

**FOR
INFORMATION**

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TECHNICAL ASSISTANCE REPORT

SOUTH AFRICA

STRENGTHENING TRANSFER PRICING CAPACITY

AUGUST 2019

PREPARED BY

DALE HILL



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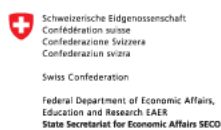


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ABBREVIATIONS AND ACRONYMS

AFS	Regional Technical Assistance Centre for Southern Africa - AFRITAC South
APA	Advance Pricing Agreement
BEPSSG	Base Erosion and Profit Shifting Steering Group
FAD	IMF's Fiscal Affairs Department
MAP	Mutual Agreement Program
SARS	South African Revenue Service
SIOL	SARS Institute of Learning
TA	Technical Assistance
TCEI	Tax, Customs and Excise Institute
TD	Tax Department
TP	Transfer Pricing
TPSDP	Transfer Pricing Strategic Development Plan

EXECUTIVE SUMMARY

At the request of the Commissioner, the Regional Technical Assistance Centre For Southern Africa (AFRITAC South--AFS) arranged a technical assistance (TA) assignment visit to Durban, Gauteng and Western Cap, South Africa during the period May 8-22, 2019. The purpose of the assignment was to assist the South African Revenue Service (SARS) to strengthen its transfer pricing (TP) program. This was the fourth mission on the same topic since the TP capacity building program started in April 2018. The mission was delivered by a Fiscal Affairs Department (FAD) expert, Mr. Dale Hill, in collaboration with the SARS Institute of Learning (SIOL). The mission conducted training sessions and workshops for the following organizational units: Audit, including TP auditors; Case Selection, including TP Case Selection; Legal; Governance; Taxpayer Services/Strategy; Customs Audit; Customs Case Selection; and, Legal – Customs.

The mission worked with the SIOL to enhance the current Introduction to Transfer Pricing (TP) course. The enhancement includes a learner manual, presentations on official SARS templates and incorporation of South African TP legislation and definitions. The enhanced training course was delivered over two training sessions to 55 participants in the Western Cape, bringing the total of officers trained on introduction to TP to 264 since the program started in April 2018. The Cape Town training sessions were led by a SARS instructor with the mission providing back-up support. This is meant to transfer skills to SARS and build capacity that will be used to rollout future TP training within the organization.

The mission held a strategy meeting for Senior SARS officials to discuss progress and agree a way forward. The meeting also discussed: feedback from the training events; development of an advanced course for TP auditors including customs valuation issues; enhancement of the structure and organization of the TP audit area to make it more effective and efficient; and the development, approval and implementation of the Advance Pricing Agreement (APA) pilot. It was decided by SARS management (Base Erosion and Profit Shifting Steering Group-BEPSSG) that APA program should not form part of the current TA support by the Fund, but rather that focus should be on intensely developing the TP capacity to a required level of effectiveness.

The mission recommended next steps to be taken before the next visit in October 2019 and further actions to guide the capacity development initiative to December 2020. In addition, it followed up on recommendations of the previous missions and encouraged the authorities to implement these recommendations in line with agreed timelines. The mission recommendations include need for SARS to: approve the Transfer Pricing Strategic Development Plan (TPSDP) developed in earlier missions; development of a stakeholder engagement and communication plan; and review of the processes for case selection.

I. INTRODUCTION

1. The purpose of the assignment was to assist SARS to strengthen its capacity for TP audits. The assignment was carried out during the period May 8-22, 2019. The mission worked with the SARS officials to create and deliver the assignment outputs. The mission tasks included: reviewing progress in implementation of the action plan developed during the two missions in 2018 (April and November), and the third in January 2019, and providing guidance to advance progress; updating the transfer pricing course delivered during the last mission to make it more suitable to the South African context and take into account practical challenges faced by SARS in managing TP cases; and delivering the revised course to 55 officers in the Western Cape.

2. The mission also discussed with the authorities some of the observations of previous missions, amongst which were the following:

- SARS expanding its TP audit program beyond the current large taxpayers' coverage.
- The case selection procedures taking long (over one year) and case selection officers performing activities akin to audit, including visiting or contacting taxpayers.
- The need for customs and tax to understand transfer pricing and work together to mitigate TP risks across the entire institution.

