SOUTHERN AFRICA GLOBAL COMPETITIVENESS HUB

Trade Facilitation: VAT Treatment of Swazi Exports/Imports through South Africa

Draft Report

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I. Introduction

Swaziland, a landlocked country surrounded almost entirely by South Africa except for a few miles of its eastern border with Mozambique, is dependent on its neighbors in regard to trade. Imports from and exports to overseas markets are moved in transit through these two maritime neighbors, but South Africa comprises 90% of Swaziland's border and 80% of its trade.[1] Inefficiencies in trade logistics that increase direct costs, reliability of transport, or the time required to ship goods from one destination to another – including those arising from customs processing – can undermine the competitiveness of the country's private sector. In looking at Swaziland's trade competitiveness, it is important to note that the country faces several challenges that increase the per unit cost of exporting. These include the comparatively small volumes of inward and outward trade and limited resource base. Therefore, the problems that can be readily addressed should command a greater share of government attention.

Durban, Southern Africa's busiest port, plays a crucial role in Swaziland's trade. Almost all of Swaziland's imports from overseas come by sea to Durban in South Africa, and from there by road or rail to Swaziland. Despite its on-going capacity expansion plan, many observers suggest that Durban remains overcrowded with ships waiting as long as give days to berth. Generally, time-sensitive goods, such as fresh produce, are transported by road to and from Durban or Johannesburg International Airport. Most exports to the United States are transported by road in order to be able to comply with the manifest closing requirements. With the important exception of sugar, which mostly goes through the port of Maputo, most of Swaziland's exports also go through the port of Durban. Time-sensitive exports can be picked up from Maputo by trump vessels, which call as and when captive cargo is available.

Maputo, which is about 250 kilometers closer to Matsapha than Durban, was once Swaziland's port of choice for exports. Mozambique's long civil war and resulting degradation of infrastructure, decline in transport security, and loss of importance as a functioning trade hub increased Durban's importance for Swazi exporters and importers. Although infrastructure investment and improvements in port services have helped increase the volume of trade from Maputo, its capacity is at least 15 times less than Durban and its ship calls are comparatively infrequent, with no direct sailings to Europe, East Asia, and the Americas.

Since Swaziland is a landlocked country, the importer must decide on the appropriate term of delivery. If the importer would not like to take delivery at the port of Durban he or she can insist on CIF to Matsapha where the Dry Port is located. If the importer opts for CIF or C & F Durban the importer must arrange for taking delivery in Durban and transporting the goods to Swaziland. Whatever option is taken will be reflected n the Letter of Credit, which is the most common mode of payment.

A. Trade Facilitation Issues

Some of Swaziland's companies have experienced various problems in importing and exporting through South Africa. These include unsynchronized hours of operation for border posts, inadequate notice when administrative changes are implemented by the

[1] *Improving Transportation Logistics for Competitiveness of Swaziland,* 2005, pg. 11

South Africa Revenue Service (SARS), incompatibility between Swazi and South African customs in regard to electronic systems and filing procedures, and processing of provisional Value Added Tax (VAT) on goods that are ultimately exported beyond the territory of the Southern Africa Customs Union (SACU). The issue VAT treatment is among the top trade facilitation concerns for certain of Swaziland's companies. Most Swazi exports shipped outside of SACU go through South Africa and through the port of Durban, so transit problems through South Africa have a large impact on the Swazi business community.

There are three dimensions to the VAT treatment issue about which Swazi companies have complained. First, at a reported average of 90 days, the length of time required to receive a refund of VAT is considered excessive and causes cash-flow constraints on firms. The cash flow constraint is exacerbated when Swazi companies must maintain a security bond in a South African bank to offset potential South African VAT payments. Second, the administrative fee charged by SARS as part of the process imposes a direct cost on Swazi trade. This means that every individual shipment from Swaziland involving the payment of provisional VAT will have an actual, unrecoverable cost. Third, some companies report variances in the procedure that impose additional opportunity costs. For example, some state that sometimes the acquittal process requires the exporter to demonstrate documents that confirm the goods have reached a final destination beyond South Africa. Such a requirement would delay the filing of the acquittal form that triggers the issuance of a VAT refund and also represents a cost in time and effort to obtain an additional document.

Some observers suggest SARS is concerned about smuggling of goods from Swaziland into South Africa VAT free. In particular, some Swazi companies note that in the past some companies in the apparel sector were accused of evading VAT by partially manufacturing goods in Swaziland, sending them to South Africa for further processing, and then declaring them defective or surplus and selling them in South Africa.

