Briefing Note: Update on SARS Compliance Programme

The SARS Compliance Programme for 2012-2017 was launched by the Minister of Finance on 1 April 2012. A year later, SARS is in a position to give initial feedback on progress made across the five priority areas of the tax base that were identified as key focal points for the next five years.

The prevailing economic environment is putting considerable pressure on the compliance behaviour of a wide range of taxpayers. SARS will continue to pursue non-compliant behaviour to ensure that every taxpayer pays the correct amount of tax.

SARS has developed a robust and detailed view of taxpayer behaviour across sectors.

For each focus area of the compliance programme, SARS strives to enhance its understanding of international and local trends as well as good practice cases from other tax jurisdictions. For the next 4 years, the SARS Compliance Programme will focus on 7 key areas identified as posing a specific risk to the work of SARS, to the fiscus, and ultimately to the economic future of South Africa.

1. **Large Businesses and Transfer Pricing**

   This segment of the tax base is attracting considerable focus from governments across the world, especially where multinationals use the protection of double taxation agreements to minimise their tax obligations. It will remain a SARS priority for the medium to long term given the risk it poses in terms of the erosion of South Africa's tax base.

   During the 2012/13 financial year, 16 cases with audit results of just over R3.2 billion have been finalised. The settlement of these cases resulted in R652 million cash collections during 2012/13. Two more transfer pricing-related cases with potential audit results in excess of R6 billion are being finalised.

During 2013/14 the focus will be on

- Transfer pricing concerns within the Mining, Automotive, Pharmaceutical and Financial sectors. Specific areas of focus will include management fees, interest payments, service fees, royalty payments, and the selling or transfer of intangible assets.
- 30 transfer-pricing cases with potential audit results in excess of R8 billion

2. The Construction industry

Last year the construction industry has been highlighted as the least tax-compliant sector in the formal economy. Despite efforts to improve compliance, industry participants collectively owe SARS over R4 billion in outstanding taxes. This comprises of VAT at R 2.6 billion (56.45%), CIT (22.71%) and PAYE (20.84%). There are 129 759 outstanding returns, of which over half are VAT-related.

The analysis and profiling of companies and individuals that received government tenders resulted in 172 profiled cases, with 88 companies being selected for a full audits. To date, audits of 216 cases involving small and medium businesses yielded over R479 million.

SARS will have a specific focus on those companies that receive government tenders, ensuring that these recipients of taxpayer funds are themselves tax-compliant.

An important development this year was improved cooperation between SARS and both the Construction Industry Development Board and the National Home Builders Registration Council. A strong commitment by these bodies to ensuring better tax compliance by their members will support the work SARS is doing in this regard.

Important focus areas for 2013/14 include:

- Ensuring continued compliance for the duration of a government tender – rather than only requiring a Tax Clearance Certificate (TCC) at the beginning of the process.
- Introducing an early contact strategy with non-compliant taxpayers to ensure that unexpected tax debts do not threaten their ongoing viability.
- 1,310 cases with a potential additional assessment of R15 billion been identified and selected for audit as a result of risks related to Income Tax and VAT.

3. Wealthy South Africans and their associated trusts

High Net-Worth Individuals (HNWIs) are under the spotlight around the world. According to an OECD study they pose specific challenges to tax administrations as a result of the complexity of their tax affairs; their relative contribution to tax revenues; the opportunities that their wealth provides for aggressive tax planning and the impact that non-compliance in the HNWI segment can have on community confidence in the tax system.

SARS defines HNWIs as individuals whose gross income exceeds or is equal to R7 million and/or gross wealth exceeds or is equal to R75 million. There are currently 2 300 such individuals on SARS' register.

HNWIs pose a range of challenges, including, but not limited to:

- Using non-residency status to reduce taxable income (especially investment income)
- The establishment of Public Benefit Organisations (PBOs) to avoid tax liability on the transfer or donation of assets
- The use of trusts to shield assets from tax liability
- Profits being expropriated to tax havens without tax being paid in South Africa
- Salary structuring where a director may choose to receive dividends instead of a salary or bonus – thus avoiding higher tax rates.

Over the last 12 months, 280 HNWIs have undergone compliance reviews and analysis, resulting in 109 of them being identified as high risk and earmarked for a full audit. A total of 62 full audits have been conducted, yielding a total of R184 million, and 14 individuals in the HNWI category have been identified as potential serious offenders as a result of the magnitude of their outstanding returns. Also, 4 criminal cases involving HNWIs are currently under investigation.

4. Illicit cigarettes

The ongoing trade in illicit cigarettes in South Africa poses serious health risks to consumers and also results in a considerable loss of revenue to the fiscus.

The 2012/13 financial year saw 2 580 seizures of *contraband* cigarettes (138 million sticks, with a value of R63.4 million), and 22 seizures of *counterfeit* cigarettes (666 510 sticks, with a value of R467 860). Duty paid on cigarettes increased by just over 89%, with 943 million sticks being declared (up from 499 million sticks).