II. PROGRESS SINCE LAST VISIT

3. The technical assistance to SARS started with a scoping visit by a HQ led scoping visit during November 27-December 1, 2017. Following the scoping visit, the first TP course in April 2018, and a request from the Acting Commissioner of SARS on May 17, 2018, a 24-months 2018/20 TP capacity building program was agreed with missions under the program rolled out from November 2018. The first mission in November 2018 covered both introduction and advanced TP topics to select specialist and senior SARS officials.

4. The mission and the SIOL agreed a workplan for 2019, comprising visits in January, May and October 2019. The training on introduction to TP continued in January 2019 covering Audit, Risk and Case Selection, Customs and Legal officers. The training was carried out in Durban, and Pretoria. In addition, a seminar on TP in the mining area was organized by the Tax, Customs and Excise Institute (TCEI) and was delivered with approximately 125 participants attending. A workshop was also held in Pretoria to discuss the legal cases relating to TP.

5. The TP program, initially aimed for auditors in the TP Case Selection Unit and TP auditors in the Large Business Centre, has now been expanded to include all units within the audit value chain. The expanded program entails training on TP delivered to participants from the Investigative Audits, the Customs and Excise Audit, CSU in Customs, Legal, Governance and Taxpayer Services. SARS initially requested that the current TP program includes

development of APA processes and rollout its pilot with the IMF assistance. However, the BEPSSG has decided to take out the APA work from the current TP program to focus all the effort to development of TP capacity development.

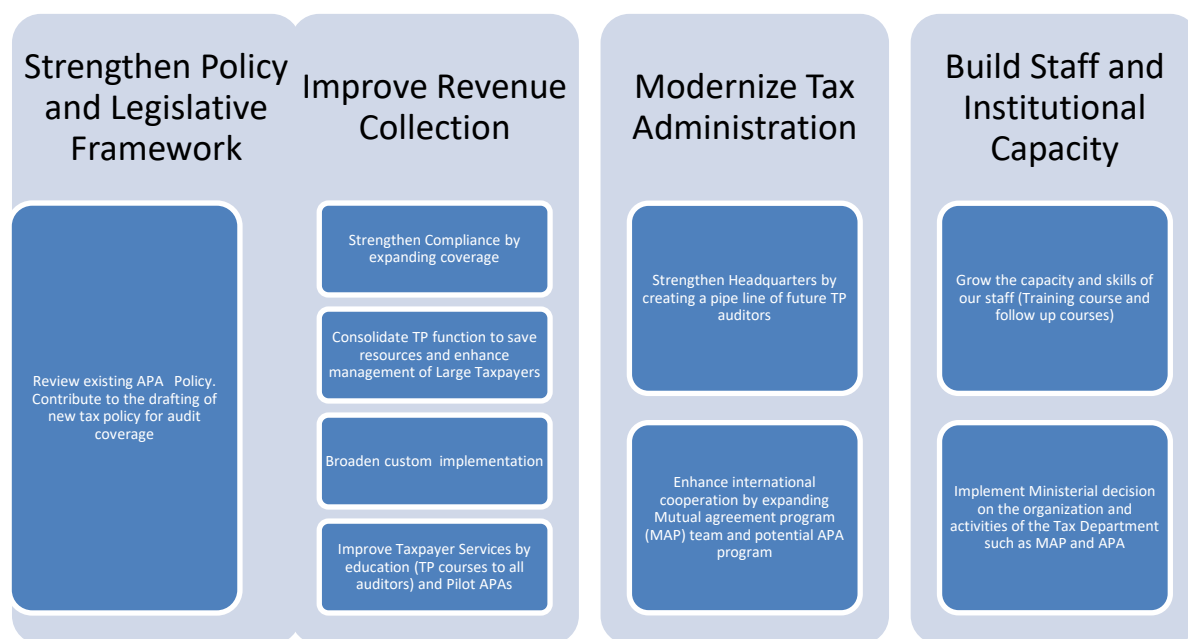
III. TA DELIVERED

6. The mission reviewed the existing TP course, delivered two training sessions, and agreed the TPSDP, which gives details on the next steps. The TPSDP is to be completed for final review by the Tax Department (TD). *The plan will be titled TPSDP 2018-2020.*

7. The mission also presented relevant TP concepts to Customs in Pretoria. It also held a strategy meeting on May 13 with Senior SARS officials to discuss: training courses given during the mission; feedback from courses; development of advanced TP course; required improvements to the organization structure within the TP area; need for approval of the TPSDP; and need to intensively involve Senior SARS management in moving forward to implementation.

