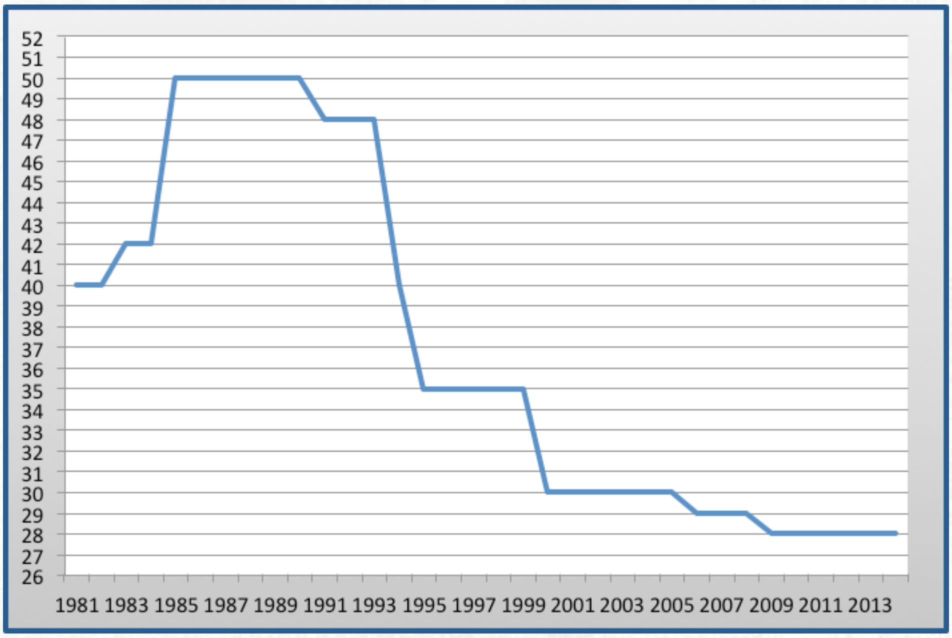

Figure 15: CIT rates 1980 to 2014

The STC regime was not aligned to how dividends are treated by other jurisdictions – where dividends are taxed in the hands of shareholders. A complete reform of the STC regime was first announced in 2006 that involved phasing out STC and introducing a dividends tax.

The reform happened in two phases. In the first phase STC at a rate of 10% (the STC rate was reduced from 12.5% in October 2007) was applied to a broader category of profit distributions and the second phase introduced the taxation of dividends at shareholder-level, although collection was effected through a withholding tax.

Before dividends tax could be implemented a number of tax treaties with other countries not allowing South Africa to impose dividends tax had to be renegotiated and then had to be ratified. Once the vast majority of these treaties had been renegotiated the dividends tax regime came into full effect in April 2012, although the rate was increased to 15% to compensate for the narrower base of the new tax.

7.3 Value-added tax (VAT)

General sales tax (GST) was imposed from 1987 until it was replaced, on 1 October 1991, by value-added tax (VAT).

One advantage of VAT over GST is that GST is collected and paid when the final product is sold to the end-consumer, and VAT is collected at each step along the value-added chain. The tax is collected by a broader group of businesses in the VAT system and the risk of loss to the *fiscus* is therefore reduced.

As discussed in 1.1 GST was challenged with inherent structural problems that distorted the way normal economic activity was carried out and it was difficult efficiently regulate aspects of the tax. For these reasons a policy decision was taken to substitute GST with VAT.

The VAT Bill had been drafted by 1990 but before commencement Inland Revenue officials presented 3 000 seminars to 82 000 entrepreneurs explaining how the new VAT system would function. A toll-free line was set up to help with registration and teething problems and over 50 000 queries were dealt with. By February 1992 over 278 000 vendors had registered for VAT. In order to ease in the new system, no penalties or interest were levied for late payment or filing for the first two months.

VAT commenced at the rate of 10% and in 1993 it was increased to 14% – the rate at which it still is today. The number of zero-rated goods was originally small, however, over the years the number of goods subject to zero-rating has grown, in part to minimise the cost of staple food products.

At the time VAT was introduced there were challenges in subjecting supplies in the financial markets to VAT.

As an alternative a turnover tax of 0.75% was introduced on financial institutions' interest income and finance charges. This turnover tax remained in place until financial services were partially included in the VAT net in 1995. From October 1996, VAT was levied on all fee-based financial services which effectively subjected almost all services provided by banks to VAT. Banks were exempted from the "proxy" financial services levy, and in 1997 the levy on financial services was abolished.

The graph below indicates how total tax collections are made up.

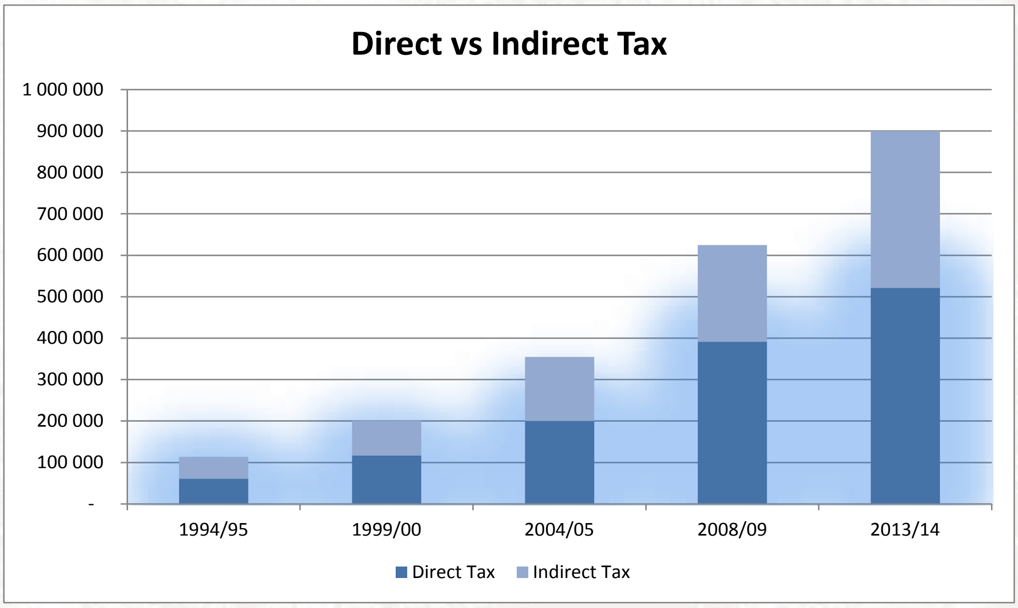

Figure 16: Contribution of direct and indirect tax to total revenue

The contribution that GST made to total revenue was 27% in 1990/91 and the contribution of GST/VAT in 1991/92 amounted to 25.1% of revenue. In 2013/14 VAT accounted for 26.4% of total revenue.

7.4 Broadening the tax base, closing loopholes and countering abuse

There is no single meaning of broadening the tax base. It is considered to include bringing more payers into the net, subjecting more economic activities to tax and closing tax loopholes.

Tax professionals are often used to identify opportunities created by loopholes in legislation to minimise or neutralise the tax burden and these efforts are normally the preserve of taxpayers who can afford the services of professionals. This practice effectively avoids the intended incidence of tax and those who game the tax system are able to gain a competitive advantage over others. Public sentiment and confidence in the fairness of a tax system is also affected when disproportionately low tax contributions by big names become public, as was evidenced in public demonstrations and boycotts in the United Kingdom and the United States. A decline in the confidence in a tax system can lower overall compliance levels and tax morale which are good reasons to close loopholes and stop abuse.

Closing loopholes to counter abuse and opportunities for arbitrage is therefore necessary and has multiple benefits to a tax system. While an objective of closing loopholes is to minimise economic distortions and neutralise inequitable tax burdens, these efforts also bring stability to the tax system, foster fairer commercial competition and lower the revenue authority's compliance efforts.

Simply abolishing incentives because of abuse can distort the overall scheme of tax policy because tax incentives and favourable allowances give effect to policy – for instance to encourage capital expenditure, promote economic development in a specific area and promoting employment. Closing opportunities for abuse can therefore take the form of adding "redflags" to the risk matrix that trigger enforcement action by

SARS, communicating awareness of the abuse and imposing appropriate penalties when abuse is identified and amending the legislation to remove the opportunity for manipulation. This approach upholds the original economic purpose of the incentive and the social factors that initially informed the decision.

The effect of not adequately protecting the tax system against abuse is the erosion of the tax base and the compromise of the principle of horizontal equity. Below are some examples of how abuses and loopholes have been handled.

7.4.1 General

From 1990 there was increasing concern that tax reductions and allowances were being abused and the option of introducing a minimum tax for individuals and companies was considered as a method of curtailing abuse. However it was reasoned that a more appropriate approach would be to address the underlying cause which was the skilful use of tax concessions.

Steps were taken in the early 1990s to combat the abuse through the removal or limitation of allowances and concessions. For instance more realistic depreciation allowances were introduced and the method of valuing trading stock was refined. By 1993 allowances for marketing, sport sponsorship and hire-purchase reserves (on debtors) were phased out and penalties of up to 200% were introduced for PAYE and transfer duty to deter serious non-compliance.

Tightening continued throughout the 1990s and the general export incentive scheme exemption, that was systematically abused, was withdrawn in March 1995. Also in 1995, the Katz Commission confirmed earlier concerns that tax incentives created loopholes that could be exploited, complicated the tax system and increased the administrative burden on the revenue authority. The Commission recommended that incentives should be reduced as far as possible.

The abuse of allowances available on the acquisition of ships and aircrafts had already been highlighted in the Katz Commission's Interim Report, and in 1995 this allowance was withdrawn and replaced with a 20% annual allowance in order to limit abuse. At the same time normal recoupment replaced the provision which allowed the recoupment on the disposal of ships and aircrafts to be off-set against the replacement cost of a ship or aircraft.

Further tightening included the requirement that non-residents had to be absent from South Africa for a period of at least 183 days a year in order to qualify for an interest-exemption and the withdrawal of an interest-exemption for foreign companies that carried on business locally. Amendments were also made to the taxation of long-term insurers – which is discussed later in this Chapter.

The pace with which loopholes were being closed through legislative amendments speeded up in 2000. For example expenditure deductions were required to be matched with the timing of benefits and practices that had developed to manipulate the tax treatment of remuneration were addressed. In this respect legislation was introduced that taxed a restraint of trade payment in the hands of the recipient and allowed a deduction by the payer over the longer of the period of the restraint or three years. A trend had also developed whereby individuals effectively provided services to an employer through a company, thereby avoiding PAYE being deducted. The misuse of these “employment companies” were tackled when the legislation subjected what was effectively “remuneration” to PAYE, limited deductions to the amount of remuneration received, taxed the company at the rate of 35% and subjected any dividend to STC.

Measures to counter abuse have continued to be introduced through legislative amendments. For instance, the deduction of future expenditure was limited, directors of companies were brought into the PAYE system and shareholders could be held personally liable for unpaid tax if a company was liquidated – if the shareholder had taken assets of the company within a year of liquidation. Furthermore persons who controlled the financial affairs of a company could, in terms of this legislation, also be held personally liable for unpaid tax under certain circumstances. The tax treatment of intangible assets was streamlined and losses made by individuals carrying on secondary trades were ring-fenced in order to counter the practice of setting-off losses sustained through hobby-like activities against taxable income earned through remuneration or professional fees.

The above is not a thorough review of all the loopholes closed and anti-abuse measures taken, but it is intended to provide an indication of the extent to which tax policy has developed as a response to loopholes and abuse.

The 2010 Budget Review announced that measures to close sophisticated tax loopholes were being developed, and that specific transactions had been identified. Transfer pricing, cross-border insurance payments and interest exemptions, "protected cell" companies and preference share transactions were some schemes specifically mentioned. Since the announcement amendments have been implemented to address transfer mis-pricing, the limitation of the deduction of insurance premiums on investment policies, the exemption rule for interest earned by non-residents, third party backed preference share financing schemes and protected cell companies in the context of controlled foreign company rules.

Following the financial crisis there was a global effort to regulate financial services and to prevent tax abuse within the financial industry. In 2010 a comprehensive review of the financial industry began with a focus on financial instruments and transactions.

7.4.2 Amnesties

Tax amnesties have been used over the years by many tax jurisdictions to collect outstanding taxes in an inexpensive way, improve compliance with the tax laws of the country and to identify taxpayers outside of the tax net. Another advantage of an amnesty is that tax laws can be applied more strictly after an amnesty because non-compliant taxpayers have been given the opportunity to regularise their affairs and have elected not to. On the other hand, amnesties must be approached cautiously, since they have the potential to undermine compliant taxpayers' morale.

- ***The 1995 and 1996 amnesties***[11]

At the beginning of the era reviewed there were serious challenges with regularising tax compliance after past non-compliance, and the Katz Commission was requested to investigate whether an amnesty was an appropriate method of resolving these tensions.

In 1995 a general tax amnesty was approved and offered to persons who voluntarily came forward and remedied their affairs. The amnesty given was generous and sought to broaden the tax base and decriminalise past non-compliance. A second relief programme ran from November 1996 until February 1997 and offered relief from all taxes which were payable before 1 March 1994. This was an important point in the administration of the tax system as it dealt with complex social and moral arguments concerning supporting the pre-1994 regime.

After the relief programme, SARS was given a clear mandate to enforce tax laws without fear or favour.

- ***Foreign exchange amnesty of 2003***

The residence-based tax had been adopted and South African residents were taxed on their world-wide earnings. The administration of tax had improved and internationally the tolerance of illicit funds held in foreign jurisdictions was waning.

Government was aware that from the early 1980s money had been shifted off-shore in a variety of ways and that the income on these funds was not being declared. A joint amnesty, for both exchange control and domestic tax, was made available to give people in this position the opportunity to regularise their affairs.

Applications had to be made within a relatively short period and all foreign income had to be disclosed in the 2003 return. Under the amnesty a 5% levy was imposed on the value of assets held off-shore and repatriated to South Africa, and a 10% levy was imposed if the applicant elected not to repatriate offshore assets. A 2% levy was charged for tax violations.

The amnesty ended on 29 February 2004 and a total of 42 672 applications were made with an asset disclosure of R68.6 billion. Applicants paid levies totalling R2.9 billion.

- ***Small business tax amnesty of 2006***

A tax system for small businesses was introduced from 2001 and was expanded over the years. However, in the process it was acknowledged that small businesses had been marginalised over the years, and that the benefits of being tax compliant had been a gradual journey. The fear of exposure to penalties for past non-compliance was identified as one of the obstacles to improving compliance among small businesses, and in 2006 a small business amnesty was made available to qualifying businesses.

Figure 17: Small business tax amnesty publication

- ***Voluntary disclosure relief programme – from temporary to permanent mechanism***

Before the introduction of a permanent voluntary disclosure programme in the Tax Administration Act (TA Act) in 2012, a stand-alone voluntary disclosure process was made available in 2010/11. This programme was not as generous as the amnesties that had been provided previously, although it did provide relief from penalties and interest.

The permanent voluntary disclosure programme now provides a mechanism that taxpayers can access to regularise their affairs and to obtain relief in the form of a lower rate of understatement penalties. The extent of relief from understatement penalties depends on whether application is made before or after the notification of an audit. The reduced rates range from 0% to 10% of the amount of the shortfall if application is made before notification and 5% to 75% if made after. A further benefit is that a successful applicant is protected from facing a criminal prosecution in connection with that non-compliance.

Between 2011 and 2014 a total R6.7 billion was collected through voluntary disclosures.

7.4.3 Capital gains tax (CGT)

The absence of capital gains tax (CGT) was considered to be a structural weakness in the South African tax system which provided opportunities for arbitrage through the manipulation of revenue and capital receipts, and the absence exacerbated the inequalities in wealth distribution.

The debate whether to introduce CGT had started in 1969 when the Franzsen Commission recommended a limited CGT. In 1987 the Margo Commission recommended that capital gains should not be subjected to tax. In 1995 the Katz Commission acknowledged the case for CGT and identified the taxation of capital gains as one of the means of entrenching horizontal and vertical equity. As mentioned earlier, at this time revenue and customs administration had deteriorated significantly and there was an urgent and compelling need to transform the administration in order for it to meet the transformational needs of the country.

The Katz Commission recommended that the introduction of CGT should be postponed because the complexity in administration of a CGT would put the revenue authority under significant strain.

In 2000 it was felt the time had come to introduce CGT in order to address structural weaknesses in the South African tax system and to align it with international best practice. Government was also confident that SARS had gained the administrative capacity to administer CGT efficiently. An extended consultative process was then followed and an appropriate lead period was given to allow the financial industry and other taxpayers to develop appropriate information systems.

