



**PARLIAMENT**  
OF THE REPUBLIC OF SOUTH AFRICA

**RESEARCH UNIT**

PO Box 15 Cape Town 8000 Republic of South Africa  
Tel: 27 (21) 403 8273 Fax: 27 (21) 403 8118  
[www.parliament.gov.za](http://www.parliament.gov.za)

**Summary on presentations by SARS, NT, SARB and FIC on PALAMA and BEPS**

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**1. Background**

Since 2015, the Joint Committee of the Standing Committee on Finance (SCOF), the Portfolio Committee on Trade and Industry and the Portfolio Committee on Mineral Resources in Parliament has been kept abreast of issues relating to Base Erosion and Profit Shifting (BEPS) in South Africa by National Treasury (NT), the South African Reserve Bank (SARB), the South African Revenue Services (SARS) and the Financial Intelligence Centre (FIC). However these entities are unable to give detailed information on the actual economic loss that arises from weaknesses in combatting BEPS and related activities. This is due to lack of a comprehensive disclosure of information by companies and other entities.

BEPS and related activities lead to government tax revenue being lost in South Africa, as it is in other developing and developed countries. As a result, Parliament took an initiative to strengthen its oversight over the tax revenue and related legislation to combat BEPS and related activities

There is clearly a need for Tax Legislation proposals by the Executive to deal with loopholes that presently allow exploitation by taxpayers. In the wake of the leaked 'Panama Papers' scandal, SCOF, and the Portfolio Committees on Trade and Industry and Mineral Resources invited various players to discuss the implications for South Africa.

The Joint Committee requests the NT, SARS, FIC and SARB to respond to the questions and comments below, which arose from the briefing on 25 May 2016.

**2. Summary of the presentations by SARS, NT, SARB and FIC**

The presentations as outlined by the four institutions (SARS, NT, SARB and FIC) covered similar grounds to those covered last time they appeared before the Joint Committees in September 2015. The presentations covered cross-cutting issues on progress in addressing illicit flows and transfer mispricing loopholes. The questions by Joint Committees to government institutions meant to combat BEPS and related activities in 2015 focused on how the different government institutions mitigate weaknesses leading in legislation and implementation to BEPS and related activities. Some of these questions asked were:

- How can South Africa stop and recover and bring to book all the transgressors of illicit flows?
- What are authorities doing to deal with illicit flows?

In addition to the state entities detailing their mission and vision statements, they provided a useful glossary of tax jargon.

- ***Illicit Financial Flows***

In respect of data, there is a common theme amongst government institutions in South Africa that due to complexity in illicit flows and lack of information sharing agreements with other countries, government is unable to quantify the level of illicit flows. All agree that illicit flows and related activities are prevalent in South Africa. But all quantified economic losses presented in the media from publicly available reports by the African Union Commission (AU), Global Financial Integrity (GFI) and other entities are merely estimated figures. As a result, government entities are of the view that besides unsubstantiated media reports, there is still lack of “hard” evidence that has been brought forward with regards to illicit flows.

The key objectives of anti-illicit financial flow measures include catching those responsible for illicit flows out and in of South Africa and improving preventative mechanisms. Some of the measures presented during the May 2016 Joint Committees sitting are listed below.

- Cross border focus to identify risk
- Detect and disrupt activities: enhanced due diligence, engagement with stakeholders. In this regards there has been arrests in KwaZulu-Natal, Mpumalanga, Western Cape and Gauteng Province by SAPS. Awareness training ,increased enforcement action under exchange control regulations (77 new investigative cases, 145 bank accounts “frozen”)
- Identify high-risk areas: freight payment , advance payments for imports