8. The TPSDP was updated during the visit to address review points by the TD. The plan has four strategic goals and nine strategic objectives, as set out in Figure 1.

Figure 1. Transfer Pricing Strategic Development Plan Goals and Objectives



9. The mission reiterated advice for SARS to develop a holistic and more detailed action plan to support and provide detailed steps to guide the rollout of the TPSDP. The intention by the SARS' senior officials is to discuss the final action plan with officials and get it disseminated to everyone who will be involved in its implementation. The TPSDP is meant to set out the high-level strategies over a multi-year time frame. The planning for each strategy is left

as a further step in the planning process and is to be achieved through development of the detailed action plan.

10. The mission further reiterated the advice that accountabilities for strategies must also be decided. Allocating accountabilities will ensure that enterprise responsibility for delivering the strategies is clear.

11. Advice was also reemphasized for a stakeholder engagement and communication plan to be developed, as part of the plan to rollout the TPSDP. The purpose and principles for stakeholder engagement and communication were further discussed during the visit. Involvement of Senior SARS officials in the delivery of the training course and the implementation of the TPSDP is crucial and critical for success. In addition, the engagement plan needs to embody steps to discuss in detail with relevant officers in SARS any need for, and actual reorganization of the existing structure to facilitate TPSDP rollout. The mission alerted SARS that documenting the plan shall be a significant milestone, beyond which the real challenge will be implementation which shall need strong leadership in managing the reform. In this instance, the role of leadership in setting a clear and longer-term view of the changes required was agreed to be important for successful implementation.

IV. AGREED ACTION PLAN

12. A preliminary plan has been developed for key milestones to be achieved by December 2020. To maintain the momentum of the work commenced, it is important that the actions in table 1 are completed.

Table 1. Action Plan to Further Develop TP Capacity in SARS

Action	Who	Completed by
More detailed case related course and consultation with experienced transfer pricing staff	SARS/ IMF	December 2019
Develop an advanced TP course	IMF/SARS	December 2020
Follow up training on advanced topics to auditors that received the training in 2018	SARS/IMF	December 2020
Further courses in Johannesburg, Durban and Cape Town on revised introduction to TP course and a new advanced TP course.	IMF/ SARS	December 2019-2020
Hold the next high-level seminar on TP	TCEI/IMF	October 2019
Approve the TPSDP, develop implementation plan, and communication plan	SARS/IMF	December 2019

V. DOCUMENTS DEVELOPED DURING THE VISIT

The mission worked with SARS to review the TP course to include customs valuation matters and to validate the program for the October 2019 mission (Appendix 2).

Appendix 1. Agenda for the Mission

INTERNATIONAL MONETARY FUND (IMF)

