Current State Assessment of the Customs Division

Version 3

27 July 2018

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1. Executive Summary

Customs' performance (collect revenue, facilitate legitimate trade and eradicate illicit trade) has regressed since the role-out of the new operating model in late 2015. Service delivery, revenue flows and detecting and deterring illicit trade have been negatively impacted since 2016. Much of the progress made in the 2011-2012 modernisation of customs, appears to have been undone.

The Customs Modernisation Programme delivered wide ranging efficiency gains and compliance improvements, including halving the time it takes to import, world class automation and substantial compliance improvements relating to illicit cigarettes, clothing and textile products and narcotics. Further customs modernisation to evolve into a world-class Customs agency envisaged in the New Customs Acts Programme was delayed in 2014/15 and has delayed delivery by three years.

The self-assessment and internal current state assessment reflect how far customs has regressed since the role-out of the new operating model in late 2015 and the negative impact that has had on service delivery, revenue flows and detecting and deterring illicit trade. So too does it emphasise the lack of progress by customs leadership in instituting the 2015 and 2016 diagnostic recommendations.

By 2018, South Africa has regressed (47 points down) on the World Bank's Ease of Trading across Borders, back to pre-modernisation ratings (South Africa received special mention in the 2013 World Bank Doing Business Report for having improved the most in the ease of trading across borders). Inspection processes are the longest they have been in 7 years (currently 23 days, from 2 days in 2013), the leadership team is described as fragmented, resourcing to risk has regressed and the capacity to deal with illicit trade has been fragmented and is inadequate.

The customs and excise revenue gap identified in the 2015 operating model diagnostic has not been realised. Customs revenue collections have actually declined (R3 billion under target last FY). The new operating model has had the consequence that the units who impact the most on the bulk of the compliance improvement activities in customs report separately into the chief officer at different seniority levels which does not engender end-to-end value chain management of revenue flows and undermines accountability and coordination. Efficiency has deteriorated and inventories have grown substantially (by 319%). Risks are increasing (duty suspension declarations have grown by 8% in the last FY and R9.1 billion gap in Chinese imports of clothing in 2015).

Over 79% of the strategic recommendations made by the WCO in their 2006 diagnostic have been implemented and by 2015, divergent customs systems and processes were a thing of the past. So too, were the reliance on paper based, labour-intensive processes gone. By 2018, very little traction on the recommendations made by the WCO in 2016 has been gained.

The large customs revenue gaps identified in the Bain and Company 2015 Diagnostic have not been realised and the initiatives identified to close the gap have proved largely ineffective. The diagnostic reflects no appreciation for the immense strides of the Customs Modernisation Programme or the fundamental Customs reform planned for through the New Customs Act Programme. It is evident that that the consultation in defining the scope of the Customs diagnostic was extremely limited. The diagnostic offers no explanation for the fact that an operating model that differs substantively from that proposed was implemented. Data quoted to substantive many of the diagnostic findings are unreliable.

The diagnostic is fraught with inaccurate and misleading statements. For example:

- Contrary to what is stated in the diagnostic, in 2015/16, South Africa's World Bank Customs Efficiency rank was the highest it's ever been and puts South Africa on par with developed countries like France and the United States of America.

- Contrary to what is stated in the diagnostic, SARS corruption is not high and is in fact very low compared to its peers. The report quoted is outdated (2010 survey) and the sample size is extremely limited.

- Contrary to what is stated in the diagnostic, empirical literature concludes that the country partner method of estimating the extent of trade mispricing is not robust enough to produce reliable and quantitative measurement of trade mispricing.

- Contrary to what is stated in the diagnostic, penalties are not arbitrarily imposed but are governed by the legislative framework.
- Contrary to what is stated in the diagnostic, the accountability for all Customs Operations, effective 1 July 2012, was made clear.

2. Purpose

The purpose of this paper is to provide an assessment of the Customs and Excise Division's performance post the new operating model's operationalisation in 2015.

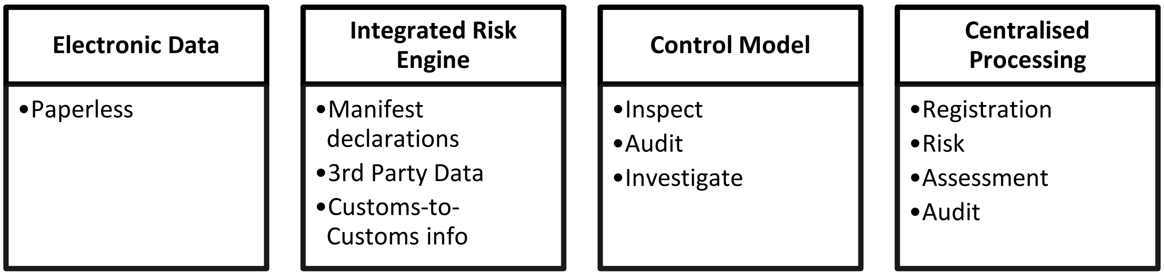
The paper assesses the efficiency gains and compliance improvements from the Customs Modernisation Programme as well as improvements to systems, policies, processes and capacity management. The subsequent comprehensive customs modernisation envisaged in the new Customs Duty Bill and the Customs Control Bill, commonly known as the New Customs Act Programme (NCAP), are also discussed.

The paper details the performance inefficiencies and regression post the new operating model identified by a self-assessment conducted by the current Customs leadership in June 2018 and prepared for a meeting with the acting Commissioner. A separate assessment of performance based on audited, publically available documents and an assessment of the Bain and Company Diagnostic is also included. Independent assessment from international bodies such as the World Bank and the World Customs Organisation (WCO) are also relied upon. The report culminates in an assessment of the customs diagnostic completed by Bain and Company in 2015.

3. Customs Modernisation Programme

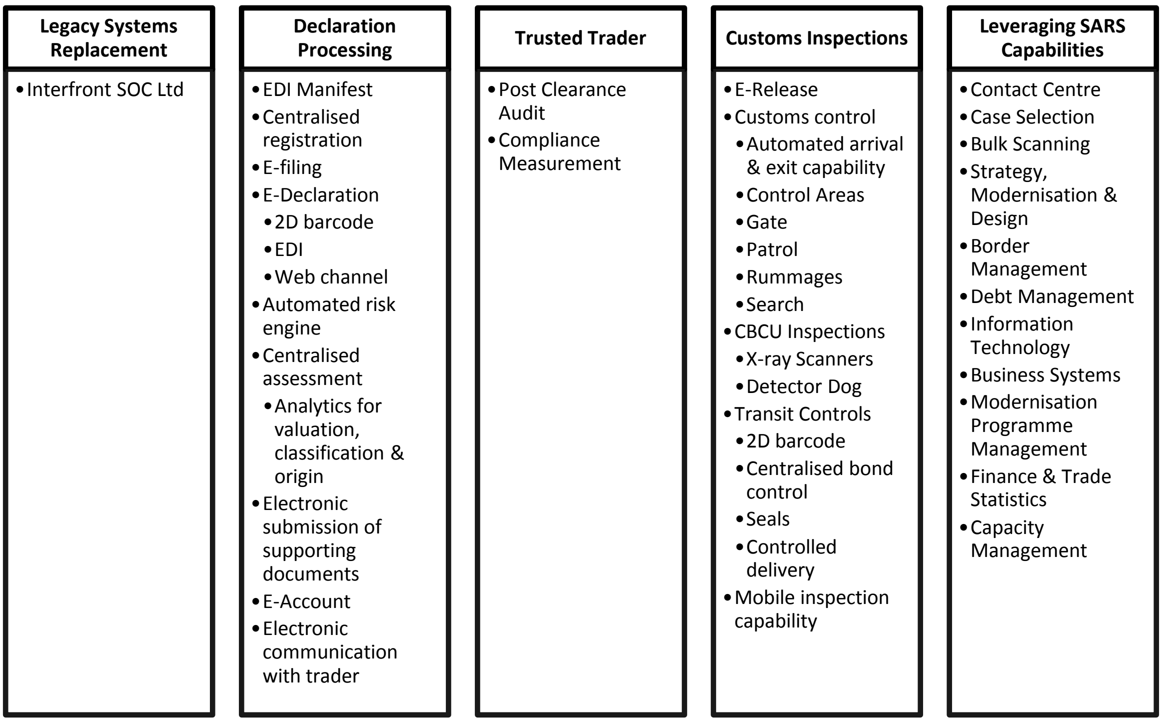
In 2006, customs was characterised by divergent systems and processes were mainly paper-based and labour-intensive. The Customs Modernisation Programme was launched in 2009 to give credence to the WCO's Phase 1 Diagnostic recommendations and the Customs Blueprint. The stated objective of the programme in the SARS Annual Reports was "*to improve the efficiency and effectiveness of Customs and enhance the operations of traders that use its services*" (SARS 2013, p24.) The programme gained traction in 2011 which impacted various areas of Customs and trade by a number of key changes.

Figure 1: Principles of Customs Modernisation



The programme focussed on the end-to-end modernisation of the supply chain process.

Figure 2: Five Programmes of Customs Modernisation



All of the identified Customs Modernisation initiatives were delivered on by FY2014/15. All further Customs Modernisation initiatives attached to the NCAP were halted by the SARS executive in FY2014/15.

