REGULATORY REQUIREMENTS PERTAINING TO OWNERSHIP, OPERATIONAL AND FINANCIAL DISCLOSURE IN SOUTH AFRICA

BENEFICIAL-OWNERSHIP AND TAX-BENEFIT DISCLOSURES

WORKING PAPER **ONE**

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1. Introduction

There has been an increased focus on corruption in recent times, particularly in terms of the role of the private sector and its harmful effect on state economies. With the spotlight increasingly being shone on the activities of multinational companies and their attempts to exploit loopholes in order to evade taxes and maximise tax benefits, countries across the world are adopting coordinated approaches to close the gaps that are adversely affecting the ability of governments to generate tax revenue.[1] Also, with increasingly scarce resources and the ever-increasing divide between the rich and poor globally, it has finally been recognised that inequality is one of the most significant problems that threaten our world today and that illicit financial flows, particularly from developing countries, need to be tackled head-on with a view to addressing this crisis.[2] In its most recent report, Oxfam notes:

> [About] *a third of rich Africans' wealth – a total of $500bn – is held offshore in tax havens. Oxfam's finding shows that the problem of illicit financial flows is not* [only] *about foreign exploitation of African resources or repatriation of profits by multinationals,* [but] *is also about wealthy, powerful and educated Africans contributing to the continued underdevelopment of the continent* [for the purpose] *of personal gain. It is estimated that these activities costs African countries $14bn a year in lost tax revenues.*[3]

These are revenues that could be used for health care and education in Africa. It is against this background that the International Bar Association has rightly described tax avoidance as a form of human rights abuse.[4]

There are two particular initiatives that have gained prominence in recent times. The first concerns disclosure of the ultimate 'beneficial' owners of the profits of a company, while the second concerns the true beneficiaries of various tax benefits and arrangements. These recipients are usually hidden behind the veil of corporate structures across different jurisdictions and have been the subject of intense research across different structures.

The purpose of this working paper is to determine whether the disclosure regime in South Africa that is applicable to the extractive industry creates a satisfactory framework for the discovery of beneficial ownership and tax-benefit arrangements in order to ensure adequate state oversight and the enforcement of accountability in the extractive industry. This paper therefore focuses on 'ownership, operational and financial'[5] disclosure requirements in the extractive industry in South Africa.

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1 'A new global partnership: Eradicate poverty and transform economies through sustainable development: The report of the High-Level Panel of Eminent Persons on the post-2015 development agenda', 2013, United Nations.

2 'Illicit financial flows from developing countries: Measuring OECD responses', 2014, Organisation for Economic Co-operation and Development. Oxfam's 2016 report showed that the total wealth of the richest 62 individuals in the world equalled that of the 3.6-billion people with the lower half of the world's income. Oxfam further calculated that USD7.6 trillion of individual wealth was held offshore in tax havens – 'An economy for the 1 percent – briefing paper' (hereafter 'Oxfam briefing paper'), 2016, Oxfam. In addition, Thomas Piketty, in his book, *Capital in the 21st century*, argues that the question of inequality has not been centre stage of economics research and that the division of income from production between labour and capital remains at the heart of distributional conflict.

3 Oxfam briefing paper, p. 5.

4 Ibid.

5 In general terms, 'ownership information' means information held by companies that relates to operational licences and beneficial interests in listed companies, 'operational information' means information held that is relevant to the functioning of a company, particularly with regard to the production and extraction of mineral resources, and 'financial information' broadly means the various forms of payment made by corporations to various governments, which payments include taxes, royalties and other prescribed payments.

2. Background

In 2013, the South African government announced the establishment of a tax-review committee to assess South Africa's 'tax policy framework and its role in supporting the objectives of inclusive growth, employment creation, development and fiscal sustainability taking into account recent domestic and global developments' (the Davis Tax Committee).[6] The Committee is headed by Judge Dennis Davis. In its first interim report on mining, released in December 2015, the Committee attempted to propose sustainable approaches that take into account the current vulnerabilities in the mining industry.[7] While the Committee did not deal with the question of tax-benefit disclosures or beneficial ownership in its report, it supported all meaningful attempts by the state to enhance existing reporting and transparency efforts, such as considering joining the Extractive Industries Transparency Initiative (EITI).[8]