B. Sectoral Focus

Interviews with Swaziland government officials and company representatives have pinpointed the problems faced by certain companies in relation to VAT. It is important to identify which companies and products are affected by SARS' treatment of VAT at the sectoral level. Companies from certain sectors have adopted strategies to mitigate against the problem. For example, Swaziland's sugar producers, which ship their exports through the Swaziland Sugar Association (SSA), move most of their product by rail through Mozambique, to a bonded warehouse in Maputo for loading onto cargo ships thereby avoiding transshipment through South Africa altogether. The SSA suggests that Mozambique's anti-smuggling protocols are quite stringent in part because the country has its own sugar industry and taxes imports heavily. The SSA suggests that freight charges are lower going through Maputo (approximately two hours distance from the Swazi border) than to go through Durban (approximately five hours distance) and there storage space is more readily available at the port of Maputo than Durban. About 1,000 tons of sugar is transshipped through South Africa for ultimate export through Durban.

Swaziland's produce exporters are not subject to VAT payment and therefore do not encounter difficulties. The National Agricultural Marketing Board, a parastatal Swazi company, markets the country's agricultural products on behalf of the nation's farmers nationwide. The Board ships most of its agricultural exports through South Africa to Johannesburg international airport by truck. According to the Board, it relies on a freight forwarder to handle customs transactions because only freight forwarders are allowed to obtain an exporters code, which is required by customs.

Several large manufacturers with sister companies in South Africa have shifted the burden of VAT payment and refunds to the South African company. In this way, the sister company in South Africa will register with SARS for VAT payment and refunds and the goods exported through South Africa leave the Swazi company's custody at the border.

Other large manufacturers can negotiate with buyers and shipping companies in South Africa to take on the VAT burden once goods enter South African customs territory. In this way, the Swazi exporter would be relieved from registering with SARS, obtaining a bank guarantee in a bank in South Africa, and paying provisional VAT.

The companies that do face problems related to VAT treatment include smaller companies and exporters in the handicraft sector. According to several companies, SARS has required Swazi companies to post a bond at a South African bank approximating the annual VAT owed on exports transshipped through South Africa as well as exports sold directly in South Africa. The funds required to satisfy the bond negatively affects firm cash flow, as the amount of capital tied up in the bond cannot be used for other purposes.

II. Customs Procedures

A. Exports

As mentioned earlier, most exports go through the Port of Durban. Sugar exports go through the port of Maputo where they are picked by a chartered vessel. Most exports to Durban go by road since this mode provides more certainly about meeting deadlines for manifest closing.

The companies interviewed pointed out that the process for exportation is less involved than that of importation. However, they still use professional CCAs or freight forwarders since they can handle the export logistics in South Africa, which include provision of a security bond to cover the goods while they are in transit to Durban. For exports the bond covers taxes and any duty and taxes that were rebated or suspended pending exportation of goods manufactured under the inward processing procedure.

The specific steps required for a generic export are outlined below.

Step 1) Load the transport unit. If the exportation of goods will result in the refund of duty or taxes or in the discharge of a security, Swazi Customs should be called to supervise the loading if it is taking place at the exporter's premises. The supervising customs officer will write a record of the goods loaded or approve a packing list that will be submitted with the export and supporting documents to get a refund or to discharge the security.

Step 2) Prepare export documents. The required export documents will include the export bill of entry, Form CE550, Exchange Control Form F178 and supporting documents like the invoice, road manifest, and certificates of origin. There is little that the processing of documents involves since there are no issues of valuation and calculation of duties. The consignment may be examined especially if there will be a claim for refund or discharge of a security after their exportation.

Step 3) Seal the unit of transport. Following document processing and examination of the goods, the unit of transport is sealed by Swazi Customs with Customs seals and released for exportation. When a unit of transport is sealed, the Customs offices en route, even in South Africa, are supposed only to check the integrity of the seal. If it is intact it is assumed that the goods have not been interfered with.

B. Payment of Provisional VAT to SARS

Companies that export through South Africa must pay provisional VAT on the items to be exported. They then have 30 days to file an acquittal with SARS that proves that the items have been exported from South African territory. The 30 days period begins when the CCA1 form is date stamped at the time of entry into South African Customs territory. This 30 day period can be extended through a specific application to SARS. The bill of lading stamped by the outward shipping company serves as proof that an item has been shipped out of South African customs territory.