3.1. Customs Operating Model 2011-2015

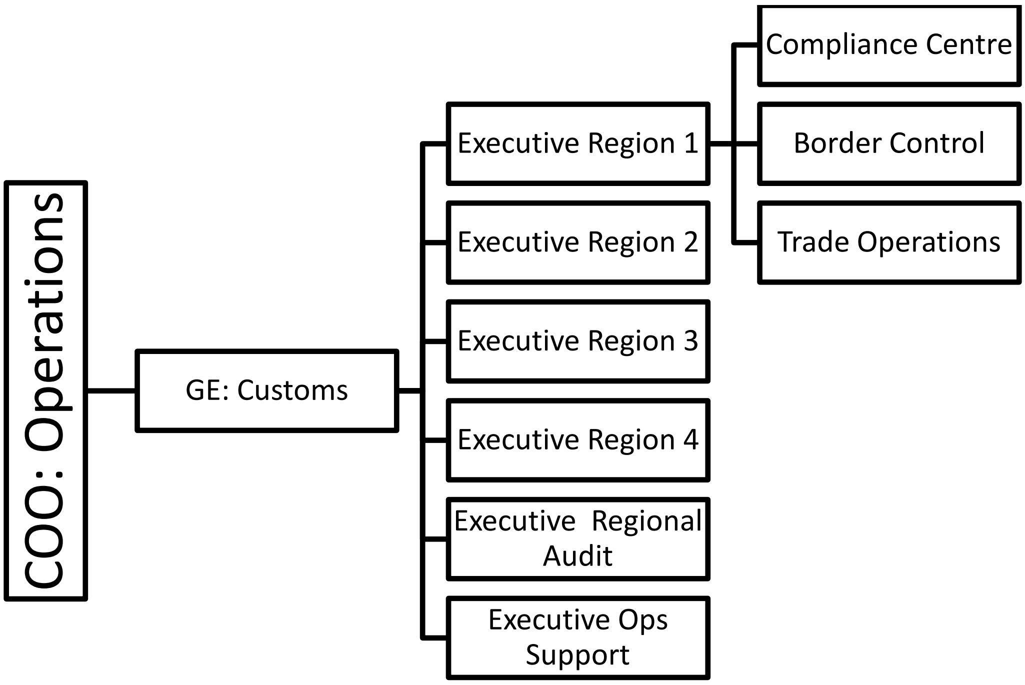
In late 2010, revised operating model changes saw the trade operations aspect of customs moving to the greater operations portfolio and the customs border control (CBCU) functions moving to the enforcement portfolio. In June 2012, further changes to the operating model saw three hundred officers from the Customs function being assigned to the newly formed Enforcement Investigations portfolio (the digitisation of the Customs processes enabled the release of these resources). Customs functions undertaken by the CBCU (management of ports of entry, routine inspections and examinations, baggage and traveller searches and cargo scanner operations) were incorporated into Customs Operations[1].

The revised Operating Model sought to address the question of how best to reorganise the broader Customs function to address the following challenges:

a) Eliminating overlaps of responsibility within the broader Customs function which lead to conflict, lack of alignment and, crucially, lack of responsibility and accountability.
b) Combating illicit economic activity, which includes unscrupulous trade practices which threaten local industry and jobs.
c) Ensuring alignment and coordination of all external Customs engagements to ensure maximum benefit to South Africa.

[1] 29 June 2012 – Newsflash - Announcement by the Chief Operations Officer: Barry Hore

Figure 3: Operating Model 2012/15



The design of the operating model sought to engender efficiencies through healthy competition between regional units. Regional units were therefore designed to ensure parity in structure, inventory levels, staffing, expenditure budgets and income budgets. The high inventory levels at O.R. Tambo International Airport however overburdened region 2 and plans were afoot to create a fifth region.

Within the Operations portfolio, the operating model was designed to leverage on existing capabilities. For example, the group executives of the following portfolios all provided services to customs:

- Contact Centre;
- Case Selection;
- Bulk Scanning;
- Strategy, Modernisation & Design;
- Border Management;
- Debt Management;
- Information Technology;
- Business Systems;
- Modernisation Programme Management;

- Finance & Trade Statistics; and
- Capacity Management.

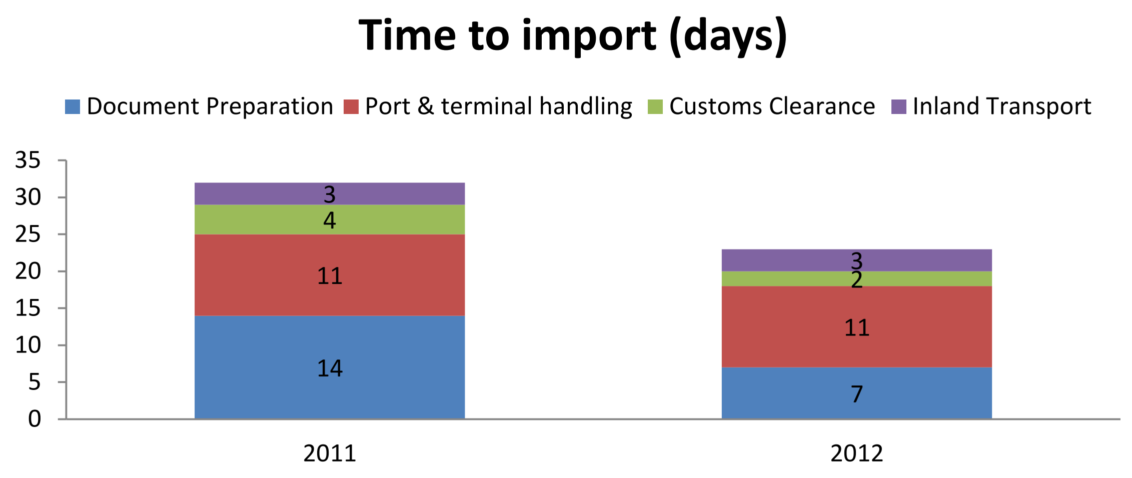
3.2. Achievements 2011-2015

The phenomenal efficiency gains and compliance improvements from the Customs Modernisation Programme as well as improvements to systems, policies, processes and capacity management are listed in the subsequent paragraphs of this report.

3.2.1. Halved the Time it takes to clear Customs

The new Customs Management System enabled customs to respond to traders within seven seconds (from two hours). This is a world class benchmark. In 2013, according to the World Bank Ease of doing Business Report, South Africa reduced the time; cost and documents required for international trade by 9 days and improved its world ranking on the World Bank Ease of Trading across Borders rank by 29 points through its customs modernization program (World Bank 2013, p.86). South Africa continued to progress its ranking up until 2015 where it had advanced 48 points from the pre-modernisation rank in 2010.

Figure 4: World Bank Time to Import 2011 vs. 2012[2]



[2] World Bank Ease of Doing Business 2013.

South Africa received special mention in the 2013 Doing Business report and commendation for having improved the most in the ease of trading across borders (World Bank 2013, p.86). The World Bank also noted that improvements in South Africa have effects throughout southern Africa since overseas goods to and from Botswana, Lesotho, Swaziland and Zimbabwe transit through South Africa, traders in these economies are also enjoying the benefits (World Bank 2013, p.86).

At land border posts, trade facilitation had reached an all-time high with a reduction of average processing time from 2 hours to only 20 minutes. This is a phenomenal achievement if one considers the negative impact of delays to trade on the growth of our economy. Inspection times at borders where reduced from eight hours to two hours.

Productivity at processing centres was increased from 35 cases per person per day to 75 cases per person per day.

3.2.2. World Class Automation

The Customs Modernisation Programme changes have impacted policies, processes and systems, making life far simpler for traders and staff. Release 2 of the programme started in June 2011 and saw 15 Customs offices introduce world class technology to improve the efficiency and effectiveness of customs and enhance the operations of traders. The substantial technological advancements are listed table 1.

Table 1: Technological Advancements at 15 International Ports

Service Manager as a front-end workflow system and advanced case management
New state of the art Customs risk management approach in dealing with cargo
Submission of electronic supporting documents
High-speed bulk document scanners
Electronic release system
Centralisation of declaration processing at four national Compliance centres enabled the concentration of scarce skills
Tariff Management System

In February 2012, the focus shifted to the 17 South African Customs Union (SACU) Customs offices. Release 3 of the programme introduced world class technology to improve the efficiency and effectiveness of customs and enhance the operations of traders. The substantial technological advancements are listed table 2.

Table 2: Release 3 Technological Advancements

Replacement of the legacy processing system which has enabled customs to respond to traders in seven seconds
Automated inspection process to eliminate corruption
Centralised automated risk assessment and case generation giving customs a national view of risk for the 1st time ever
Centralised assessment of declarations away from the border to curtail collusion opportunities
No entry of commercial cargo into the port without pre-clearance
Electronic release system using 2D bar coding ensures that goods are appropriately declared before they enter control areas and that all Customs formalities are finalised before the goods leave the control area
Reregistration of customs clients
Wi-Fi capabilities to enable mobile inspections in the control areas
Mobile inspection devices – 1st in the world
Redeployment of staff to value-adding roles in the port to deal with non-compliant goods
A new Passenger Processing System (PPS) that enhances security and facilitates the exchange of information between border agencies. It comprises an extensive end-to-end business process that extends beyond SARS and incorporates other Government agencies
An automated Traveller Card system that streamlines and automates key processes
New Traveller Cards are scanned together with passports and traveller signatures are captured electronically using a digital signature pad
Automated production reports through Service Manager Dashboard
SAP payment and account management applications replace Customs' legacy financial systems
A new declaration form using dynamic technology for capturing and displaying information
Single registration which consolidates the profiles of taxpayers and traders
Container X-ray scanners at Durban and Cape Town
Baggage scanners at all international mail centres, border posts and international airports

Price referencing tool for undervalued textiles

3.2.3. Substantial Compliance Improvements – Cigarettes

Substantial compliance improvement has been reported in the SARS Annual Reports due to enhanced customs controls on cigarettes in FY2012/13, FY2013/14 and FY2014/15.

a) In FY2012/13, improved inventory management in Customs warehouses reduced the volume of cigarettes warehoused for export by 1.5 billion sticks. A 74.23% decrease in the use of "Warehouse for Export" from 2 billion sticks to 528 million sticks was experienced. Similarly, "Warehousing for home consumption" dropped 57.49% from 647 million sticks declared to 275 million sticks. Duty paid declarations submitted increased from 582 million sticks to 1.2 billion sticks (SARS 2013, p. 23).

b) In FY 2014/15, new warehouse processes were implemented to improve the control of cigarettes moving in and out of the country. Over 1 billion cigarette sticks were prevented from illegal diversion from customs warehouses as a result (SARS 2015, p. 24).

c) Destruction of illicit and counterfeit cigarettes, estimated to be worth R100-million.

d) Seizure of R3 million in smuggled cigarettes which had been concealed in a fuel tanker crossing the border.

3.2.4. Substantial Compliance Improvements – Illicit Clothing and textile products

Substantial compliance improvement has been reported in the SARS Annual Reports due to enhanced customs controls on clothing and textiles in FY2012/13, FY2013/14 and FY2014/15.

a) In FY 2012/13, a new Reference Pricing risk identification for clothing and textiles was introduced and a 16% increase in average unit prices of specific items being monitored against reference prices was experienced (SARS 2013, p. 24).

b) In FY 2013/14, as a result of the Reference Pricing risk indicators on textiles and clothing, the average unit price of textiles climbed 34.6%, the price of curtains rose 30.2%, toilet and kitchen linen 19.4%, bed linen 19.9%, clothing 23.2% and blankets 7.5% (SARS 2014, p. 24).

c) In FY 2014/15, as a result of the Reference Pricing risk indicators on textiles and clothing the unit price of imported bed linen increased 23.9% and the average price of baby clothing climbed 22%. The declared price of imported curtains rose 9.1%, clothing and apparel increased 8% and toilet and kitchen linen increased by 7.6% (SARS 2015, p. 24).