However, the Davis Tax Committee, in its interim report on base erosion and profit-shifting (BEPS Interim Report), addressed the problem of transfer pricing, which involves companies inaccurately 'pricing their charges on goods and services in an effort to transfer profits and expenditure between jurisdictions'. This is usually done by companies so as to minimise tax exposure.[9] In the BEPS Interim Report, the Committee indicated that the lack of a clear meaning relating to beneficial ownership lessens the potential advantages of beneficial-ownership disclosures, particularly in relation to the prevention of treaty abuse.[10] A problem that the Committee appears keen to address is that of multinational companies relying on double-taxation agreements to completely avoid the payment of taxes in their home and host countries. The Committee's Report suggested that, in order to curb tax evasion, not only beneficial ownership but also the problem of treaty-shopping needs to be addressed.[11]

While the Davis Tax Committee was tentative about the matter of beneficial ownership and sought a broader solution to the problem of treaty-shopping and tax avoidance, the South African Cabinet, in its 2015–2017 Open Government Partnership Action Plan, has reiterated its commitment to introduce and implement South Africa's Action Plan on the G20 High-Level Principles on Beneficial Ownership Transparency.[12] The aim is to improve transparency in relation to legal persons and arrangements in order to protect the integrity and transparency of the global financial system.[13] This process involves the:

> *establishment of an inter-departmental committee responsible for developing, implementing and reporting on a country implementation/action plan and the development of the country implementation plan in order to address the challenge of transparency of legal persons and arrangements in the global financial system.*[14]

The Financial Intelligence Centre (FIC) Amendment Bill was also recently tabled in Parliament in a bid to improve South Africa's anti-money laundering laws.[15] The concept of beneficial ownership has been introduced in the Bill, as well as the term 'foreign and domestic prominent influential persons'.[16] The aim of introducing these concepts is to assist financial institutions in properly identifying their

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6 Davis Tax Committee, 'First interim report on mining', 2014, p. 14.

7 Ibid, p. 13.

8 Ibid, p. 115.

9 Ibid, p. 116.

10 This relates to double-taxation agreements which are sometimes used by corporations to avoid taxes altogether.

11 Davis Tax Committee, 'Preventing base erosion and profit shifting in South Africa', 2014, p. 18.

12 Department of Public Service and Administration, 'The 3rd South African Open Government Partnership action plan 2015–2017', 2015, p. 12.

13 Ibid.

14 Ibid.

15 B-2015.

16 See the definitions section of the Bill. 'Beneficial owner', in respect of a juristic person, means a natural person who, independently or together with a connected person, and directly or indirectly, including through bearer shareholdings, (a) owns the juristic person or (b) exercises effective control over the juristic person.

In its first interim report on mining, released in December 2015, the Committee attempted to propose sustainable approaches that take into account the current vulnerabilities in the mining industry.

clients, thereby enabling such institutions to apply appropriate standards of due diligence.[17] It also provides that accountable institutions must keep identity and verification records, as well as transaction records, in order to conduct ongoing due diligence that includes prominent influential persons, their families and associates. While this process is very much in its initial stages, it does signify a positive move towards a global regulatory regime for addressing illicit financial flows.

As South Africa joins the global effort to combat tax evasion and promote financial transparency, it is necessary to understand the content of the current global initiatives and how these might shape current and future developments in South Africa.

3. Global initiatives regarding beneficial-ownership and tax-benefit disclosures

A basis for the assessment of beneficial-ownership and tax-benefit disclosures is the EITI model introduced in 2014, a model that had been recommended for adoption by the Davis Tax Committee.

The aim of the EITI beneficial-ownership project is to reveal the ultimate beneficiaries of the activities of a company. The EITI recommends that implementing countries should 'maintain a publicly available register of the beneficial owners' of corporations that 'bid for, operate, or invest in extractive assets', as well as of their level of ownership.[18]

Through this register, the EITI is seeking to increase the tax-collection capacity of government and believes that the resultant openness will lead to a more credible process involving government and companies.[19] In a bid to build accountability within the corporate sector and enable public revenue to be monitored, companies operating in EITI-participating countries will be required to disclose their payments to the host government.