SARS' fines for not filing the acquittal paperwork on time include the payment of VAT for the shipment in question. SARS' fines for errors on paperwork are R 1,000 (US $153.84) per form. One company noted that SARS sometimes loses paperwork. If SARS loses an acquittal for the provisional VAT, the company may be charged incorrectly and will need to argue with SARS officers about who lost the form. In some cases, SARS will have lost an acquittal and attempt to fine the exporter.

Several companies note that SARS typically takes 90 days to process the VAT refund and also charge customs fees. Swazi companies complain that when they apply for refunds of South African VAT on an item exported beyond SACU, they will not receive the full refund because customs charges hefty fees amounting to 14% of the VAT refund due. Refunds for the 14% VAT also take a long time to be received, creating cash flow problems for Swazi exporters.

Further, SARS decides how much money a Swazi exporter will need to post in bond to cover customs tariffs and this also ties up capital. It is not clear who is entitled to the interest earned on money tied up in bond.

The problem of provisional VAT refund processing is not limited to goods transshipped through South Africa for ultimate export beyond SACU. Several companies noted problems related to equipment and refunded merchandise. In the case of equipment and machinery repair, companies are required to pay VAT provisionally on the value of the equipment as if they were exporting it to South Africa. As with other provisional VAT transactions, the Swazi company must demonstrate within 30 days that the equipment has been repaired and repatriated to Swaziland or else file for an extension. Depending on the complexity of the repair, the machinery may need to be in South Africa for more than 30 days. As noted previously, applying for extensions is a somewhat cumbersome process.

One investor noted that there are cases where a product exported to South Africa is returned by the purchaser and sent back to Swaziland and VAT is never refunded. In such circumstances, VAT can be reclaimed. In some cases, even if the South African customer has a VAT account, SARS will require the exporter to pay the VAT.

C. Imports

Customs transit is a very important Customs procedure for Swaziland, and the efficient movement of the country's imports and exports is dependent on the facilitation of transit traffic by its two neighbors. Other Customs procedures are importation for home use, outright exportation, warehousing in bond, and removal in bond. These procedures are governed by the Swaziland Customs and Excise Act and Customs Regulations made under the Act.

As mentioned in the analysis section below, Swaziland is introducing the computer system called CAPE which is used by the South African Revenue Services to automate the processing of Customs clearance. Because of this, the Customs clearance procedures and documentation will change drastically over time. In view of this change, only the salient features of the present procedures and documentation are explained here.

In most cases, imports from overseas to Swaziland enter SACU through the Port of Durban. Under the Customs laws of SACU, Customs clearance of imports into the Customs Union can take place at the first office of entry into the Customs Union or at their final destination. For the convenience of importers and for commercial and administrative purposes, goods are often cleared at their final destination. For example, if the terms of the letter of credit include a through bill of lading, the importer would not like to take delivery in Durban. Furthermore, it is more convenient for importers to clear goods at destination where all the formalities for home use can be accomplished. These include payment not only of import duties but also sales tax.

From Durban imports have to be declared for transit. Transit formalities require a security bond if the goods are being moved by road, to cover the duty and taxes due on them should the goods be illicitly diverted into home use in South Africa. No security is required for goods moving by rail because of the very low probability that they can be illicitly diverted for home use. If goods are entered for home use in Durban, South African value added tax (VAT) would have to be paid unless the goods are declared for movement to Swaziland. If so, a security would be required to cover the risk of losing South African VAT should the goods be illicitly diverted into South Africa. There is therefore no advantage of clearing goods consigned to Swaziland for home use at Durban.

Most of the companies interviewed either use a customs clearing agent (CCA) located in Swaziland to do their Customs clearance or have an in-house import-export section to handle Customs clearance the logistics. This is because the process is complex process and can be time-consuming and costly if not done professionally. The other advantage of using a CCA is that the importer need not then be concerned with formalities in South Africa. A reputable CCA will entrust the task to a correspondent in South Africa that is registered with the South African Revenue Service. Transporters, freight forwarders, and CCAs that are accredited to SARS have a general security bond that is debited with the amount required by a particular transaction and credited when the transaction is discharged. Furthermore, the amount of bond required depends on the probability of loss; the least amount will be required of a reputable CCA or freight forwarder that has a clean record. Such a CCA may also afford to charge a cheaper premium.

When the goods arrive in Swaziland they can be entered for home use or for processing as raw materials or inputs that will enjoy the rebates. The goods can also be entered for warehousing where they will be stored in bond until the importer is ready to enter them for home use or for re-export

Following are the specific steps required to import into Swaziland.