3.2.5. Substantial Compliance Improvement – Narcotics

The compliance improvements in narcotic seizures are too numerous to quote. Alternatively, a snapshot of the narcotic seizures detailed in various SARS media releases in 2012 and 2013, provide a comprehensive view of the breadth and depth of compliance improvements in this area.

a) In 8 days, 3kg of cocaine valued at around R1.5 million concealed in a lap top and 11kg of cocaine, valued at R5.5 million, concealed in three jackets, the soles of 2 pairs of sandals, and a duvet.

b) Crystal Meth (“Tik”) weighing a total of 200kg with a value of over R59 million 10kg of Methamphetamine / Crystal Meth (street value of R3.7M) concealed in shoes, rolls of ribbon and lever arch files.

c) 7kg concealed as “body wraps” under clothes, in the soles of shoes and in false bottoms in luggage, and as “bullets” which were concealed anally. More bullets were found discarded in the sewage system of one of the aircraft.

d) In 72 hours over 54kg of drugs were seized:

- 28kg of “Crystal Meth”, valued at around R8.4 million concealed in a number of ladies handbags;
- Towels which had been soaked in liquid cocaine, estimated at around 9kg, and valued at just under R2.5 million;

- 80 bullets of cocaine swallowed valued at around R216 000; and
- 80kg cocaine, valued at over R23 million, was concealed in an “empty” truck attempting to enter South Africa from Zimbabwe – having started its trip in Malawi.

e) 1 to 30 April 2013 prevented just over 63 kilos of narcotics (nearly 29kg cocaine, 35kg “tik” and ephedrine, and 1.5kg heroin) valued at over R19 million from entering the country.

f) 1 to 31 May 2013 prevented just over 84 kilos of narcotics (nearly 81kg cocaine, 3kg “tik” and ephedrine) valued at almost R24 million from entering the country.

4. New Customs Act Programme

The Customs Duty Bill and the Customs Control Bill were approved by the State President of the Republic of South Africa and published in the Government Gazette No.37821 of July 2014 and No. 37862 of 23 July 2014, respectively. The Customs and Excise Amendment Bill was approved by the President of the Republic of South Africa and published as the Customs and Excise Amendment Act, 2014 (Act No. 32 of 2014) in the Government Gazette No. 37863 of 23 July 2014. The Acts will take effect on a date determined by the President.

The purpose of the rewrite of the existing legislation is to deliver the capability required for SARS Customs to evolve into a world-class Customs agency. The rewrite was to support international legislative requirements, to keep pace with global trade trends and technological advances, and to ensure customs procedures are efficient, predictable and transparent for trade to flourish.

The intended outcomes of the new acts are comprehensive and build on the advancements already operationalised through the Customs Modernisation Programme. The delivery of these comprehensive enhancements was delayed by the halt of modernisation referred to above.

Figure 5: New Customs Acts

Facilitation of trade

- **Transparency and predictability of doing business**
  - Advance ruling regime
  - Fixed penalty regime
  - Tax Court and Ombud
- **Promote exports**
  - Allows for incomplete export clearance declaration
  - Allows for simplified clearance
- **Business competitiveness and stimulating domestic activity**
  - Allows for interest fon approved refunds not paid within 21 days
  - Does away with multiple warehouse clearances
  - Does away with multiple cargo reporting
- **Promote Small, Medium and Micro Enterprises (SMMEs)**

Instrument of control

- **Secure the supply chain by registration and licensing of all entities**
- **Oligation to report cargo before loading in the export country allows Customs to prevent prohibited goods from being loaded onto the export vessel**
- **Improved sealing of containers, vehicles and packages**

The May 2014 New Customs Bill Project Charter envisaged that the changes to the rules, policies, processes, procedures, technology, operating model and structure and the VAT Act and Excise Act would be complete by April 2015 and that the new acts could be operationalised by September 2015 (SARS, slide 8).

However, given the halt to all modernisation programmes and the onset of the new operating model, these timelines were reviewed in October 2015. The project document revised delivery of only three phases and deferred delivery for another two years (November 2017) (SARS, slide 4). It was envisaged that Chapter's 28, 29 and 30 relating to Registration, Licensing and Accreditation, Chapter 3 relating to the reporting of Conveyances and Goods and Chapters 5-20 and 24 relating to Declaration Processing would be operationalised by the end of 2017.

In November 2017, the timelines for delivery of the three phases of NCAP mentioned above were again moved out, this time by just over a year, to the first quarter of 2019. The Reporting of Conveyances and Goods was moved to April 2018, Registration, Licensing and Accreditation to April 2019 and Declaration Processing Tactical release 1 to the end 2018 (SARS, slide 3).

5. Current Customs Leadership's 2018 Self-Assessment

The customs current state self-assessment is contained in an internal presentation titled "*Capability Building Blocks 20180612 V1*" that was prepared for a meeting with the acting Commissioner on 15 June 2018. The presentation identifies various challenges in customs that have transpired since the 2015 Operating Model changes. The challenges are listed in figure 5 (SARS 2018, slide 11).

Figure 6: Self-Assessment Burning Platform

People	Process	Technology	Policy
• Lack of skills • Leaders lack technical skills • Training is sub-standard • HR pipeline does not meet needs • Poor quality performance	• Fragmented operations lack command & control • Client base not segmented & all treated the same • Excessive delays due to revenue focus • Mulitiple interventions & rework due to revenue focus • Extreme processes deviations due to revenue focus • No end-to-end risk management • Neglected control processes • Poor balance of revenue, facilitation and control function	• Technology constrained by NCAP golive date • Many manual processes still to be automated • Risk not automated • Workflows not automated • Lack 3rd party data	• Poor knowledge of the law • Poor policy and SOP adherence • Inconsistent policies

Customs indicated that they do not "*appropriately balance trade facilitation with customs control*" and that they have "*regressed to the gate keeper role*" (changed to risk based approach in 2011) with the consequence of "*delays, excessive costs and generally poor service offering for trade*"(SARS 2018, slide 16).

5.1. Fragmented Leadership

During the meeting discussions around the poor leadership cohesion experienced in the team ensued. The document also avers that there is poor morale within customs and that the leaders of the Customs business lack of technical knowledge (SARS 2018, slide 20). The assessment states that the Customs structure is fragmented and a silo approach to operations is prevalent (SARS 2018, slide 20). During the meeting, a specialist who was intimately involved in the 2015 diagnostic and resultant operating model design vehemently denies that the current structure adopted by Customs was that proposed during the diagnostic. Poor levels of trust between operational units are experienced and service delivery is weak (SARS 2018, slide 20).

It also states that Customs is "*not performance driven*" (SARS 2018, slide 16) that "*performance outcomes are not quality driven*" (SARS 2018, slide 11), that "*quality in execution requires attention*" (SARS 2018, slide 16) and execution is characterised by inconsistent application (SARS 2018, slide 23). Opportunities for leadership and management development have been limited (SARS 2018, slide 20).

The assessment also avers that relationships with other government agencies who work in the port are below standard and results in duplication of processes (SARS 2018, slide 21).

5.2. Defective Inspection Processes

Customs presented inspection statistics that reflect that all steps in the inspection process are overloaded. In most instances, the overload is caused by high levels of rework created throughout the process and which impacts negatively on the efficient management of inventory levels which are the highest they have been in six (6) years. In 2011, during the Customs Modernisation, capacity was designed to efficiently and effectively deal with daily inflow identified by the risk engine. However, the high prevalence of rework coupled with manual case creation (new operating model initiative) which are mainly revenue focussed, has had the effect that various stages of the inspection workflow (still capacitated according to the 2011 risk appetite) are under capacitated. The 2011 capacity design principles are juxtaposed against the 2018 inflow in table 3.

Table 3: Inspection Workflow Design

Inspection Workflow Stages	Daily Inflow		Design Capacity	Daily Overload
Documentary Inspection (DI)	New	1870		
	Rework	561		
	Total	**2430**	**2220**	**210**
DI Technical Review	New	798		
	Rework	212		
	Total	**919**	**551**	**368**
Case Finalisation (FIN)	New	268		
	Rework	80		
	Total	**348**	**598**	**-250**[3]
FIN Technical Review	New	268		
	Rework	80		
	Total	**348**	**567**	**-219**[4]

The leadership of Customs indicated that the average turnaround time for the inspection process has regressed by an enormous 1,050% since 2013 from 2 days to 23 days. Even more shocking is the fact that some consignments are detained, at exorbitant cost per day to the client, for up to 88 days. Customs also indicated that the process was marred by repetitive interventions and unreasonable or senseless requests and unprofessional service (SARS 2018, slide 21). Control processes have been neglected and are characterised by deficient balancing of the revenue collection, trade facilitation and control imperatives (SARS 2018, slide 11).

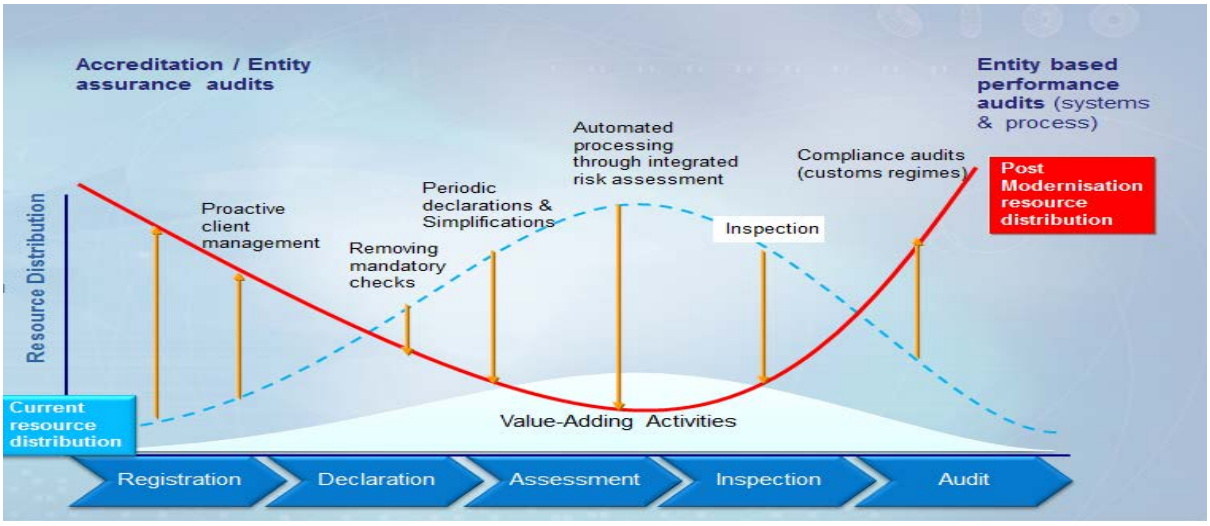
5.3. Regression of Resource Allocation to Risk

[3] The customs leadership team did not address the fact that the case finalisation stages in the inspection work flow are not working at full design capacity which may account for the large inventories mentioned in paragraph 3.3.4. of this report (inventory has grown by alarming 319% since March 2017). This is an opportunity for improved performance management of this stage of the inspection process.

