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Submission File

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South African Revenue Service
Private Bag X923
Pretoria
0001

BY E-MAIL:

Dear SARS

COMMENTS ON THE DRAFT AMENDMENTS TO THE RULES UNDER SECTIONS 40(3)*(a)*(I)(C) AND 41(4)*(b)* AND 120 OF THE CUSTOMS AND EXCISE ACT 1964

We herewith take an opportunity to present our comments on behalf of the South African Institute of Chartered Accountants ("SAICA") on the draft amendments to the rules under sections 40(3)*(a)*(i)(C) and 41(4)*(b)* and 120 of the Customs and Excise Act 1964.

We once again thank SARS for the ongoing opportunity to provide constructive comments in this regard.

SAICA continues to believe that a collaborative approach is best suited in seeking solutions to complex challenges and should you wish to clarify any of the above matters please do not hesitate to contact us.

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Yours sincerely

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The South African Institute of Chartered Accountants

1. We understand that this rule is intended to address the **manner** in which bills of entry may be adjusted as a result of a transfer pricing adjustment (as defined in the draft amendments) and the **process** to be followed as set out in the draft amendments:

   "The following rule is hereby inserted after rule 40.02:

   *"**Manner** in which bills of entry may be adjusted where customs value declared is affected by transfer pricing adjustments*

   *40.03 Where, as a result of a transfer pricing adjustment contemplated in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, an adjustment to a bill of entry is required in terms of section 40(3)(a)(i) in relation to the customs value of goods, the **relevant bills of entry may be adjusted by following the process** contemplated in rule 41A.01.".*

2. The draft rules define a transfer pricing adjustment as:

   *"transfer pricing adjustment" in relation to the customs value of goods, means an adjustment contemplated in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, **to the price** at which goods were imported into the Republic by a multinational enterprise;"* (our emphasis)

3. The OECD Guidelines are intended to provide guidance on the implementation of Article 9 of the OECD Model Tax Convention between contracting parties to a Double Tax Convention. Article 9 sets out the taxing rights of the parties to the convention when Associated Enterprises enter into transactions which are not conducted under terms and conditions considered to be arm's length.

4. Article 9 specifically provides for an adjustment to **profits** where the profits of an enterprise of a Contracting State are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises.

5. The OECD Guidelines are also not binding on a state unless the domestic legislation of that state so provides. They are intended as a guideline for contracting states to use in implementing their domestic transfer pricing legislation.

6. South Africa's transfer pricing legislation is contained in Section 31 of the Income Tax Act ("the Act"). Section 31 allows for SARS to make an adjustment to the **taxable income** of a person as defined, if any of the terms and conditions under which the transaction occurs are not consistent with the arm's length principle.

7. Furthermore, it is noted that the term "transfer pricing adjustment" may also apply in certain circumstances where an importer's taxable profit is increased or decreased as the case may be by virtue of a debit note or a credit note, which would increase/decrease the cost of goods sold subsequent to the transaction but before the financial accounts are closed for the year.

8. The purpose of this is for the importer to achieve an arm's length profitability. This is often referred to as self-affected true-up/retrospective or year-end adjustment.

However, this adjustment ensures arm's length pricing and is therefore not subject to Section 31 of the Act.

9. Given the wider implications that arise and for the fact that the OECD Guidelines do not provide SARS or a taxpayer with the legal basis to make a transfer pricing adjustment it is requested that SARS revisit the definition and provide clarity.

10. Furthermore, the definition of "transfer pricing adjustment" should be clarified.

11. At this point it is not possible for us to provide further comment on the process of adjustment to a bill of entry as a result of a transfer pricing adjustment until SARS clarifies the definition of transfer pricing adjustment.

12. In the interest of time, however, we have further comments as set out below, but we note that depending on what the definition of "transfer pricing adjustment" will be, these comments may change.

