IMPLEMENTING RECOMMENDATIONS OF NUGENT COMMISSION OF INQUIRY

Progress report to SCOF
24 November 2020

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

STAY SAFE
SAVE SOUTH AFRICA

NUGENT FINDINGS AND RECOMMENDATIONS

national treasury
Department: National Treasury
REPUBLIC OF SOUTH AFRICA

STAY SAFE
SAVE SOUTH AFRICA

- Final report of Nugent Commission was published around 14 Dec 2018, following Interim Report in Oct 2018
  - Report presented to SCOF in Feb 2019, and discussed in Sept 2019
- Report confirmed instances of maladministration and mismanagement at SARS between 2014 and 2017
  - The premeditated restructuring of SARS was intended “to take control of SARS”, and ultimately “bound to cause disruption and bewilderment”
  - As a result, enforcement was weakened, as “the units that investigated the illicit trades ceased to exist”
  - Revenue collection suffered, corroborated by falling tax payer compliance
  - Also evidence of abuse of procurement processes - particularly large-scale consulting contracts to reform SARS’ operations and information technology systems
  - Confirmed occurrences have been referred for investigation, including criminal investigation – as the final report recommended these be followed up by the proper authorities
- The final report contained 27 specific recommendations
  - The report itself discusses many other challenges, though those do not necessarily flow through to the direct recommendations – often because there is not a simple solution to organizational challenges
  - The recommendations aimed primarily to correct past infractions, halt poor governance practices and start to prevent any future recurrence of SARS’ decline
- Long term objective: a robust organisational and decision making culture for SARS.
  - Implementing these recommendations are therefore necessary, but insufficient to put SARS on a long-term trajectory of excellence

PARALLEL TRACKS FOR IMPLEMENTATION

national treasury
Department: National Treasury
REPUBLIC OF SOUTH AFRICA

STAY SAFE
SAVE SOUTH AFRICA

Governance processes in SARS	Governance and oversight of SARS
Prerogative of Commissioner for SARS	Prerogative of Minister of Finance
Actions implemented by SARS	Policy developed by Treasury for approval by Cabinet
Immediate focus (stabilize SARS; restore collection capacity)	Medium term work (legislative; build hard and soft institutions)

DIMENSIONS OF TAX REFORM

- Three areas of previous recommendations – not always clearly delineated
  - Tax policy: best addressed incrementally as implementation takes time. Announcement in Budget, NT releases discussion documents, workshops, TLAB cycle contains amendments, often affects fiscal framework.
  - Tax administration: affects the relationship between taxpayers and SARS, TALAB amendment process, but also determined by IT (e.g. this year's automated PIT assessments)
  - **Oversight and Governance:** Determines how SARS is set up, the functions of SARS, how decisions are made; amendments to SARS Act.
- Today our focus is on third, but interrelated: form follows function

HOW DID WE ARRIVE AT THIS POINT?

national treasury
Department: National Treasury REPUBLIC OF SOUTH AFRICA

STAY SAFE
SAVE SOUTH AFRICA

Franzen Commission (1969)

Margo Commission (1987)

Interim Constitution (1993)

Katz Commission (1994 – 1998)

Constitution of RSA (1996)

SARS established (1997)

Amendments to SARS Act (2002)

Advisory Davis Tax Committee (2013)

Nugent Commission (2018)

(Mpati Commission 2020)

(Zondo Commission)

Katz Commission objectives:

1. *Ensure tax policy and admin comply with constitutional ideals*
2. *Ensure tax policy and admin generate sufficient resources to finance constitutional ideals progressively*
3. *Self-sufficient financing (GEAR)*

Increased SARS Autonomy

Policy review

Response to State Capture

MARGO COMMISSION (1987)

- **Margo Commission:** "If, as a special case, it were possible to restore some of its **original authority** to Inland Revenue in these matters, it would be of positive assistance in resolving some of the present staff problems."
- **Katz Commission:** "An autonomous administration is able to retain competent and qualified staff through competitive compensation scales, is able to invest in appropriate training, office equipment and working conditions. No less important, will shed redundant staff or an independent office under public scrutiny and subject to rigorous reporting requirements ineffective methods as it adapts its structure and operations to specific objectives and tasks."
- **Section 2 of SARS Act (1997):** "The South African Revenue Service is hereby established as an organ of state within the public administration, but as an institution outside the public service", originally with a board. Requirement for a board removed in 2002.