[4] Refer 1 above.

The fact that current resource allocation is almost back to the pre-modernisation (2011-2012) distribution curve was bemoaned by Customs and underscores the statement in paragraph 5 of this report about the regression back to gate keepers rather than risk based management. The diagram reflected in figure 7 was the diagram used during the 2011-2012 Customs Modernisation programme (SARS 2018, slide 8). The presenter indicated that current resource allocation was very close to that reflected in the blue dotted line; in other words also pre-modernisation.

Figure 7: Balancing Requires a Risk-based Approach



5.4. Ineffective Risk Management

The assessment identified inadequate segmentation of the trade and non-existent tailor made responses from the business as an issue that result in multiple interventions from different customs units all focusing on similar activities (SARS 2018, slide 11). The assessment also identified a lack of end-to-end risk management and value chain automation as a critical issue to be addressed together with the lack of third party data from business, government and other customs administrations for enhanced risk assessment (SARS 2018, slide 11). Risk feedback loops and the quality of field reporting were identified as requiring improvement (SARS 2018, slide 22). The authorised economic operator and preferred trader implementation was identified as being too slow and devoid of appropriate trader benefits (SARS 2018, slide 21). The fact that risk management is largely declaration focussed and not entity based was raised as a key issue (SARS 2018, slide 23).

5.5. Inadequate Capacity to deal with Illicit Trade

The assessment states that neither customs nor the SARS organisation as a whole has an integrated approach to addressing illicit trade and that the enforcement capacity is under skilled and inadequate (SARS 2018, slide 22).

5.6. Restricted Automation

Manual entity management processes do not support dynamic and just-in-time stakeholder processes resulting in the repetitive submission of entity supporting documents, manual application processes and lengthy delays (SARS 2018, slide 21). Automated workflows require expansion to include the audit process, front-line activities and the investigative processes (SARS 2018, slide 23).

Manual processes exist and are dependent on the NCAP role out which, currently, has an implementation date of 2025. At the same time, the constraint on information technology resources required for NCAP implies an opportunity cost for the development required elsewhere in customs (Licensing and Registration). Customs also identified a need for automation of the seizure, intervention and activity databases and performance management data sources (SARS 2018, slide 24).

5.7. Below Standard Capacity Building

The Customs self-assessment identified current skills levels in customs as "*insufficient*" and training programs as "*below standard*" (SARS 2018, slide 11). According to the assessment, recruitment, career growth and succession planning of customs officers requires reconsideration. The uniqueness of Customs requires tailor-made recruitment-, induction-, and career progression processes (SARS 2018, slide 20).

The development of a "*skilled, engaged and disciplined workforce"* (SARS 2018, slide 16) was identified as one of the fundamental shifts in how customs conducts its business to improve the quality of its output.

The fact that there are limited customs trainers who deliver theoretical and systems training was highlighted as a key issue. The lack of a curriculum and qualification framework, specialised training, and competency based practical training were equally cited as issues (SARS 2018, slide 20).

5.8. Deficient Policy Adherence

The Customs Self-Assessment identifies deficient policy and Standard Operating Procedure adherence in the business. Equally, poor policy administration is cited as placing key industries under threat. Similarly, weak legislative knowledge by staff has been identified as a critical issue as have inconsistencies in existing policies (SARS 2018, slide 11).

6. Internal Current State Assessment

The internal current state assessment draws on audited and approved internal reports such as the annual reports, the Quantum Leap document, customs daily revenue reports and the Enterprise Capacity Management Dashboard.

6.1. Quantum Leap Assessment[5]

Attrition over the years has left a dearth of customs audit professionals to audit complex high revenue yield industries such as the motor vehicle and clothing and textile industries. Customs core competencies in valuation of goods, rules of origin and tariff classification are not at the expert levels required to extensively audit traders' activities in these areas. Although training in these complex competencies is on-going, the attainment of expert level in these competencies is a long term programme. Added to this is the global growth in corporate transfer pricing and advance import payments which require expert customs valuation skills to audit properly. Trade mispricing and associated illicit financial flows are also on the rise and equally require expert customs valuation and rules of origin skills to appropriately audit.

[5] 2017 *Quantum Step Change In Tax, Customs And Excise Administration*

The growth in global trade coupled with the increasing complexities thereof requires improved risk profiling and case generation for customs front-line officers, auditors and investigators. In line with international best practice, Customs requires the establishment of a National Targeting and Command centre to effectively monitor, manage and direct all customs interventions and ensure appropriate risk mitigation nationally. To keep apace of the growing phenomenon of illicit financial flows which usually manifests in trade mispricing, Customs' ability to identify trade mispricing and Illicit Financial Flows must be enhanced.

Enhancing the capacity of Customs frontline staff has over the years enjoyed substantial investment from a technology and tools perspective. However, capacity to maintain sufficient Customs presence at risk areas within our seaports, airports, land borders and non-designated ports has not received as much investment with the consequence that front line staffing is understaffed, shifts are not appropriately manned to deal with increased trade and traveller flows and high levels of overtime is resorted to.

Customs administrations around the world are increasingly investing in smarter ways to detect non-compliance and non-intrusive inspection [NII] equipment to radically enhance their ability to detect illicit goods and contraband and facilitate legitimate trade. Specialised units such as the Marine, Detector Dog and Scanner units remain a focus area in this regard.

6.2. Declining Revenue Collections[6]

Customs duty and VAT collections have grown exponentially year on year and actual collections outstripped revised estimates year on year by substantial amounts. However, in FY2016/17, collections were almost R3 billion less than the previous financial year and R3.2 billion less than the revised estimate. Weak import growth and contractions in key chapters of vehicles, electrical machinery and clothing on the back of weak local demand conditions, weak merchandise imports and upward pressure on inflation were cited as the reasons for this poor performance.

The potential negative impact of the immense changes to the customs and excise operating model and leadership that coincide with this poor performance has not been evaluated.

[6] Includes revenue from enforcement activities viz. post clearance audit, campaigns, increased inspections etc.

Table 4: 6 Year Comparison of Customs Revenue Collections[7]

	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Revised Estimate	R134 370	R150 170	R174 346	R175 804	R198 535	R197 998
Actual	**R136 013**	**R151 057**	**R175 795**	**R177 981**	**R197 612**	**R194 844**
Difference on Revised	+R1 643	+R888	+R1 450	+R2 177	-R924	- R3 154

In September 2017, through the Regional Revenue Forums, customs identified various factors that impact negatively on customs revenue performance and identified ten (10) expanding the base initiatives to claw back revenue.

Figure 8: 10 Expanding the Base Initiatives Identified by Customs[8]

Increases in the prevalence of duty suspense transactions will be substantively investigated.

Empty containers will be thoroughly inspected to ensure that they do not contain dutiable goods.

Focus on the decommissioning and sale on the local market of containers.

Increased frequency of interventions at non-designated border posts to detect non-declaration of commercial goods.

Cross-border information sharing to confirm the veracity of the import declaration details.

Manual risk profiling using the air cargo manifest as a source document focussing on Clothing and textile, eyewear, gold coins, jewellery and underwear.

Specialised initiatives within and outside border ports to detect non-declaration of commercial goods.

Focus on advance import payments.

Focus on integrated audits of transfer pricing.

Focus on trade mispricing and Illicit Financial Flows (IFFs)

Customs continues to allocate resources to and measure protecting the base initiatives as “extra effort” revenue initiatives rather than focussing on new money or expanding the base initiatives. For example; the campaigns, increased inspections and audit initiatives contain elements of business as usual duties which have existing policies and SOPs such as temporary imports, clothing and textile cases, and increased risk based inspections, and business-as-usual initiatives. A case in point; a target of R1.7 billion has been set for campaigns, R1.2 billion for increased inspections and R6.9

[7] Revenue figures published in the SARS Annual Reports

[8] 2017 *Executive Summary: Customs Regional Revenue Performance*

billion for audit whilst the true expanding the base initiatives of advance import payment (trade mispricing) and transfer pricing have targets of only R250 million and R500 Million, respectively in FY2018/19[9].

Expanding the base initiatives returns do not emulate the Bain 2015 Diagnostic which estimated the revenue gap in these two areas to be R24 billion import VAT, R5 billion in duties and R26 billion in CIT. Consideration should be given to greatly extending the focus and capacity allocation to expanding the base initiatives such as Illicit Financial Flows and Transfer Pricing audits to realise the potential revenue identified.

Table 5: FY2017/18 Expanding the Base Initiatives Collections[10]

Expanding the Base Initiatives	Actual Collection	Target
Advance Import Payments	R82 Million	R240 Million
Transfer Pricing	R453 million	R495 million[11]

The performance and targets set for FY2018/19 must equally be viewed against the revenue gap postulated by the Bain diagnostic. The performance of the protecting the base initiatives (campaigns netted R1.2bn, increased inspections netted R1.2bn and BAU Audit netted R3.3bn[12][13]) indicates that there are still large performance gaps that require improved and accelerated performance improvements and management. The performance could also be as a result of the increased capacity that was focussed on these initiatives and the poor performance of the expanding the base initiatives may be indicative of the opportunity cost of focussing resources elsewhere.

Currently, the units who impact the most on the bulk of the compliance improvement activities in customs, viz. processing, audit, preferred trader and branch operations, report separately into the chief officer at different seniority levels. The does not engender end-to-end value chain management of revenue flows and undermines accountability and coordination. As a result, revenue coordination functions, which operate outside the current operating model and therefore without structural accountability for revenue collections, has been created.