Although the EITI is a voluntary mechanism, its influence has led to the introduction of mandatory regulations by countries, regulations that have seen the introduction of similar rules relating to disclosures by public companies. In the United States of America (USA), the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 ('the Dodd–Frank Act') requires the disclosure of tax and other payments to host governments by extractive-industry companies listed with the United States (US) Securities and Exchange Commission (SEC). In terms of the Dodd–Frank Act, disclosures must include: the total amounts of the payments, by category; the currency used to make the payments; the financial period in which the payments were made; the business segment of the resource-extraction issuer that made the payments; the government that received the payments, the country in which the government is located; and the project of the resource-extraction issuer to which the payments relate.[20]

17 See IMF report above.

18 See https://eiti.org/pilot-project-beneficial-ownership.

19 A. Ravat & S.P. Kannan, *Implementing EITI for impact: A handbook for policy makers and stakeholders*, 2013, World Bank.

20 Section 1504 of the Dodd–Frank Act.

In a bid to optimise tax collection globally, and to curb illicit financial flows, 30 countries recently adopted a cooperative tax model designed to improve tax compliance while promoting transparency.

However, the implementation of the aforegoing was successfully challenged by corporate entities, and, as a result, the SEC was obliged to redraft the relevant provision of implementation in June 2016.

Other countries such as Norway, Canada, the United Kingdom (UK) and the European Union (EU) have adopted similar rules to the EITI model, rules that focus more on tax payments by multinationals to governments than on the tax breaks and benefits to be enjoyed by these multinationals.

Another initiative that is gaining traction is the Model Tax Convention led by the Organization for Economic Co-operation and Development (OECD). In a bid to optimise tax collection globally, and to curb illicit financial flows, 30 countries recently adopted a cooperative tax model designed to improve tax compliance while promoting transparency.[21]

The OECD Model Tax Convention deals with beneficial ownership but does not define it. According to the commentary on the Convention, 'beneficial ownership has been introduced in the OECD model treaty to try to eliminate the avoidance of (withholding) taxes in especially structured transactions'.[22] However, the Convention adopts a definition used in the International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation developed in 2012, as developed by the Financial Action Task Force. The Standards define beneficial owner as 'the natural person(s) who ultimately owns or controls a customer and/or the person on whose behalf a transaction is being conducted. It also incorporates those persons who exercise ultimate effective control over a legal person or arrangement.'[23]

The EU Anti-Money Laundering Directive defines a beneficial owner as 'any natural person(s) who ultimately owns or controls the customer and/or the natural person on whose behalf a transaction or activity is being conducted'.[24] The Directive suggests that, in the case of corporate entities, a beneficial owner would be a natural person who:

> *ultimately owns or controls a legal entity through direct or indirect ownership or control over a sufficient percentage of the shares or voting rights in that legal entity, including through bearer share holdings, other than a company listed on a regulated market that is subject to disclosure requirements.*[25]

The Directive further recommends that 'a percentage of 25 percent plus one share shall be evidence of ownership or control through shareholding and applies to every level of direct and indirect ownership'.[26] This establishes a threshold requirement in determining the calibre of beneficial owners that the EU Directive is more concerned about.

21 OECD, '2014 update to the OECD Model Tax Convention', 2014.

22 Withholding taxes in this case are recommended so that governments can curb tax avoidance by making sure that a portion of the income payable to someone in a different jurisdiction is paid to the foreign government as tax. See also: S. Kilonzo, 'Benefits and costs of the IFF targets for the post-2015 development agenda', 2015, working paper, Copenhagen Consensus; 'OECD Model Tax Convention: Revised proposals concerning the meaning of "beneficial owner" in articles 10, 11 and 12'.

23 Ibid; OECD Model Tax Convention commentary, p. 12.

24 Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 L141/86.

25 Ibid.

26 Ibid, article 3(6)(a)(i).

The Africa Mining Vision and its Action Plan prioritise tax harmonisation, transfer pricing and beneficial ownership as concerns to be addressed by way of regulation.

In the context of Africa, there have been similar developments aimed at establishing regional convergence around beneficial-ownership and tax-benefit disclosures. The Africa Mining Vision and its Action Plan prioritise tax harmonisation, transfer pricing and beneficial ownership as concerns to be addressed by way of regulation.[27] In the 2015 African Union (AU) report on illicit financial flows (IFFs), transparency was considered as key across all aspects of such flows and the AU panel recommended proposals such as:

> *the automatic exchange of information, country-by-country reporting, project-by-project reporting, disclosure of beneficial ownership, public information about commercial contracts that African governments enter or implementation of the recommendations of the Financial Action Task Force.*[28]

South Africa was among the AU countries that adopted the Africa Mining Vision in 2009. However, the Vision is currently not being funded by African governments, and, as a result, realisation of the objectives of the Vision has stalled. South Africa has also committed to implementing other global initiatives, such as the G20 High-Level Principles on Beneficial Ownership Transparency through its Open Government Partnership commitment referred to above. Despite this commitment, South Africa's laws currently provide very limited scope for the implementation of these initiatives and an overhaul of the regulatory framework of the country might be necessary.