FACILITATOR: DALE HILL

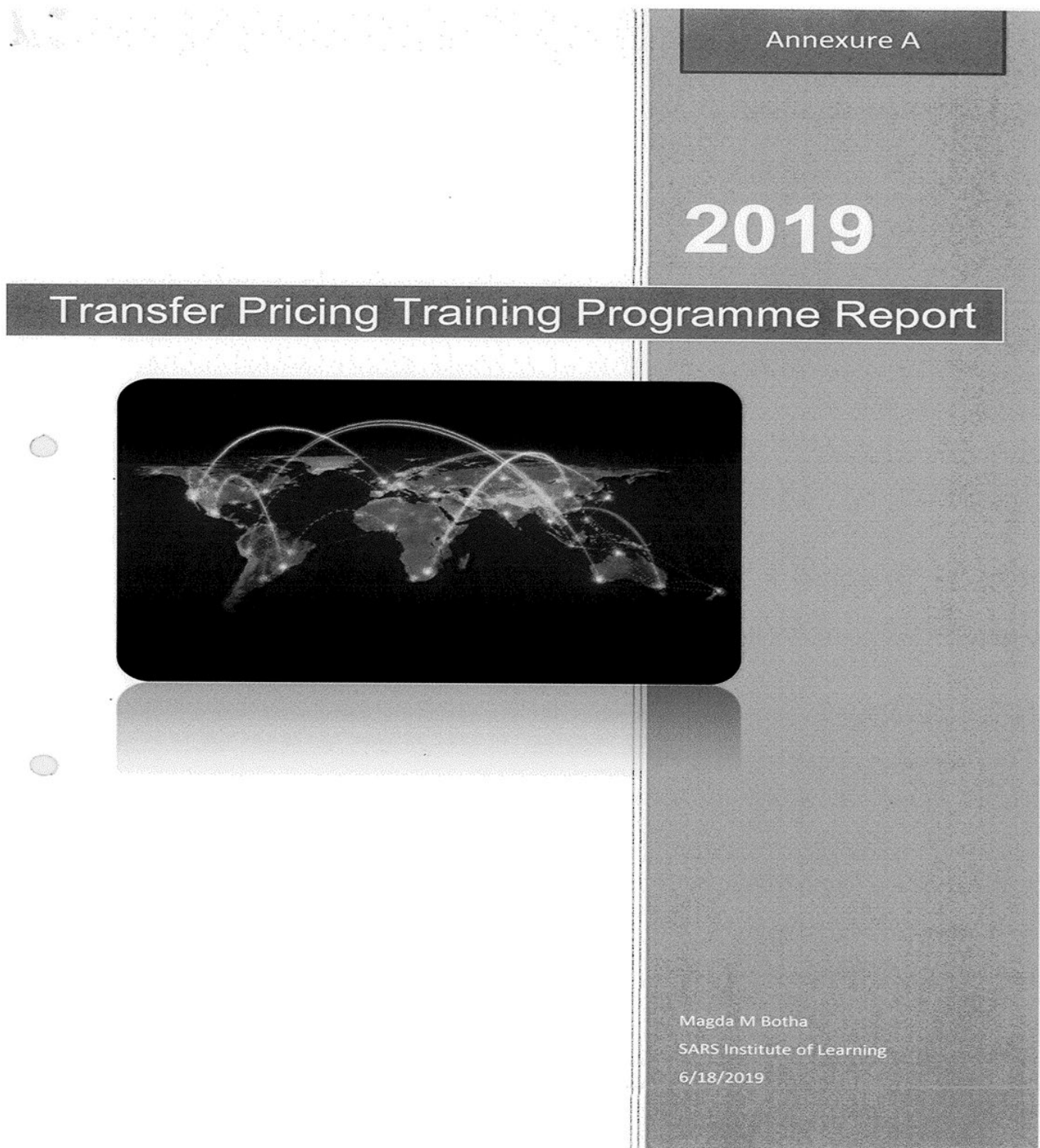
Transfer Pricing capacity development plan from January 2019

May 2019 (08 – 22 May 2019)			
Action	Where	Target Audience	When
Development: (5 days) <ul style="list-style-type: none"> • Include the SA Legislation and terminology on Introduction to TP course (finalization) • Scope and Develop the Customs/TP product • Scope and plan the TP Advanced topics panel 	Kwa-Zulu Natal Durban	SIOL developers and facilitators	08 – 10 May 2019 (KZN)
	Gauteng: Pretoria	Subject Matter Experts from TP and Customs Audit and Case Selection	13 – 14 May 2019 (Gauteng) (5 days)
TCEI Workshop Topic: <i>To be determined</i>	Gauteng Pretoria	TCEI	15 May 2019
Training (two days) Introduction to TP (include the extra two hours with SA legislation and terminology – SIOL co-facilitate)	Western Cape Cape Town	Audit Customs Case Selection Legal Taxpayer Education (BOE)	16 – 17 May 2019
Training (two days) Introduction to TP (include the extra two hours with SA legislation and terminology – SIOL co-facilitate)	Western Cape Cape Town	Audit Customs Case Selection Legal Taxpayer Education (BOE)	20 - 21 May 2019
Development: Finalization	Western Cape Cape Town	SIOL developers and facilitators	22 May 2019