[9] Enterprise Capacity Management Dashboard accessed at 13:08 on 11 June 2018
[10] *Customs Initiatives Report 29 Mar 2018*
[11] Customs Initiatives Report dated 29 March 2018
[12] Customs Initiatives Report dated 29 March 2018
[13] In FY206/17, audit initiatives netted R4.3bn, increased inspections R134m and strategic plan initiatives R103m. Customs Initiatives report dated 31 March 2017.

6.3. Inconsistent Actions to Stem Illicit Trade[14]

Inconsistent reporting over the last six years on matters normally associated with illicit trade (narcotics, cigarette seizures etc.) makes it difficult to analyse performance in this area or draw any conclusions about performance in detecting illicit trade. The analysis is also made more convoluted by the various different operating models for the enforcement arm of customs, the Customs Border Control Unit (CBCU), during this period. From 2010 until 2012, the CBCU was split out of customs and reported into the enforcement structure. In 2012, a dedicated enforcement and a specialist tactical Customs enforcement facility in enforcement was created and the bulk of the CBCU was reunited with customs trade operations in the Operations portfolio.

Table 6: YOY Comparison of Illicit Trade Seizures and Risk Targeting

		2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Illicit Cigarette Seizures	No million sticks	755	54		204	134	
	Value Millions	R278.4m	R37.8m		R110m		
Narcotic Seizures	No	2,937					788
	Value Millions	R200.9m	R128.4m				R450.7m
Clothing Seizures	No	7,348,937 items	254,000	274 cases	630 cases	495,436	
	Value Millions	R1,100m	R178.2m	R28.3m	R68.8m	R8.7m	

Seizures of illicit goods appear to be regressing.

6.4. Efficiency has deteriorated

[14] Figures published in the SARS Annual Reports

Efficiency has drastically deteriorated year on year. The current customs inventory has grown by alarming 319% since March 2017. There has been significant growth in processing inventories to 19,078[15] (vs 5,982 in March 2017[16]). Pended case inventory is 15,751 (82%) with an average age of 255 days and represents a 48% increase on the FY2016/17 pended case inventory.

The high levels of inventories coupled with the high prevalence to pend cases rather than finalise them are cause for concern and concerted effort is required to clear out these cases as a potential source of revenue in the short term.

6.5. Trade Statistics Indicators[17]

The trade statistical data is utilised to assist the Customs and Excise Division and Regional Revenue Steercoms to identify potential Customs duty, Import VAT and Excise revenue leakage. Specific attention has been paid to areas traditionally abused by traders to circumvent payment of duties and import VAT.

The extraction of revenue has increased by 0.1 percentage point when compared to the previous financial year. Duty paid declarations for home consumption has increased by 1.3%. Of concern, is the increasing growth in duty suspension declarations entries which have increased by 7.4% (warehousing for home consumption) and 29.4% (warehoused for export). At the same time, removal in transit declarations have increased year-on-year by 10.8%.

Although warehousing and removal in transit is a legal practice, the increases should be investigated to understand whether the removal to the warehouse is legitimate and whether the movements from the warehouse or in transit through South Africa were not subject to abuse (ghost exports etc.).

6.6. Mirror Trade Statistics Analysis[18]

[15] Enterprise Capacity Management Dashboard accessed at 14:57 on 11 June 2018
[16] Customs Inspections Daily Report - 2017-03-02
[17] Extended EXCO Economic and Revenue Report April 2018
[18] 2018 *South African and Peoples Republic of China Trade Asymmetries*

Despite the compliance improvements relating to the valuation of clothing and textiles reported in paragraph 3.2.4. of this report, recent bilateral engagement with the General Administration of Customs of the People's Republic of China (GACC), where the GACC's trade data was shared with SARS, has identified concerning discrepancies. In 2015, Chapters 61[19], 94[20] and 62[21] imports recorded by South Africa were R13.8 billion less than exports from China.

Articles of apparel and accessories of Chapter 61 were R4.8 billion less than exports from the China. Furniture and accessories of Chapter 94 were R4.6 billion less than exports from the China. Articles of apparel and accessories of Chapter 62 were R4.3 billion less than exports from the China.

Table 7: Imports Asymmetry by Chapter - 2015

Imports Value in R'000								
Year 2015								
Chapter	Chapter Description	China's exports to South Africa	South Africa's imports from China	Asymmetry	Absolute Asymmetry	Relative Asymmetry (%)	Share of Total Absolute Asymmetry (%)
'61	Articles of apparel and clothing accessories, kn	9 693 222	4 804 913	4 888 309	4 888 309	67.4%	22.9%
'94	Furniture; bedding, mattresses, mattress suppo	9 344 582	4 727 846	4 616 736	4 616 736	65.6%	21.7%
'62	Articles of apparel and clothing accessories, no	10 070 260	5 807 351	4 262 909	4 262 909	53.7%	20.0%
'67	Prepared feathers and down and articles made	3 965 335	229 653	3 735 682	3 735 682	178.1%	17.5%
'87	Vehicles other than railway or tramway rolling	6 731 860	3 919 140	2 812 720	2 812 720	52.8%	13.2%
'10	Cereals	980 369	1 679 867	-699 498	699 498	52.6%	3.3%
'69	Ceramic products	6 129 545	7 187 830	-1 058 285	1 058 285	15.9%	5.0%
'22	Beverages, spirits and vinegar	1 865	1 748 854	-1 746 989	1 746 989	199.6%	8.2%
'86	Railway or tramway locomotives, rolling stock	28 482 221	37 419 806	-8 937 585	8 937 585	27.1%	41.9%
'27	Mineral fuels, mineral oils and products of thei	38 457 137	49 030 995	-10 573 858	10 573 858	24.2%	49.6%
Total (selected chapters)	**Total (selected chapters)**	**113 856 396**	**116 556 255**	**-2 699 859**	**2 699 859**	**2.3%**	**12.7%**
Total (other chapters)	**Total (other chapters)**	**87 282 187**	**68 667 741**	**18 614 446**	**18 614 446**	**23.9%**	**87.3%**
Grand Total (all chapters)		**201 138 583**	**185 223 996**	**15 914 587**	**21 314 305**	**11.0%**	**100.0%**

Although, trade asymmetries exist due to certain methodological and partner country discrepancies, the asymmetries are concerning given that the discrepancy that appears to have the greatest effect on mirror trade analysis (CIF-FOB valuation difference) is not prevalent in this instance as China exports on a FOB basis and South African imports are reported on a FOB basis. Therefore, in this instance, there is a very high possibility that the asymmetries are a reflection of fraud relating to type, quantity, value and origin that must be investigated.

[19] Chapter 61: Articles of apparel and clothing accessories, knitted or crocheted
[20] Chapter 94: Furniture: bedding, mattresses, mattress supports, cushions and similar stuffed furnishings: lamps etc.
[21] Chapter 62: Articles of apparel and clothing accessories, not knitted or crocheted

7. Independent Assessment

The independent assessment from international bodies' draws on the last 10 years of World Bank Ease of Doing Business reports, specifically, the Ease of Trading across Borders rating. The WCO has completed diagnostic missions in South Africa in 2006 and, ten years later, in 2016.

7.1. Trading across Borders Rating has degenerated

Table 8: World Bank Ease of Trading Across Borders 10 Year Comparison

World Rank	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
	147	148	149	144	**115**	**106**	**100**	130	139	147

In 2013, South Africa improved its world ranking by 29 points through its customs modernization program and implemented measures that reduced the time, cost and documents required for international trade. South Africa continued to progress its ranking up until 2015 where it had advanced 48 points from the pre-modernisation rank in 2010. Unfortunately, by 2018, the rank has degenerated 47 points and is back at pre-modernisation ranking experienced 10 years ago.

South Africa received special mention in the 2013 Doing Business report and commendation for having improved the most in the ease of trading across borders (World Bank 2013, p.86). The World Bank also noted that improvements in South Africa have effects throughout southern Africa since overseas goods to and from Botswana, Lesotho, Swaziland and Zimbabwe transit through South Africa, traders in these economies are also enjoying the benefits (2013, p.86).

7.2. World Customs Organisation Diagnostics

The WCO conducted a comprehensive diagnostic of Customs systems, procedures and structures in 2006 and completed a follow-up progress evaluation in 2016, focusing on an overall Operating Model for SARS Customs and Excise Division, risk management related initiatives and direction, the implications of the New Customs Act Programme (NCAP), the nexus between IT advances and subsequent process implementation and strategic human resource management and development.

In 2006, customs was characterised by divergent systems and processes were mainly paper-based and labour-intensive. Of the 33 strategic recommendations made by the WCO, 79% have been implemented. Various changes to operating models and strategic direction have changed the focus of 18% of those recommendations initially implemented. However, some of the recommendations are still valid capacity building recommendations and could be considered for further performance improvements.

A summary of the overall recommendations made by the WCO in 2006 are reflected in figure 1 hereunder.

Figure 9: 2006 WCO Recommendations[22]

Launch campaign to improve the visibility of Customs at the points of entry.
Adopt risk-based approach to the management of goods and people crossing the border.
Adjust the parameters for the selection of transactions for examination to include economic compliance and anti-smuggling/security indicators.
Consider the introduction of a flatter organizational structure.
Consider establishing Customs Operational Centres of Excellence.
Review export controls.
Organize the anti-smuggling function on a national level.
Engage a Customs computer expert to review the proposed IT strategy.
Play a key role regionally in leading the development of SACU Customs Services.

During the course of the 2016 WCO evaluation, evidence of progress was found for each of the above overall recommendations (WCO 2016, p.4). Five (5) key recommendations were made during the 2016 diagnostic and are reflected in figure 5 of this report.

[22] 2006 *Summary of WCO Diagnostics recommendations*

Figure 10: 2016 WCO Recommendations[23]

Refine the operating model to clarify command and control lines at the senior level to front-line level, ensuring that the supporting functions of intelligence and risk management complement decision-making.
Consolidate the Risk Management functions and activities under a single functional structure supported by appropriate governance.
Rationalise IT information holdings and collection methods, bringing together multiple locally designed databases.
Include Leadership and Management professional development in training
Strategic Human Resource development and proposed work to assign competencies to existing job descriptions.
Conduct a WCO Time Release Study (TRS) as a useful baseline to improve coordination and processes.

Although some progress has been made against these recommendations, none have, to date, been fully implemented.

8. 2015 Bain Diagnostic Findings

During the course of 2015, Bain and Company completed an operating model diagnostic of SARS with a transformation ambition of materially increasing revenue and ensuring control over border posts by 2017. To achieve this ambition, five (5) strategic initiatives, reflected in figure 11, were recommended.