4. Beneficial-ownership disclosures in South Africa

To achieve beneficial-ownership disclosures in South Africa, an audit of the laws and regulations applicable to the disclosure of ownership information by companies is first of all necessary. This has been done in the Open Society Foundation (OSF) report on the disclosure of ownership, operational and financial information, a report which forms the basis for this working paper. Secondly, an audit of companies' registers, of mechanisms for reporting ownership information to the different oversight institutions, and of the extent to which this information is publicly available, is also necessary. The accuracy and verifiability of the information recorded in the registers and reports are also central to maximising the value of beneficial-ownership disclosure. Some of the salient features of the laws and regulations applicable to beneficial-ownership disclosure in South Africa are briefly enumerated below.

4.1 The Companies Act 71 of 2008

In South Africa, the Companies Act regulates corporations. While the term 'beneficial ownership' is not defined in South African law, the Companies Act requires every company to maintain records relating to its Memorandum of Incorporation, directors, annual general meetings, annual financial statements and accounting, notices and minutes of all meetings of shareholders, and its securities

27 O. Bello, 'Africa's extractive governance architecture: Lessons to inform a shifting agenda', 2014, SAIIA policy briefing.

28 'Illicit financial flows: Report of the High Level Panel on illicit financial flows from Africa commissioned by the AU/ECA Conference of Ministers of Finance, Planning and Economic Development (hereafter 'Illicit financial flows report'), 2015, p. 67.

register.[29] The Act further provides for people who hold 'beneficial interests'[30] in the securities of the company to have access to these records. Other persons may access these records on payment of a fee in accordance with the Promotion of Access to Information Act (PAIA).

The Companies Act also provides for information on a company's directors to be disclosed and for a securities/shareholder register to be publicly available.[31] Section 24(1b) of the Companies Act requires companies to keep information on former directors and shareholders for a period of seven years.

In addition, section 25 of the Act requires that transactions in respect of listed securities that result in a change of beneficial ownership must be reported to the Registrar. The Registrar may list the information required for reporting, as well as the time frames and manner according to which the report must be submitted. Section 25(3) stipulates that the Registrar must disclose information about a reported transaction to the stock exchange on which the relevant securities are listed. The section also provides that the Registrar may disclose such information to the public if he or she believes that such disclosure would further the objectives of the Act.[32]

Where there are changes in share ownership, section 51(6) of the Companies Act provides that a 'company must enter in its securities register every transfer of any certificated securities', including the name of the transferee.

Where shareholders hold information on behalf of another party, this information must be disclosed in terms of section 56 of the Companies Act, which section states that 'the names and addresses of the registered owner of the security and any holders of a beneficial interest in the security' should be reflected.

In South Africa, the current transparency regime regulating the private sector, which includes the extractive industry, is therefore focused largely on enhancing information disclosure to shareholders or investors rather than to the public and local host communities.

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29 Disclosure of audited financial statements: Companies Act 71 of 2008. Section 50 of the Companies Act provides as follows:

(1) Every company must –
  (a) establish or cause to be established a register of its issued securities in the prescribed form; and
  (b) maintain its securities register in accordance with the prescribed standards.

(2) As soon as practicable after issuing any securities a company must enter or cause to be entered in its securities register, in respect of every class of securities that it has issued –
  (a) the total number of those securities that are held in uncertificated form; and
  (b) with respect to certificated securities –
    (i) the names and addresses of the persons to whom the securities were issued;
    (ii) the number of securities issued to each of them;
    (iii) the number of, and prescribed circumstances relating to, any securities –
      (aa) that have been placed in trust ...; or
      (bb) whose transfer has been restricted;
    (iv) in the case of ... –
      (aa) the number of those securities issued and outstanding; and ...
      (bb) the names and addresses of the registered owner of the security and any holders of a beneficial interest in the security; and
    (v) any other prescribed information.