Appendix 2. Agenda for October 2019 Mission

October 2019 09 – 22 October 2019			
Action	Where	Target Audience	When
Training: Pilot (2 – 3 days) Pilot the Customs/TP course developed in May	Gauteng Pretoria	Customs/TP/Risk/Legal/Intelligence/VAT Specialist/TCEI	09 – 11 October 2019
Workshop: (2 – 3 days) - TP Advanced Topics Delivery method: Panel Discussion Industry Specialists Workshop (TP Audit and Case Selection present their cases/profiles to the “panel” for debate and discussion)	Gauteng Pretoria	TP Audit and Risk (Panel: Mr Hill, SIOL, TP Audit/Risk, TARA, TCEI)	14 – 15 October 2019
TCEI Workshop Topic: Advance Pricing Agreements (APA) (subject to SARS Leadership approval)	Gauteng Pretoria	TCEI & SARS Leadership	16 October 2019
Training: Introduction to TP <i>(SIOL will facilitate – Mr Hill to observe and provide guidance)</i>	Gauteng Alberton	Customs Case Selection and Audit	17 – 18 October 2019
Training: Introduction to TP <i>(SIOL will facilitate – Mr Hill to observe and provide guidance)</i>	Eastern Cape Port Elizabeth	Audit, Customs, Case Selection	21 – 22 October 2019

Appendix 3. SARS TP Capacity Building Progress Report to Management



INTERIM REPORT ON THE TRANSFER PRICING TRAINING PROGRAMME FROM APRIL 2018 TO MAY 2019

1. Purpose

The purpose of this report is to provide feedback on the progress of the Transfer Pricing Programme delivered from April 2018 to May 2019.

This report should be read in conjunction with Annexure B: The Transfer Pricing Programme Agenda.

2. Background

Transfer Pricing (TP) has become one of the most reviewed and controversial tax issues facing governments around the world. It is highly contentious because it relates to the allocation of income, resulting from the business assets, functions and risks that generate business income, which each government apply their tax rate to. With the emergence and rapid growth of the digital economy, it is becoming more and more difficult to determine where the income has been determined.

The Income Tax Act section 31 introduced in 1 most recent amendments in principle in 2011 and 2014, provides that transfer prices (cross border transactions between connected persons as defined under s1 of the ITA) must at arm's length and subject to arm's length adjustment to the taxable income or tax payable, to reflect the terms and conditions from those of independent third parties at arm's length.

As per the SARS Annual Performance Plan 2017/18 (APP), developments in the global tax and customs environment includes Base Erosion and Profit Shifting (BEPS) which continues to be a challenge globally and South Africa.

In an internal memorandum, Ref: US/TP/1720, dated 27 October 2017, the then Commissioner, Mr. Tom Moyane, approved an exploratory visit by representatives of the International Monetary Fund (IMF) to determine the level of Transfer Pricing learning and development assistance that may be required by SARS as well as to curb the skills and knowledge gap pertaining to Transfer Pricing.

Herewith events in chronological order:

2.1 The IMF, represented by Messrs. Andrew Okello and Dale Hill, conducted an exploratory visit to SARS from 27 November to 1 December 2017 in order to determine the level of Transfer Pricing (TP) learning within SARS as well as to understand the development assistance needs of SARS. This visit included meetings with senior management, the technical auditors and the SARS institute of learning (SIOL).

Dale Hill visited SARS 9 to 20 April 8 to assist the design and delivery of an introductory level course to Transfer Pricing. Although the topic is of complex and advanced nature the delivery is pitched at a basic level aligned to the Bloom Taxonomy level 1, understanding and remembering.

- Following the conclusion of the visit by Mr Dale Hill, the Acting Commissioner, Mark Kingon, signed a letter, dated 17 May 2018 to Mr Victor Gaspar, Director in the IMF's Fiscal Affairs Department, to thank the IMF for their technical assistance date and to request the continuation of the assistance programme for a further 24 months. Mr Gaspar responded positively and advised that the IMF programme will be continued for a further 24 months.
- The IMF contracted Mr Hill to provide SARS with the required assistance on TP and possible assistance in the development of Advanced Pricing Agreements {APAs}.
- During the November 2018 visit, Mr Hill and SIOL prepared the TP Programme for the 2019/2020 period. The November visit also included training on a basic and advanced level, workshops and meetings with various SARS specialists and senior officials.
- According to the TP Programme, Mr Hill's visits to SARS were scheduled for January, May and November 2019 (see Annexure B).