Figure 11: Bain 2015 Recommendations[24]

Reinvent risk engine and principles that drive it.
Regain control and final release authority at ports/borders.
Establish strong and visible customs and excise enforcement.
Modernise and align excise to customs operations.
Enforce customs and excise compliance.

The 2015 diagnostic asserts that the customs and excise revenue gap could be as high as R70 billion (8% of total collections) (SARS 2015, p.6). The diagnostic claims that there was potential to increase revenue by R20-45 billion per annum by implementing the recommendations (SARS 2015, p.7). According to the diagnostic, five (5) drivers of the revenue gap were identified.

[23] 2016 *WCO Phase 3 Progress Evaluation*
[24] 2015 *Customs and Excise, Phase 2a Consolidated Diagnostic*

a) Undeclared imports where goods arrive at the port and are not declared to customs resulting in a revenue gap of R20 billon import VAT and R4 billion duties. Assumptions that inform the revenue gap assumptions are that 11% of all goods imported by sea and air and 5% of goods imported over land are not declared.

b) Undervalued imports result in a gap of R5 billion import VAT and R1 billion duties. Assumptions that inform the revenue gap assumptions are that 20% of all low risk cases and 70% of all high risk cases are undervalued.

c) Inflated export values and subsequent overstated refunds result in a gap of R4 billion import VAT and R1 billion in duties. Assumptions that inform the revenue gap assumptions are that 5% of all exports are either false exports (so called ghost exports) or are overvalued.

d) Trade mispricing on exports, assumed to be 20% of CIT, results in R26 billion revenue gap in CIT.

e) Non- or under declaration by travellers results in R10 million revenue gap. Assumptions that inform the revenue gap assumptions are that a 25% increase in searches and a 10% increase in yield per search will raise the revenue.

The diagnostic identified three strategic initiative charters with timelines for delivery and potential revenue collections which are reflected in table 14 of this report. The substantial potential customs revenue gap identified has not been realised.

8.1. Incorrect World Bank Customs Efficiency Rank

The submission to the Commission of Inquiry into Tax Administration and Governance by SARS is misleading in that it states that SARS customs efficiency was ranked by the World Bank at "*61st out of 143 benchmarks*" (Extract from the submission, paragraph 4)b.i.). Evidence of a ranking that low for South Africa since 2007 (when the first LPI was launched) cannot be found on the World Bank site and this statement is incorrect.

During the time period of the diagnostic, South Africa's custom's efficiency ranking was the best it's ever been at 18th out of 160 countries (improvement of 24 points in the ranking from 2013). The lowest efficiency rank was 42nd out of 160 countries (2013/14).

Table 9: South Africa's World Bank LPI Customs Scorecard[25]

Year	Customs World Rank	Customs Actual LPI Score
2016	18	3.6
2014	42	3.11
2012	26	3.35
2010	31	3.22
2007	28	3.22

The 2015/16 rank actually puts South Africa on par with developed countries – just short of the rank for France and the USA.

Table 10: LPI Global Customs Rankings 2016[26]

Country	Customs World Rank	Customs Actual LPI Score
Austria	15	3.79
United States	16	3.75
France	17	3.71
South Africa	18	3.6

Of concern is the fact that the diagnostic fails to mention that the World Bank Ease of Trading across borders ranking improvements and South Africa's accolades received special in the 2013 World Bank Doing Business report (discussed in more detail in paragraph 7.1. of this report). The omission of the Ease of Doing Business ranking and the use of incorrect data in the diagnostic is misleading.

8.2. Transparency International Statement Incorrect

[25] The World Bank, *International LPI Country Scorecard*

[26] The World Bank, *International LPI Global Ranking*

The submission states that transparency international rated SARS corruption "*high*" (Extract from the submission, paragraph 4)b.i.1.). Conversely, the slide deck states that "*SARS is better than developing peers*" but "*performing poorly against benchmarks*" (SARS 2018, slide 35). The "*benchmarks*" referred to are not unpacked and are therefore open to conjecture.

The "*Daily Lives and Corruption: Public Opinion in Southern Africa* report is too outdated (7 years ago) for it to be considered relevant for a diagnostic performed in 2015. The survey relates the low percentage of respondents who have come into contact with tax revenue and customs in 2010 and paid a bribe to those institutions in that year (4+13=16).

Table 11: Transparency International bribery by institution across six countries in Southern Africa

Service	DRC	Malawi	Mozambique	South Africa	Zambia	Zimbabwe
Tax revenue	52%	12%	9%	4%	7%	14%
Customs	48%	41%	33%	13%	25%	36%

The percentage of people who bribed the tax revenue service (4%) and customs (13%) in South Africa is very low compared to the other southern African countries surveyed (the report does not suggest a norm). The sample size of people who responded that they had had contact with SARS was limited viz. only 37.1% had contact with tax revenue and only 14.7% with customs.

It appears that the inclusion of an outdated report, assigning incorrect statements like SARS corruption is "*high*" whereas the report concludes that corruption in SARS is low compared to the other countries surveyed, is misleading.

8.3. Undeclared Consignments Statement Misleading

The submission states that there is a lack of goods control and in support of this, quotes the that in Durban, "*~20% of containers are undeclared before ship arrival*", "*~6% remain undeclared after 28 day(s)*" and "*~3% are transported to City Deep although SARS does not control road traffic*" (Extract from the submission, paragraph 4)b.ii.2.). The submission fails to take into account the fact that an integrated set of policies and procedures are required to ensure increased safety and security, as well as effective trade facilitation and revenue collection.

Existing international conventions, international standards, guidelines and frameworks, national legislation and the set of policies and SOPS provide the requirement and obligation for customs clearance. Sanctions are applied to those who do not comply. For example: Standard 4 of Specific Annex A.1 to the WCO's Revised Kyoto Convention (RKC)[27] holds the carrier responsible to Customs for ensuring that all goods are included in the cargo declaration or are brought to the attention of the Customs in another authorized manner. In other words, until the goods are customs cleared, they are still under customs control, are not considered "*undeclared*" and the carrier is obligated to ensure that all customs formalities are met.

The RKC equally provides standards to deal with transhipment goods and allows goods to be transported under customs transit from an office of entry to an inland Customs office (City Deep in this instance). In other words, until the goods are transhipped, they are still under customs control, are not considered "*undeclared*" and the carrier is obligated to ensure that the goods are transhipped. Goods can therefore move from one port to another on the basis of the bill of lading which consigns it to that port and the goods are still deemed to be under customs control.

So too does the submission, by virtue of its reference to undeclared containers as a "*lack of control*", ignore that the application of risk management as set out in the RKC is an invaluable best practice to carry out effective and efficient Customs control[28] and to allow better use of available resources[29].

[27] The RKC is the blueprint for modern and efficient Customs procedures and it supports the international trading system by creating predictability, efficiency and a level playing field that modern trade requires.

[28] Faster release of goods at borders is beneficial directly and indirectly for both Customs administrations and businesses. For example, it enables Customs administrations to process more transactions without delay at borders, so that they can deploy their limited resources to high-risk cargoes. Assuming that trade costs were reduced by 1 percent on average world-wide, it is estimated that world income would increase by about USD 40 billion (OECD, 2003).

[29] The WCO provides a non-exhaustive list of instruments, tools and guidelines to aid customs administrations to ensure integrated supply chain management. For example: Revised Kyoto Convention (RKC)1 General Annex (GA) (Standard 6.1); Revised Guidelines to Chapter 6 of GA to RKC; Guidelines on Integrated Supply Chain Management (ISCM); Guidelines for the Development of National Laws for the Collection and Transmission of Customs Information; Model Bi-lateral Agreement; International Convention on Mutual Administrative

Through the implementation and use of a risk management programme, Customs can determine which goods and which traders are in compliance with Customs law and thus pose a low risk for control purposes.

In exercising the control that is limited to that necessary to ensure compliance with the Customs law (RKC Standard 6.2):

- Customs must use risk management (RKC Standard 6.3) and risk analysis to determine which goods, including means of transport, should be examined and the extent of the examination (RKC Standard 6.4);
- Risk management includes audit-based controls (RKC 6.6); and
- Information technology and electronic commerce must be used to the greatest possible extent to enhance Customs control (RKC Standard 6.9).

Therefore, customs will assess the risk prevalent in any goods and act appropriately based on the risk management framework and compliance programme – shift from gate-keeper to risk-manager. Un-cleared goods are not necessarily an indicator of lack of control and the failure to highlight the nuances of customs control in the diagnostic is misleading. So too, by not referring to the relaxations of customs control contemplated in the Customs Control Act (incomplete clearance declaration and simplified clearance) and the enhancements to customs control contemplated (registration and licensing of all entities in the supply chain, obligation to report cargo before loading in the export country and improved sealing of containers, vehicles and packages), the diagnostic creates misleading perceptions.

8.4. Bain Initiative to Enhance Goods Control was Ineffective

The goods control project launched in Durban as a result of the Bain and Company proposals proved largely ineffective (only R20 million collected over 2 years)and does not underscore their proposition that there is a lack of controls in Durban that leads to revenue leakage. The poor performance of

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Assistance in Customs Matters (Johannesburg Convention); Risk Management Compendium; WCO Recommendations on UCR 2004; WCO Data Model; AEO Implementation Guide; AEO Compendium; MRA Guidelines.

these initiatives must be viewed against the backdrop of the fact that the consultants asserted that the revenue gap due to undeclared imports was R24 billion[30].

Table 12: 2016/17 and 2017/18 Goods Control Project Results

Financial Year	Office	Target	Achievement
2016/17[31]	Durban	R7M	R5.3M
	City Deep (Johannesburg)	R1.5M	R240K
2017/18[32]	Durban	R30M	R14.4M
	City Deep (Johannesburg)	R100K	R160K

The reference to a lack of goods control and the quantum of the revenue gap as R24 billion in the diagnostic is misleading.

8.5. Misleading Statement on X-Ray Scanner

The submission states that there is a lack of goods control and in support of this, quotes that the container x-ray scanner in Durban "*only*" has a 3% success rate and operates at 25% capacity (Extract from the submission, paragraph 4)b.ii.1.).

The diagnostic fails to mention that the x-ray scanner is integrated with SARS risk and case management systems and provides leading technology to process searches in a fast[33] and efficient manner. The number of scans (capacity) that can be conducted is dependent on a number of issues and will vary on a daily basis. Issues that have the greatest impact on the daily scanning capacity are:

[30] The 2015 diagnostic asserts that the revenue gap for undeclared imports where goods arrive at the port and are not declared to customs is R20 billon import VAT and R4 billion duties.