Step 1) Prepare the necessary documents. Whatever customs procedure is opted for Customs clearance requires a number of documents, the following of which are standard:

- The bill of entry (Form CE 500): this is the declaration showing the country of importation, the means of transport used, the port where the goods were discharged, the point of entry into the country, the exporter, the importer, the nature and quantity of the goods, their tariff number, their value and the basis of the value, the rates of duty and taxes applicable to them, and the amounts.
- Supporting Documents: these include the commercial and transport documents like invoices, bills of lading, road manifest, packing list, and administrative documents like import permits, SPS certificates, and certificates of origin.

The SACU tariff is based on the Harmonized System of the World Customs Organization, and subdivisions are at 8-digit level. Swaziland, like the other members of SACU, also applies the WTO Agreement on Customs Valuation for the purposes of valuing imports with ad valorem rates of duty. Value for duty purposes is based on the FOB price of the goods. The value for the purposes of the other taxes includes the FOB price and the duty amount payable.

Step 2) Submit documents to Customs for processing. The processing of documents includes checking:

- that all the necessary documents are attached and are completed properly;
- the correctness of codes entered for different purposes;
- the tariff headings entered for the goods;
- the basis of the value for the goods and the correctness of the calculation;
- the calculation of the amounts of duty and taxes; and
- entitlement to rebates and exemptions.

Where Customs concludes that the invoice price is too low, they require the importer to justify the circumstances warranting such a low price. If Customs are not satisfied with the importer's justification, Customs may value the goods on the basis of previously imported identical or similar goods.

Step 3) Pay import duty and taxes. Once Customs are satisfied with the declaration, the importer is required to pay the duty and taxes where goods are not duty-free or duties and taxes not rebated. Before releasing the goods, Customs may decide to examine them physically. The decision is based on a number of factors, like the nature of the goods, the perceived integrity of the importer or the CCA clearing them, and other circumstances surrounding the importation.

Step 4) Take delivery of the goods. Once the Customs formalities are completed, the goods are released by Customs. On average clearance takes one day, but can take up to three days in case there are issues to settle, like the value of the goods, and their Customs tariff classification.

A broader spectrum of companies face difficulties related to machinery and equipment imports. Swaziland requires that the importing company have a bond raised on this equipment. The procedures are legally cumbersome and several taxes are assessed. The cost of importing equipment and machinery is a concern for investors, and almost all equipment and machinery must be imported.

Box 1 below illustrates the impact of provisional VAT on a medium sized Swazi craft producing company.

Box 1: Case Example – Craft Producer

Interviews with several Swazi companies in the craft sector confirm that the delays and cost of the provisional VAT refund system imposes undue hardship for the sector. A case study, based on one of the Swazi craft exporters illustrates the impact of the present regime on a medium sized exporter.

Craft Producer sells approximately 75% of its exports in retail stores in South Africa. Its goods travel from Swaziland by road to various places in South Africa, and its exports go through Durban. On these transactions, the company pays South African VAT on behalf of its retailers and the retailer files the CCT form in South Africa to reclaim the VAT as goods are sold. The VAT amount is then refunded to Craft Producer from retailers on an on-going basis negotiated between the producer and vendor.

For goods transshipped through South Africa, the Craft Producer has problems related to the payment of provisional VAT. The company must pay VAT provisionally on all of its goods as they enter South African customs territory and then has 30 days to file an acquittal form to reclaim the VAT after the goods have been exported from South Africa. For medium sized companies like Craft Producer, the documentary fees paid to freight forwarders are a consequential expense. The paperwork filing of the VAT refund acquittal form is completed by a Swazi freight forwarder (with a presence in South Africa), and fees range from E 250-1,000 (US $38.46-153.84) per form, not including the administrative fees charged by South Africa. The company ships approximately 120 export consignments per year and 600 consignments destined for final sale in South Africa. For goods shipped into South Africa for final sale, the document fee equals E 150 (US $23.07). While the fees paid to the freight forwarder are more expensive than if the company handled these transactions directly, Craft Producer states that trying to deal with SARS directly for refunds is a time-consuming process, often taking three visits to a SARS office to complete the transaction.

Because the company is Swazi-based without a sister company in South Africa it must establish a VAT deferment account in South Africa and obtain a bank guarantee in a South African bank. The bank guarantee is set by SARS but equals the estimated VAT liability of the company's average monthly exports. In the case of Craft Producer, this amounts to E 25,000 (S $3,846) in cash flow that cannot be accessed. The bond must be renewed annually. Craft Producer's average annual revenue is E 3.5 million (US $538,462); as such the bank guarantee represents 0.007% of its annual cash flow. For a company the size of Craft Producer, this requirement imposes a significant cash flow constraint.