- ***Panama Papers***

The ‘Panama Papers’ are leaked confidential information concerning clients of the Panama-based law firm, Mossack Fonseca, who have “secret” bank accounts in offshore jurisdictions. South African legislation allows residents or citizens to transfer a certain amount of money abroad annually. There are approximately 1700 individuals according to SARS with varying roles ranging from directors to shareholders who are named in the Panama paper leaks and it is unclear whether they are in compliance with South African foreign exchange transfer legislation. Panama is one of the countries that have not committed to the exchange of information clause at the Global Forum on Transfer Pricing. As a result South African authorities find it difficult to access records of South Africans with investments routed through Panama. SARS has agreed on an international action plan aimed at obtaining more information and sharing it efficiently amongst tax administrators, SARS has further emphasised that the recently announced Voluntary Disclosure Program (VDP) would encourage taxpayers with foreign accounts to declare their income for tax purposes.

- ***Base Erosion and Profit Shifting (BEPS)***

Update on Transfer Pricing: There are many challenges for tax administrators (locally and internationally). There is a scarcity of experienced human resources. SARS must compete for tax and legal experts with the private sector. There is a lack of updated infrastructure to track and deter abuse of taxation and related legislation, and there is a lack of effective coordination models within South Africa and Internationally. There is however a recruitment process underway for hiring additional capacity by SARS and other government entities meant to combat transfer pricing related weakness.



Generally, the presentations on BEPS focused on transfer pricing, transparency and other aspects affecting international taxation. In line with the OECD/G20 2014 BEPs action plans outcomes, SARS has made specific revisions to guidelines that with assist in countering BEPS and related activities using the sections in the Income Tax Act.

- Action 8-10
  - Amendments relating to sections 42A, 46, 47 and 49 of the Tax Administration Act (TAA), No. 28 of 2011 : information relating to access to foreign based information
  - Section 99 of TAA: broadening scope of the corporate tax return, inclusion of inbound services and extending the prescription period to submit information.
- Action 13
  - TAA, section 1 definition of "international tax standard" extended to Country-by-country (CbC) reporting and a signed multilateral competent agreement of exchange of CbC reports is now operative.

### **3. Parliament: BEPS Way forward**

Taking into account Parliament's limited role with regards to combating BEPS and related activities, Parliament's approach has involved separating its oversight over the roles played by government entities from the task of ensuring that the taxation and related legislation addresses BEPS and related weakness. Although BEPS and related activities are policy-orientated due to effects of economic losses on poorer citizens, there is currently lack of political consensus within Parliament on the approach to be pursued.

Even though government entities attempted to provide more details about action plans to address BEPS and related activities, there are several questions to be addressed by SARS, NT, FIC and SARB in future engagements with Parliament. A key instance here is defining clearly the specific roles and responsibilities amongst government entities and resolving the issue of who coordinates various government entities' actions to avoid duplication or lack of information and instead encourage coordination.

**Specific questions and comments to be addressed by government entities in further engagements with Parliament include the following:**

- a) What steps has the South African Government taken to quantify the economic losses as a result of BEPS and related activities?
  - We do know there are illicit flows, but do we know how much?
  - What are the different types of illicit flows?
  - What are legitimate flows and should we monitor or approve all outward (and inward?) flows?
  - Are amnesties/VDP best way to get to get more information? How does this interface with enforcement against those who do not come forward?
  - What are government authorities doing to deal with past and future illicit flows?
- b) Since the previous discussion in Parliament about BEPS in 2015, has there been any improvement to the South African legislation approach or otherwise taking into account the work and recommendations of the Davis Tax Committee work and other institutions like civil society, NGOs and labour movement?

- Action 8- 13: Can SARS provide details of the draft regulations which will be released for public comment in April 2016? How long will the consultations period be?
  - How much co-ordination and sharing of info between entities reporting to different Ministers?
- c) South Africa has various institutions –SARS, NT, SARB and FIC- that are somehow involved in combatting BEPS and related activities, how has coordination improved amongst the work of these institutions to eliminate duplications and ensure efficiencies?