3. Transfer Pricing Programme

3.1 Introduction to Transfer Pricing

The Introduction to Transfer Pricing course was designed and delivered by Mr in 2018 and 2019. In May 2019 the product was enhanced with the assistance of the SARS Institute of Learning (SIOL) development team under leadership of Mr Ricardo Kock. The enhancement of the product includes a learner manual, presentations on official SARS templates and South African TP legislation and definitions.

Course introduces the audience to what transfer pricing is and the most common TP methods used by companies to allocate profits within tax and customs jurisdictions.

Course was initially aimed at only the TP value chain at the inception thereof which included the TP Case Selection Unit (CSU) in BAIT and the TP Auditors in Large Business Centre. Subsequently, and in response to the 2017/18 APP transfer pricing challenges documented, a need was identified to roll this training out to the rest of the audit value chain (Investigative Audit, Customs and Excise Audit) as well as the rest of the CSU. The intention being to impart knowledge awareness of TP, the risk it pose and the implication thereof in the broader risk and audit environments.

To accommodate the broader audience, this product has been revised to include specific local TP tax and Customs legislation relating to valuation.

After attending the course, the learner will be able to:-

- 3. Recognise the applicable South African Transfer Pricing Legislation;**
- 4. Explain the different transfer pricing methodology;**
- 5. Identify current Transfer Pricing trends;**
- 6. Discuss OECD updates on BEPS;**
- 7. Review Significant Canadian Court Decisions; and**
- 8. Discuss transfer pricing risks and remedies**

This course is delivered over a period of two days to SARS employees from different divisions in BAIT, Enforcement, Customs and Legal.

Year to date approximately 264 SARS employees received training on the Introduction to Transfer Pricing.

During May the enhanced TP product was delivered to 55 SARS employees in Cape Town. The primary presenter was Mr. Dale Hill and the co-presenter was Mr. Ricardo Kock from SIOL with the eventual objective being that a transfer of topic presentation skills takes place from Mr. Hill to the SIOL team.

In general, the classes are fully engaged on the topic. The only concerns raised are that learners not placed in the Large Business Centre will not be exposed to Transfer Pricing cases in near

- **Transfer Pricing Seminar**

The Tax, Customs and Excise Institute (TCEI) under leadership of Ms Mamiky Leolo arranged TP seminars in January and May respectively. The January seminar addressed TP in the Mining Industry and the May seminar addressed TP on intangibles, intercompany financing transactions and TP vs. Customs Valuations. Mr Hill was the principle presenter at both the seminars. Approximately 125 employees attended.

- **Transfer Pricing and Customs Valuation Product**

During the May visit, Mr Hill and the SIOL development team designed the scoping document on the TP and Customs Valuation {CV} product.

The purpose of this product is to provide SARS employees a training product which includes the impact of transfer pricing and customs valuations on both the tax and customs risk and audit divisions.

TP risks impacts both the tax revenue in terms of pricing irregularities for goods, services and intangibles between connected persons/ parties; and the customs valuations for imported goods from related persons/ parties. The risks however, affects tax revenue differently as it would affect customs valuations and hence, a greater need for these two audit units within SARS to understand these risks from both a tax revenue perspective as well as from a customs valuation perspective with an aim to identify means of synergising audit efforts attempt to combat these risks.

With reference to the Income Tax Act and Customs regulations, it can be concluded that the TP risks for income tax purposes is that goods, services or intangibles between connected parties might be overstated (not at arms-length) which results in a greater outflow of cash from a South African entity. Whereas, for Customs purposes, the risks is that the goods, imported from a related party may be understated thus, yielding reduced customs duty on these imported goods.

The training product will include the following learning outcomes which were agreed with the subject matter experts in the Tax and Customs Risk and Audit divisions.

