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Ms Adele Collins
South African Revenue Service
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By email: acollins@sars.gov.za

Dear Ms Collins

**SAICA COMMENTS ON THE DRAFT PUBLIC NOTICES IN RESPECT OF THE
ADVANCE PRICING AGREEMENT PROGRAMME**

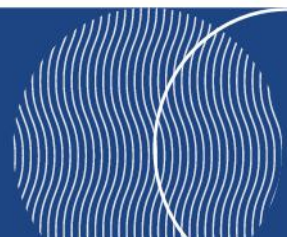
The Transfer Pricing Subcommittee of the South African Institute of Chartered Accountants (SAICA) hereby makes a submission to the South African Revenue Service ('SARS') on the draft public notices issued regarding the Advance Pricing Agreement ('APA') programme, specifically those specified in sections 76C, 76D, 76I, 76J and 76P of the Income Tax Act, 1962 ('the Act'). This submission is made with the kind support and endorsement of the Banking Association of South Africa.

We once again thank SARS for the ongoing opportunity to engage with the public on crucial matters, and look forward to further engagement on this matter.

Christian Wiesener
Chairperson: Transfer Pricing Subcommittee

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The South African Institute of Chartered Accountants



GENERAL COMMENTS

1. Where SARS refers to an application being made under a double taxation agreement (DTA), SAICA recommends that the relevant article of the applicable DTA be identified expressly, for example Article 25 of the OECD Model Tax Convention.
2. The APA programme, in section 76A of the Act, defines the term ‘affected transaction’ as a cross-border intragroup transaction as defined in section 31(1)(a). However, section 31(1) of the Act defines an affected transaction as a cross-border intragroup transaction that is not at arm’s length, i.e. subsections (a) and (b) should be read together. There is ambiguity in that the first paragraph of all six draft public notices states that “*Any term or expression in this notice to which a meaning has been assigned in a “tax Act” as defined in section 1 of the Tax Administration Act, 2011 (Act No. 28 of 2011), has the meaning so assigned, unless the context indicates otherwise.*” However, the term “affected transaction” is defined differently in section 31(1), where affected transaction essentially means a cross-border intragroup transaction, which is not at arm’s length, and section 76A of the Act, where the term is defined with reference to section 31(1)(a) of the Act, which essentially means a cross-border intragroup transaction, which may be at arm’s length or not (i.e., the reference to “not at arm’s length is missing).
3. SAICA therefore recommends that the draft notice refer instead to a “potentially affected transaction” or otherwise make it clear that the reference is only to paragraph (a) of the definition of “affected transaction” in section 31 of the Act.
4. Overall, the rules set out in the South African APA legislation and the draft public notices appear relatively restrictive, and the application process costly.

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| <ol style="list-style-type: none">5. <u>Submission</u>: SAICA submits that the draft public notices should expressly identify the relevant DTA article and either the definition in section 76A of the term “affected transaction” should be amended, or the draft public notices should distinguish clearly between an “affected transaction” as defined in section 31(1) of the Act and a “potentially affected transaction” for purposes of the APA programme.6. <u>SARS should consider sending a strong signal indicating that it is open to entertain APA applications</u> and some suggestions are set out in the submissions to the various draft public notices below. |
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COMMENTS ON THE DRAFT NOTICE IN TERMS OF SECTION 76C – PERSONS ELIGIBLE TO APPLY FOR A DTA ADVANCE PRICING AGREEMENT

7. SAICA notes that the eligibility criteria require reference to anticipated turnover in the year of assessment preceding the year in which a pre-application consultation meeting is requested.
8. In addition, the proposed annual turnover threshold of more than R50 billion per taxpayer is excessively high and appears disconnected from the commercial realities of the South African market. For example, the Country-by-Country Reporting threshold is R10 billion

for consolidated group revenue, as opposed to a single company's revenue, and only approximately 60 MNE Groups in South Africa meet the R10 billion consolidated group revenue threshold. Very few taxpayers in South Africa would meet the R50 billion revenue threshold, which would render the APA programme inaccessible to the vast majority of taxpayers facing genuine transfer pricing complexity and uncertainty.