13. We would be happy to discuss further once the definition of the term has been clarified/confirmed.

Credit notes and debit notes

14. The draft rules state that where, as a result of a transfer pricing adjustment as contemplated above, "*an exporter has effected an amendment to an invoice by issuing an amended invoice or a debit or credit note to reflect any transfer pricing adjustment, the importer must within the timeframe referred to in section 41(4)(b)(ii)(bb) disclose the circumstances of such transfer pricing adjustment to SARS by submitting a letter of notification on the letterhead of the importer*" –

15. The following is noted.

16. If the exporter effects a credit note or debit note as a result of the identification that the transaction price does not comply with the arm's length principle, the exporter has corrected the price to an arm's length amount. If this is undertaken pre the year-end financials being closed, there will be no transfer pricing adjustment made under section 31 of the Act thereby nullifying the draft rule.

17. Where the transfer pricing adjustment is effected by the South African importer on the ITR14 income tax return, there will be no credit note or debit note as the adjustment is an income tax adjustment only.

18. Where the transfer pricing adjustment is made as a consequence of a transfer pricing audit by SARS, there will also be no credit note or debit note.

19. The requirement for a credit or debit note is confusing in the context of a transfer pricing adjustment as contemplated in the OECD Guidelines and should be clarified.

20. Clarity needs to be given on the process for applying for a customs duty adjustment where the transfer pricing adjustment is made by the importer on the tax return, or where the adjustment is made by SARS.

Timing

21. The draft rules state "*the importer must within the timeframe referred to in section 41(4)(b)(ii)(bb) disclose the circumstances of such transfer pricing adjustment to SARS".*

22. Section 41(4)(b)(ii)(*bb*) states "*the importer shall produce such amended invoice or certificate or credit or debit note to the Controller within one month of receipt thereof and report the circumstances to him".*

23. The following is noted:

24. Income tax is an annual event and a transfer pricing adjustment made by a taxpayer is made in the ITR14 income tax return prior to submission. Typically, this is 12 months following the end of the financial year in which the transaction giving rise to the adjustment occurs.

25. Where a transfer pricing adjustment is made by SARS as a result of a transfer pricing audit, this could be several years after the end of the year in which the transaction giving rise to the adjustment occurred.

26. It is therefore clear that the timing as indicated in section 41(4)(b)(ii)(*bb*) needs clarification for these circumstances.

27. The time limit for these circumstances needs to be incorporated into the draft rules. The following suggestion is made:

28. The timing for application for a customs duty adjustment be references to the finalisation of the transfer pricing adjustment for income tax purposes to align with the crystallisation of the incidence of double taxation as envisaged in Article 9; for instance the date of assessment where the taxpayer makes the adjustment in the ITR14 tax return, or the date of the additional assessment where the adjustment is made by SARS.

29. The draft rules state that an "*"adjustment period" means the accounting period to which the transfer pricing adjustment relates."*

30. Clarity is sought regarding the timing of correction of a bill of entry. If an importer is required to amend retrospectively in the accounting period, this could have other implications requiring for example, the restatement of financial statements.

Supporting documentation

31. The draft rules require substantial documentation to be submitted in support of the application for a customs duty adjustment. As indicated above, a transfer pricing adjustment as contemplated in the OECD Guidelines is undertaken to determine the taxing rights of contracting parties to a double tax convention when the terms and conditions do not comply with the arm's length principle. As also indicated above, in South Africa, such an adjustment would be made under section 31 of the Act.

32. Whether the adjustment is made by the taxpayer or by SARS following an adjustment, many of the documents referred to in the draft rules would not be available.

33. The documentation requirements need to be revisited in light of the intended rules relating to a transfer pricing adjustment as contemplated in the OECD Guidelines. The following suggestion is made.

34. A copy of the ITR14 income tax return evidencing the transfer pricing adjustment made by the taxpayer in the event the adjustment is voluntarily made by the taxpayer, or a copy of the Finalisation of Audit Letter from SARS together with the additional assessment in the case where the transfer pricing adjustment is made by SARS.

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