30 'Beneficial interest' in relation to a company's securities means the right or entitlement of a person, through ownership, agreement, relationship or otherwise, alone or together with another person to: (a) receive or participate in any distribution in respect of the company's securities; (b) exercise or cause to be exercised, in the ordinary course, any or all of the rights attaching to the company's securities; or (c) dispose or direct the disposition of the company's securities, or any part of a distribution in respect of the securities.

31 Sections 24(4) and 50.

32 Financial Markets Act 19 of 2012.

4.2 Johannesburg Stock Exchange Listing Requirements

Companies listed on the Johannesburg Stock Exchange (JSE) have to comply with the JSE Listing Requirements. These Requirements define 'beneficial owner' in relation to a security and indicate that it means the person or entity holding any one or more of the following: the de facto right or entitlement to receive any dividend, interest or other income payable in respect of that security; and/or the de facto right or entitlement to exercise or cause to be exercised, in the ordinary course of events, any or all of the voting, conversion, redemption or other rights attached to such security; and/or the de facto right or entitlement to dispose or cause the disposal of the company's securities or any part of a distribution in respect of the securities.[33] The JSE Listing Requirements further require information on whether beneficial owners are BEE-compliant (i.e. comply with legislation relating to black economic empowerment).[34]

Other important disclosures include a statement on: the aggregate of the direct and indirect beneficial interests of the directors; major shareholders who are directly or indirectly beneficially interested in 5% or more of any class of the listed company's capital, together with the amount of such shareholder's interest; on issues for cash; and on mineral resources and mineral reserves.[35]

In the financial statements of mineral companies and companies with substantial mineral assets, mineral companies (including subsidiaries, joint ventures, associates and investments) are required to disclose details[36] on an attributable beneficial-interest basis.

4.3 Financial Intelligence Centre Act 38 of 2001

South Africa's Financial Intelligence Centre Act (FICA) requires information on financial transactions to be kept for a period of five years, including the identity of the client, the nature of the business relationship and the amounts involved.[37] In the draft amendments to the FICA, the Financial Intelligence Centre (FIC) will also have access to beneficial ownership obtained by financial institutions maintained by legal entities and recorded in company registers.

The draft FIC Amendment Bill requires accountable institutions to establish the identity of people before entering into a business relationship with them. The FIC Amendment Bill further provides that, when accountable institutions are about to enter into a business relationship, they should obtain information on: the nature of the business relationship concerned; the intended purpose of the business relationship concerned; and the source of the funds which the prospective client expects to use in the business relationship.[38]

For juristic persons, and natural persons acting on behalf of juristic persons, the Bill also provides that the nature of the client's business, as well as the ownership and control structure of the client, must be established.[39] In addition, it requires accountable institutions to establish the identity of the beneficial owner of a juristic person and to take reasonable steps to verify the identity of such beneficial owner.[40]

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33 See the definitions section of the JSE Listing Requirements.

34 4.32 of the JSE Listing Requirements.

35 8.63 of the JSE Listing Requirements.

36 Described as beneficial 'see through' basis. 'Beneficial' in relation to any interest in a security means the de facto right or entitlement to directly receive the income payable in respect of that security and/or to exercise or cause to be exercised, in the ordinary course of events, any or all of the voting, conversion, redemption or other rights attaching to that security; in relation to any other interest means the obtaining of any benefit or advantage, whether in money, in kind or otherwise, as a result of the holding of that interest; and/or in relation to the aforementioned interests means the de facto right or entitlement to dispose or cause the disposal of the company's securities or any part of a distribution in respect of the securities – definitions section of the JSE Listing Requirements.

37 Section 22 and 23 of the FICA.

38 Section 21A.

39 Section 21B.

40 Section 21C.

All these regulatory requirements provide a solid framework for the establishment of beneficial-ownership disclosure in South Africa, particularly if the FIC Amendment Bill is passed and the government abides by its commitment to develop an implementation plan for beneficial-ownership transparency in terms of its Open Government Partnership commitment.