1. Explain the significant legal provisions of the relevant Act that pertains to:
 - Customs Valuation and WTO Valuation Agreement
 - Income Tax in relation to Transfer Pricing
2. Distinguish between Customs Valuation Adjustments and Transfer Pricing Adjustments
3. Explain the effect of a Customs Valuation adjustment (on Transfer Pricing) on Income Tax and conversely the effect of a Tax Transfer Pricing Adjustment on Customs Valuation.
4. Discuss the entire process flow from the time that a client/case is selected for Customs and Transfer Pricing risk assessment and handed over to Customs and Transfer Pricing Audit for finalisation.
5. Identify risk indicators for Customs valuation and Transfer Pricing for consideration by case selection and audit
6. Explain the perceived risks that have been identified by Case Selection through data analysis and risk assessment.
7. Identify source documents that can be used during Risk Profiling and Audit.
8. Describe the audit approaches utilised to address the identified Customs Valuation/ Transfer Pricing risks from both a Customs and Income Tax perspective.

3.4 Advanced Pricing Agreements (APA's)

During the initial 2017 discussions, SARS had requested the IMF to assist SARS with the development of APA processes with a view to possibly introducing an APA pilot programme. However, during deliberations of the SARS Base Erosion and Profit Shifting (BEPS) Steering Group in 2019 it became evident that SARS' TP capacity needs strengthening first before an APA programme can be considered.

As such, SIOL and International Relations met with Mr Hill and advised him that SARS would like the IMF's assistance to focus on advanced TP topics and the Integrated TP and Customs Audit programme and that APA assistance will not be required.


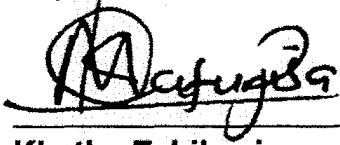

1. Summary of the May 2019 Transfer Pricing Programme

Summary of May 2019 TP Programme		
Date and Intervention	Outcome	Further Action Required
Product Development Workshop <ul style="list-style-type: none"> Introduction to Transfer Pricing Learner Manual Transfer Pricing: An Audit Approach for Customs and Tax – scoping and content Date: 09 May to 14 May 2019 (four days)	Mr Hill and the SIOL development team together met with subject matter experts in KZN and Gauteng to discuss the scoping and content of the products.	<ul style="list-style-type: none"> SARS requested Mr Hill to sign-off on the final product content and quality as a subject matter expert. SARS requested Mr Hill to attend the TP vs CV pilot session in October as a subject matter expert and advisor to the SIOL team.
Seminar: Transfer Pricing Date: 15 May 2019 (one day)	TCEI arranged a seminar on Transfer Pricing on intangibles, intercompany financing transactions and Transfer Pricing vs. Customs Valuations	<ul style="list-style-type: none"> The next TCEI seminar will be held on 16 October 2019 The topic for the next session will be communicated well in advance to Mr Hill
Training: Introduction to Transfer Pricing Western Cape Dates: 16 & 17 May 2019 20 & 21 May 2019 (four days)	<p>The Introductory to Transfer Pricing course was presented to 55 learners in Cape Town.</p> <p>The primary presenter was Mr. Dale Hill and the co-presenter was Mr. Ricardo Kock (SIoL) with the eventual objective being that a transfer of topic presentation skills takes place from Mr. Hill to Mr. Kock</p> <p>Although the topic is regarded as complex, the delivery was pitched at a basic level.</p> <p>The class was fully engaged on the topic and provided valuable input and discussions in the learning environment.</p>	<ul style="list-style-type: none"> The training of this course will continue in October 2019. Mr Kock will be the primary presenter and Mr Hill will be the observer and expert advisor.
Meeting: International Relations, SIOL and Mr Hill on Advance Pricing Agreements	SARS' TP capacity needs strengthening first before an APA programme can be considered	<ul style="list-style-type: none"> The subject on APA's will not be included in this programme. There should be more

Summary of May 2019 TP Programme		
Date and Intervention	Outcome	Further Action Required
		emphasis placed on advanced Transfer Pricing learning and development topics.

2. Conclusion

In conclusion it was agreed that Mr Hill will visit SARS again in October 2019 to present advanced TP training topics, advice and review the new product pilot as well as assess SIOL on the delivery of the Introduction to TP in Alberton. (Annexure B: TP Training Programme: Agenda)

Requestor/Report writer  Magda M Botha Specialists: School of Enforcement Date: 2019/06/18	
Supported/Not supported-  Khathu Tshikosi Senior Manager: School of Enforcement Date: 2019/06/25	Comment:
Approved/Not Approved  Maropeng Sebothoma Executive: SARS Institute of Learning Date: 28/06/2019	Comment: