

# COUNTRIES' EXPERIENCE REGARDING BASE EROSION AND PROFIT SHIFTING ISSUES – SOUTH AFRICA

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- 1) The negative impact of base erosion and profit shifting (BEPS) on South Africa is evident in the escalating rates of poverty, inequality and unemployment. This continues despite some impressive developmental strides taken by the government (Oxfam, 2012). The reason for this is that only 1.6 out of 2 million registered companies in South Africa are active and pay their tax revenue (Oxfam, 2012). This shows that about 400 000 registered companies are not paying taxes, thus resulting in loss of *fiscus* for the country. As a result, this reduces the ability of the government to provide the socio-economic rights like housing, health and education for the people in the country (Dlamini and Tromp, 2014). One would assume that since the MNE's are capable of profit shifting, they are amongst the companies that are not paying taxes.
- 2) The most common practice or structure used for base erosion and profit shifting is the weak or rather lenient tax regime in South Africa. The much needed foreign investment from multinational enterprises provides these companies with the advantage of lobbying for favourable tax rates from the government, which then results in them being able to erode the profits from their tax base and shift it to tax havens. The South African government is mostly involved in granting tax incentives to MNEs in the Industrial Development Zone (IDZ) programmes such as the automobile and mining industries (Dlamini and Tromp). Another weakness that the MNE's take advantage of, is the inability of the South African government to negotiate favourable tax treaties, monitoring and addressing the abusive tax practises. This is clearly the result of a political offensive on developing countries to keep them in a weak economic and political situation. It is thus, not an accident but a conscious strategy that has been propagated and put into action by the World Bank, the International Monetary Fund, World Trade Organisation, a host of Transnational Corporations on whose behalf the afore-mentioned multilateral organisations were doing the bidding.

We must not exclude powerful aid agencies which connived with these institutions to privatise and deregulate our economies in the name of economic competitiveness, via promoting of exports and reducing taxes amongst others – all in the search for Foreign Direct Investment (FDI).

Therefore, the lawyers and economists employed by MNEs to negotiate favourable tax rates are part of the strategy but the mandate has already been made. This pressure is thus placed on our governments to adopt templates of laws that are deliberately crafted in a weak manner, with weak regulation on corporations.

It is this very excuse that corporations like Google and Starbucks used when the Parliamentary Committee on Finances in the UK highlighted their miniscule corporate tax contributions: they were merely following the law. They did not say, that they – collectively – ensured that the law was deliberately weak or market friendly.

Civil Society Organisations (CSO) and the NGO's have been lobbying the government for transparency of their contracts with the MNEs so that they can monitor the payment of the fair share of tax by MNEs and that the government does not offer unnecessary tax incentives to companies. The South African government is also encouraged to engage in bilateral agreements with other African countries so that they do not compete for the investment from the MNEs but work together to reduce base erosion and profit shifting in developing countries.

- 3) The entry point would be to assess whether they have committed to avoid harm by adopting the 'polluter pays principle.' For this reason, we must start with the externalities that extractive – mining in particular impose on poor communities in the forms of injuries, poor health and deaths. This includes environmental degradation and harm to animal life and community livelihoods.

If they comply with these, we can then start to talk about the value of the weight of gold, or platinum, the needs of workers (wages and working conditions) and the control of corporate chief executives play.

In addition, they must ask if there is local employment or opportunities for self-employment creation and beneficiation. Therefore a total scrutiny about how business is done should be included.

However the question of what is deemed ‘an appropriate tax share’ for the MNEs to pay is a difficult one to answer. This is largely due to the lack of transparency of contracts between governments and MNEs.

As a result, monitoring and evaluation for purposes of accountability proves a profound hurdle in combating corruption on all levels. It is thus difficult to ascertain whether the MNEs have reported the correct amount of profit.

The methods of assessing base erosion and profit shifting must be on a project by project basis, and all countries must be part of the compact. We note that there is progress now, because of the financial crisis hitting particularly the advanced economies, which has resulted in a crisis of leadership particularly of the corporations and western governments. There is a hope that this attempts to regulate MNEs corporate behaviour will result in a change in priorities away from excessive greed – growth model, that benefits only a few.

- 4) The main problem that has been encountered in assessing whether the appropriate amount of profit is reported and tax paid on such profit is that of transparency. This is because the tax regime in South Africa does not require MNEs to report on their transactions outside of South Africa and this makes it difficult to know whether the company has shifted their profits to tax havens (Curtis,2011). Another issue is the inability of the authorities to monitor or address harmful tax practices from these companies as a result of their lack of expertise.
- 5) To a certain degree, we are of the opinion that these points are not far reaching but limited to experiences of countries in the developed world. This is further elaborated upon in our submission which calls for a UN-led approach towards BEPS.
- 6) The most important OECD action points we see as important for our country are Action Points 12, 13, 11 and 6. We foresee these priorities changing overtime depending on the progress made and compliance thereof. This is because according to

the economic principle of marginal cost and marginal benefit, that assumes that a person or business is in equilibrium when marginal cost is equal to marginal benefit.

The moment the marginal cost is higher than marginal benefit, then the consumer would reduce their consumption of that product, so as to remain in equilibrium. Therefore by increasing the cost of tax avoidance, it would be expected that the companies will reduce their consumption of tax avoidance.

- 7) Yes, we believe that Action points 3, 5, 7, 14 and 15 are also of importance to the developing countries.
- 8) With regard to other recommendations please find the attached copy of our recent submission on BEPS to the national Davis Tax Committee, who has been tasked with reviewing the current South African tax regime.
- 9) Please refer to both the submission to the BEPS sub-committee (Davis Tax Committee) as well as the Recommendations made by the African civil society organisations.
- 10) Yes.