The Bill moreover requires accountable institutions to 'establish the identity of each natural person who, independently or together with a connected person, has a controlling ownership interest in the juristic person; and take reasonable steps to verify the identity of each natural person…'.[41] The same applies to establishing and verifying the identities of natural persons in a partnership, of founders of a trust, of trustees and of beneficiaries – regardless of where these institutions were established or incorporated.[42]

The Bill further requires accountable institutions to take steps to establish the source of wealth and source of funds of a client and to conduct ongoing monitoring of the business relationship.[43]

Whenever there is doubt about the veracity of information submitted by a client, the Bill requires that the steps be repeated, and, in cases where the identity of a client cannot be verified, accountable institutions are expected to terminate the business relationship.[44]

All these regulatory requirements provide a solid framework for the establishment of beneficial-ownership disclosure in South Africa, particularly if the FIC Amendment Bill is passed and the government abides by its commitment to develop an implementation plan for beneficial-ownership transparency in terms of its Open Government Partnership commitment. However, a robust framework is still needed to deal with the scope of disclosures, the extent of application to private companies, and the level of disclosure that should be required. International best practice can help in this regard. For instance, the EU Directive on a public register in respect of beneficial ownership has been recommended by the AU for consideration by African states in terms of developing beneficial-ownership regulation.[45]

The FIC Amendment Bill is an important step forward, because undisclosed beneficial ownership implies that there is a possibility that potential profits paid to undisclosed corporate investors may escape the payment of taxes, which, in turn, lessens revenue for the government to provide much-needed socio-economic programmes in order to address inequality. In the absence of a register on beneficial ownership, it will be difficult for the South African Revenue Service (SARS) to effectively collect taxes, with the result that money laundering and the hiding of illicit wealth will continue.

5. Beneficial ownership to what end?

There are several reasons to support beneficial-ownership disclosure. Such disclosure aids the work of government oversight institutions in fulfilling their mandates of curbing corruption and enhancing tax collection, thereby aiding social development. These disclosures prevent IFFs as well as tax evasion, which is vital in plugging leakages that may hamper the socio-economic development of South Africa.

41 Section 21D.
42 Clause 21D.
43 Clause 21D.
44 Clause 21G.
45 See Illicit financial flows report, p. 46.

Perhaps the greatest benefit of beneficial-ownership disclosure is that it reduces corruption. The term 'politically exposed persons (PEPs)' has risen to prominence recently and means 'an individual who is or has been entrusted with a prominent public function'.[46] Quite often, there is a danger of conflicts of interests, bribery and other corrupt practices in situations where PEPs own companies that require government licensing or contracts. The corresponding term in South Africa is 'prominent influential persons', which is defined in terms of the FIC Amendment Bill. As the Bill rightly expands on, the term 'beneficial ownership' does not simply mean the shareholders of a company who own 'direct legal title to equity in the company'. It also extends to people in control of the company who enjoy financial benefits.

The term 'beneficial owner' usually applies to natural persons only and does not include directors and board members of a company. However, certain corporate vehicles such as trusts, partnerships and any other juristic vehicle that might mask the identity of natural persons behind a juristic person, are also included. Beneficial-ownership disclosures therefore target the ultimate owners of a company and not the proxies, subsidiary companies, institutional investors, nominees or managers.

Since there might be several beneficial owners of a company, it is useful, so as to limit the focus of beneficial-ownership disclosures, to establish an ownership threshold in order to focus on the owners whose control of resources is likely to be significant for governments in terms of tax collection.

While a maximalist approach should be taken in the disclosure of beneficial-ownership information, it is important that this approach be balanced against the privacy of owners. Accordingly, releasing information that sufficiently identifies an owner should be possible without compromising the right to privacy of such person, especially with regard to the safeguarding of personal information.

Also, while beneficial-ownership disclosure requirements as prescribed by the EITI and other emerging laws on the subject are important, there are other categories of ownership information that are required to be taken into account with regard to the transformation aspirations of South Africa as far as historical and socio-economic disadvantage is concerned. A central disclosure requirement in South Africa would relate to the broad-based black economic empowerment (BBBEE) and affirmative-action policies of the government which impose ownership targets on the extractive industry in order to redress race, gender and socio-economic imbalances in such industry.

In addition, the concept of beneficiation, which deals with local value-addition to minerals, is linked to the ownership requirements in the regulations governing the extractive industry. With South African regulations also requiring the disclosure of information on the racial composition of supplier companies as part of a preferential-procurement strategy to empower companies owned by historically disadvantaged South Africans, beneficial-ownership disclosure assumes a different dimension and requires more purposeful oversight and application in South Africa.