#### **Capacity**

- d) Insufficient or incapable human resources (HR) capacity from SARS and other institutions meant to deal with BEPS and related activities was seen as one of the reasons that BEPS continues in South African and internationally. To what extent are the HR problems being addressed and what are some of obvious benefits in this regards?
- e) Are there further plans by South African government to reform the Bilateral Investment Treaties (BITs), Double Taxation Agreements (DTAs) and other International Cooperation Agreements and processes, in response to BEPS and related activities? For example, in the current treaty agreements, to what extent are articles in the agreements being amended or what measures are being taken to ensure that these are renegotiated? Are there any limitations in contractual negotiation - insertion of clauses, etc?

#### **Sectors**

- f) There is a realisation by many countries that multilateral rules need to play an increasing role in regulating the use of tax measures, especially where these measures affect international movement of goods, services, capital etc.
1. According to the SARS briefing in 2015, the Mining and Extractive Industry had more cases of BEPS than any other industry. Which other sectors have being heavily impacted by anti-avoidance tactics employed by taxpayers?
  2. In relation to the customs unit: are there any major problems that have arisen in importing and exporting of goods that have led to profit shifting that involves multinationals? What penalties have been imposed?
  3. In the context of Department of Trade and Industry (DTI) - what is being done to address this in the World Trade Organisation (WTO) and Free Trade Agreements (FTA) which have a potential to prevent BEPS? What measures have been put in place to prevent avoidance?

#### **Transparency and International cooperation**

- g) In 2014, G20 Finance Ministers endorsed the Common Reporting Standard (CRS) for automatic exchange of tax information. What are some of the benefits and outcomes of CRS? Are there any plans to extend the CRS to countries beyond G20?
- h) What are the outcomes of the G20/OECD 15 Action Plan project? How does NT and SARS intend to incorporate relevant G20/ OECD 15 Action Plan Outcomes into South African legislation or practice or both? In particular what in the domestic law should the Committee be looking at to close the gaps?



- i) How many of the G20/OECD member countries have adopted or are implementing the BEPS 15 Action Plan outcomes, and how many are not?
- j) What opportunities have been discovered through exchange control regulations to date to address BEPS and related activities? In particular does the SARB surveillance department have access to all international transactions going in and out of South Africa?
- k) One of the recent milestones attained is the adoption by G20/OECD Country by Country (CbC) reporting, the CbC provides an overview of group revenues, profitability, tax, employees and assets around the world for this purpose. Do South African Institutions, SARS and others, have necessary capacity to derive benefits from CbC information?
- l) Are there any other and specific Non-G20/OECD Jurisdiction BEPS Action Plan Frameworks, particularly for developing countries?

#### **Observations from desktop readings**

- There is growing concern with regards to the significant losses of national tax revenues because of sophisticated tax planning by Multinational Enterprises (MNEs) aimed at shifting profits in a way that erodes the tax base.
- Filling the gaps in current bilateral taxation treaties would be the most effective and realistic way to deal with taxation. The rules that apply to the arms-length principle, controlled foreign companies (CFCs) and exemptions need to be elaborated.
- There is a need to strike a balance between combatting BEPS and related activities and attracting investments. This is particularly important in a domestic and international economic environment that continues to deteriorate.

#### **4. Issues for consideration for Parliament oversight- BEPS and related activities**

Parliament will continue to monitor government strategies and mechanisms that aim to combat BEPS and related activities in South Africa. In particular, Parliament proposes the following measures for government entities to consider:

- Government entities led by the National Treasury should conduct a study that will provide an estimate of economic losses for the South African economy as result of BEPS and related activities.
- Government entities should regularly update Parliament with regards to progress in either recovering monetary losses or reaping benefits brought by the improvement of legislation or capacity building. These updates may be provided to Parliament as part of quarterly oversight reports or annual oversight reporting or both.
- It has been reported that South Africa is currently a member of global and local collaborations or platforms meant to combat BEPS and related activities. The benefits or outcomes of these collaborations or platforms should reported to Parliament during quarterly or annual reports by government entities.