9. The proposed threshold risks undermining the broader policy objectives of the APA regime. APAs are intended to encourage proactive compliance, provide certainty and reduce disputes before they arise. Restricting access to only a very limited number of exceptionally large taxpayers materially reduces the utility and relevance of the programme.
10. A substantially lower threshold, such as R1 billion in annual turnover, would still target taxpayers with significant and complex cross-border transactions while making the regime accessible to a broader and more appropriate segment of the taxpayer base. This would also better align with international practice, where APA programmes are generally not reserved exclusively for the very largest multinational groups.
11. SAICA also notes that the transactions for which an APA may be requested are limited to the sale of goods, including distribution and manufacturing, and the receipt of services.
12. The draft notice refers to distribution and manufacturing rather than the underlying transactions of the sale or purchase of goods. SAICA considers these to be functional descriptions rather than transactional descriptions and recommends that SARS refer instead to the purchase or sale of goods.
13. SAICA further questions why SARS proposes to consider only the importation of services and not the export of services.
14. The same concern arises in paragraph 2.4.1, where the value parameters for these transactions are stated. A threshold of R1 billion in relation to a distribution or manufacturing function is unclear because it does not indicate whether it refers to turnover from the sale of goods or to costs incurred in respect of the purchase of goods.
15. SAICA also considers that limiting the programme to only the largest multinationals may not be in SARS's best interests. These taxpayers are already a key focus of SARS through its audit programme. Medium-sized multinational groups may also present complex transfer pricing issues and could provide SARS with valuable practical experience across a broader range of industries. Setting the threshold too high would limit the applicability of the APA Programme and send the wrong signal to potential applicants.
16. SAICA further suggests that consideration be given to allowing the parties to enter into a memorandum of understanding governing the APA process and timing, including circumstances involving delays not attributable to the taxpayer, accelerated payment obligations, or a process duration that materially erodes the practical period of APA coverage.
17. Submission: The turnover threshold should be reconsidered and reduced to a more appropriate level, such as R1 billion per taxpayer per annum, so that the APA programme can achieve meaningful practical application in the South African context.

18. The eligibility test should be aligned to the year for which the APA is sought, or the draft notice should clearly explain why the preceding year is the appropriate reference year. This becomes particularly relevant to businesses entering the South African market and wishing to obtain certainty from a transfer pricing perspective.
19. The transactions within scope should be described accurately as the sale or purchase of goods and the receipt or supply of services, and SARS should consider widening the scope of the programme to include a broader range of affected transactions.
20. The exclusion of medium-sized multinational groups should be reconsidered so that taxpayers with significant and complex cross-border transactions are not excluded solely by reason of size.
21. SARS should consider permitting a memorandum of understanding to regulate process assumptions, milestones and timing.

COMMENTS ON THE DRAFT NOTICE IN TERMS OF SECTION 76D – FEES PAYABLE BY AN APPLICANT UNDER THE DTA ADVANCE PRICING AGREEMENT SYSTEM

22. SAICA notes that a cost-recovery fee of R1 million is required for the processing of an application, of which R200 000 is payable within seven days of invoice. In addition, a pre-application fee of R100 000 is payable, and both fees are non-refundable. It is noted that the fees appear to be on the higher side when compared with international levels, which may result in potential applicants deciding against pursuing an APA application.
23. It is further noted that SARS may request additional amounts from the applicant as part of the cost-recovery fee. Given the non-refundable nature of these amounts, applicants face significant uncertainty regarding the total cost of participation, particularly as the basis of the cost recovery, such as hourly rates or other cost components, is not disclosed.
24. It is also noted that, once an application has been received, SARS must consult the competent authority of the other country to obtain agreement to proceed with the application, and that the application will be rejected if that authority does not agree.
25. The timing of these steps relative to the payment obligations is unclear.
26. In particular, it is not clear whether the fees must be paid before SARS engages with the other competent authority and before the applicant is informed whether the application will proceed.
27. Submission: SAICA recommends that the sequencing of payment and acceptance steps be stated more clearly so that applicants understand what amounts must be paid before it is confirmed that the application will be considered.
28. Alternatively, a portion of the fee should be refundable where the application cannot proceed because the other competent authority does not agree to the process.
29. The timing of payment obligations should also be clearly linked to the procedural stages of the APA process rather than only to the issue of invoices.