[31] SARS, *Strat Plan Initiatives Report 31 March 2017*

[32] SARS, 2018, *Customs Regional Initiatives Report 29 March 2018*

[33] Able to scan >100 Containers per 24 Hr period at an average (end to end) processing time of 13 minutes per truck

- Weather conditions impacting on port closure[34]; and
- Number of risk cases alerted by the automated risk engine.

The scanner statistics reported on 21 July 2015[35] paint a different picture to that reported by Bain and Company.

The scanner went live on 11 August 2014 and in less than a year:

- 9039 scans were conducted;
- Throughput was better than capacity at 8-10 minutes per scan;
- 188 successes were reported; and
- 7 seizures were affected.

The extract of the submission fails to mention that the scanner successes and throughput they report are "*self-reported by Scanner Team*" (SARS 2018, slide 125) and that they did not triangulate this data against the automated data disseminated on a daily basis via "*PROD Customs Cargo Scanner*" report. The use of self-reported data to inform conclusions, without triangulating the data, is misleading.

8.6. Misleading Statement on Trade Mispricing Revenue Gap

The submission states that there is a lack of goods control and in support of this, quotes that the SARS data indicates potential export mispricing with a net understatement of ~R1.5T (Extract from the submission, paragraph 4)b.ii.4.). The submission fails to take into account the wide range of

[34] It is not unusual for the Port of Durban to experience port closures due to adverse weather conditions. For example, on 03 November 2015 09:57 AM, the customs regional manager for KZN reported "*severely reduced scanner throughput in the past three days. This is mainly due to the port been closed for the better part of the three days due to severe wind conditions*".

[35] I provided the acting Chief Officer: BAIT with these statistics on Tue 2015/07/21 at 06:44 AM

empirical literature that advocates against using mirror trade statistics (partner country method) to determine potential revenue leakage.

The most recent study report, *WCO Study Report on Illicit Financial Flows via Trade Mis-invoicing*, by the WCO commissioned as a result of the G20 Leaders' Communiqué September 2016[36] concludes that "*estimates of IFFs/TM (trade mispricing) are not sufficiently robust across the two methods"* and that "*the high estimates of IFFs/TM which feature prominently in current literature, research and even media outlets, should not be understood as a reliable quantitative measurement of the scale of IFFs/TM".*

The consultants asserted in the 2015 diagnostic that trade mispricing on exports, using the country partner method, results in R26 billion revenue gap in CIT. The statement is misleading in that it assigns a revenue gap using unreliable and implausible methodology.

8.7. Misleading Perception Created relating to Penalty Imposition

Penalties imposed are governed by existing legislation (Customs and Excise Act no. 91 of 1964, as amended). Customs penalties are imposed in accordance with Sections 78 to 86A of the Act. The Act distinguishes between less serious offences and serious offences and the severity of the penalties increase in direct relation to the extent of the infringement. Internal policies[37] and SOPS specify the legislative framework for the imposition of Customs penalties and forfeiture and clarify the delegation of powers for demanding and imposing penalties and applying remission. The Promotion of Administrative Justice Act (PAJA) No. 3 of 2000 is also applicable in that it ensures that customs, in imposing administrative penalties and forfeiture, act lawfully, reasonably and are procedurally fair.

Offences may render the client liable to monetary penalties, criminal prosecution and/or suspension and/or cancellation of their deferment account, registration, license, accreditation and/or designation. Officers are entitled to detain any ship, vehicle, plant, material or goods at any place for the purpose of establishing whether it is liable to forfeiture under this Act.

[36] The 2018 WCO Study Report on Illicit Financial Flows via Trade Mis-invoicing has been prepared in collaboration between experts and scholars from the WCO, OECD, GFI, academia and Customs administrations, under the responsibility of the Secretariat of the WCO.

[37] SARS Offences and Penalties - Internal Policy SC-CO-01-01 Revision 9 and SARS Customs Contravention List SC-CO-01-01-A01 Revision 6.

Given the legislative framework in place, penalties imposed are not arbitrary and cannot therefore be cannot be "*too low*" (SARS 2018, Slide 25) or "*ineffective*" (Extract from the submission, paragraph 4)b.iii.3) or "*do not sufficiently deter non-compliance*" (SARS 2018, slides 26 and 28). They are lawfully imposed in terms of the current legislation based on the seriousness of the contravention.

The submission creates the impression that penalties are arbitrarily imposed. It also ignores the enhancements to penalty imposition contemplated in the Customs Control Act soon to be implemented.

8.8. Ownership of Customs Statement Misleading

The submission states that there is unclear ownership of Customs (SARS 2018, Slide 52). In line with the operating model at that time, the Chief Officer: Operations had full accountability and responsibility for all customs administration and enforcement actions in the customs control areas and post clearance audits. The Chief Officer: Tax and Customs Enforcement Investigations had full accountability and responsibility for all customs enforcement actions outside the customs control area and customs investigations.

This clarity was announced in a SARS newsflash in June 2012 (The following people will assume full accountability for all Customs Operations effective 1 July 2012: Rae Cruikshank – Group Executive: Customs Operations[38]). All performance scorecards, including the SARS Strategic Scorecard, reflect this clarity of accountability.

8.9. Consultation on Diagnostic Scope for Customs was Limited

The submission states that Mpho Mashaba was interviewed to establish the customs and excise scope of the diagnostic (SARS 2018, slide 4). At that time, Mr Mashaba was not employed in Customs and had not been employed in customs for approximately five years prior to 2015. He therefore had very little experience, if any at all, of the Customs Modernisation Programme that was launched in

[38] 29 June 2012 – Newsflash - Announcement by the Chief Operations Officer: Barry Hore

2011. He equally had no experience of managing a customs operations post customs modernisation in 2011.

Unlike other areas of the business, the Group Executive: Customs Operations was not interviewed by the consultants. The executive of the Customs Modernisation Programme at that time was not consulted. The project manager of the New Customs Acts Programme (NCAP), the next customs modernisation programme, was not consulted.

None of the customs external stakeholders were interviewed, and none of the international best practice WCO standards and frameworks, guidelines or recommendations was consulted by the consultants in establishing the scope. The 2006 WCO comprehensive diagnostic of SA customs procedures, systems and structures was not consulted.

8.10. Misleading Infrastructure Statements

The submission creates the impression that port, airports and depot infrastructure management, including access gates (Extract from the submission, paragraph 4)b.ii.3.) and access controls, security camera surveillance etc. (SARS 2018, slide 23), is the mandate of SARS.

This is factually inaccurate as Transnet National Ports Authority and Airports Company South Africa own and manage port and airport infrastructure whilst the depots are privately owned SARS registered facilities.

8.11. Operating Model Conclusions Unclear

No explanation is proffered for the reasons why the operating model proposed for Customs and Excise (SARS 2018, slide 67-69) differs substantially from that finally adopted (SARS 2018, slide 71).

Figure 12: Operating Model Proposed by Bain & Company

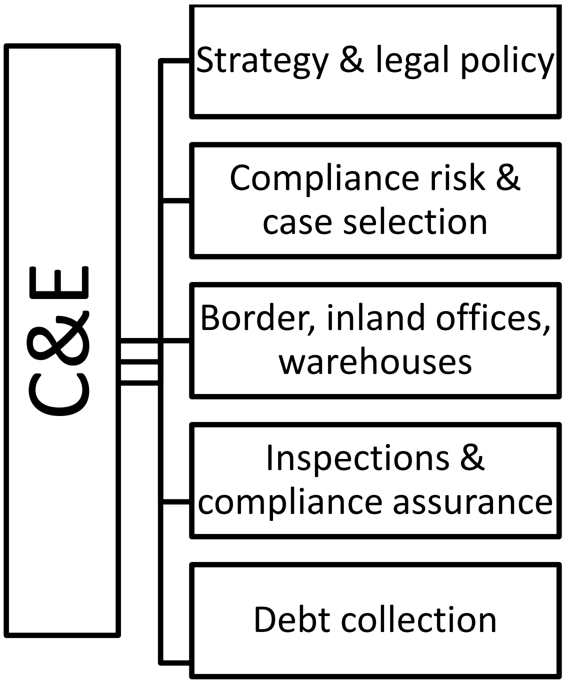
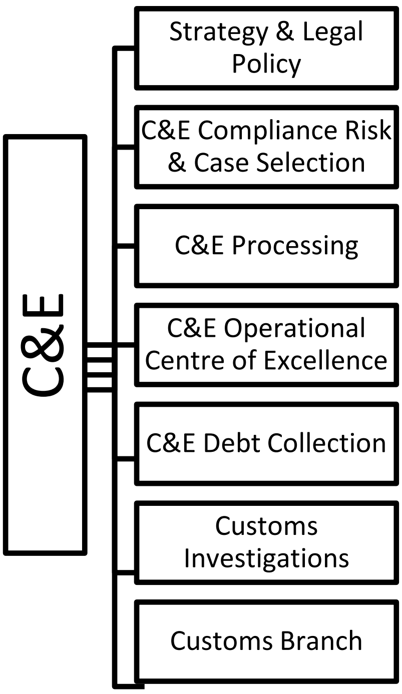


Figure 13: Operating Model Implemented by SARS



8.12. Data is Unreliable

In many instances, the submission caveats the data displayed as "*based on management estimations*" (SARS 2018, slide 124) or "*self-reported" by staff* (SARS 2018, slide 125). No attempts appear to have been made to triangulate the data against the automated reports that are disseminated on a daily basis viz. "*Customs Inspections Daily Report*" and "*PROD Customs Cargo Scanner*".

9. Conclusion

Customs' performance (collect revenue, facilitate legitimate trade and eradicate illicit trade) has regressed since the role-out of the new operating model in late 2015. Service delivery, revenue flows and detecting and deterring illicit trade have been negatively impacted since 2016. Much of the progress made in the 2011-2012 modernisation of customs, appears to have been undone.

The Customs Modernisation Programme delivered wide ranging efficiency gains and compliance improvements, including halving the time it takes to import, world class automation and substantial compliance improvements relating to illicit cigarettes, clothing and textile products and narcotics. Further customs modernisation to evolve into a world-class Customs agency envisaged in the New Customs Acts Programme was delayed in 2014/15 and has delayed delivery by three years.

By 2018, South Africa has regressed (47 points down) on the World Bank's Ease of Trading across Borders, back to pre-modernisation ratings (South Africa received special mention in the 2013 World Bank Doing Business Report for having improved the most in the ease of trading across borders). Inspection processes are the longest they have been in 7 years (currently 23 days, from 2 days in 2013), the leadership team is described as fragmented, resourcing to risk has regressed and the capacity to deal with illicit trade has been fragmented and is inadequate.