CGT was then introduced in 2001 and the effect of CGT was softened because of the application of the time apportionment basis formula and the optional valuations conducted by taxpayers in 2001.

Guides have been published by SARS on CGT, and are regularly updated. These guides include a comprehensive guide, and separate guides on CGT for individuals, companies and on the valuation of assets.

Since the introduction of CGT the provisions have been amended in line with a policy to simplify the legislation, protect the domestic economy and curtail areas of abuse. The rules that excluded from CGT the proceeds of the sale of a primary residence were simplified in 2009 so that currently no CGT applied if the sale price was below R2 million – this exclusion is in addition to the current net exclusion of R2 million of capital gain or capital loss.

7.4.4 Fringe benefits

Through non-cash benefits a non-taxable advantage could be provided to mainly higher-level employees thereby skewing the burden of tax. A constant theme from the 1980s is reforming the taxation of fringe benefits. In 1984 specific rules were introduced to tax fringe benefits. In 1987 the Margo Commission confirmed that legislation should dissuade non-cash benefits in exchange for cash remuneration.

This policy position informed legislative amendments over the years that sought to align fringe benefits with the cash equivalent of such benefits and close the abuse of non-cash equivalents.

7.4.5 Excessive interest deductions

Historically, interest was not deductible if used to acquire shares, and a practice had arisen whereby the corporate rules were used to allow the deduction of interest that was in essence incurred to fund the acquisition of shares. By 2011 this practice was creating significant concerns. The level of debt that generated interest deductions in the target company in some transactions accounted for between 75% and 95% of the target company's balance sheet. There were also concerns that hybrid equity instruments were being presented as debt instruments.

On 3 June 2011 government stated its intention to suspend the corporate rules for a period because of the concern that they were being abused. After consultation with industry the proposed suspension was withdrawn. Section 23K of the Income Tax Act was instead introduced as a temporary measure to curb abuse. The provision denied the deduction of interest incurred in respect of debt used to fund reorganisation of intra-group transactions and liquidation transactions but allowed SARS to approve the deductibility of interest if the level of debt and interest was appropriate. In 2013 the legislation was amended to replace section 23K with more objective rules regulating the deduction of interest.

7.4.6 The taxation of interest

Serious mismatching occurred between claiming interest deductions and declaring interest income upon the same financial instrument. The area of law was not certain, and to address the risk to the tax base legislation was introduced in 1995 in terms of which interest on certain financial instruments should be calculated on a day-to-day basis for all tax purposes. In 1996 the accrual basis was extended to financial instruments that were issued before 1995.

Following the introduction in 1995 of section 24J of the Income Tax Act which regulates the timing of the incurral and accrual of interest, a review of the distinction between debt and equity began in 1996/7. At the time hybrid instruments were being developed to circumvent the accrual regime, for instance through substituting interest receipts for another receipt, for example, dividends.

7.4.7 The taxation of hybrid instruments

Financial instruments can traditionally be classified as either debt or equity instruments. If this traditional characterisation can be applied then the proceeds and payments made in terms of the financial instrument can be identified as being either of a revenue, an exempt or a capital nature. The consequence is that the tax treatment is then easily ascertainable.

However, over time through "financial engineering" the ability to distinguish between debt and equity financial instruments has become increasingly difficult. There is an increasing number of financial instruments that are constructed to mask the instrument's character and shrewdly create a deductible expense in one entity with no corresponding income accrual in the other, or generate a double deduction resulting from a single economic expense.

In 2003 anti-avoidance legislation was considered and introduced to address hybrid financial instruments, with specific focus on convertible instruments, perpetual debt and shares with required payment of capital.

Sections 8E and 8EA of the Income Tax Act are intended to address transactions that usually involve preference shares to "disguise" otherwise taxable interest as tax-exempt dividends. Under these rules, dividends that are declared in respect of affected instruments are deemed to be interest from a South African source in the recipient's hands while the payment retains its character as a dividend in the issuer's hands. The effect is to ensure that income from hybrid instruments is treated as a revenue receipt, while in the issuer's hands the amount is not deductible.

Sections 8F and 8FA, which apply with effect from April 2014, deems any interest on a hybrid debt instrument as a dividend in specie which is not deductible for income tax purposes.

Internationally, tax authorities are also challenged to address the treatment of the constantly evolving financial product environment, which is complicated when transactions cross borders. The Organisation for Economic Co-operation and Development (OECD) released a report on hybrid mismatch arrangements (Action 2 of the Base Erosion and Profit Shifting (BEPS) Action Plan) on 16 September 2014. It recommends changes to domestic law and to the OECD Model Convention on Income and Capital. This report states that the approach to neutralise hybrid mismatches has been agreed, and involves adopting a primary rule and an alternative defensive rule. The primary rule seeks to deny a deduction when a payment is not included in the recipient's income or if a double deduction for a single economic expense results. The alternative to the primary rule, the "defensive" rule, seeks to include the income in the recipient's hands.

National Treasury has recognised that the financial sector is at the heart of the economy[12] and therefore South Africa is not shielded from the complexities and challenges involved in keeping the tax treatment of financial instruments appropriate and relevant. This is so because South Africa is both integrated with the global economic community and because South Africa has a well-developed financial sector.

7.4.8 The financial sector

The low effective tax rate on the financial services sector was identified as a concern in the 2001 Budget Review released by National Treasury. A variety of tax-saving mechanisms has been used by the industry to avoid or defer tax.

- ***The banking sector***

At the time it was said that banks made use of "sophisticated financial instruments" in addition to "structured, asset-based transactions" so as to minimise their tax liability.

Following a questionnaire issued by SARS to the banking industry, the following were identified as some areas that resulted in reduced tax liabilities:

- Differences between the mark-to-market treatment of derivative financial instrument transactions in currency, commodities and equities for accounting purposes and their tax treatment.
- Local and foreign dividends received.
- Structured asset-based financing.
- Income accrued for accounting purposes but not for tax purposes.

- Characterisation of income as of a capital nature.
- Income earned from non-South African sources.

Some of these issues were addressed through the introduction of tax on foreign dividends, capital gains tax and residence-based income tax.

Over eight years SARS and the Banking Association of South Africa (BASA) engaged in discussions to establish a framework for co-operation to improve levels of compliance, discourage impermissible tax avoidance arrangements and enhance service. On 29 January 2009 a formal Accord was signed between SARS and BASA, in terms of which BASA undertook to, amongst others, monitor banks' effective tax rates, raise tax governance to board level and enhance risk and governance processes to ensure optimal tax compliance. SARS also undertook to enhance communication and service provided to banks.

As is evident from the graph below, the contributions made by banks have increased substantially from 2000 as a result.

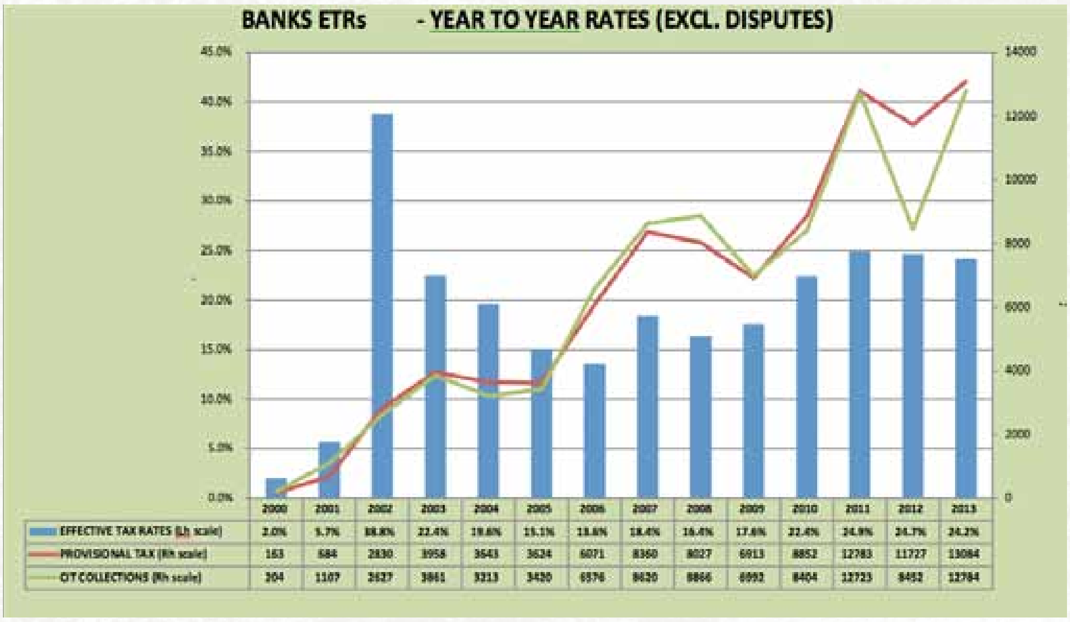

Figure 18: Banks Effective Tax Rates 2000 to 2013

Improved enforcement has also enabled SARS to challenge various tax avoidance schemes, which accounted for an additional R792 million tax revenue collected in 2001/02.

Over the years the provisional tax collections for the banking sector have been growing at a steady pace. The 2006/07 fiscal year saw a massive growth as it nearly doubled. The National Credit Act came into effect in June 2006. In 2009/10 provisional tax collections slumped due to the global meltdown as the impact of the recession took hold and the impact of the 80:20-rule which resulted in much lower 3rd provisional tax payments. Some recovery was seen from 2010/11 post the recession. The rapid growth in unsecured lending is also considered to have contributed to the recovery in the banking sector.

STC collections were in line with provisional tax payments and remained consistent between 2000/01 to 2005/06. The global recession of 2009 had a significant impact on STC as it halved in 2009/10 and subsequently declined again in 2010/11. This is indicative that banks remained cautious and were keeping reserves.

Large refunds occurred during 2012/13 due to the finalisation of disputes in older tax years which, combined with the provisional tax decline of 9%, accounted for the 34% decline in year-on-year net collections.

- ***Long-term insurers***

Before 1993, a long-term insurer's taxable income was determined in accordance with a formula. In essence, it represented the gross amount of investment income less 55% of expenses. Certain fees for managerial or secretarial services were also included. Investment income included interest, rental income from the letting of property and one-third of dividends received.

In 1993, a new section 29 was inserted in the Income Tax Act, 1962, which introduced a new method of taxation of life insurers and their policyholders. This approach is, in ordinary terms, referred to as the four-fund approach and was introduced following the recommendations of the Jacobs Committee. The approach is based on the trustee principle and the recognition that insurers hold and administer certain of their assets on behalf of various categories of policyholders while the balance of their assets represents shareholders' equity. The effect is that the taxable income generated by assets administered in the policyholder funds is taxed in the hands of the insurer and not in the hands of the millions of policyholders.

The application of the four-fund approach requires that insurers allocate their assets and liabilities to separate funds representative of the various policyholder or corporate interests and that each fund be taxed as a separate entity in accordance with the applicable taxation principles. The four funds consist of a corporate fund and three policyholder funds. Each of the above policyholder funds is permitted to hold only assets having a market value equal to the insurer's liabilities to policyholders. The balance of the insurer's assets (excluding certain residual surpluses) is to be transferred to the corporate fund.

For purposes of the calculation of the taxable income of the different funds, the normal provisions (subject to certain exceptions) of the Income Tax Act, apply. However, the following are some of the exceptions provided for in terms of section 29:

- Selling expenses are averaged over a period of five years.
- Premiums and claims, as well as reinsurance premiums and claims, are excluded from the tax computation.
- Certain transfers from one fund to another are taken into account in the determination of the taxable income of the relevant funds, while certain special transfers are disregarded for tax purposes.

It, however, became apparent after the phasing-in period of the four-fund approach that the amount of tax payable by the long-term insurance industry was decreasing, despite the fact that substantial profits were reflected in the annual financial statements of the insurers. The method of the taxation of long-term insurers was, therefore, investigated. Certain deficiencies in the method of calculation of tax were identified which were thought to explain the relatively small amount of tax collected from the industry. The low tax yield from the industry was considered to be ascribed to the following:

- In terms of section 29, the insurer's expenditure was required to be allocated to the fund in which the business, to which the expenditure exclusively relates, was conducted. Expenditure that did not exclusively relate to business in any one fund was allocated to the different funds in the proportion that business is conducted in the respective funds. The bulk of these expenses were allowed as a deduction against the investment income of policyholder funds. As the base of the taxable income which mainly consists of investment income in each respective policyholder fund was relatively small compared to the amount of the deductible expenses, especially the selling expenses, the taxable income in the policyholder funds was drastically reduced.

- An insurer charges administrative and management fees in respect of the income or assets of the policyholders. These charges were not taxed appropriately as transfers from one fund to another. Although taxable in the transferee fund, these charges were fully deductible in the transferor fund.
- The system of transfers provided for opportunities to defer taxation. In order to address the deficiencies in the then current provisions, without doing away with the trustee principle underlying the four-fund approach, it was proposed that a new section 29A be inserted in the Income Tax Act in 1999. The effectiveness of the proposed measures would, once implemented be monitored closely and, if necessary, adjusted appropriately. Such adjustments may also have included a re-evaluation of the appropriateness of the four-fund approach and the trustee principle.

Another legislative initiative came into effect in 1998 with the demutualisation of two large life insurance companies. The Demutualisation Levy Act was promulgated through which a demutualisation levy at the rate of 2.5% of the value of a portion of the free reserves was payable by the mutual insurers which enters into demutualisation schemes.

The graph below illustrates the improved tax contributions.

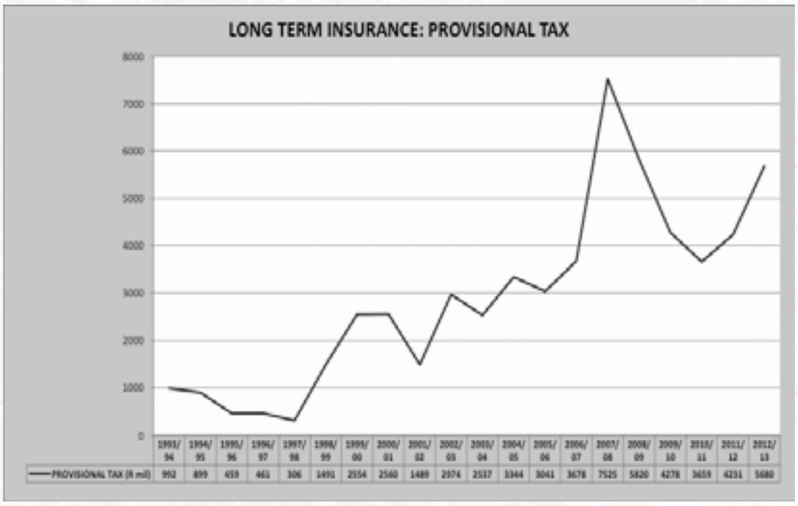

Figure 19: Long-term insurance: Provisional tax from 1994 to 2013

The long-term insurance tax payments grew steadily from 2002/03 to 2006/07 from R3 billion to R3.7 billion respectively. It saw a massive growth to R7 billion in 2007/08 before the recession – which represented a 104.6% increase from the 2006/07 year. Exceptional high collections in this year was due to the requirement that capital gains also needed to be included in provisional tax estimates and this resulted in the significant increase in collections during the year.

The 2008/09 to 2010/11 period saw losses averaging R1.2 billion per annum (21.2%) as a result of the global meltdown emanating from the financial crises.

The change in legislation in the long-term insurance sector in 2012/13 which resulted in the phasing in of capital gains on unrealised profits of funds under administration at the end of the 2012 tax year saw massive growth of R1.5 billion (34.3%) in tax collections.

7.4.9 Withholding taxes

Although international agreements may provide mechanisms to enforce a tax debt due by a non-resident in a foreign country, the process is complex, lengthy and expensive. An administratively efficient alternative is to tax and collect the tax at source.

A dividends tax, which is dealt with in detail in 6.6 was introduced after broad engagement with industry. Although the tax is levied on beneficial owners of dividends, the tax is withheld at source and paid to SARS.

In 2004 a withholding tax on the sale of foreign-owned property was introduced, and in 2005 a final withholding tax for visiting entertainers and sportspersons was introduced.

7.4.10 General anti-avoidance rule (GAAR)

The abnormality and business context tests in the anti-avoidance rules were amended in 1996 and the imposition of interest from a date connected to the year in which the transaction was carried out was introduced in an effort to remove the cash flow advantage gained when avoidance mechanisms were used.

At that time the anti-avoidance provision was based on notions of legal form and intent and reliance was also placed on common law concepts such as substance over form.

In November 2005 a discussion document was published proposing a new GAAR. The GAAR provisions were introduced in 2006. The new provisions mark a move to an objective measure of purpose in relation to the function of the arrangement or the goal that it was designed to achieve.