30. It would also be helpful if SARS could consider and identify circumstances in which a refund of fees would be appropriate, particularly where an application cannot proceed for reasons beyond the taxpayer's control.
31. Furthermore, SAICA recommends that SARS puts in place a fee framework in order for the applicant to be able to estimate the fees to be charged by SARS.
32. In addition to the above, the draft notice addresses the fees payable by a South African applicant in relation to a proposed bilateral APA. However, there appears to be no equivalent clarification where a bilateral APA is initiated from abroad.
33. Submission: Clarity is required regarding the process to be followed in such a case, including whether the South African entity will be required to pay fees once the application is accepted by SARS from the foreign revenue authority.
34. The draft notice (*REQUIREMENTS FOR PROCESSING AN APPLICATION FOR A DTA ADVANCE PRICING AGREEMENT IN TERMS OF SECTION 76J(1) OF THE INCOME TAX ACT, 1962 (ACT NO. 58 OF 1962)*) provides that, where practical, functional analysis interviews, site visits and information gathering will be coordinated and conducted jointly.
35. However, no guidance is given on the allocation of the costs associated with such activities, particularly site visits undertaken by competent authorities.
36. Submission: Clarity is required on who will bear the costs of travel, accommodation and related expenses. In the absence of explicit guidance, this uncertainty may create practical difficulties and deter participation in the APA programme.

COMMENTS ON THE DRAFT NOTICE IN TERMS OF SECTION 76I(b) – REJECTION OF AN APPLICATION FOR A DTA ADVANCE PRICING AGREEMENT

37. SAICA is concerned about several of the proposed criteria that may result in the rejection of an application.
38. The issue of whether the competent authority of the other country is willing to engage is material and should be taken into account in relation to the timing and refundability of fees, as noted above.
39. In addition, certain rejection criteria refer to transactions that would fall within Part IIA of the Income Tax Act dealing with impermissible tax avoidance arrangements.
40. As such transactions are already addressed under that statutory framework, SAICA does not consider it appropriate to include them again as a separate basis for rejection within the APA framework.
41. The draft notice further states that an application may be rejected if it concerns an issue that is the same as, or substantially similar to, an issue subject to dispute resolution under Chapter 9 of the Tax Administration Act or an article of an agreement for the avoidance of double taxation.
42. However, the notice does not define what is meant by "an issue". Clarification is required as to whether this refers to:

- a specific transaction,
 - a transfer pricing methodology,
 - a tax position adopted by the taxpayer, or
 - a broader set of related facts and circumstances.
43. Without a clear definition, the provision may be applied too broadly and may exclude applications merely because there is some overlap with matters under audit, objection or dispute.
44. Furthermore, the rejection of an application that relates to a transaction previously subject to a tax dispute or mutual agreement procedure appears inappropriate.
45. While SAICA acknowledges that SARS may not wish to permit rollback arrangements for years already under dispute, a forward-looking APA covering the same transaction should not necessarily be barred where the historical matter has already been resolved.
46. It is also recommended that SARS provide context or examples of what it considers to be “frivolous or vexatious” for purposes of the rejection criteria.
47. Furthermore, the proposed ground for rejection where the applicant fails or refuses to provide additional information requested by SARS is drafted very broadly.
48. SAICA recommends that this be refined so that only information directly relevant and necessary to the evaluation of the covered transaction may give rise to rejection if not provided.
49. Another pertinent issue is the treatment of taxpayer information submitted as part of an APA application.
50. The draft notice does not indicate whether such information will be ring-fenced within the APA process or may be shared with other SARS divisions. In the absence of express protection, applicants may be concerned that information submitted in good faith could be used for general audit, risk profiling or enforcement purposes if the application is rejected or withdrawn.
51. The notice also appears to permit rejection merely due to a lack of SARS resources.
52. If an applicant has already paid significant non-refundable fees before the application is rejected on this basis, it is submitted that the absence of a refund mechanism would be unreasonable.
53. Finally, if one of the objectives of the pilot programme is to enable SARS to build experience, limiting the programme to only goods and services transactions may not achieve that aim.
54. SAICA therefore suggests that SARS consider allowing applications in respect of a broader range of transactions and assessing admissibility on the merits of each application rather than excluding categories of transactions in advance.

