

“MUST-KNOW” INFORMATION SURROUNDING SARS' DIESEL REBATES

INTRODUCTION

This document is intended as a guideline that has been built on our experience with numerous diesel audits, as well as intensive discussions with SARS officials during information sessions. It is not intended as legal advice, but as a practical guideline for handling your diesel refund claim correctly. If you follow the guidelines, it is highly likely that SARS will be satisfied with your record-keeping, and that your claim will pass muster. If, on the other hand, you choose to ignore it, it is almost certain that SARS will catch you out, and then you are probably beyond the point of no return.

It is a matter of fact that SARS has become dramatically stricter with the application of the law, and as a consequence it is much more difficult to compile a successful (and legally compliant) refund claim. This document has been written to identify problems and misconceptions clearly, and in doing so, to hopefully eliminate them in practice. It is an attempt to confront the issues squarely rather than to take an ostrich approach. The pressure SARS is under to collect revenue under circumstances of slow or no economic growth means that a return to an easier dispensation is extremely unlikely.

A lot of effort has gone into making the document easy to read and to understand. We have tried to address each of the typical misconceptions that exist among our clients.

BACKGROUND: EXISTENCE OF THE REFUND SCHEME

The scheme came into existence because the state wishes to support primary production in the primary industries (mainly agriculture, mining, forestry and fishing), and uses the mechanism of refunding a portion of the diesel utilised in primary activities. The fact that much of the diesel used in these industries is consumed off public roads theoretically makes the portion of the diesel price that goes into the Road Accident Fund and the maintenance of roads available to use as an incentive. Please note: It is NOT a repayment because you are not using the roads, but intended to incentivise primary production. For example: When primary products are transported to market on public roads, you are entitled to claim the refund, in spite of the fact that you are definitely using public roads.

This also partly clarifies why there are apparent impracticalities or illogicalities. For example: The trip taking produce to market may be claimed for, but the return trip NOT, unless it happens to carry a meaningful load of farming inputs.

BACKGROUND: LEGISLATION

The scheme is legislated in the "Customs and Excise Act, 1964". There is also a Schedule 6 to the Act (pages 48 to 50 in the Schedule deal with farming). It is further expanded on by a set of rules "Customs and Excise Rules 1995 as amended". Part 3 of the Rules (pages 42 to 54) deals with farming. As an aside: Note that, even though the scheme is operated via the VAT system at SARS, the VAT legislation does not underlie the operation of the system except tangentially, for example where VAT invoices are involved. There appears to be a possibility that this will change in future, with a dedicated system for administering the refund scheme.

The above-mentioned documents create a very rigid framework within which SARS officials have to apply and enforce the law. Ignorance of the law on your behalf is not an excuse, and this places a definite duty of care on you, to ensure that you do not move outside the parameters of the law. There are specific prescribed punitive measures and penalties that can cause monetary pain and other disruptions. Court decisions over time have emphasised that the law must be interpreted and applied strictly, also precisely because it is an incentive scheme.

Lastly you need to understand that the SARS officials know their law better than any outsider, and that your chances of winning a legal argument against them are pretty slim. Your best chance is to present the facts (your records) as correctly, honestly and fully as possible.

OPERATION OF THE SCHEME:

The system is based upon the principle of self-assessment and therefore places the duty to provide proof 100% on the farmer. SARS does not normally have direct access to the documentation required to perform an assessment (although this will typically be required when you are subjected to an audit). This means in principle that you determine the assessment yourself, but also means that, by signing the declaration, you state that you are legally entitled to the refund you are claiming and that you have the necessary documentary proof at your disposal. Misrepresentation (purposefully or through ignorance) may lead to specific punitive measures.

The diesel refund payment described in the law is a preliminary payment based on the detail in your claim. It may be reversed after an inspection or audit. The refund is only paid out by SARS if they do not perceive undue risk in doing this. Alternatively it may also be held back until completion of the audit. You must therefore take note that the fact that your claim has been paid out, does not necessarily mean that you are not going to be audited.

Standard practice at SARS means that prior to any substantial refund being finalised, there will almost always be an audit. Therefore, the question is not WHETHER your records will be audited, but rather WHEN. It is not a lottery and definitely not worth taking any chances.

REASONABLE AND PROPER RECORDS

SARS officials talk about a golden thread that they need to be able to follow from the initial purchase of the diesel, through delivery into your bulk tank, from there into the tractor or other item, up to and including the actual use or consumption of the diesel in your own farming business on a specific eligible activity.

Proper record-keeping means that you build the records day by day as the farming activity progresses. This is one of the reasons why SARS has a clear preference for hand-written logbooks and trip sheets - producing the records afterwards with something like Excel automatically creates a flashing red light for the auditor. Our experience is that you need the original written records in all cases, even if you do make use of an electronic dispensing system.