7.5 Conformity with the Constitution

A major issue dealt with by the Katz Commission was the reform needed to enhance tax administration. The proposal was endorsed by government in 1995. The recommendations underscored the need to improve the predictability of tax through practice notes, rulings and handling queries efficiently. The Commission pointed out that improvements were to be found in the application of modern technology and business principles and a customer-centric administration. A further recommendation was that a cost-benefit review of all incentives had to be conducted and should be justifiable against the objectives of the Reconstruction and Development Programme.

A balance was also needed to be struck between equity and efficiency. An immediate review was needed of all legislation against constitutional principles, and all discriminatory provisions that discriminated on the basis of marital status or gender were to be removed. Provisions and administrative practices that affected the right to privacy, and which concerned recovery and the burden of proof were recommended for expeditious review. In 1996 government supported the publication of a statement of taxpayer rights as recommended by the Katz Commission, which led to the publication of a draft SARS Client Charter in 1997.

7.5.1 Parity between men and women

The Margo Commission initially recommended that individuals – men and women – should be taxed in their own hands. This recommendation was accepted and efforts were made to achieve equal taxation but full parity was not achieved until South Africa became a constitutional democracy. In 1995 a single tax rate table was introduced following the Katz Commission's recommendation that separate rates were unconstitutional. At the same time the primary rebate was increased to alleviate the removal of child-rebates.

7.5.2 Laws governing domestic relationships

In 2001 the definition of "spouse" was amended to include a partner in a customary relationship or union which is recognised as a marriage under South African law or any religion. The definition also includes a same-sex or a heterosexual relationship which the Commissioner is satisfied is intended to be permanent.

Partners may now qualify for the exemptions that were previously only limited to spouses such as the exemption from donations tax, the exemption from estate duty on bequests by the deceased and the exemption from the payment of transfer duty of property transferred as a result of the death of a spouse.

7.5.3 Laws protecting the right of privacy and of self-incrimination

Before 1996 a search and seizure could be conducted if the Commissioner authorised it and in 1996 the provisions in the tax Acts were radically amended to recognise the constitutional right to privacy. The effect of the amendment was that a search and seizure could only be carried out if a judge authorised SARS officials to conduct an unannounced search and seizure.

The right which an accused has against self-incrimination was also given effect to through the introduction of provisions that any information provided during the course of a formal inquiry under subpoena was prohibited from being used against that person in subsequent criminal proceedings.

The TA Act which came into effect in 2012 entrenches the provisions which protect the right to privacy and the right against self-incrimination, and the legislation further reinforces the constitutional rights of taxpayers. For example, the TA Act protects self-incriminating information that is obtained by SARS in the course of an audit from being used in certain circumstances against that person in subsequent criminal proceedings. In addition, processes that SARS' officials must follow have been written into the legislation and certain limitations, which curtail the impact of administrative acts, have also been included in the legislation.

7.5.4 The burden of proof

The Katz Commission had recommended that a review be undertaken of the evidential burden of proof that rested on a taxpayer in tax disputes. The tax Acts at the time provided unequivocally that the burden of proving that an assessment was wrong lay with the taxpayer. The TA Act retains the general burden of proof on a taxpayer, however, now SARS bears the burden of proving the facts which underlie the imposition of understatement penalties (which replaced additional tax) and also to prove the reasonableness of any assessment that is based on an estimate.

7.6 Promotion of business

Over the years tax policy has been developed to promote economic growth.

7.6.1 Advance tax ruling (ATR) system

The transparency, predictability and certainty in the application of tax law are hallmarks of a good tax system in that they contribute to the measure of stability. A holistic advance tax ruling system was introduced in 2006 to promote clarity, consistency and certainty in the interpretation and application of tax laws. This advance tax ruling system provides a procedure through which taxpayers can apply for binding general, private or class rulings and also apply for non-binding private opinions from SARS. The binding rulings are published on SARS' website, but taxpayers' identity is excised from binding private and class rulings. During the period under review (1994-2014), SARS has published 185 binding private rulings, 44 binding class rulings and 24 binding general rulings.

In addition to the advance tax ruling system SARS periodically issues interpretation notes aimed at providing guidelines to taxpayers and SARS' officials on the official interpretation and application of specific provisions in the Acts administered by SARS. These interpretation notes are modified or withdrawn to keep pace with change, and there are 75 current interpretation notes in issue. Over time, interpretation notes will replace all existing general notes, practice notes and internal circular minutes.

7.6.2 Corporate restructuring transactions

In 2002 the group relief measures contained in sections 41 to 47 of the Income Tax Act were introduced and provided general relief from the normal tax consequences that would normally follow transactions involving corporate restructuring. The corporate rules cover intra-group, unbundling and amalgamation transactions as well as the consequences that would normally flow when a company is deregistered, liquidated or voluntarily wound-up. In 7.4 the response to the perceived abuse is considered.

7.6.3 Industrial incentives

South Africa's broad economic policy includes schemes designed to encourage and promote international competitiveness in the country's manufacturing sector. This is set out in the government's Economic Programme of Action, in which special zones were created to encourage increased levels of foreign direct investment in the economy and the export of value-added commodities.

Incentives were introduced as a strategy to promote economic growth and to integrate South Africa into the global market. The result was an industrial development zone (IDZ) incentive, which is to be replaced by the special economic zone (SEZ) incentive.

- ***Industrial development zones (IDZs)***

A tax incentive was introduced in 2008 to support new industrial projects that use only new and unused manufacturing assets (that is, Greenfield investments), as well as expansions or upgrades of existing industrial projects (that is, Brownfield investments).

- ***Special economic zones (SEZs)***

With the introduction of SEZs, to replace and extend incentives for industrial economic zones, certain tax interventions were announced in 2013 to support the initiative. These initiatives entail reduced tax rates for companies operating within the zone, accelerated deductions for buildings based on the urban development zone benefits (dealt with below) and incentives for employers relating to employees earning below a set threshold (currently R60 000) who are employed within an SEZ.

7.6.4 Allowances

Over the years certain allowances have been introduced to promote business development in specific areas and which are aligned to the country's macroeconomic policy.

- ***Depreciation allowance for infrastructure***

By 2000 the economic landscape had changed and South Africa's development relied in part on infrastructure development and private public partnerships were emerging. Government recognised the need to provide a depreciation allowance for permanent infrastructure such as oil and gas pipelines, electricity and telephone transmission lines and railway tracks. Depreciation allowances were introduced for new permanent structures of this nature that are brought into use. The allowances are periodically reviewed in order to make adjustments for new technology as well as to align with international norms – for instance the allowance for telecommunications was adjusted to reflect the move from copper to fibre optics and to align the allowance with international norms.

In 2001 a 5% per year allowance was introduced in respect of airport hangars and runways and in 2007 the allowance was extended to certain port facilities and a preferential allowance (a five year write-off period) was introduced for rail locomotives and wagons.

- ***Accelerated allowance for manufacturing***

An accelerated depreciation allowance was provided in 2002 in respect of assets directly used in manufacturing enterprises.

- ***Research and development (R&D) expenditure***

An accelerated allowance, similar to the depreciation allowance for manufacturing assets, was introduced for research and development in 2003. In 2006 the allowance was increased to 150% of R&D expenditure and an accelerated depreciation deduction was allowable for capital expenditure incurred on any building or part of the building, machinery, plant, implement, utensil or article used for R&D purposes.

- ***Depreciation of commercial buildings***

A 20-year straight line allowance for new or refurbished commercial building was introduced in 2007.

- ***Hotel refurbishment***

In 1993 a 20% annual allowance was introduced for the cost of refurbishment incurred by hotel owners. This allowance is allowed in addition to an allowance for the cost of erecting a hotel.

- ***Urban development zones (UDZs)***

In 2003 a special depreciation allowance was made available for building and refurbishment costs incurred in certain designated areas. The purpose of this allowance is to regenerate densely populated urban areas, and was extended to March 2020.

7.6.5 Other tax provisions that promote business

In addition to beneficial allowances, other provisions have been introduced that are intended to promote the growth of the South African economy.

- ***New tax regime for ships***

Over the years the tax treatment of shipping companies had not kept pace with international developments as shipping companies were taxed in South Africa on business income. In 2006 a new method of taxation based on the ship tonnage was considered, but in 2013 domestic shipping companies operating South African flagged ships in international traffic were provided an incentive in the form of exemption from normal tax, dividends tax as well as cross-border withholding tax on interest.

- ***Diamond export levy***

A diamond export levy, enacted in a separate Act in 2007, regulates the supply of rough diamonds for the domestic market and promotes domestic beneficiation.

- ***Securities lending***

In a move to support liquidity on the Johannesburg Stock Exchange (JSE) and enhance South Africa's position as an international financial market, exemptions were introduced in 2003 and 2012 that encouraged securities lending.

- ***Islamic finance***

In 2010 provisions were introduced to provide the tax framework for Islamic financial products which aligned the tax treatment of these products with conventional financial instruments.

- ***Business asset re-investment relief***

Since 2003 relief was provided to companies that disposed of assets and reinvested the proceeds within an 18-month period. In effect the relief deferred taxable income or gain on the asset sold for the life of the newly acquired asset.

- ***The disposal of short-life assets***

In 2003 the scrapping regime was substituted for one that allowed taxpayers to claim a loss on the sale of a depreciable asset that has a short useful life.

- ***Headquarter companies***

Legislation was announced in 2010 to promote South Africa as a base for African operations by providing for a "headquarter company" system. It provides relief from transfer pricing adjustments, dividends tax and controlled foreign company provisions.

- ***Film industry***

In the early 1990s the abuse of film schemes had been unravelled and had reached the courts by 1993. By 2005 there was growing interest in the South African film industry and the tax regime was cautiously put under review to encourage growth in the industry. From 2012 an exemption from tax was granted to receipts and accruals that are derived from the exploitation rights of a film.

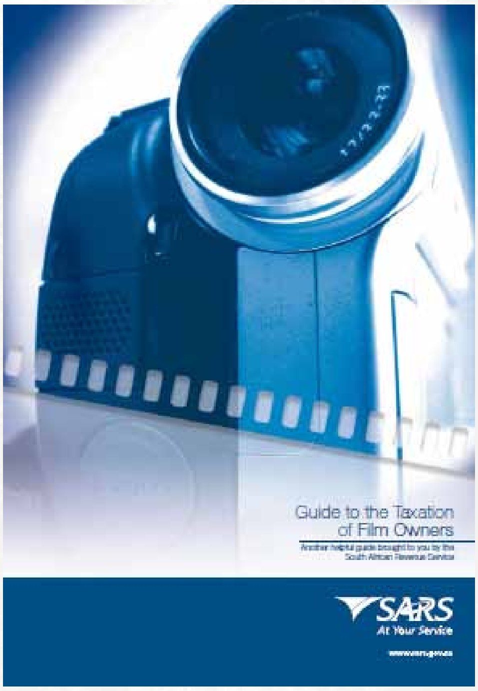

Figure 20: Cover of SARS' Guide to the Taxation of Film Owners

- ***Tax practitioner regulation***

During 2002 the effort to regulate tax practitioners commenced with the release of a discussion document for comment, and a separate Tax Practitioner Bill was proposed in 2005. In the course of drafting the Tax Administration Bill (TAB) it became apparent that a strep towards the regulation of tax practitioners could be incorporated in the TAB. The registration and regulation of practitioners is currently provided for in the TA Act and practitioners are required to be a member of a controlling body which has appropriate professional regulatory authority.

7.7 Social development

Like many developing countries there is a need in South Africa to improve the living conditions of lower income households and create job opportunities alongside taking measures to grow the economy. The South African tax system has numerous tax incentives that are designed to promote these objectives.

7.7.1 Educational incentives

The development of incentives to promote job creation and the formalisation of existing jobs was announced in 2001. Legislation was prepared in 2002 that provided for learnership allowances for employers, linked to both the commencement and the completion of a learnership qualification. By the end of September 2002 a total of 228 884 learners were registered and 2 861 had completed their learnership.

The incentives were originally intended to expire in 2006, but alongside government's broader initiative to improve skills, the incentive was extended to October 2016. At the same time the employment of disabled persons was further incentivised through the granting of increased allowances. Longer term apprenticeships for trades such as electricians, plumbers and mechanics were accommodated in the incentive scheme from 2008.

Bursaries to employees are also exempt from tax if certain conditions are met.

7.7.2 Youth employment subsidy

The Employment Tax Incentive Act 26 of 2013 became effective on 1 January 2014 and aims to encourage employers to employ young workers by providing a tax incentive. The incentive will reduce employers' cost related to hiring young people by permitting an incentive amount to be deducted from the PAYE withheld from employees' remuneration. The incentive currently operates for a maximum of two years and reduces in the second year.

7.7.3 Housing for low income households

Providing housing for low income earners remains a significant government objective, and a concerted effort is needed to encourage employers, developers, PBOs and landlords to increase the supply. Reducing the value of the fringe benefit attaching to employer-provided housing began in 2008 and the depreciation allowances claimable by employers and developers were revisited. In 2013 the fringe benefit rules were amended to allow employers to transfer houses to lower income employees at a below market value in certain circumstances.

A "gap market" exists in respect of housing where individuals do not qualify for housing subsidies but also earn too little to afford a conventional mortgage bond. In order to promote housing for this market a tax incentive was introduced in 2012 to encourage developers to provide houses marketed at below R300 000.

7.7.4 Tax-free shares to employees

The granting of tax-free shares to employees became effective in 2004 to promote broad-based employee equity participation. The policy was to promote long-term investment rather than short-term profit-making.

7.7.5 Medical scheme contributions

The method of calculating deductions for medical scheme contributions was revised in March 2006 when a monthly monetary amount replaced the provision that employers could contribute two-thirds tax-free. The purpose of this amendment is to encourage self-employed persons to join medical schemes and provide almost total relief for the more affordable medical aid schemes. The conversion of the formula-based deduction to a non-refundable tax credit was debated from 2009, and after giving the industry the opportunity to provide input, was introduced in 2012. The benefit of the new scheme is that the benefit does not increase at higher income levels, thereby supporting equity.

7.7.6 Public benefit organisations (PBOs) and exempt institutions

In 1997 legislation was amended so that all bodies that enjoyed exempt tax status were to apply to SARS for formal approval of their exempt status.

By 2000 it was recognised that organisations were emerging that served the needs of society but that existing legislation did not fully accommodate and foster the important role these organisations played.

New provisions were drafted for PBOs which created an entirely new area to be administered by SARS.

In 2001 a list was published of public benefit activities that organisations were to be involved in, in order to obtain exempt status. This list was revised and extended in 2002 and 2003 when it included organisations involved in areas of welfare and humanitarian aid, health care, land and housing, education and development, and to providing student loans in 2008. PBOs which provide housing to low-income earners are granted exempt status only if the household income is below a set threshold, which threshold has been raised to provide for inflation and salary increases.

In 2003 PBOs were permitted to accept foreign donations without losing exempt status, and in 2005 it was recognised that business activity was often required to enable the PBO to survive. Business activity that exceeded a set threshold was taxed but did not automatically jeopardise the PBO's tax exempt status.

Tax exempt status is an attractive benefit that is open to abuse, and sports recreational clubs, perhaps inadvertently, expanded their business activities far beyond their direct members. This was tightened in 2006.

During 2008 restrictions that required 85% of their activities in South Africa were removed.

In order to encourage donations, donations in excess of the permissible deductible amount are from 2013 to be carried forward.

7.8 Small businesses

Government has recognised the important role that smaller businesses play in the economy and fostering the growth of smaller business has been a consistent feature in tax policy development from 2000.

From 1 April 2000 a progressive tax scale was introduced for small and medium sized businesses that were essentially labour intensive. In order to qualify, the company had to have a gross income not exceeding R1 million and the shareholders had to be natural persons who had no interest in another company. The rate applicable was 15% of the first R100 000 and 30% on taxable income that exceeded this threshold. An accelerated allowance was introduced in 2001 for qualifying small businesses that invest in manufacturing assets to encourage manufacturing within this segment of the economy. The allowance permits a full deduction of the cost of the asset in the year the asset is brought into use.

The R1 million turnover threshold that characterised a small business was increased to R3 million in 2002 and steadily increased to R14 million in 2006 and to R20 million in 2013. Cooperatives that operate in a similar manner to small businesses were allowed to benefit from the small business dispensation from 2006.

In 2003 further stimulus was extended to businesses which are allowed to claim start-up expenses incurred before operations began.

In 2005 various amendments were effected to expand the application of the small business rules and more advantageous provisions were added. Companies, which would otherwise be excluded because their shareholders provided certain professional services through the companies, were categorised as being eligible if they maintained at least three full-time employees unconnected to the shareholders, and a simplified 50:30:20 depreciation allowance for non-manufacturing businesses was introduced.

Enterprises with an annual payroll of under R500 000 were exempted from skills development levies in 2005.

A simplified tax regime for very small businesses with a turnover less than R1 million was introduced in 2008, which coincided with the increase in the VAT threshold to R1 million.

The encouragement of smaller enterprises was also stimulated by venture-capital incentives introduced in 2008 in order to promote investment in smaller enterprises by the private equity industry. Access to investment capital by small and medium sized enterprises was seen as a factor limiting the start-up of smaller enterprises. In order to encourage start-up and seed-capital funding of smaller enterprises, venture capital incentives were introduced in 2008. The incentives were increased to a R50 million asset limit and a deduction was allowed for the full amount of the investment made. Provided that the investment is held for a minimum period of five years no revenue recoupment occurs on the disposal, which further encourages funding.

One of the areas that the Davis Tax Committee is mandated to consider is the tax regime for small businesses. It is therefore anticipated that as the work of the Committee progresses further changes will be made. The Committee is discussed in 15.1.

7.9 Promotion of savings and the retirement fund industry

In 1996 recommendations for the reform of the retirement fund industry were partially accepted, which included acknowledging that private and public funds should be treated consistently, a lifetime annuity should be incentivised and room for arbitrage should be removed.

At the time contributions made to a fund were deductible, income of a fund was exempt, and benefits received were taxable.

The first step to comprehensive remodelling was the imposition of a 17% levy on the gross interest and the net rental received or accrued by all funds in the industry including all state funds and self-administered funds.

Exemptions were applied to those receipts or accruals that were attributable to members whose benefits had accrued before March 1996 and provisions were made to limit the levy where the value of interest and rental bearing assets exceeded 50% of the fund's total assets.

The taxation of the retirement industry represented a significant step towards broadening the tax base, improving equity in the distribution of the tax burden and removing distortions that affected savings and retirement choices.

Amendments were made in 1997 to include certain dividends and other compensation in the amount that would be subject to the 17% levy introduced in 1996.

In 1998 the levy was increased from 17% to 25%; however by 2003 it was apparent that the rate impacted mainly on middle and low income earners and it was reduced to 18%. Interest rates had stabilised at lower levels by 2006 and the levy was reduced from 18% to 9%. As part of a package of reform measures, the levy was abolished with effect from 1 March 2007.

A holistic approach to the taxation of the retirement fund industry was placed on the 2004 agenda.

From 1998 lump sum benefits from both private and public funds were taxable which represented a significant shift to ensuring that the tax burden was shared equitably. In 1999 the exemption enjoyed by the Public Investment Commissioner on the purchase of equities was removed. This exemption had effectively reduced the cost to the Government Employees Pension Scheme of acquiring equities and the removal of the exemption promoted parity between public and private funds.

By 2000 pension funds had accumulated an estimated R80 billion of surplus assets, and had won the legal right to repatriate surplus assets to participating employers and members. From 23 February 2000 legislation taxed the full amount of any repatriated surplus without the set off of assessed losses.

In 2005 the industry was undergoing a wider reform, and National Treasury issued a discussion paper outlining reform proposals to address weaknesses in the industry including fee structures and risk exposure. By 2007 a tax policy review was done and as mentioned the first step was abolishing the retirement fund tax. The withholding tax on lump sums was seen as overly complicated and the first step in simplification was to abolish the withholding tax for individuals with taxable income below R43 000.

In a further step to encourage savings, tax-preferred savings accounts are proposed to be introduced by 2015 in which returns and withdrawals are tax-free. Limited annual contributions and a lifetime cap are proposed to limit the revenue cost of the incentive.

7.10 Supporting the protection of the environment

In 2006 National Treasury issued a draft policy document "A Framework for Considering Market-Based Instruments to Support Environmental Fiscal Reform in South Africa" for comment.

This draft policy document focused on how taxes could support regulatory measures to promote environmental protection. The use of market-based instruments, such as taxes, to deter practices that prove detrimental to the environment as well as to promote positive actions, have proved an effective regulatory measure.

From 2006 tax reform included measures to promote long-term environmental protection and conservation. By 2009 South Africa's greenhouse gas emissions was accounting for 1.8% of the world's emissions and 42% of Africa's emissions, and further tax measures were introduced.

7.10.1 Environmental capital expenses

The rehabilitation of mines is intended to address long-term environmental issues and, in a move to promote mine-rehabilitation, mining enterprises are entitled to deduct financial provisions made for rehabilitation. In 2006 in response to a request from the industry, the relief measures were extended to insurance products that are dedicated solely to mine rehabilitation.

Businesses that are required to incur expenses to comply with regulations concerning environmental issues were normally not entitled to a deduction as the expenditure was considered to be of a capital nature. In 2007 allowances were provided for expenses related to capital structures, and other expenditure incurred on matters such as environmental clean-ups and decommissioning was made tax-deductible.

7.10.2 Encouraging investment in renewable energy

In order to facilitate production of biofuels a three-year 50:30:20 allowance was introduced from 2003 in respect of plant and machinery, and was extended to solar and wind technology in 2005.

An electricity levy, collected at source by the producer, was introduced in 2008 partially to support demand-side management and, as the levy applies to electricity produced from a non-renewable source, encouraged long-term investment in renewable energy generation. This levy was the first step towards a carbon tax.

7.10.3 Certified emissions reduction certificates

After the inception of the first commitment period under the Kyoto Protocol in 2008, there was limited uptake of clean development mechanism projects within South Africa. As a result, an income tax incentive was introduced in 2009 for any person holding a clean development mechanism registered project. The incentive exempts amounts received or accrued upon disposal of certified emission reduction certificates from income and capital gains tax.

7.10.4 Other measures

The following levies were introduced in the effort to promote environmental protection and conservation:

- In 2005 a levy on plastic shopping bags was introduced in order to contain indiscriminate littering.
- A levy on high-energy incandescent light bulbs applied from October 2009 to encourage the use of low-energy equivalents.
- In 2009 CO^2 emissions tax was introduced on new passenger vehicles.

7.11 International links

Although South Africa's evolution into the global economy is dealt with in Chapter 10, it is appropriate to introduce it as topic within the context of policy development.

The initiative to integrate the South African tax system with other countries' systems began in 1993 when other countries and revenue authorities started to demonstrate a keen interest in the affairs of South Africa. In that year, although only six tax treaties were in place, 15 tax treaties were being discussed or negotiated with countries such as France, Hungary Poland, the Republic of China, Rumania, the Russian Federation, Namibia, Mauritius and Lesotho. This pace of negotiating and renegotiating international agreements kept momentum from 1994 until 2014 when, on 1 March 2014 the Multilateral Convention on Mutual Administrative Assistance on Tax Matters entered into force.

International organisations, such as the World Bank and the IMF, and regional aid organisations, such as the African Development Bank, began actively engaging with South Africa. Customs also experienced greater support and cooperation from foreign administrations with improvements being made in the detection of smuggling and fraudulent activities, and in cross-training initiatives being held.

7.12 Taxes phased out

During the development process, levies or taxes that proved difficult to administer and not satisfying economic reality tests, have been phased out.

The regional services council levies were payable by businesses to the local authority at a flat rate of gross sales and payroll. The levies were considered not to represent a "good tax". There were many flaws in its administration, which made the cost of revenue collection very high. The scheme did not bring the informal sector into the net and thereby created another source of horizontal inequity, and it was feared that the levy could deter job creation. The regional services council levies were abolished with effect from 30 June 2006.

Stamp duties on certain transactions were administratively burdensome and generated little revenue, and its phasing-out began in 2000. Exemption of transactions gained momentum over the years and stamp duty was abolished in 2009.

Standard Income Tax on Employees (SITE) was introduced in 1988 on the recommendation of the Margo Commission to remove the administrative burden of lower income recipients having to file tax returns. SITE became unnecessary with the modernisation programmes introduced and was discontinued in 2011.

CHAPTER 8
THE TAX ADMINISTRATION ACT, 2011

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THE TAX ADMINISTRATION ACT, 2011

In the 2005 Budget Review the Minister of Finance announced the commencement of a project "to incorporate in one piece of legislation certain generic administrative provisions, which are currently duplicated in the different tax Acts".

This Chapter discusses the purpose, legislative process and some of the most important inclusions in the Tax Administration Act (TA Act).

8.1 The purpose of a single tax administrative statute

Before the promulgation of the TA Act the administrative provisions were contained in the various Acts administered by SARS. In an effort to simplify administration, the Income Tax Act was often used as the primary Act to introduce or refine administrative provisions, with the other Acts incorporating the Income Tax Act provisions. Through this process the Income Tax Act began to lose its character as primarily a fiscal or charging Act and the cross-referencing between the Income Tax Act and the other Acts was not the ideal position.

The objective of a single body of administrative tax law was to standardise administration and, through the consolidation of similar provisions in various Acts into a single Act, to simplify the tax system.

The TA Act has impacted on how SARS' officials administer the tax base and it is suggested that the TA Act has ushered in a "new professional discipline of 'tax administration' ".[1]

8.2 The legislative process

The Draft Bill with the Explanatory Memorandum was first circulated for comment in October 2009. After the initial commentary phase, a redrafted Bill was provided to external counsel who were considered to be experts in the areas of constitutional and administrative law. A second round of public comment was held between October and December 2010, before the Minister of Finance introduced the Bill to Parliament in June 2011. Certain submissions were prepared for presentation to the Standing Committee on Finance.

Comments on the Bills were carefully scrutinised and either not accepted, partially accepted or fully accepted. As an indication of the extent to which comments were taken into account, the following were incorporated into the final Bill:

- The introduction of a Tax Ombud.
- The removal of the requirement for advance notice of leaving South Africa.
- The limitation of information requests to available records.
- The requirement that information requests should be subject to a "reasonable specificity" test.
- The protection of information over which legal professional privilege is claimed during a seizure.
- The right to claim damages in certain circumstances arising from search and seizure.
- SARS bearing the burden of proof concerning the basis of an estimated assessment.
- Provision for a permanent voluntary disclosure programme.

The final Bill was passed into law by the National Assembly on 24 November 2014, and the TA Act was promulgated on 4 July 2012 and all the provisions, except certain provisions governing interest, were implemented with effect from 1 October 2012.

8.3 Some new aspects introduced by the TA Act

The TA Act is drafted using simple language and is constructed to follow a normal tax cycle.

As mentioned in 7.5 soon after 1994 there was a move to align the tax Acts with constitutional principles. This objective was carried into the TA Act which sought to balance the powers and duties of SARS officials and the obligations and rights of taxpayers. The introduction of a Tax Ombud was lauded as a positive move that promote the integrity of tax administration by giving taxpayers an alternative route to follow in order to resolve service and administrative complaints, at no cost.

In many ways the TA Act sets the foundation for the fair administration of taxes, for instance through the introduction of the delegation of powers to senior SARS officials to take certain decisions, by prescribing standard procedures to be followed before an administrative action is taken and by specifying set factors that are to be taken into account when certain decisions were made. The expedited recovery mechanisms are perfected by the requirement to provide notice to the taxpayer before a "tax judgment" is obtained, and once tax debts are settled SARS is required to withdraw a "tax judgment".

The opportunity was also taken to clarify areas that were historically unclear. For example, SARS' authority to compel the production of information was extended to include taxpayers who fall into an objectively identifiable class or whose identity was unknown but who could be objectively identified.

There are also various new provisions that permit positive enforcement action to be taken when circumstances are warranted. For example, an assessment can be raised before the due date for submission of a tax return in order to secure the collection of tax that would otherwise be in jeopardy. SARS may also, in certain circumstances that are designed to protect the *fiscus*, move for a preservation order over a taxpayer's assets before an assessment is raised, but is anticipated.

CHAPTER 9
DISPUTE RESOLUTION AND SELECTED CASES

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As mentioned, certainty in the application of tax laws is an important element of a good tax system and can be promoted through access to rulings from the tax authority as well as through formal documentation that indicates the revenue authority's application of tax laws. However, the reality is that disputes will inevitably arise between taxpayers and the revenue authority concerning the correct interpretation and application of tax law.

When disputes do arise – as is sometimes the case – it is important that the tax regime has mechanisms that provide for the swift and inexpensive resolution of disputed tax in an appropriate forum.

This Chapter discusses the dispute resolution mechanisms available to taxpayers who disagree with SARS' application of tax law as well as the role that specialist tribunals and courts play in dispute resolution.

Through the compulsory publication of tax court decisions and the principle of *stare decisis* the principles of transparency and of certainty are promoted when tax disputes are concluded in the more formal tax courts and higher courts. Certain cases have stood the test of time as they are considered to be the correct statement of the law on fundamental tax issues and certain of these cases are dealt with briefly in the latter part of this Chapter.

9.1 Dispute resolution

9.1.1 The tax court

The Commissioner of Taxes' Report to the Houses of Parliament in 1915 on the introduction of the 1914 Income Tax Act announced that approximately £9 000, of the total assessments of £482 000, was either on appeal or was due under late assessments, and that special courts for hearing appeals were being appointed.

The tax courts that were formed to handle tax disputes continue to function today as special courts within the provincial divisions of the High Court. Tax courts were established in terms of the 1962 Income Tax Act and continue to function under the current TA Act. The President of South Africa may establish or abolish a tax court by proclamation.

The tax court is presided over by a judge of the High Court, known as the President of the Tax Court, who is appointed by the Judge-President of the area in which the tax court sits. The tax court comprises the President, an accountant and a commercial member. If the dispute involves mining then the commercial member may be an engineer and a sworn appraiser if the dispute concerns the valuation of an asset. Interlocutory matters, or disputes of pure law, may be decided by the President alone.

Although only suitably qualified legal professionals may appear for SARS, there is no similar limitation on who may represent a taxpayer. The court is one of record, has the power of subpoena and follows proceedings that are contained in published Rules.

In civil litigation a losing party usually pays the costs of the successful party, however, in tax cases the tax court will not order one party to pay the other party's costs except under very limited circumstances such as if the Commissioner's grounds of assessment or the taxpayer's appeal is considered unreasonable. Removing the risk exposure to additional legal costs is intended to promote the airing of tax disputes.

Although tax court judgments are not binding on other tax courts, they are persuasive, and there is a right of appeal first to the full bench of the relevant provincial division and thereafter to the Supreme Court of Appeal. In certain cases an appeal can be made from the tax court directly to the Supreme Court of Appeal.

9.1.2 The tax board

Tax boards came into operation in 1992 as less formal forums to consider disputes that were originally under R20 000. The Explanatory Memorandum to the 1991 Income Tax Bill explained:

> *In view of the fact that over the past few years the annual number of appeals lodged has increased drastically, there are long waiting periods before a case can be enrolled for hearing because the number of judges who may act as presiding officers, is limited. The need for a more streamlined system to deal with appeals more swiftly and to give taxpayers the chance to present their cases sooner, therefore arose.*

Tax boards are presided over by Chairpersons who are appointed by the Minister of Finance and are selected from independent legal practitioners practising in the area in which the tax boards convene. The proceedings are informal and the Chairperson has the discretion to determine how the proceedings are to be conducted. The tax board is not a tribunal of record although the decision is handed down in writing and is binding on the parties. There is a right of appeal *de novo* to the tax court.

Tax boards are currently authorised to adjudicate on assessments of amounts in dispute under R500 000.

9.1.3 Alternative Dispute Resolution (ADR) and Settlements

Proceedings before the tax board and the tax court are a more traditional approach to resolving disputes and in 2003 the Alternative Dispute Resolution (ADR) was introduced as a resolution process that was based on voluntary participation and facilitation. At the same time that ADR was introduced the Income Tax Act was amended to allow SARS to settle a dispute without conceding on the merits or on an issue of law – provided that a settlement met various criteria and was the most appropriate course of action.

In 1993, almost exactly 10 years before generic settlement of dispute provisions were incorporated into the Income Tax Act of 1962, section 61 of the Income Tax Act 113 of 1993 was introduced to allow the Commissioner to settle certain disputes that involved certain tax avoidance schemes that were identified in Regulations. Under these Regulations the Commissioner was empowered to settle tax avoidance schemes that related to the investment in films or music recording, the investment in aircrafts or schemes that involved the investment in plantations.

While the section 61 enactment empowered the Minister of Finance to identify avoidance arrangements that should, in the best interest of the state, be settled, the generic settlement provisions were both broader and more comprehensive.

The generic settlement provisions were repealed and incorporated into the TA Act in Part F of Chapter 9. Only a senior SARS official may settle a dispute and Part F sets out the purpose that must be achieved by a settlement, the circumstances that must be considered as well as the circumstances that prohibit a settlement from being entered into. Part F requires every settlement to be recorded in writing and for the Commissioner to report annually on the amounts of tax written off.

9.2 Selected cases

Even though tax law is continually evolving and being developed through cases, there are certain court decisions that are considered seminal decisions.

9.2.1 Gross income and Lategan v CIR[14]

Lategan concerned a wine farmer who had sold wine produced during the year, with a portion of the purchase price being paid within that year and the balance being payable after the year of assessment. The case concerned the meaning of amount accrued in the context of what fell into the definition of "gross income".

Two important principles were established in Lategan. The first was that the word "amount" was open to a wide interpretation and was not limited only to money. The second principle established that "accrued" meant had become entitled to, meaning that "a right had vested in him, had accrued to him in the year of assessment and it was a valuable right which he could turn into money if he wished to do so".

In 1990 the entitlement principle was upheld by the Appellate Division in *CIR v People's Stores (Walvis Bay) (Pty) Ltd*[15] and was treated as an established principle in the Appellate Division judgment of *Cactus Investments (Pty) Ltd v CIR*[16].

The Lategan principle, that "amount" has a broader meaning than just money, was confirmed in the Supreme Court of Appeal in the matter of *C: SARS v Brummeria Renaissance (Pty) Ltd*[17]. The Court found that "all that is required is that rights of a non-capital nature are capable of being valued in money". The judgment caused some speculation as to how the principle would be applied by SARS, and SARS issued Binding General Ruling 8 "Application of the Principles Enunciated by the *Brummeria Case*".

9.2.2 Capital vs revenue receipts: *Natal Estates Ltd v Secretary for Inland Revenue*[18]; *CIR v Pick n Pay Employee Share Purchase Trust*[19]

Over the years different tests have been used to distinguish capital receipts from revenue receipts. This distinction is important as no half-way house was known to the courts[20]. The courts have sought to determine the character of receipts by distinguishing whether the flow emanated from the disposal of fixed or floating capital such as in *CIR v George Forest Timber Co Ltd*[21] or from the sale of fruits of a tree rather than from the disposal of the tree itself, as in *Visser v CIR*[22].

Arguably, the leading case in the characterisation of proceeds as revenue or capital is *CIR v Pick n Pay Employee Share Purchase Trust*[23] which affirmed the Lategan principle that the test involved ascertaining whether the taxpayer had intended to embark on a profit-making scheme.

The Appellate Division explained what the test involved:

> *Contemplation is not to be confused with the intention … In a tax case one is not concerned with what possibilities apart from his actual purpose, the taxpayer foresaw and with which he reconciled himself. One is solely concerned with his object, his aim his actual purpose...*

9.2.3 Deductibility of expenditure

Capital expenditure is not deductible under the general provisions and, as there is no definition of "capital", the courts have, over the years, developed certain tests to ascertain what expenditure of a capital nature is. One of the earliest and most cited decisions was handed down by the Appellate Division in *CIR v George Forest Timber Co. Ltd*[24]. This judgment, delivered by the Chief Justice, described the distinction between capital and revenue expenditure as follows:

> *In the absence of any authoritative and comprehensive definition of capital expenditure it is well to bear in mind the characteristic quality of capital … Now, money spent in creating or acquiring an income-producing concern must be capital expenditure. It is invested to yield future profit; and while the outlay does not recur the income does. There is a great difference between money spent in creating or acquiring a source of profit, and money spent in working it. The one is capital expenditure, the other is not.*

This description has been accepted and applied by the Appellate Division in numerous cases that followed, including the case of *New State Areas Ltd v CIR*[25]. The New State Areas case is considered by many to have expressed the most accurate description of what amounts to capital or revenue expenditure where, after a review of the existing cases, it was held:

> *Its true nature is a matter of fact and the purpose of the expenditure is an important factor; if it is incurred for the purpose of acquiring a capital asset for the business it is capital expenditure even if it is paid in annual instalments; if, on the other hand it is in truth no more than part of the cost incidental to the performance of the income producing operations, as distinguished from the equipment of the income producing machine, then it is a revenue expenditure even if it is paid in a lump sum.*

Although the judgment in *Port Elizabeth Electric Tramway Co v CIR*[26] is only a provincial division decision, it has had a lasting impact on what is considered to be deductible expenditure. This judgment characterised deductible expenditure and coupled section 11(*a*) and section 23(*g*) in a manner that has become known as the general deduction formula. Over the years various aspects of this judgment have been confirmed as being a correct statement of the law. The court identified that in order to determine deductibility the purpose of the expenditure was a relevant consideration, that there should be a connection between the expenditure and the income and that the expenditure need not be actually paid in order to be deductible.

The purpose for incurring and the connectivity between the expenditure and the trade have been accepted as correctly setting out the law when considering the deductibility of expenditure for tax purposes. This is evidenced in cases such as *CIR v Allied Building Society*[27], *CIR v Standard Bank of South Africa Ltd*[28], *Ticktin Timbers CC v CIR*[29] and *Warner Lambert SA (Pty) Ltd v CSARS*[29].

9.2.4 Simulated transactions and the avoidance of tax

Tax legislation in South Africa has general anti-avoidance provisions and there has therefore been a limited need for common law principles to develop that deal with tax avoidance. However, the courts have applied the common law to tax avoidance and it is now settled law that the incidence of tax is not maligned by disguised transactions. Two important decisions of the Appellate Division and the Supreme Court of Appeal demonstrate the application of this principle: the *Erf 3183/1 Ladysmith (Pty) Ltd v CIR*[31] and the more recent decision of the Supreme Court of Appeal in *CSARS v NWK Ltd*[32]. Lewis JA, in the NWK Ltd case, confirmed:

> *There is, in principle, nothing wrong with arrangements that are tax-effective. But there is something wrong with dressing up or disguising a transaction to make it appear to be something that it is not.*

9.2.5 Recovery of tax

No exposition of tax cases is complete without reference to the Constitutional Court decision in *Metcash Trading Ltd v CSARS*[33]. In the Metcash case the Constitutional Court upheld the "pay now, argue later" principle of disputes that had arisen in relation to VAT. Although the case is considered to be a watershed one that emphasises the important public role that tax plays, the judgment is also considered to confirm the necessity that SARS is required to act in a balanced and accountable manner. Shortly after the judgment was handed down, a media statement was issued that affirmed how SARS would apply the "pay now, argue later" principle. The criteria have been included in legislation since.

CHAPTER 10
TAXATION IN AN INTERNATIONAL CONTEXT

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The dawn of democracy in South Africa in 1994 has had a tremendous impact on the international aspect of taxation in South Africa. The fundamental change in the political dispensation evolved with the phasing out of exchange control regulations and coincided with the rapid growth in electronic commerce which was unbound by country borders. The combination of these elements removed trading barriers in South Africa and local businesses began to spread their wings to expand their trading activities into foreign markets and further into Africa. The evolution of an open economy also resulted in foreign traders entering the South African market.

The acceptance of South Africa into the global business community meant that the tax regime had to change to be both internationally competitive and to protect the local market from potential abuse.

Although the post-1994 dispensation underlies numerous changes to the tax regime this Chapter highlights the adoption of a residence-based system of taxation and the negotiation and conclusion of international agreements after 1994. This Chapter also discusses SARS' growing involvement in the international tax community which followed South Africa's recognition as a legitimate member of the global community.

10.1 Residence-based tax system

10.1.1 The early debate

In 1997 the Katz Commission submitted its Fifth Interim Report which contained recommendations to the Minister of Finance on whether SARS should adopt a residence-based system of taxation.

At the time the tax laws contained provisions that deemed certain limited income sources as South African, but these were considered ineffective in practice. From July 1997 South African tax residents were taxed on foreign-sourced passive investment income in the form of interest, annuities, rental and royalties. At the same time controlled foreign entity rules were introduced to tax South African tax residents on the passive investment income of foreign companies and trusts controlled by them.

10.1.2 Announcement of residence-based taxation

By 2000 exchange control had started to be relaxed and South Africa's integration into the global economy had grown to such an extent that the debate whether South Africa should adopt a residence basis of taxation needed finality. In February 2000 it was announced that a residence-based system of taxation would be adopted.

At the time, and as an interim measure to avoid erosion of the tax base through round-tripping, all foreign-sourced dividends were subjected to tax in South Africa from 23 February 2000.

The transition from a source-based to a residence-based tax system was complex and required an extensive review of impacted provisions, consequential amendments to the Income Tax Act and a different focus in the negotiation of tax treaties.

In 2001 the adoption of a residence basis of taxation was completed. Residents are now taxed on their worldwide income and no longer just on income from a source within South Africa. Persons who are not residents are subject to tax in South Africa on their income from a source within or deemed to be within South Africa.

10.1.3 Summary of residence-based tax

The residence of a natural person is determined by an "ordinarily resident" test and a "physical presence test" and the place of residence of juristic persons is determined by the place of incorporation or of effective management.

The characteristics of the residence-based system include:

- Allowing foreign tax credits against South African tax on foreign-sourced income.
- Imputing an amount of net income of controlled foreign entities to residents who have an interest in the entity.
- Profits attributable to a permanent establishment of a controlled foreign entity in designated countries were excluded.
- Taxing foreigners on South African sourced income only.
- Dividends from designated countries would not be taxed, but local companies would not be able to claim foreign dividends as a credit in the calculation of their STC liability.

By 2003 the impact of the residence-based method of taxation was becoming apparent and certain amendments were effected. For example, it had become evident that the tax on foreign dividends was restricting inflows and repatriations were being delayed, and a participation exemption was introduced for foreign dividends if the taxpayer held an interest of more than 25% in the non-resident company declaring the foreign dividend. A similar CGT exemption was introduced for the sale of shares in foreign companies. The level of the shareholding to qualify for the exemptions has been reduced over time to 10% (since early 2012).

Residence-based tax is complemented by international agreements for the avoidance of double taxation (DTAs), and the network of agreements has grown extensively since 1994, as is discussed below.

10.2 International tax treaties

Since 1994, when there were only six DTAs in force between South Africa and other countries, an extensive network of international agreements have been entered into with other countries that are aimed at preventing double taxation, enabling the exchange of information and to provide mutual assistance in the combating of avoidance and evasion.

From these beginnings there are currently 73 DTAs; eight Tax Information Exchange Agreements, one Multilateral Convention of Mutual Assistance in Tax Matters, and 15 Customs Mutual Assistance Agreements.

Figure 21: Map indicating international agreements between South Africa and other countries

10.3 SARS' involvement in international bodies

The evolution of SARS into a globally participative tax and customs authority has not been limited to this extensive network of international tax and customs agreements, but is also evidenced in the international recognition of SARS as an efficient and effective tax authority. The practical contribution of SARS in the development of the objectives of international bodies and the prestigious positions some SARS officials have assumed on the global tax and customs stage, have furthered SARS' international image.

From 2001 to 2006 the Commissioner was appointed as the Chairperson of the World Customs Organisation, while SARS was afforded official observer status to the OECD's Committee for Fiscal Affairs in 2004 and was also elected to serve on the Bureau of the Forum on Tax Administration (FTA) after its establishment. The Commissioner served as Chairperson of the FTA from 2008 to 2009.

In 2008 SARS hosted the International Conference on Taxation, State Building and Capacity Development in Africa. One of the outcomes was the commitment to take forward the establishment of the African Tax Administration Forum (ATAF), and the Commissioner was elected as the Chairperson of the steering group tasked with establishing the Forum. ATAF is now well established and contributes actively in the development of taxation in Africa.

In 2012 South Africa was elected as the Chair of the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum), with a SARS' representative in the position of chairperson. SARS is actively involved in the work of the Global Forum, and provides assessors to assist the Global Forum carry out peer reviews of other countries. SARS has already assisted with peer reviews in Botswana, India, Cayman Islands, Panama, United Kingdom, Argentina, Mexico, Chile and Belize.

SARS has also hosted the Commonwealth Association of Tax Administrators (CATA). SARS contributes to the progression of tax development internationally through the periodic secondment of officials to certain programmes such as the OECD's base erosion and profit shifting (BEPS) action plan, and South Africa is one of the early adopters of the new standard of information sharing on an automatic basis.

CHAPTER 11
CUSTOMS AND EXCISE

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CUSTOMS AND EXCISE

The modernisation of the customs environment was implemented separately from the tax environment, and this Chapter briefly gives an overview of customs and excise in South Africa.

11.1 Introduction

During the period from 1996/07 to 2006/07 the number of import transactions had grown from 1.55 million to approximately 2 million, while export transactions grew from 0.9 million to 2.2 million.

SARS has applied the same strategy to its customs operations that it used to modernise its tax systems and processes.

11.2 A short history on the rewrite of the Customs and Excise Act

11.2.1 Background

The Customs and Excise Act, 1964 was drafted to accommodate rigid control rather than trade facilitation and for manual rather than electronic processes and trade. Although this Act was extensively amended over the years to keep pace with technological advances, increased facilitation and customs modernisation, the basic structure of the Act remained unchanged and still contains a strong undercurrent of rigidity reminiscent of the era in which it was written. As such the Act was not structurally suitable to serve as a vehicle for implementing a modern system of customs administration in accordance with current international trends and best practice.

With the advent of globalisation, a changing world environment and the importance of international trade and tourism, there is increasing pressure worldwide on countries to work towards a better balance between rigid customs control and facilitation of the international movement of travellers and goods. Whilst the need for an effective customs control system as a mechanism for revenue collection, protection of society and combating of crime is recognised, the international trend is to modernise customs systems in order to minimise, as much as possible, the disruptive effect on legitimate trade and tourism. This balance can be achieved through simple, predictable and efficient customs procedures and the optimal use of technology.

A fundamental restructuring of South Africa's customs and excise legislation was required not only to give effect to the Revised Kyoto Convention, which serves as a blueprint for customs administrations in their modernisation efforts (and for other binding international instruments), but also to establish a sound, clear, logical and flexible legislative framework.

11.2.2 A phased approach to the rewrite of the Customs and Excise Act

The rewrite of the Customs and Excise Act was announced in the 2000 Budget Review. As the dissection of this Act and its rewrite was a mammoth task, requiring several years to complete, it was decided to split the customs and the excise aspects of the task and to complete the project in two phases.

The first phase involved the drafting of two Customs Bills and the second phase involved drafting the Excise Duty Bill. The intention then was to proceed only with the two Customs Bills, and once enacted into law, to retain the 1964 Customs and Excise Act, in an amended form, in order to regulate excise duties and the other related levies. The Customs and Excise Act is therefore intended to remain in operation until the proposed Excise Duty Act comes into effect.

The two Customs Bills will therefore replace the provisions of the current Customs and Excise Act, in relation to customs only and an amended 1964 Act will, for the time being, continue to apply to excise duties.

In order to achieve this, an Amendment Bill amending the 1964 Act was introduced simultaneously with the two Customs Bills.

11.2.3 The Customs and Excise legislative framework

The new legislative framework consists of the following three separate pieces of legislation that will replace the Customs and Excise Act:

- A Customs Control Act, which establishes a customs control system for all goods imported into or exported from the Republic and prescribes the operational aspects of the system.
- A Customs Duty Act, which provides for the imposition, assessment and collection of customs duties.
- An Excise Duty Act, which provides for the imposition, assessment and collection of excise duties, fuel levies, Road Accident Fund levies, environmental levies and air passenger tax.

The drafting of the three Bills focused on providing equal attention to imports and exports, simplification and transparency and reviewing the current 1964 Customs and Excise Act against the Customs Green Paper, other relevant national legislation, case law, international benchmarking and international conventions acceded to in order to close gaps identified by the review.

Plain language drafting was adopted and the chapters followed the topics contained in the Revised Kyoto Convention. In this way the Bills were sought to be simplified and the procedures harmonised.

Certainty and transparency are goals sought to be achieved through an advance ruling system and through the authority to issue interpretation notes and guidelines.

New provisions for the tax court and Tax Ombud will facilitate fair and timeous resolution of disputes and complaints. The new legislation supports SARS' modernisation efforts and serves as a vehicle for implementing a modern system in accordance with current international best practices.

The Customs Acts also support the National Development Plan in that exports and business competiveness, domestic manufacturing and small, medium and micro enterprises (SMMEs) are supported and stimulated.

Provision is made for simplified export clearances for certain categories of goods to promote exports.

Business competiveness is enhanced by, amongst others, removing the requirement for multiple customs clearances in the case of warehousing and the submission of multiple cargo reports.

Compliant traders are placed in a more equitable position as they will receive interest from the customs authority on approved refunds not paid within 21 days.

The Customs Acts provide for an environment in which SMMEs can flourish. For example, to encourage their participation in the processing of goods, an exemption from licensing is provided if the subcontracted processing falls below certain thresholds.

The Customs Control Act improves control over the supply chain by, amongst others, requiring the reporting of cargo before loading in the export country to allow the customs authority to prevent prohibited goods from being loaded onto the export vessel and by the enhanced provisions relating to the sealing of containers, vehicles and packages.

11.2.4 The legislative process

SARS initiated discussions with South African Customs Union (SACU) members in September 2003, as it is a requirement of the SACU Agreement to have similar customs and excise legislation.

The Minister of Finance approved the release of the Customs Green Paper and the first Customs Bill for distribution among SACU Members, other government departments and a small group of international experts in December 2007. Briefing sessions were held with all relevant government stakeholders during March 2008.

A second split version of the Customs Bill (in the form of the Customs Control Bill (CCB) and Customs Duty Bill (CDB)) was circulated to SACU Members and other government departments in June 2009.

The first SACU Customs Legislation workshop to assist member states in their drafting process was held in February 2010 with subsequent workshops held in November 2011 and in December 2012.

The draft CCB and CDB were released to the general public for comment for the first time in October 2009. Workshops were then held with relevant stakeholders in order to clarify concerns raised and to enable them to achieve a better understanding of the draft Bills.

A revised CCB was released in April 2010 and a revised CDB in May 2011. The comments received were evaluated and the draft Bills were tabled in the National Economic Development and Labour Council (NEDLAC) in 2009 and finalised in November 2012.

Cabinet approved the Bills in June 2013 and the Minister of Finance introduced the Bills in Parliament in October 2013.

During the subsequent Standing Committee on Finance public hearings SARS proposed certain amendments to address concerns raised by stakeholders. The Committee, in its adoption of the report on the Bills, accepted all the proposed amendments. Both Bills were then adopted by the Select Committee on Finance in March 2014.

The CDB was assented to by the President of the Republic of South Africa and published as the Customs Duty Act, 2014 (Act No. 30 of 2014) in *Government Gazette* No. 37821 of 10 July 2014. The CCB was assented to by the President of the Republic of South Africa and published as the Customs Control Act, 2014 (Act No. 31 of 2014) in *Government Gazette* No. 37862 of 23 July 2014. The Customs and Excise Amendment

Bill was assented to by the President of the Republic of South Africa and published as the Customs and Excise Amendment Act, 2014 (Act No. 32 of 2014) in *Government Gazette* No. 37863 of 23 July 2014.

Currently the subordinate legislation to support the new Acts is being drafted and circulated for comment in batches. The new Acts will only take effect on a future date determined by the President by proclamation informed by systems, operational and stakeholder readiness.

11.3 Customs transformation programme

Although the customs transformation programme was launched in September 1998, work had already been done on improving customs efficiency.

The number of ports and places of entry or exit were rationalised from 52 to 27, which included the designation of 17 land border posts between South Africa and the BLNS countries (Botswana, Lesotho, Namibia and Swaziland) and 10 airports. The designation of these land border posts involved staffing the posts with trained staff and providing essentials such as infrastructure and living quarters, computers and equipment including satellite communication functionality for remote posts.

Certain railway stations were prescribed as ports of entry and exit to combat any shift from road to rail, and a Mobile Detection Unit was established as a joint effort between Customs and Border Police.

11.4 Customs modernisation programme

Early in 2008, driven by increasing operational pressure and a need to modernise Customs' technology and business processing infrastructure, work began on the SARS Customs modernisation programme. After considerable analysis of the end-to-end customs processes and current environment, a clear understanding of the major customs business issues from a people, process, technology and legislative point of view were gained. A high-level solution design based on leading practices, was defined to address these business challenges, and was backed by a business case and roadmap. The cornerstone of the modernisation programme was to be the replacement of the existing information technology systems with a locally developed customs software platform. The new system would replace over 30 legacy systems within SARS' customs environment, many of which were developed over time to cope with increasing growth in trade.

The Customs modernisation programme was launched in July 2010 to focus specifically on addressing fundamental changes in the Customs operational and local supply chain process to bring about 'step change' improvements in operational efficiencies and effectiveness benefitting both customs and trade. The most significant highlights included the harmonisation of customs clearance processing at ports, airports and land borders.

August 2013 saw the implementation of the bigger customs management system (CMS), developed by SARS subsidiary, Interfront. This has substantially improved efficiency, productivity and service levels within the organisation. The new declaration management system enables Customs to process travellers entering and leaving South Africa, and to centralise the clearing of all import, export and cross-border declarations through a single processing engine. The new automated management system for cargo replaces a variety of systems and paper-based manual administrative processes. By managing customs declarations and supporting documents in electronic format, the processing of cargo movements by land, sea and air is much quicker and accurate.

The CMS has already processed more than four million customs declarations, valued at R2.1 trillion, and collected revenue of around R123 billion. Nearly 99.99% of all customs declarations were submitted electronically in the 2013/14 year. Previously it took 40 million pieces of paper to process 5.5 million declarations. Now the paper used to process the same amount of declarations has been reduced to about 800 000 pieces of paper. Implementation of this CMS has also made it possible to reduce physical inspection processing time from eight hours to about two hours. The integration of the CMS with the SARS risk engine enables illicit or illegal trade to be more accurately identified and the activities of unscrupulous traders to be better analysed.

The Interfront CMS will provide the platform for future enhancements to customs operations processes.

11.5 Major elements of the Customs modernisation programme

The Customs modernisation programme is intended to not only improve the efficiency and effectiveness of Customs but also to enhance SARS' whole "value chain". This includes traders, transporters and agents.

Notable advances introduced by the Customs modernisation programme include the following:

- Centralising the processing of customs documents at four strategically-located hubs equipped with advanced high-volume scanning equipment and transaction processing systems. This improved efficiency, reduced costs and accelerated the migration from cumbersome paper documents to more efficient and secure electronic information.
- Introducing a risk-management system that provides a broad spectrum of analysis of import and export declarations as well as manifest data and offers several options for intervention by customs personnel. A total of 3 096 cases, identified by the risk-management system, were completed in the 2012/13 financial year.
- Re-engineering the imports and exports process to facilitate the electronic submission of customs declarations. This eliminated the need for the mandatory submission of paper documents to support customs declarations. Documents are now required to be submitted electronically on SARS' request.
- Introducing an electronic facility for notifying importers and traders of the release of goods brought into the country. The e-Release service has dramatically reduced turnaround times, improved efficiency, cut costs and reduced fraud.
- Implementing new procedures for declaring import information that provides detailed information about the forward movement of goods and the onward processing of associated documents. This has improved the efficiency and speed of acquitting declarations.
- Introducing an electronic declaration interface (EDI) channel for international import and export declarations including the capability to submit electronic supporting documentation.
- Introducing an automated cargo management system that accurately tracks imported and exported cargo.

- Improving the goods inspection process through an automated workflow and case-allocation system. Inspectors were equipped with handheld devices for onsite electronic data capture.
- Advanced passenger processing systems were installed at border posts to speed up the processing of travellers entering and leaving South Africa. The system also enhances border security by electronically sharing passenger information with other state agencies.
- Security at South Africa's international borders has been tightened through advanced telephony technology and the Service Manager Business Automation System at the Border Control Operational Co-ordination Committee (BCOCC) Contact Centre.

CHAPTER 12
IMPROVING SERVICE

CHAPTER 12
IMPROVING SERVICE

One of the pillars of SARS' transformation initiatives has been to improve the service provided by SARS. In addition to the improvements generated by the modernisation programme, SARS has improved the service offered to taxpayers in other areas. This Chapter highlights some of the notable improvements in this regard. As modernisation is integrated into these other areas it has been necessary to mention the related or underlying modernisation initiatives.

12.1 Introduction

Years of sustained economic growth followed the normalisation of South Africa's political and economic landscape. This saw an exponential growth in the number of transactions being processed, revenue collection and growth in the tax and trade register.

During the period from 1996/07 to 2006/07 the number of import transactions grew from 1.55 million to approximately 2 million, while export transactions grew from 0.9 million to 2.2 million. During the period from 1996/07 to 2006/07 revenue collection grew from R147.3 billion to R495.5 billion. The fast-growing number of new registrants increased the demand to deliver efficient, professional and timely service to the expanding tax base.

SARS recognised that meeting this demand was one of the pillars of an effective revenue authority, and the ease of doing business was adopted early on as one of SARS' key objectives.

The tables below demonstrate the growth in the number of individuals and companies registered for tax from 1994 to 2014.

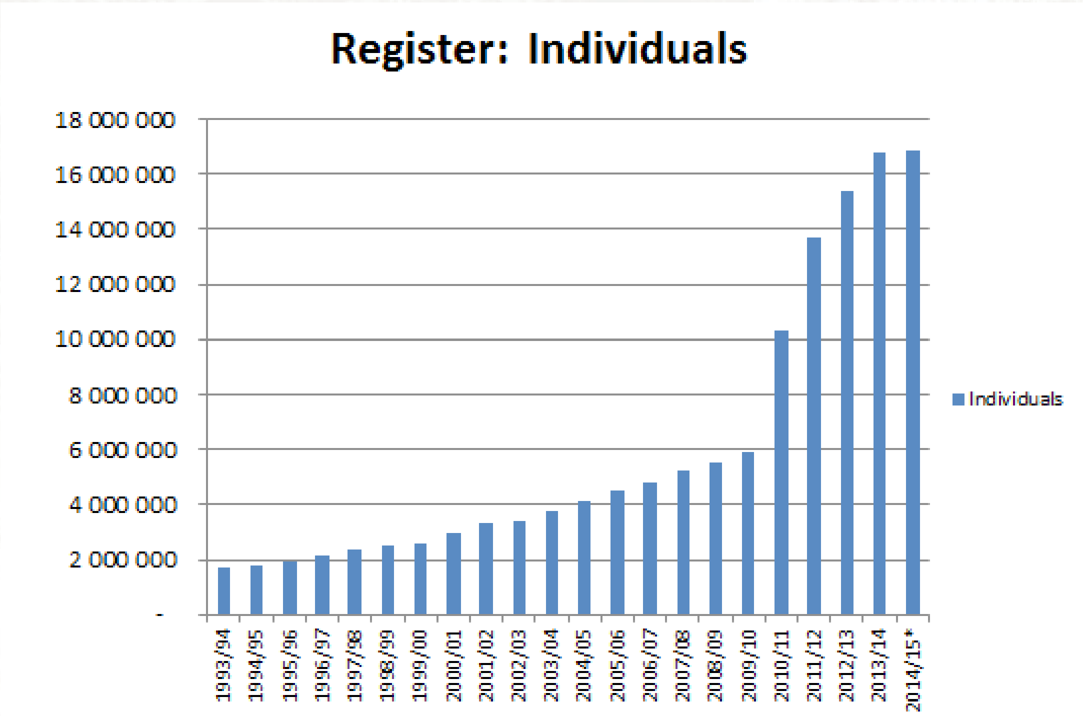

Table 2: Growth in number of individuals registered (1993 – 2014)

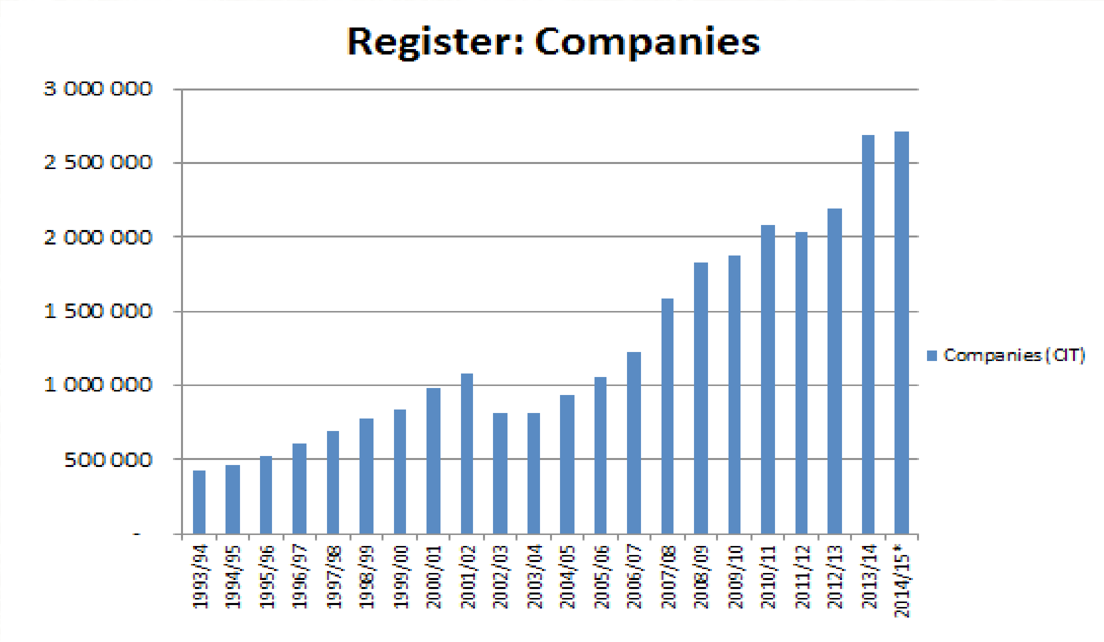

Table 3: Growth in number of companies registered (1993 – 2014)

Enhancements made to the ease of filing have contributed to the growing number of PIT returns filed on time, as illustrated by the following table.

Financial Year	Returns Required	Returns on Time	Returns on Time (%)
2008/09	4 186 834	2 418 286	57.8%
2009/10	3 961 391	3 116 024	78.7%
2010/11	4 084 151	3 296 024	80.7%
2011/12	4 232 027	3 519 157	83.2%
2012/13	4 896 969	4 213 996	86.1%
2013/14	**4 894 081**	**4 479 348**	**91.5%**

Table 4: The number of PIT returns filed on time between 2009 and 2014

12.2 Branch offices and contact centres – 2007-2013

Together with improvements to the PIT and PAYE systems and processes, SARS also revamped the operations of its branch offices and contact centres.

The success of the Operations Contact Centre, which services clients using a wide variety of different tax types, prompted SARS to create separate contact centres for SARS' Large Business Centre (LBC) and the BCOCC units. By differentiating the services provided by these separate contact centres SARS is able to resolve queries faster.

The SARS Service Manager Business Automation System, as well as the Branch Queue Management System, which is discussed in Chapter 6, underpin and support the efficiency of service provided to taxpayers.

12.3 Branch office positioning and co-locality

During 2007, as part of a strategy to improve accessibility to all taxpayers, SARS began reviewing its 'footprint' to ensure a wider and more equitable spread of SARS branches in all regions. In this process SARS reviewed the locality of offices against the population or tax base, the economic activity in the area, the distances between SARS offices and the cost to the taxpayer of visiting a SARS office. In some areas offices were closely clustered, while there was a lack of presence in other populated areas. For instance in the East Rand there were five offices in a 20 kilometre radius – the Benoni office was seven kilometres from the Brakpan office and the Springs office was nine kilometres from the Brakpan office.

SARS' approach was to integrate separate offices into a single branch when there was an inequitable concentration of offices. This exercise entailed extensive engagement externally with stakeholders including tax practitioners, local businesses and local authorities as well as internal engagement with SARS staff that would have to relocate.

By 2013 SARS had positioned 50 branch offices strategically located across the country, from the 86 branch offices in 1998. This equitable distribution of branch offices is supplemented by SARS offices that are co-located either within government institutions or in Thusong Service Centres. During the 2012/13 financial year SARS was co-located at 79 different locales and SARS officials provided services from these centres 1 632 times.

The map below provides an overview of all SARS offices throughout South Africa.

Figure 22: Overview of SARS offices throughout South Africa

12.4 Mobile tax units (MTUs)

MTUs with satellite connectivity are deployed to reach taxpayers in more remote areas and are capable of providing a broad range of services to those taxpayers. The first of the current six MTUs were deployed in August 2011 in KwaZulu-Natal, Eastern Cape, Northern Cape, Free State, Limpopo and Mpumalanga and there are currently nine MTUs operating; one in each province. In the 2012/13 financial year, the MTUs assisted with the filing of 4 560 returns for taxpayers.

12.5 Points of service

During filing season the need for service increases dramatically, and points of service are set up to assist taxpayers with general enquiries and filing at advertised times at public events and malls.

The Points of Service Programme was well-received and is now held regularly throughout the financial year and not only during filing season.

During the 2012/13 financial year a total of 6 902 points of service were set up across the country.

12.6 Branch Operations Engagement units

A dedicated Branch Operations Engagement unit now functions within Branch Operations and is responsible for enhancing outreach, education, service and promoting compliance by building collaborative partnerships with relevant sectors.

This dedicated unit conducts workshops and seminars to explain and assist with the understanding of tax "products" introduced and administered by SARS. The unit also provides technical assistance to employers with employees' tax reconciliations, and provides on-site assistance to those employees who have enquiries or need help with the filing of returns.

During the 2012/13 financial year over 9 000 on-site workplace visits were held.

12.7 Mobile website and applications

SARS officially launched its innovative eFiling mobile website and application systems in 2012. The SARS MobiApp is available on Android, Apple and Blackberry smart devices.

SARS is the first revenue authority in Africa to introduce this innovative method of submitting income tax returns and this milestone keeps SARS and South African taxpayers at the forefront of international tax technology.

12.8 Improved turn-around times

A significant benefit to the uptake of electronic return submission is that it enables SARS to improve the time it takes SARS to process the return (which is almost instantaneous), pay out a refund or issue an assessment.

In 2012, a significantly faster SARS eFiling application was introduced alongside the eFiling Mobile Application system. More recently live assistance was introduced through the SARS Help-you-eFile (HYEF) system.

The table below illustrates the improvement in turnaround times to pay refunds.

Financial Year	2007	2008	2009	2010	2011	2012	2013	2014
Current year	43.79	31.28	8.26	1.69	0.82	0.36	0.23	0.16
Other years	74.72	77.54	81.23	42.35	38.86	12.16	10.05	9.44
Total	50.18	41.34	41.34	12.84	9.37	3.53	3.06	2.72

Table 5: Turn-around times measured in days for the finalisation of assessments

CHAPTER 13
IMPROVING COMPLIANCE

CHAPTER 13
IMPROVING COMPLIANCE

High levels of voluntary compliance reduce the administrative burden on the revenue authority, improve recovery and free-up scarce resources that may be focused on other important areas such as enforcement activities as well as service-oriented engagements.

How to improve levels of voluntary compliance is a topic that is debated and discussed by every revenue authority and it is agreed that to improve compliance levels requires a multi-faceted approach.

In 1915, when the Commissioner of Taxes reported to the Houses of Parliament after the introduction of the 1914 Income Tax Act, the issue of compliance was dealt with. The Commissioner reported to the Houses:

> *There is bound to be leakage, but this will be gradually reduced as the Department's organisation is extended, and information is accumulated.*
>
> *It is of course futile to expect that every one liable to tax will be caught in the collector's net. All that can be hoped for is that the proportion escaping will be reduced from year to year.*

This Chapter briefly discusses SARS' efforts to increase levels of voluntary compliance.

13.1 Elements of compliance

Tax authorities continuously seek to improve the level of voluntary compliance among taxpayers. High levels of compliance with legislation allow a tax authority to concentrate resources in order to improve areas such as education, raising service levels and simplifying the tax system.

A low level of compliance distorts trading patterns as those who do not comply with their tax obligations gain an unfair competitive advantage over those taxpayers who do comply. Low compliance rates can also affect the morale of taxpayers generally and can also lead to a broader unwillingness to comply.

Improving voluntary compliance relies upon a strong legislative foundation that provides for appropriate enforcement action to be taken. Internationally, tax legislation often contains extensive enforcement powers. The legislation administered by the Commissioner contains such authority, and includes expedited collection powers, the ability to restrain assets pending determination of liability and far-reaching information-gathering authority.

How legislation is enforced is equally, if not more, important than the legislative environment. How enforcement action is exercised gives legitimacy to the enforcement environment, and in this respect, SARS has adopted an approach that is widely known as responsive enforcement or regulation. "Responsive regulation"[22] suggests that compliance levels are best improved through a balanced and multi-disciplinary approach.

Responsible enforcement therefore requires enforcement powers to be exercised responsibly and reasonably. South Africa's legislation contributes to responsible enforcement and balances enforcement with reasonableness. In most instances where legislation allows SARS to take enforcement action, the legislation contains provisions that measure the exercise of the discretion. This check on the exercise of the more impactful enforcement action is achieved in a number of ways. It is common that the empowering legislation requires that the decision must be taken by a senior SARS official who is designated by the Commissioner. In practice the designation as a senior SARS official is made in line with an employee's experience, qualifications and experience.

It is also common for legislation to stipulate what factors should be taken into account before particular enforcement action is taken, or to prescribe a procedure that must be followed. This generally gives substance to the constitutional demand that administrative action must follow a fair process and be reasonable. In some instances, the prior authority of a judicial official is also required.

It is clearly preferable to encourage voluntary compliance. One of the first steps taken after 1994 to improve voluntary compliance was the introduction of the two amnesties in 1995 and 1996. These amnesties provided those who had opposed taxation before with the opportunity to regularise their affairs in the new democratic dispensation. Apart from bringing people into the tax net, the amnesty legitimised SARS' enforcement actions taken after the deadline for applications for amnesty had passed.

These amnesties also saw the initiation of SARS "walkabouts" – where SARS' officials engaged directly with taxpayers on their turf. Apart from demonstrating SARS' commitment to service the process also gave staff a better understanding of taxpayers' needs and knowledge of tax issues, which contributed to improving taxpayer engagement and education.

Over the years SARS has developed a compliance model that expresses the policy that assistance will be given to those who try to comply, but that enforcement action will be used when there is a refusal to comply.

In 2012 SARS' compliance programme was announced. This programme identified certain sectors where compliance levels were considered not to be at appropriate levels. The programme was launched under the banner "CALL US BEFORE WE CALL YOU!" and served as a caution to taxpayers, in these segments, to remedy their affairs. This announcement dovetailed with the permanent voluntary disclosure programme mechanism contained in the TA Act which now provides taxpayers with a clear procedure that can be used to regularise past non-compliance.

SARS' internal environment is also geared towards compliance capability. SARS transformation process included physically bringing together customs and tax, as well debt management, audit and investigations. This co-location improved communications between SARS' staff involved in enforcement activity. Coupled with this, is the underlying risk identification capacity built into the modernisation programme. This risk identification capability allows SARS to identify risks early and to respond in an appropriate manner through, for instance, diverting declarations for closer scrutiny.

SARS has also put a great deal of effort into educating taxpayers and tax practitioners, and moving tax offices closer and making them more accessible to the taxpaying population. Tax workshops and bilateral forums are held periodically to inform taxpayers, employers and practitioners of new initiatives, processes and developments.

In order to improve the certainty of taxation, various guides and brochure are made available and are continually updated. Rulings and interpretation notes complement the need to provide greater certainty.

SARS' approach to compliance involves a multi-faceted approach. Hard enforcement action is reserved for those who refuse to comply, and this action is taken within policy guidelines and by suitably qualified, experienced and senior officials. The willingness to comply is supported by educational initiatives and clarity is provided through current guides, interpretation notes and further certainty is available through the advance tax ruling procedure.

13.2 Office positioning

The move to accommodate the needs of different taxpayers began as early as 1993. Government provided an additional R40 million to Inland Revenue and Customs and Excise and the immediate spin-off was the establishment of a specialised company taxation office in northern Johannesburg.

Since these early beginnings large business centres located in larger centres now provide for the requirements of large businesses. Similarly PBOs have unique requirements which are provided by a specialist unit familiar with their demands and needs.

At times, SARS' mandate intersects with the mandate of other government agencies and when appropriate SARS engages and interacts with these agencies in the performance of its duties. As an example the BCOCC is an affiliated structure of the Justice, Crime Prevention and Security Cluster and is mandated to manage the South African border environment. Until recently, SARS was the lead agency of the BCOCC and was required to facilitate inter-agency coordination of functions in a manner that ensured agencies did not exceed or compromise their mandates.

SARS' structure separates functional areas into common areas so that there is minimal duplication of functions. Enforcement activities are carried out by a specialised unit that consists of investigators, forensic auditors and lawyers. Typically the unit carries out intensive audit work using advanced systems to interrogate and analyse source data, specialised recovery of outstanding taxes and criminal investigations. Underpinning the work of the specialised unit is a sophisticated case selection system that analyses risk to identify suitable cases. This process removes any potential for personal bias to inform hard enforcement activities.

Verification of accuracy in returns comprises a generous portion of SARS' work, and is an area in which trained officials conduct first-level checks of returns filed. From the verification process cases can be escalated for further audit and even criminal investigation.

Debt Management is a stand-alone division with a presence throughout the country, tasked with the responsibility to collect overdue taxes. Their responsibility is to use the expedited recovery legislative provisions within the parameters of detailed standard operating processes and policies.

A dedicated Alternative Dispute Resolution unit within the Legal and Policy Division is responsible for the resolution of disputes through the informal alternative dispute resolution process or through the more formal tax boards, tax courts and for appeals to higher courts.

13.3 Tax Clearance Certificates (TCCs)

The TCC process is based on a sound principle of public administration that a person's tax affairs should be in order before doing business with government. The process supports the fair and equitable procurement procedure required by section 217(1) of the Constitution.

As mentioned in 6.9 over 785 000 TCCs were issued in the 2011/12 financial year.

The new tax compliance status system, which is being implemented, will further contribute to a whole of government approach to compliant behaviour.

CHAPTER 14

BENEFITS OF SARS EVOLUTION

CHAPTER 14
BENEFITS OF SARS EVOLUTION

This Chapter sets out the benefits of SARS as a semi-autonomous revenue authority and which have resulted from the transformational initiatives undertaken.

14.1 Internal efficiency

The cost of tax revenue collection is an important indicator of the efficiency of revenue authorities and is used for comparative purposes when benchmarking countries.

In the *OECD's* "Tax Administration 2013" publication the total revenue collections (that is, administered revenue) is used to calculate the cost of collection ratios. Most countries' ratio ranges around the international benchmark of 1%, with the USA at a low of around 0.6% and Germany at a high of 1.5% while Brazil and Russia's ratio is approximately 1%.

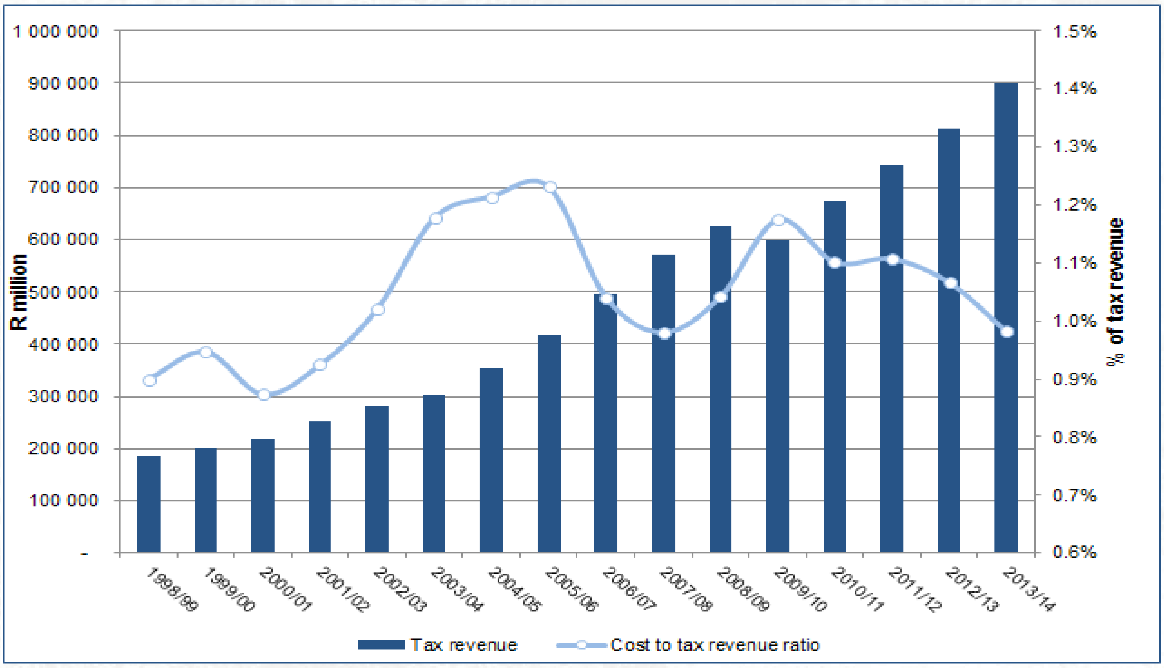

Figure 23: Cost of revenue collections

The ratio is calculated by dividing the cost of internal operations by the total tax revenue. South Africa is in line with the international benchmark of 1% for this ratio. The 2012/13 ratio of 1.07% drops to 1.02% if administered revenue is used instead of tax revenue to calculate South Africa's revenue collection ratio.

14.2 Revenue receipts

Tax revenue collected increased from R113.8 billion in 1994 to R899.8 billion for the 2013/14 fiscal year. In 2009/10 the tax-to-gross domestic product (GDP) ratio declined to 24.4% because of the global financial crisis. According to the OECD most countries reported low levels of tax-to-GDP ratios in 2008 and 2009 because of the global economic crisis.

The collection of R899.8 billion in 2013/14 increases the tax-to-GDP ratio from 25.4% in 2012/13 to 26.1%, indicating a continuing trend toward higher revenues, as shown in the table below.

Fiscal year	Tax Revenue	Tax Revenue % growth y/y	Tax Revenue as % of GDP	GDP
1993/94	97 488		22.0%	442 135
1994/95	113 775	16.7%	22.9%	497 189
1995/96	127 278	11.9%	22.6%	564 159
1996/97	147 332	15.8%	23.2%	635 187
1997/98	165 327	12.2%	23.6%	699 825
1998/99	184 786	11.8%	24.4%	757 087
1999/00	201 266	8.9%	24.0%	837 241
2000/01	220 119	9.4%	23.1%	951 736
2001/02	252 295	14.6%	24.1%	1 048 506
2002/03	281 939	11.7%	23.4%	1 203 145
2003/04	302 443	7.3%	23.2%	1 303 907
2004/05	354 979	17.4%	24.5%	1 449 020
2005/06	417 196	17.5%	25.9%	1 613 812
2006/07	495 549	18.8%	27.0%	1 832 762
2007/08	572 815	15.6%	27.6%	2 075 413
2008/09	625 100	9.1%	27.2%	2 296 571
2009/10	598 705	-4.2%	24.4%	2 456 629
2010/11	674 183	12.6%	24.5%	2 749 532
2011/12	742 650	10.2%	24.9%	2 981 828
2012/13	813 826	9.6%	25.4%	3 198 579
2013/14*	899 849	10.6%	26.1%	3 448 980

Please note that the outcome for 2013/14 is still preliminary

Table 6: Revenue collections and tax as a percentage of GDP

The OECD's annual "Revenue Statistics 2013" reveals that the average ratio in OECD countries was 34.6% in 2012, compared to 34.1% in 2011 and 33.8% in 2010. Denmark, with a ratio of 48% in 2012 has the highest ratio amongst OECD countries, and is followed by Belgium and France at 43.5%. The lowest tax-to-GDP ratios, among the OECD countries, are Mexico at 19.6%, Chile at 20.8% and the United States at 24.3%.

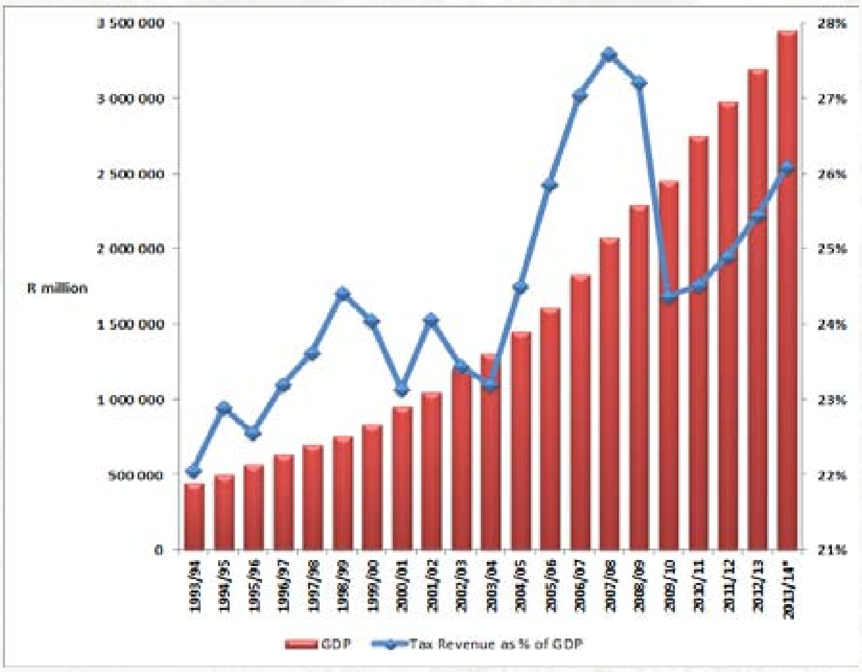

Figure 24: Tax-to-GDP ratio from 1994-2014

14.3 Tax relief

While tax revenue is anticipated to increase by 10.4% to R993.6 billion in 2015, the total PIT relief over the period from 1994 to 2014 amounts to R139 billion. The total company income tax relief over the same period amounts to R12.7 billion.

Tax relief follows as a consequence of, amongst others, lowering effective marginal rates, additional revenue from limiting allowable deductions and granting tax incentives and is a factor relevant when considering the vertical equity, or the fair distribution of the tax burden.

Over this period the CIT rate reduced from 40% to 28% while the top marginal rate for PIT reduced from 45% to 40%.

Summary effects of tax proposals – 1994/95 to 2013/14									
Year	Direct				Indirect				Total relief
	PIT	CIT	Other	Total	Excise	Fuel levy	Other	Total	
	R million	R million	R million	R million	R million	R million	R million	R million	R million
1994/95	1 460	1	510	**1 971**	350	-	-800	**-450**	**1 521**
1995/96	-875	50	-235	**-1 060**	410	255	-455	**210**	**-850**
1996/97	-1 450	620	2 675	**1 845**	500	1 060	465	**2 025**	**3 870**
1997/98	-1 681	800	350	**-531**	668	800	759	**2 227**	**1 696**
1998/99	-1 700	400	1 318	**18**	1 110	1 660	550	**3 320**	**3 338**
1999/00	-3 850	-1 510	-60	**-5 420**	753	572	521	**1 847**	**-3 574**
2000/01	-9 078	668	-	**-8 410**	765	670	1 638	**3 073**	**-5 337**
2001/02	-8 878	860	-51	**-8 069**	569	110	1 335	**2 014**	**-6 055**
2002/03	-15 018	-346	-330	**-15 694**	663	-4	-130	**529**	**-15 165**
2003/04	-13 426	-210	-2 285	**-15 921**	92	642	130	**864**	**-15 057**
2004/05	-4 062	-	-100	**-4 162**	1 223	909	-270	**1 862**	**-2 300**
2005/06	-7 110	-3 385	-542	**-11 037**	1 299	950	-593	**1 656**	**-9 381**
2006/07	-12 125	-400	-6 940	**-19 465**	1 348	-	-1 010	**338**	**-19 127**
2007/08	-8 565	-785	-5 005	**-14 355**	1 395	950	-390	**1 955**	**-12 400**
2008/09	-7 700	-6 900	-	**-14 600**	1 350	1 250	* 1 500	**4 100**	**-10 500**
2009/10	-13 550	-1 000	-	**-14 550**	2 100	4 890	* 2 985	**9 975**	**-4 575**
2010/11	-5 400	-1 350	-	**-6 750**	2 250	3 600	450	**6 300**	**-450**
2011/12	-8 850	500	-750	**-9 100**	1 935	1 900	1 150	**4 985**	**-4 115**
2012/13	-9 800	1 100	-1 950	**-10 650**	1 840	4 517	1 985	**8 342**	**-2 308**
2013/14	-7 382	-860	-	**-8 242**	2 065	3 270	495	**5 830**	**-2 412**
2014/15	**-9 250**	**-1 000**	**-**	**-10 250**	**2 110**	**2 565**	**-**	**4 675**	**-5 575**
*Note: * The electricity levy was not introduced in 2008/09 but postponed to 2009/10.*									

Table 7: Table of tax relief measures

14.4 Modernisation

As mentioned in Chapter 6 the modernisation programme has improved taxpayers access to current account information through the eFiling service, and the chance of payment misallocations have been reduced through including unique payment reference numbers on VAT and PAYE forms.

The programme has also enabled SARS to redeploy many of its employees into areas where they perform higher-value work such as serving taxpayers and participating in initiatives to broaden the tax base, improve compliance and enhance revenue collection. The redeployment (or mobilisation) of staff also provides these employees with an opportunity to diversify their skills and build experience.

Since SARS first launched a comprehensive website on 1 October 1997, tax registrations and electronic submission of returns have increased. Individuals registered grew from 5.9 million in the 2009/10 financial year to 15.4 million in 2012/13, and the number of tax return transactions processed by SARS increased from approximately 42 million to over 60 million.

During the 2012 tax season 5.66 million income tax returns were submitted while 1.37 million outstanding returns for previous years were filed. By 2012 almost 99.86% of all returns were submitted electronically, and only 5 529 manual returns were submitted compared to 32 071 in 2011 and 123 674 in 2010.

The graphs below reflect the number of returns filed electronically and manually for individuals and companies.

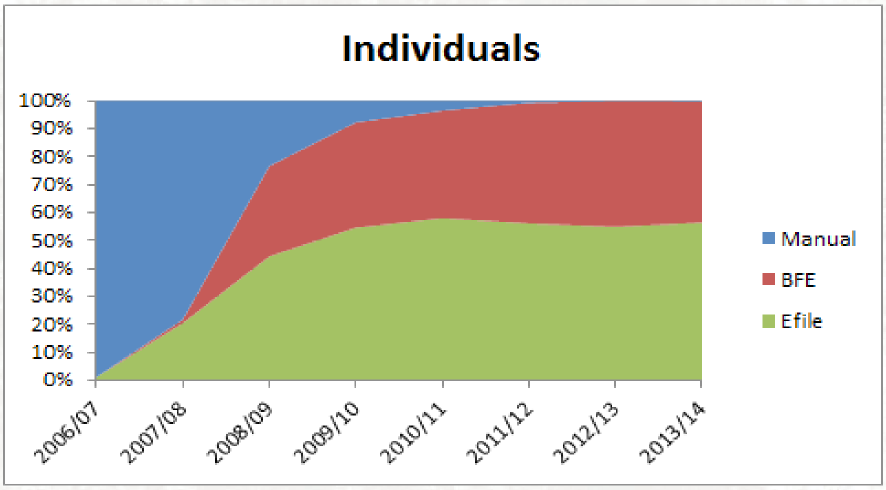

Figure 25: Comparison between electronic and manual returns filed by individuals

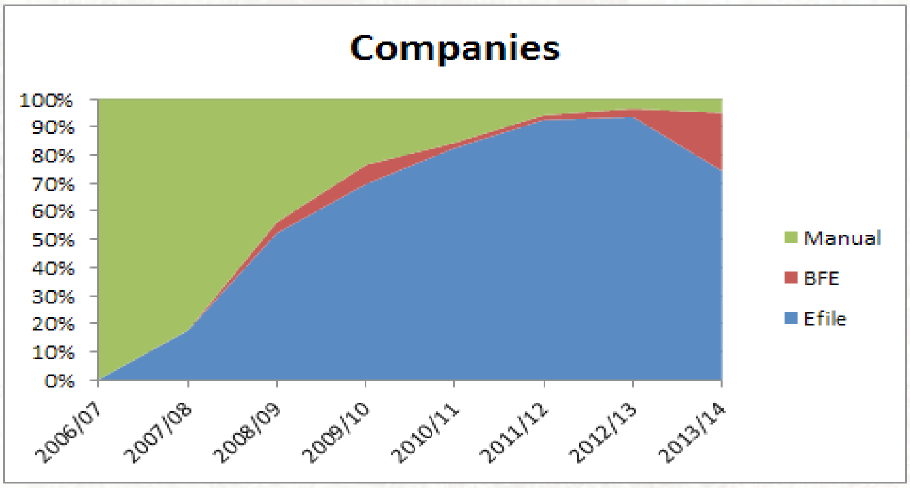

Figure 26: Comparison between electronic and manual returns filed by companies

CHAPTER 15
2014 AND BEYOND

CHAPTER 15
2014 AND BEYOND

The development of SARS over the last 20 years has created a revenue authority that is based on solid principles of good governance, efficiency and responsiveness. An effective systems platform has been developed and a lot has been invested in staff. Despite this, there is much to prepare for, and this Chapter surveys some of the major issues to address in the coming years.

15.1 Davis Tax Committee

When the Minister of Finance tabled the 2013/14 Budget he announced that a tax review would be initiated *"to assess our tax policy framework and its role in supporting the objectives of inclusive growth, employment, development and fiscal sustainability"*.

Since then the Davis Tax Committee was appointed and the terms of reference were defined to include:

- An examination of the overall tax base and tax burden including the sustainability of corporate tax, personal tax and VAT.
- An examination of the impact of the tax system on small and medium-sized enterprises.
- A detailed examination of the corporate tax system, with emphasis on efficiencies in the system, tax avoidance, incentives and effective tax rates in various sectors.
- Taxation in the mining sector.
- Taxation within the financial sector.
- The efficiency of and equity within the VAT system.
- A review of the legislative process, with a view to simplifying the process.

As the work of the Davis Tax Committee unfolds the findings and recommendations will possibly influence further tax policy reform. This is evidenced by the publication of the Committee's SME Interim Report on 14 July 2014 and the First Interim Report on Base Erosion and Profit Shifting (BEPS) on 23 December 2014 for public comment.

15.2 Base Erosion and Profit Shifting (BEPS)

The United Nations' Millennium Development Goal to halve extreme poverty by 2015, together with the evolving research into questionable tax practices and the impact of these practices on developing countries, has seen an unprecedented convergence of global discourse by the world's countries, lobby groups and development agencies on the urgent need for tax reform. In a joint report by the African Development Bank and Global Financial Integrity it is estimated that, between 1980 and 2009, African countries lost between US$597 billion and US$1.4 trillion in net resource transfers away from the continent. The report identifies that the outflow of money includes illicit outflows that includes tax evasion, the manipulation of tax laws, the use of low or no tax jurisdictions and transfer pricing.

In April 2013 the G20 Finance Ministers and Central Bank Governors addressed profit-shifting and called for "a comprehensive proposal and a substantial discussion" at the July 2013 meeting and by July 2013 the OECD had completed the action plan and presented it to the G20.

On 20 July 2013 the Secretary-General of the OECD announced that the BEPS action plan "*sets forth 15 ambitious actions that will result in the most fundamental change to the international tax rules since the 1920s!*".

South Africa is neither spared nor protected from the positive or adverse impact that multi-national enterprises can have on the economy and on tax collection.

Against this background, and the work of the Davis Tax Committee, it is anticipated that there will in the future be a focus on measures to counter the adverse practices of some corporations trading in South Africa.

15.3 Single registration

SARS started overhauling its tax registration process in 2013. The modernisation programme introduces a single registration process that will accommodate all tax types.

Instead of having to register separately for each tax or customs product, taxpayers and traders only have to register with SARS once. All the tax products they use will be accommodated on a single integrated profile. Further tax products, which may be required later, can be added to the profile. The new consolidated profile will provide SARS with a comprehensive view of the tax and customs products used by a particular taxpayer or trader. It will also provide a platform for additional functions such as integrated account management, tax compliance status and a consolidated business register. Once implemented the single registration system will enable taxpayers and traders to view their tax product profile online, using the new tax compliance status system, and if necessary remedy any non-compliance.

SARS is working closely with other government departments and agencies, such as the Department of Home Affairs and the CIPC, to establish common electronic interfaces. These interfaces enable SARS to validate registration information lodged with these organisations. The single registration system will also advance government's plans to create a consolidated business registration facility, the Integrated Business Register, which will help reduce the administrative burden on small businesses and cut the cost of conducting business in South Africa.

15.4 Beyond the modernisation programme

The main thrust of the modernisation programme is planned to be completed during 2015. However, SARS will ensure that the technology infrastructure implemented as part of the programme, and the many automated systems and processes it supports, do not become obsolete. In order to maximise returns on its extensive investment in technology and to maintain high levels of performance, SARS will continue to upgrade and refine its operations. Advances in technology that could help SARS better meet its mandate will be investigated and, where suitable, integrated into the organisation's operations.

Furthermore, errant taxpayers and traders are becoming increasingly sophisticated in their efforts to evade tax and customs legislation. SARS will keep abreast of the latest international trends regarding systems and system-analysis that counter such conduct.

15.5 Information exchange

Information and access to information are crucially important to revenue administration, and it is expected that there will be a greater focus on international information exchange in the years from 2014.

The intergovernmental agreement between the USA and South Africa for automatic exchange of information between the two countries was signed on 9 June 2014. This agreement still needs to be ratified and published in the *Government Gazette*. Once the agreement comes into force the obligation to exchange information will begin.

As mentioned, SARS is a one of the early adopters of the new standard of information sharing on an automatic basis, and is committed to providing information on an automatic basis from 2017.

The Multilateral Convention on Mutual Administrative Assistance on Tax Matters, which entered into force on 1 March 2014, will facilitate exchange of information between countries.

CONCLUSION

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This document has sought to trace the history of the revenue authority in South Africa over the past 20 years with the focus on three aspects of the revenue and customs service. First is the establishment of the South African Revenue Service as an organ of state responsible for regulating and enforcing tax and customs. In the years before 1994 tax and customs were administered by departments, or sub-departments that reported to Treasury. Reporting to Treasury did not provide an optimal environment for the revenue authority to thrive and develop into the dynamic and responsive organ of state it is today. Support for this separate and semi-autonomous revenue authority emerged early on in the new political dispensation and the South African Revenue Service (SARS) was formally established in 1997. Apart from the autonomy to determine its own staffing and operational needs, the creation of SARS established an entity with a separate identity that could last in perpetuity. Much work was done to establish the vision and the values that underpin the SARS of today. Today SARS with its service-centred focus on taxpayers stands for professionalism, customer-centricity and honesty, as well as efficiency, productivity and effectiveness.

The second focus of this document details the progress made by the modernisation of processes and the impact on both the internal and external environment. The electronic platform forms the basis on which SARS interacts with taxpayers, traders and practitioners and also supports internal efficiencies. The electronic environment has enabled SARS to obtain information that was not considered possible before the extensive investment in technology. Although information is considered to be the life-blood of a tax administration, the real benefit is how this information is used. For taxpayers, the ease of filing has been improved through the pre-population of returns and in the speed with which refunds are reviewed and actually paid. The risk-analysis capability of the information systems has contributed substantially towards SARS meeting its objectives. Thus SARS' investment in technology has improved the efficiency and effectiveness of the administration as well as having contributed to the widest possible enforcement of the legislation administered by SARS.

The third focus of this document details how tax policy has evolved over the years to reflect government's developmental objectives, support for the evolution of the business environment and response to becoming a player in global developments. Policy development has always been purposeful and relevant. For instance, the first amnesty was intended to bring into the tax net those who had elected not to contribute in prior years. The introduction of residence-based taxation and the taxation of capital gains clearly signalled SARS' entry into the global economy and the need to retain a competitive tax regime. Other instances might not have had such a clear policy "signature". For instance, the introduction of fixed-amount penalties is intended to improve compliance levels. However, while this is so, there was also a need not to criminalise administrative transgressions, and the fixed-amount penalty system was intended to achieve both objectives.

Although these three themes have been dealt with in separate Chapters, they are related and mutually dependant. Once policy is determined and the statutory instrument has been developed, the implementation and administration of the policy depends on the effectiveness of the revenue authority. The effectiveness of the revenue authority to implement policy, in turn, depends on how sensitive and responsive the authority is to change and how well it is able to mobilise resources to accommodate these changes. The latter is influenced by the extent to which the authority is able to determine its own needs and resources.

Said another way, the success of the extensive modernisation programme is largely attributable to SARS' ability of self-determination that was achieved through semi-autonomy and cemented by legislation that reflected the overarching purpose of the day.

This interconnectedness can be identified in almost every aspect of the tax landscape. There is a growing recognition that SARS is part of government, and that it has a role to play in the greater-government approach to tackle challenges facing the country. The challenge is to participate in a whole-of-government approach while also protecting the confidentiality of taxpayer and trader information. The now entrenched tax compliance system is an example of the careful balance that has been struck in meeting these two important objectives. The certification of a participant's tax compliance status functions to improve government's procurement of goods and services but also protects a person's tax affairs. The legitimate sharing of non-financial information with departments is another example of how SARS will participate in a whole-of-government approach.

Finally, tax is an ever-changing landscape. Businesses evolve, trade practices evolve and the demands of a country evolve over time. The final Chapter of this document has identified some of the issues on the horizon that will influence the direction of tax in South Africa. Unidentified challenges may demand that resources be focused elsewhere. If, or rather when, this happens, the interconnectedness of policy development, legislative drafting and administrative implementation will be tested.

1961-1993 - Republic of South Africa's Coat of Arms

Also used for Department of Finance – Inland Revenue

Department of Finance – Customs & Excise Coat of Arms

1994 – Republic of South Africa

1997 till present - South African Revenue Service

South African Revenue Service

ENDNOTES

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