At one time, craft companies also had problems assuring SARS that commercial samples were not for resale in South Africa. However, this problem has been solved by the Minister of Tourism, who generated a letter for Swazi companies to give to customs when they embark on a trade show in South Africa. SARS will physically inspect to ensure that such commercial samples are being repatriated to Swaziland.

The forms the Craft Producer uses to process its exports are:

- CCA1 shipment document generated by the Swazi FSE-CCA
- Bill of lading
- Certificate of origin generated by Swazi Customs
- F178 to cover the inflow of currency covering the shipment
- Euro 1, if designated for the EU
- U.S. customs entry form, if designated for the United States
- Bill of entry form

On average, Craft Producer's exports take one to two days to clear customs.

III. Related Customs Issues

The problems confronting Swazi companies related to slow SARS VAT refunds are related and exacerbated by some other problems related to customs processing. These issues are summarized briefly below.

A. Swazi General Sales Tax (GST)

A second dimension of tax treatment is the imposition of General Sales Tax on the Swaziland side. Swaziland is the only country in SACU and one of the few countries in SADC which is still applying GST. One retailer noted that he pays an average of E 250,000 per month in GST, and reconciling these payments with VAT payments to SARS requires a significant amount of paperwork. The structure of the tax encourages firms to undervalue imports. Since meat is tax rated zero per cent, the big meat importers and slaughter house do not pay GST.

Applying for a rebate of Swazi GST requires indicating the Customs tariff number for each item applied for. Swazi Customs does not always adequately explain this process and there are no instructions or forms issued by Customs to guide the process. After registering with the Customs the rebate certificate is obtained from the Trade Promotion Unit (TPU) in the Ministry of Foreign Affairs and Trade. Several companies suggest that having to deal with another government agency for this process is inefficient and the TPU is particularly unresponsive. The certificate could be issued by the Customs or the Ministry of Finance. Another problem is that Swazi Customs does not always relieve the duty on imports of machinery and equipment when the investor is entitled to such a rebate.

B. Physical Inspections by SARS

SARS opens containers in transit, which causes a delay, and imposes high penalties for even for minor clerical errors. Several companies note that SARS inspects on a random basis but suspect that Swazi companies are more frequently inspected than others. Some Swazi companies suggest that SARS' inspections are excessive. Swazi customs seals their exports at the factory and stamps the paperwork, but SARS will still open shipments and physically inspect and count. This practice suggests that SARS does not trust the Swazi Customs or respect the seals attached by the Swazi Customs.

C. Lack of Forewarning of Administrative Changes from SARS

Even representatives from some of Swaziland's freight forwarding companies suggest that SARS does not discuss with Swaziland Customs and traders before they impose new measures. Further, the changes introduced by SARS are frequent. One freight forwarder said that sometimes he is only made aware of procedural or administrative changes upon arrival at the border. . This routinely causes delays for exporters, thereby hindering trade performance. One major Swazi manufacturer suggested that for major changes shipments can be held at the border for up to five days implementing changes based on new SARS procedures.

One observer said that the main problem with Swazi customs is that they do not seem to work well with SARS and do not know when changes in SARS procedures occur, or do not effectively communicate these changes to traders. The problem of frequent and under-publicized changes imposed by SARS is compounded by its imposition of fines. One company charged that SARS is quick to fine exporters for minor irregularities on paperwork.

D. Border Hours

Swazi customs would open 24 hours a day to help facilitate trade, but SARS will not. As such, shipments need to leave Matsapha by 5:00 pm to clear the Swazi border and meet the ship they are scheduled to go to.

E. Swazi Customs Official Availability

Sometimes at customs a company will need to find a specific individual who is the only one who is authorized to approve something or only one who knows a certain procedure. In some cases, if the person is unavailable for illness, attending other duties, or evasive trade can stop and no one will be able to help you. For example, only one official is empowered to stamp the AGOA passport, so his absences can delay exports. The Customs office does not operate as a service, and Customs officials are most unfriendly. There is no sign indicating where one is to go for a particular service or process. Often the officer who is expected to provide a service is not there and cannot be found. In such circumstances, exports are stopped at the border until the officer returns, which in some cases is the next day.

F. Documentation

On the Swazi side, several companies complain of the organizational fragmentation related to trade-related documents. Different agencies issue different documents, so the cost of processing trade transactions in time and fees passed along to the exporter is increased. For example, the TPU issues the COMESA certificate of origin, the National Agricultural Marketing Board issues import permits for a range of agricultural goods, and Customs issues the AGOA passport.