55. Submission: In summary, it is submitted that:

56. References to impermissible tax avoidance arrangements should be removed from the rejection criteria, as those arrangements are already dealt with under the Act.
57. The term “issue” should be clearly defined or limited so that the provision is applied narrowly and does not exclude applications unnecessarily.
58. The notice should clarify that a forward-looking APA is not automatically barred merely because a similar transaction was historically the subject of a dispute or MAP process.
59. Examples or interpretive guidance should be provided for the phrase “frivolous or vexatious”.
60. Requests for additional information should be limited to information that is directly relevant and necessary to the evaluation of the APA application.
61. Information submitted in support of an APA application should be expressly ring-fenced within the APA process and not shared with other SARS divisions if the application is rejected or withdrawn.
62. Where an application is rejected due to SARS resource constraints or other factors beyond the taxpayer’s control, an appropriate refund mechanism should be included.
63. SARS should consider opening the pilot programme to a broader range of transactions and determining admissibility on a case-by-case basis.

COMMENTS ON THE DRAFT NOTICE IN TERMS OF SECTION 76J(1) of the Act – POSITION PAPERS AND COMPETENT AUTHORITY NEGOTIATIONS

64. Paragraph 2.5 states that the applicant will not have a direct role during the preparation of position papers or in the subsequent negotiations between the competent authorities.
 65. However, the meaning and intended scope of the term “direct role” are unclear and require clarification.
 66. It is not evident whether the applicant may nevertheless have an indirect role in the process and, if so, the nature and extent of such participation.
 67. For example, it is unclear whether the applicant may provide input on factual matters to ensure accuracy, review or comment on draft position papers to confirm that the facts are correctly stated, respond to queries raised by the competent authorities, or make supplementary submissions where necessary.
 68. In the absence of clarity, the provision may be interpreted as excluding any form of participation by the applicant beyond the initial submission, which could limit the accuracy and completeness of the information available to SARS and the competent authorities.
69. Submission: SAICA recommends that the notice should clarify expressly whether any indirect role for the applicant is envisaged and, if so, should define the permissible scope of that participation. This would enhance transparency and assist in ensuring that the factual record before the competent authorities is complete and accurate.

COMMENTS ON THE DRAFT NOTICE IN TERMS OF SECTION 76J(3) – INFORMATION TO BE CONTAINED IN A PRELIMINARY DTA ADVANCE PRICING AGREEMENT

70. Paragraph 2.11 requires certain information relating to the relevant transaction to be included in the APA application, including the arm's length transfer price and the arm's length allocation. This wording appears to assume that both SARS and the taxpayer have already agreed that the proposed pricing or allocation is arm's length.
71. However, if the outcome of the APA process is an adjustment, as envisaged elsewhere in the draft notice, that wording may imply that the initial position was already arm's length when that may not be the case.

72. Submission: SAICA submits that paragraph 2.11 should be revised so that it does not appear to presuppose agreement on the arm's length nature of the pricing or allocation before the APA process has been concluded.

COMMENTS ON THE DRAFT NOTICE IN TERMS OF SECTION 76P – PROCEDURES AND GUIDELINES FOR THE IMPLEMENTATION AND OPERATION OF THE DTA ADVANCE PRICING AGREEMENT

73. Paragraph 2.3 appears to envisage a situation in which an APA application may include rollbacks to years that may already have prescribed under section 99 of the Tax Administration Act.
74. However, SAICA understands the APA programme to be a prospective mechanism intended to provide certainty for current and future years.
75. In addition, section 76l(b) of the Act indicates that APAs may not be accepted where they relate to transactions already subject to a dispute under Chapter 9 of the Tax Administration Act.

76. Submission: SAICA therefore submits that the drafting of paragraph 2.3 should be reconsidered to ensure alignment with the prospective purpose of the APA programme.

77. It would also be beneficial for SARS to indicate the extent of any reporting on APAs to external bodies such as the OECD, as taxpayers considering entering into an APA would need to be aware of this to make an informed decision as to whether to proceed.

END.