Compliance efforts for 2013/14 will focus on:

- Improving the manual tracking of cigarettes in transit through South Africa to ensure that declared quantities are accounted for at points of entry and exit, and that they are securely warehoused while in transit through the country.
- Enhancing collaboration with industry experts to develop targeted risk criteria for the detection of illicit cigarettes.

5. Clothing and Textiles

High volumes of undervalued clothing and textile imports have a serious effect on South Africa's clothing and textiles industry. It is encouraging to note that there has been significant progress made in terms of creating an even and fairly competitive playing field between local and international suppliers in the industry.

Key points in the 2012/13 financial year included:

- An improvement in the declaration of clothing and textile imports, after the introduction in November 2011 of a reference pricing tool. There has been a 16%

increase in the average price of specific items that are monitored against reference prices.

- During a nationwide Illicit Trader campaign by SARS Enforcement and Education divisions, 67% of 924 businesses visited were found not to be registered for either Income Tax or VAT.
- The modernisation of the Customs system has resulted in better detection of importers who change ports of entry in an attempt to avoid the detection of under-declared consignments.
- A sample of suppliers to major South African retailers has indicated that over 90% of suppliers show serious non-compliance with a range of regulations including Transfer pricing, under declaration of both VAT and Income Tax, and non-declaration of invoices to SARS. The sample findings also show that at least 190 of those suppliers have VAT returns outstanding since at least 2008, despite actively trading. It is anticipated that at least R1.2 billion will be generated from this focus area.

Focus areas for 2013/14 include:

- The enhancement and sharpening of the Price Referencing tool
- Increasing the numbers of inspectors at border posts
- Further developing systemic solutions to gaps in the clothing and textiles value chain
- Further refining the outcomes of the Customs Modernisation process

6. Small Businesses

For small businesses to prosper, SARS must ensure that its policies, procedures and systems do not inhibit the meaningful participation and contribution of small businesses in the economy and in the country’s tax system.

SARS will continue to simplify and improve requirements, processes and systems used to service the small business segment in order to reduce the compliance burden and costs to a point where these are no longer inhibiting factors to their tax compliance and growth.

Key points from the 2012/13 financial year include:

- The announcement that the turnover threshold which defines small businesses has been increased from R14 million to R20 million.
- Workshops and seminars with small businesses which reached 73 372 participants
- The simplification of company tax return processes

However, non-compliance does remain a concern. Some 64 investigations into VAT-related fraud were conducted, with 11 cases handed over to the National Prosecuting Authority (NPA) for possible prosecution, including 8 cases with a prejudice of R9.7 million. Additionally, 7 convictions have been obtained, resulting in an order to pay R2.9 million to SARS.

Focus areas for the 2013/14 year include:

- A survey to better understand reasons for a poor uptake of Turnover Tax
- Mobile registration drives in areas identified as having high non-compliance among small businesses
- Attention on the finance sector and on taxpayers claiming high-value refunds (i.e. diesel refunds).

7. Tax Practitioners and Trade Intermediaries

Tax practitioners and trade intermediaries play a vital role in facilitating tax and customs compliance. Despite the publicity raised around the non-compliance of some tax practitioners last year by the Minister of Finance, their compliance behaviour has not improved substantially over the past year.

A compliance analysis of tax practitioners has shown a number of worrying trends, including:

- An increase in complaints from the public via SARS' Suspicious Activity system, mainly around tax practitioners submitting fraudulent personal Income Tax returns in order to retain a portion of the (fraudulent) refund.
- Tax practitioners have 18 401 Personal Tax returns outstanding.
- Tax practitioners in their personal capacity are heavily indebted to SARS, to the amount of approximately R243 million.
- Five false VAT refund claims are currently under investigation, and have thus far resulted in the recovery of more than R200 million.
- Some practitioners have been found to be deducting PAYE (amounting to R41 million) from their employees but not paying it over to SARS.
- The entities through which practitioners conduct their business also pose tax compliance risks, with an outstanding debt of R1.2 billion (this includes outstanding debt practitioners in their personal capacity and their tax practices). Of the total outstanding debt, more than R 900 million is owed by the tax practices through which practitioners conduct their business

Key achievements during 2012/13 included the amendment of the Tax Administration Act with new provisions to regulate tax practitioners. It requires that tax practitioners register with SARS as well as with a recognised controlling body.

Compliance activities in 2013/14 will include:

- Pursuing deregistration of tax practitioners who remain non-compliant in their personal capacities, or who are no longer persons of good standing.
- Refining and developing a practitioners' risk rating mechanism, to more accurately identify high-risk practitioners, but equally importantly, to acknowledge and encourage low risk practitioners.
- A debt collection focus on the top 5% of practitioners who owe 96% of all debt due by practitioners
- The imposition of administrative penalties for late filing and payments

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