While South Africa may allow the disclosure of beneficial-ownership information, it is important that this not be done in a vacuum that results in 'the bigger picture' of a multinational company's global footprint and activities not being established. Consequently, it is necessary for disclosure of beneficial-ownership information to occur alongside cooperation by South Africa with other countries to ensure that information on tax arrangements, benefits and preferential treatment is shared among countries, and to allow full understanding of the exact payments made by a company to each particular government.

6. Tax-benefit disclosures

Company law rules allow companies to develop complex ownership structures for several valid reasons, including the maximisation of the benefits of different legal jurisdictions so as to reduce the tax liability of companies. While tax avoidance might be considered morally repugnant, it is legitimate. However, there is a fine line between avoidance and evasion in certain situations, such as where beneficial owners receive their profits in anonymous ways that allow them to evade tax.

46 See Financial Action Task Force (FATF).

Tax benefits, or preferential treatment, have long been used by states to promote investment. However, with the global recognition that developing states are being deprived of capital, there is now an acknowledgement that global cooperation with respect to tax collection is necessary in order to curb tax-benefit practices that benefit only investors and harm state economies. The OSF's comprehensive report deals in detail with some of the tax arrangements in South Africa and has been reproduced in part below.

The South African Tax Administration Act 28 of 2011[47] prescribes a number of tax-planning strategies that can be utilised by companies to their benefit. Section 35 of the Act describes these strategies as an 'arrangement'[48] which is subject to disclosure to SARS if a tax benefit will be derived, or is assumed to be derived, by virtue of the arrangement. The Act further provides that such arrangement must affect the calculation of interests, finance costs, fees or any other charges and give rise to an amount that is, or will be, disclosed as a deduction but not as an expense for the purposes of the Income Tax Act 58 of 1962. In addition, this arrangement must be disclosed as revenue for the purpose of the financial statements, but not as gross income for the purpose of the Income Tax Act.

Section 35(2) of the Tax Administration Act in addition provides that 'the Commissioner may list an "arrangement" by public notice, if satisfied that the "arrangement" may lead to an undue "tax benefit"'.[49] An arrangement is managed by a person described by the Act as a promoter, which means that such person is responsible for 'organising, designing, selling, financing or managing the reportable arrangement'. The Act also requires the promoter to disclose the arrangement within 45 business days after an amount is first received by or has accrued to a 'participant'[50] or is first paid or actually incurred by a participant in terms of the arrangement.[51] The participant that is the beneficiary of a tax arrangement is regarded by the Act as a company or trust, which means that, under the current rules, the ultimate beneficial owners remain anonymous.

The Act requires a broad set of information to be submitted to SARS, including: a detailed description of all the steps and key features of an 'arrangement'; a detailed description of the assumed 'tax benefits' for all 'participants', including, but not limited to, tax deductions and deferred income; the names, registration numbers, and registered addresses of all 'participants'; a list of all its agreements; and any financial model that embodies its projected tax treatment.[52] It excludes arrangements in respect of loans, advancements, debts, leases or exchange transactions.[53] If beneficial-ownership disclosure is applied in South Africa, the ultimate beneficial owners would be identifiable through these categories of information.

Section 68(3) of the Tax Administration Act stipulates that all information furnished to the tax authority shall not be shared with anyone outside the organisation, except where: the information is public information; this is authorised by the Commissioner; disclosure is authorised under any other Act which expressly provides for the disclosure of the information; access has been granted for the disclosure of the information in terms of PAIA; or disclosure is required by order of a High Court.

Given the extensive information currently subject to disclosure to SARS[54] as identified above, SARS is already in a position to collect information dealing with illicit financial flows and tax evasion. However, these categories of information disclosed to SARS are not subject to public disclosure, the

47 Available at: http://www.lexisnexis.co.za/pdf/download-Tax-Adminstration-Act.pdf.

48 Means any transaction, operation, scheme, agreement or understanding.

49 The public notice issued by the Commissioner in 2015 identified a very limited set of what is deemed to be an 'arrangement', with such set including only hybrid equity and debt instruments that are issued shares. See: http://www.sars.gov.za/AllDocs/LegalDoclib/SecLegis/LAPD-LSec-TAdm-PN-2012-05%20-%20Notice%201108%20GG%2036038%2028%20December%202012.pdf [accessed 5 February 2015].

50 Means a company or trust that directly or indirectly derives, or assumes that it derives, a tax benefit or financial benefit by virtue of an arrangement.