The customs and excise revenue gap identified in the 2015 operating model diagnostic has not been realised. Customs revenue collections have actually declined (R3 billion under target last FY). The new operating model has had the consequence that the units who impact the most on the bulk of the compliance improvement activities in customs report separately into the chief officer at different seniority levels which does not engender end-to-end value chain management of revenue flows and undermines accountability and coordination. Efficiency has deteriorated and inventories have grown substantially (by 319%). Risks are increasing (duty suspension declarations have grown by 8% in the last FY and R9.1 billion gap in Chinese imports of clothing in 2015).

Over 79% of the strategic recommendations made by the WCO in their 2006 diagnostic have been implemented and by 2015, divergent customs systems and processes were a thing of the past. So too, were the reliance on paper based, labour-intensive processes gone. By 2018, very little traction on the recommendations made by the WCO in 2016 has been gained.

The large customs revenue gaps identified in the Bain and Company 2015 Diagnostic have not been realised and the initiatives identified to close the gap have proved largely ineffective. The diagnostic reflects no appreciation for the immense strides of the Customs Modernisation Programme or the fundamental Customs reform planned for through the New Customs Act Programme. It is evident that that the consultation in defining the scope of the Customs diagnostic was extremely limited. The diagnostic offers no explanation for the fact that an operating model that differs substantively from that proposed was implemented. Data quoted to substantive many of the diagnostic findings are unreliable.

The diagnostic is fraught with inaccurate and misleading statements. For example:

- Contrary to what is stated in the diagnostic, in 2015/16, South Africa’s World Bank Customs Efficiency rank was the highest it’s ever been and puts South Africa on par with developed countries like France and the United States of America.

- Contrary to what is stated in the diagnostic, SARS corruption is not high and is in fact very low compared to its peers. The report quoted is outdated (2010 survey) and the sample size is extremely limited.

- Contrary to what is stated in the diagnostic, empirical literature concludes that the country partner method of estimating the extent of trade mispricing is not robust enough to produce reliable and quantitative measurement of trade mispricing.

- Contrary to what is stated in the diagnostic, penalties are not arbitrarily imposed but are governed by the legislative framework.
- Contrary to what is stated in the diagnostic, the accountability for all Customs Operations, effective 1 July 2012, was made clear.

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Table 13: Comparison of WCO, Bain and Customs 2018 Recommendations

	WCO 2006 Recommendations	**BAIN 2015 Recommendations**	**WCO 2016 Recommendations**	**Customs 2018 Recommendations**
Risk Management	Adopt risk-based approach	Develop risk engine for Excise and Travellers		Intelligence driven risk management
	Include economic compliance and anti-smuggling/security indicators	Reinvent risk engine and principles that drive it		Automate targeting and case management
		Case selection approach and rules		Refine risk feedback systems
		Analytical capability		Improve risk management across the entire value chain
				Enhance analytics
Operating Model	Adopt a flat structure based on grade to provide clear lines of command and authority	Resourcing to enable organization	Establish an expanded operating model to centralise and nationally coordinate commercial compliance and law enforcement efforts	Review operating model to improve command and control
	Establish regional Customs Operational Centres of Excellence as a basis for		Consolidate the Risk Management functions and activities under a single functional structure	Review structure to improve operational management

	WCO 2006 Recommendations	BAIN 2015 Recommendations	WCO 2016 Recommendations	Customs 2018 Recommendations
	harnessing the operational expertise and cascading it throughout the organisation		supported by appropriate governance	
	Review the role of BIU		Align the disparate Head Office, Case Selection and other front-line teams' risk selection and targeting through a national function supported by provincial units	Review structure to create a single accountability for capacity building
	Establishment of a national intelligence unit which is staffed by all areas of the security cluster		Single Law Enforcement Division at GE level that would provide national oversight of the entire law enforcement functions within SARS CED.	
Process	Review of export controls to introduce a security element to the clearance procedures	Regain control and final release authority at ports/borders	Reconcile all of the manifest data irrespective of the final port of destination	Embed Excise into the CET value chain
	Provide for the	Modernise and	Conduct a WCO	Create tailor made

	WCO 2006 Recommendations	**BAIN 2015 Recommendations**	**WCO 2016 Recommendations**	**Customs 2018 Recommendations**
	mandatory use of EDI	align excise to customs operations	Time Release Study (TRS) as a useful baseline to improve coordination and processes	processes for segmented client base
	Conduct cost benefit analysis of establishing inland clearance facilities	Customs control from origin to depot (Import/Export/Excise)		Enhance rail management
	Review all port approvals	Excise coverage/inspection		Adopt quality driven processes – do it right the first time
	Develop and implement SOPs	Penalty policy and application		Improve policy and procedure assurance – Internal Audit and Auditor General reviews
	Introduce computerization of all aspects of customs processing	Redesign port/post model/processes to improve Customs control		
	Introduce one dedicated, secure area in all ports in which customs inspections must be conducted			
	Develop a specialized system for this traffic for			

	WCO 2006 Recommendations	**BAIN 2015 Recommendations**	**WCO 2016 Recommendations**	**Customs 2018 Recommendations**
	express couriers			
	Customs endorsement stamps should also have improved security marking			
	Consolidation of State Warehousing			
	Extend the use of period entry and the provision of clearance at traders premises			
	Review the dysfunctional system for controlling the temporary importation of vehicles			
	Review the import and export procedures applying to post and consider suspension of the current MoU			
	Improve the visibility of Customs at the points of entry			

	WCO 2006 Recommendations	BAIN 2015 Recommendations	WCO 2016 Recommendations	Customs 2018 Recommendations
Enforcement	Organize the anti-smuggling function on a national level	Establish strong and visible customs and excise enforcement	Establish a law enforcement strategy	Enhance the enforcement capability
	Provide arrest powers to anti-smuggling staff and the mandatory licensing of Clearance Agents by examination	Enforce customs and excise compliance	Develop a national seizure/information database	Renew focus on the illicit economy: • Tobacco • Clothing & Textiles • Fuel • Pharmaceuticals • Counterfeit goods
	Extend post clearance inspection function to all large ports	Customs enforcement strategy including introduction of tactical team	Facilitate the regular and timely receipt of passenger manifests	
	Develop specialized teams for areas such as ships rummage, covert surveillance, informant handling etc.		Gain full access to electronic Passenger Name Record (PNR) and Advanced Passenger Information (API) data	
	Provide the legal basis to enable intelligence gathering, interception and covert operations by a limited number of SARS		Resolve user requirements issues related to the use of portable devices to allow live electronic Service Manager Acquittal of	

	WCO 2006 Recommendations	BAIN 2015 Recommendations	WCO 2016 Recommendations	Customs 2018 Recommendations
	staff		referrals	
			Review the current controls and infrastructure in place for the processing of international mail	
IT	Review the proposed IT strategy		Rationalise IT information holdings and collection methods	Expedite NCAP delivery
	Enhanced management reporting system		Provide an automated case management system for post clearance audit	Explore single window opportunities by expanding the SARS declaration case management capabilities to other agencies
	Develop a new operational computer system for customs			Improve third party data sources
				Automate all manual processes
				Automate all operational activities
				Automate performance dashboards and improve analytics
Regional	Play a key role		Enter into bilateral	

	WCO 2006 Recommendations	BAIN 2015 Recommendations	WCO 2016 Recommendations	Customs 2018 Recommendations
Role	regionally in leading the development of SACU Customs Services		arrangement with a SACU member around the Preferred Trader /AEO Pilot	
HR	Broader key performance indicators for to include innovation and the understanding of customs role		Include Leadership and Management professional development	Improve processes measures and standards
	Adopt management control programmes		Ensure the work being done around a competency framework captures the requirements for the audit role	Develop a training curriculum that supports a blended approach to staff and leadership development
	Performance agreements to be completed by all staff		Assign competencies to existing job descriptions	Review career paths, talent management and performance management processes
	Extend the induction course to include content on compliance, facilitation, security, control and approval		Complete: • Training policy and strategy • Finalise the training operating	Invest in technical leadership development

	WCO 2006 Recommendations	BAIN 2015 Recommendations	WCO 2016 Recommendations	Customs 2018 Recommendations
	Develop a formal system or rotation of duties		model and infrastructure • Establish a competency framework • A training needs analysis focussed on the implementation of NCAP	Develop a change management programme
	Include indicators which reflect the expertise of the individual in customs matters in KPIs			Develop and embed an Anti-corruption Strategy
	Develop a training log for all new staff which shows the training and experience they need to develop and the knowledge skills and behaviours required for their posts			Create an integrated operations committee
				Review the employer value proposition
				Create a disciplined workforce
				Improve employee engagement
				Escalate woman development
Preferred Trader		Trade facilitation (incl. Preferred trader, one-stop border post)	Review the terms of reference of the accreditation review committee	Expedite the AEO policy framework and implementation
			Utilise the good work done to date and take the Preferred Trader	Increase the preferred trader footprint

	WCO 2006 Recommendations	BAIN 2015 Recommendations	WCO 2016 Recommendations	Customs 2018 Recommendations
			Programme to the next stage by accrediting traders that have met the criteria	

Table 14: Bain Initiatives and Potential Revenue

Strategic Initiative Charters	Benefit	Objectives	Timeline
Reinvent risk engine and principles that drive it	**R 1B –R2B**	Improve overall risk detection by introducing a multi-lateral approach	December 2017
		Increase success rate and yield of the risk engine with better selection and categorisation of cases	
		Develop transparent and structured governance for the risk engine	
		Expand risk engine functionality to Customs Traveller section and locally manufactured Excise	

Strategic Initiative Charters	Benefit	Objectives	Timeline
Regain control and final release authority	**R 6B –R12B**	Improve Customs control of SA's port by closing the gap between goods arriving at port and those declared to SARS	August 2016
		Prevent opportunities or gaps in flow that allow leakage/smuggling of goods through ports and borders	
		Increase general compliance level of traders and travellers	
Establish strong and visible enforcement	**R9B-R21B**	Increase effectiveness of Customs enforcement to catch violations/leakage missed in 'line process'	June 2017
		Develop highly skilled teams able to investigate and resolve complex avoidance mechanisms	
		Close the Customs revenue gap by targeting high risk/high value opportunities	

Strategic Initiative Charters	Benefit	Objectives	Timeline
		Raise industry compliance and reduce opportunity for non-declaration of production of Excise products	