KATZ COMMISSION

- First Commission of Inquiry instituted under Pres. Mandela, on 22 June 1994, published first Interim report in Nov 1994 and last report in 1999
- Main objectives
  - Ensure tax policy and admin comply with constitutional ideals
  - Ensure tax policy and admin generate sufficient resources to finance constitutional ideals progressively
  - Put SA on a self-sufficient public finance trajectory
- Context: high public debt, low levels of tax morale and compliance, highly fractured administration
- Produced 8 reports, including policy reviews of
  - Capital transfer tax (resulted in implementation of Security Transfer Tax)
  - Residence base of income taxation (implemented from 2001)
  - Benefit funds (exemption of benefits that are paid from after-tax income)
  - Provincial taxation (set out framework for cooperation, without harmful tax competition)
  - NGO tax treatment (implemented through PBO provisions)
- The interim report is the most voluminous, and does a system-wide diagnostic exercise
  - Proposed merging of inland revenue and customs/excise into one revenue agency with greater autonomy (Interim and 3rd report 1995), that led to the formation of SARS in 1997
  - Eg. Recommended integration of the 5 tax administrations (inland revenue, customs and 3 former "home lands"
  - Recognised that highly skilled tax officials are key to improved tax collection and out of public service
  - Recommended amendments to end race-based and gender-based discrimination in tax system

KATZ COMMISSION MAIN TAX ADMIN RECOMMENDATIONS

- "**Independence and management autonomy**, analogous perhaps to the status of central banks, provides a crucial line of protection of the fiscus from the debilitating erosion of tax morality and administrative efficiency which have accompanied fiscal stress in so many countries… An autonomous administration is able to retain competent and qualified staff through competitive compensation scales, is able to invest in appropriate training, office equipment and working conditions. No less important, **an independent office under public scrutiny and subject to rigorous reporting requirements** will shed redundant staff or ineffective methods as it adapts its structure and operations to specific objectives and tasks."
- "Modernisation of tax administration to give effect, inter alia, to **the needs for institutional autonomy and a professional personnel corps**, requires legal, administrative and organisational reforms which take account of local circumstances. The Commission does not view its task as encompassing detailed proposals on appropriate institutional reforms. The Commission recommend, however, that the following broad principles should inform Government's restructuring of tax administration in South Africa:
  - **Independence of the revenues authorities**, including responsibility for their own budgetary allocation and control, administrative policies and objectives, and recruitment, training, remuneration and codes of conduct for personnel;
  - **Oversight by statutory boards** responsible for Inland Revenue and Customs and Excise, appointed by and answerable to Parliament through the Minister of Finance;
  - Maintenance of **unified Inland Revenue and Customs and Excise departments**, with responsibility both to the national and provincial governments for all aspects of tax collections; and
  - Contracting out, where appropriate, of certain administrative functions, such as computer services, warehousing of documentation and customs merchandise, printing and distribution of tax returns and notices, preparation of tax manuals and documentation and collection of minor taxes."

Source: Interim report of the Commission of Inquiry into certain aspects of the Tax Structure of South Africa, 1994, pg41-42.

ESTABLISHMENT OF SARS (1997)

- Informed by Katz commission's recommendations
- **Section 2 of SARS Act (1997):** "The South African Revenue Service is hereby established as an organ of state within the public administration, but as an institution outside the public service"
- Originally included a board, but the Board did not contribute much to institutional building. Requirement for a board removed in 2002.

DAVIS TAX COMMITTEE

- Established as an advisory committee in 2014, to assess particular tax issues and make non-binding recommendations
- Published 41 reports (excl external reports) on 19 themes, including
  - Macro analysis
  - SME tax matters (led to review of SME tax regimes)
  - Estate duty (leg to review of policy design, increase in rate)
  - More than 20 reports on BEPS implementation (assisted with transition)
  - VAT assessment (prepared the way for assessment of zero-ratings)
  - Mining, Oil& gas reports (base for NT’s current work on those matters)
  - Funding of higher education, NHI (costing exercises that have fed into policy discussions)
- One report on tax administration. Bulk of report focuses on tax payer matters (e.g treatment of HNWIs, BEPS reporting), also make following suggestions for governance improvement:
  - Institute a supervisory board for SARS, would likely perform similar functions to the HMRC board, to provide challenge, expertise, strategy, assurance and stakeholder views.
  - Amending the SARS act’s process to appoint the Commissioner for SARS
  - Review of SARS Act, TAA and tax acts to check correspondence.