51 Section 37 of the Tax Administration Act.

52 Section 38 of the Tax Administration Act.

53 See section 36 of the Securities Services Act 36 of 2004.

54 Sections 37 to 39 of the Tax Administration Act.

The FIC Amendment Bill is also a very promising addition that should be adopted urgently. The Bill provides a clear definition of beneficial ownership and defines other crucial players such as domestic and foreign eminent persons, their close associates and family members, all of whom will fall with the ambit of the Bill for the purpose of performing due-diligence checks to curb conflicts of interests, illegal money transfers and corruption.

beneficiaries are not listed, and the companies concerned are not required to disclose arrangements in their financial statements. As a result, improved legislation to address these gaps is still required.

7. Conclusions and recommendations

The South African regulatory framework is in many ways robust. Nevertheless, there are several ways to improve the framework for better regulation of the extractive industry and to maximise the economic benefits of minerals extraction. Much has been said about the unsustainability of the extractive industry. The extractive industry has many problems, and oversight regarding industry activities has been seriously flawed. Our intuitive responses will always inform the debate about mining and the complex history of South Africa. With a law that considers minerals to be the collective entitlement of everyone, and with minerals often perceived as a windfall waiting to be extracted, the debate about what should rightfully belong to investors and to the state on behalf of everyone else will continue. South Africa is in good company in this regard, with several other states seeking to administer and maximise the profits from mining so as to boost socio-economic development in ways that primarily benefit host communities and the broader state in general.

An examination of the various laws that apply to ownership, operational and financial disclosures in the comprehensive OSF report shows that there are many different structures in place that can potentially be used to develop beneficial-ownership and tax-benefit disclosure requirements. The FIC Amendment Bill is also a very promising addition that should be adopted urgently. The Bill provides a clear definition of beneficial ownership and defines other crucial players such as domestic and foreign eminent persons, their close associates and family members, all of whom will fall within the ambit of the Bill for the purpose of performing due-diligence checks to curb conflicts of interests, illegal money transfers and corruption.

While the Bill awaits passage into law, it is important that an audit of the risks associated with the financial flows related to legal persons and their tax arrangements be conducted. This audit will allow an understanding of the patterns of illegal wealth accumulation and how to eliminate these patterns.

There are several oversight authorities in South Africa that are involved in the regulation of the mining industry, tax matters, and the prevention of illegal financial practices. These institutions, such as the FIC, SARS, and other anti-corruption institutions need to work together to identify high-risk areas in their intelligence gathering and thereafter focus their due-diligence investigations in those areas. As a result, it is important that access to information by these entities should be prioritised. In order to ensure that various oversight agencies work together, any restrictions on information-sharing should be lifted and these institutions should be strengthened in order to be able to monitor compliance with regulations, collect data and enforce sanctions.

The establishment of a beneficial-ownership registry is also necessary so as to consolidate information and records about assets and their owners, thereby ensuring that the complex face of corporate secrecy is fully unmasked. The information in this registry should be verifiable and should constantly be verified against independent sources.

Lastly, with a view to the adoption of the FIC Amendment Bill, the record-keeping component of the various applicable ownership, operational and financial disclosure provisions needs to be

strengthened in order to ensure that legal entities collect and keep the required records not only for access by oversight authorities, but also for public scrutiny. Aside from the state and the mining companies, there are other players and vested interests in the extractive industry. Financiers, workers, host communities, and the general public all have an interest in the success and profitable outcomes of the industry. Their right to access information is 'no less equal' than the right of the state and its oversight authorities. With this kind of multi-layered public scrutiny in place, there is hope that the web of corruption in South Africa can begin to be slowly untangled.

About the authors

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About the series (working papers)

The Open Society Foundation for South Africa periodically commissions research papers on topics related to our portfolio on *Promoting Extractive Sector Transparency and Accountability*. This publication forms part of a series of three working papers commissioned in 2016 on select topics related to disclosure practices in South Africa's extractive sector.

The series focus is drawn from the report titled *South Africa's Extractive Industry Disclosure Regime: Analysis of the legislative and regulatory regime and selected corporate practice*, written by Prof. Tracy-Lynn Humby and Dr Fola Adeleke. While related to the larger disclosures report, this series provides deep analysis into beneficial ownership, drivers of disclosure, and experiences with the Promotion of Access to Information Act in mining related disclosure practices.

We hope that the series is a useful knowledge resource for the work of our grantees, our partners and the many mine-affected communities in South Africa.

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