NUGENT PRINCIPLES ON GOVERNANCE

- **Restore trust and tax morale**
  - *"[t]he importance of **effective governance** at SARS cannot be overstated. It is an essential pillar for the effective and efficient operations of SARS. Its impact is felt in the overall performance of SARS, including, most importantly, in revenue collection. It also impacts on the budgetary process of SARS as an institution and indeed of the nation. Tax morality is also materially affected by these considerations*" (pg 168 par 2).
- **Diffuse decision making powers and oversight**
  - "*power within the organisation was **excessively concentrated***" (pg. 24 par 13)
- **Restore fundamental link between tax admin and fiscal policy**
  - The Commission is therefore of the fervent view that *"[i]t is a non-negotiable proposition that SARS' autonomy is sacrosanct*" but it must be "*reconciled with the reality that the national budget and tax policy is the responsibility of the executive government and the management of the country's finances vests in the Ministry of Finance*" (pg 175 par 11 and 12).

NUGENT RECOMMENDATIONS

- **Immediate, urgent recommendation**: remove previous Commissioner, appoint new Commissioner following a more transparent process. ***COMPLETED.***
- The findings and recommendations cover a wide array of areas including:
  - Procurement matters (Chapters 3, 5 and 11)
  - Organisational design and staffing (Chapters 4, 5, 6, 7 and 13)
  - Operational matters (Chapters 8, 10, 12, 14 and 16)
  - Reputational damage (Chapters 17, 18 and 19) and
  - Reconsideration of governance matters (Chapter 20).
- Consistent theme running through the report, that "[*t]he principal feature of the new structure… was to fragment many of the functions that previously had operated cohesively*." (pg 52 par 12) Any proposals on the **structure of SARS' functions must avoid fragmentation**.
- Many of the recommendations relating to governance, accountability and integrity require legislative and policy changes, which the Minister of Finance (with the endorsement of Cabinet) will oversee

NUGENT GOVERNANCE RECOMMENDATIONS

- **The Commission made several proposals related to governance or strengthening organisational leadership,** requiring amendments to current legislation to be overseen by the Minister of Finance (Chapter 20)
- The establishment of an **inspectorate** was to enhance governance of SARS, as it provides a mechanism to provide oversight over SARS' functioning, in order to detect abuse in a manner that protects SARS' primary mandate and taxpayer confidentiality
- The Commission also recommends legislative provisions for a **mandatory advisory Executive Committee, including Deputy Commissioner(s)** [16.5]. The functions of this committee is envisaged to be described in broad terms by legislation
- **The Commission is not in favour of an oversight board, differing with Davis Tax Committee**. Cabinet noted that *"(t)he Commission is not persuaded that an oversight board is indeed a useful instrument*" (pg 184 par 33).
- The Commission affirmed that the current role of the Office of the Tax Ombud [16.2], whose mandate is "confined broadly to addressing taxpayer rights" which is its "appropriate role" and "it should not be involved in the governance of SARS".
- Governance and oversight of SARS can be enhanced by an Inspector General

ROAD AHEAD

- National Treasury **committed to publishing a discussion document by June 2020, which was unfortunately overtaken by the urgent work in response to Covid-19** – including 4 batches of tax amendment which had not been anticipated at the time. There has been progress on the work, and earnest engagement on the work between NT and SARS. This delay has not caused hold-ups in the implementation of other recommendations, as can be seen from SARS' progress report.

ENVISAGED TIME TABLE

Time frame	Action	Responsibility
Budget 2021	Release discussion paper for public comment	NT and Minister
April 2021	Summarise comments	NT
May 2021	Public workshops / hearings on comments	NT
June-Sept 2021 (with or after annual TLAB)	Publish draft legislation for comment	MoF, with Cabinet approval
Oct 2021 to December 2021	Processing of Section 75 SARS Amendment Bill (optimistic scenario)	NT and Parliament
Feb 202 to June 2022	Process of Section 75 SARS Amendment Bill – less optimistic time line	NT and Parliament