The law requires of you to keep record of diesel that is purchased AND USED. For this reason, it is not acceptable to claim directly against purchases - the unused portion remains in the bulk tank or in the tractor or other vehicles, and may only be claimed when it has been physically consumed.

The following documents are minimum requirements for SARS to consider your records as reasonable and proper. Please note that the list I have given is limited to the requirements in respect of the actual handling of the diesel itself - there are other requirements, such as registration for the scheme, sub-contractor contracts, farm maps and the like.

- VAT invoice made out to the correct entity, for the original purchase of the diesel;
- Proof of delivery with date and time of actual delivery;
- Record of periodic dip readings;
- Logbook: Issuing of diesel to vehicles (“Diesel storage and dispensing logbook”);
- Logbook: Usage of diesel by vehicles (“Diesel usage logbook”);
- Complete list of vehicles and equipment for which the diesel refund is claimed, INCLUDING any rented or contracted items, individually specified;
- Delivery notes of primary farming products to market, and farming requirements back to the farm.

In addition to these documents, SARS likes to see other confirmatory information, for example, a farming diary showing dates of actual tasks or activities, e.g.

Diary entry: 15-20 November 2016: Maize planted on block B30 (110ha)

The existence of such information makes it easier for SARS to form a complete picture of your farming operation, and the more of this type of additional background you can provide, the more likely it is that your claim will pass muster.

ACTIVITIES FOR WHICH THE REFUND MAY BE CLAIMED: The complete list of eligible activities for the farming industry follows below, copied verbatim from SARS' Schedule 6 (Part 3). Note that the items are defined fairly broadly in some cases, e.g. "(AA) Growing crops and harvesting and storing crops on the farming property". SARS typically requires more detail, e.g. "Ploughing of block B30 (110ha)". Our recommendation is that you use the typical sub-activities you would engage in, e.g. ploughing, planting, spraying, pruning, harvesting, transport and so on, together with an indication of where the activity was undertaken. I believe that the SARS list is mainly intended to determine whether your activity falls within the broad definition of eligibility for the refund.

- (AA) Growing crops and harvesting and storing crops on the farming property.
- (BB) Horticulture, pasturage and apiculture.
- (CC) The breeding of fish in dams and the farming of oysters.
- (DD) The breeding and caring for animals and reptiles.
- (EE) The breeding and caring for race and show horses and the transportation thereof.
- (FF) The shearing or cutting of hair or fleece of livestock, or the milking of livestock.
- (GG) The transport of livestock to a farming property for the purpose of rearing.
- (HH) The rounding up or herding of livestock.
- (IJJ) Baling of hay. *(The faulty numbering comes directly from the SARS document)*
- (KK) The planting or tending of fruit trees.
- (LL) Any activity undertaken for the purpose of soil or water conservation.
- (MM) The carrying out of fire-fighting activities.
- (NN) The construction or maintenance of fences.
- (OO) The construction or maintenance of fire-breaks.
- (PP) The service, maintenance or repair of vehicles or equipment for use in a farming activity if it is carried out at the place where farming is carried on.
- (QQ) The construction or maintenance of sheds, pens, silos or silage pits for use in a farming activity.
- (RR) The construction or maintenance of dams, water tanks, water troughs, water channels, irrigation systems or drainage systems including water pipes and water piping for use in a farming activity carried out on the farming property.
- (SS) The carrying out of earthworks for the purpose of a farming activity, carried out on the farming property.
- (TT) Searching for ground water solely for use in a farming activity, or the construction or maintenance of facilities for the extraction of such water, solely for that use.
- (UU) The pumping of water solely for use in farming if the pumping is carried out on a farming property.
- (VV) The supply of water solely for use in farming if the supply is to a farming property and the water is supplied from that property or a place adjacent to that property.
- (WW) The storage of farming products.
- (XX) The packing, or prevention of deterioration of farming products, if the packing or the prevention of deterioration of the products is carried out on a farming property.
- (YY) Weed, pest or disease control.
- (ZZ) Hunting or trapping that is carried on as part of farming operations including the storage of any carcasses or skins.
- (AAA) Game farming, excluding leisure activities such as game viewing and lodging.
- (BBB) Generating electricity or the use of other farm equipment for domestic purposes.
- (CCC) Use of locomotives for the carriage of goods by rail on the farming property.
- (DDD) Flood management on farming property.

GENERAL MISUNDERSTANDINGS AND MISCONCEPTIONS

The following are examples of common misconceptions surrounding refund claims. The majority of the examples were supplied by SARS itself - you can therefore rest assured that they will recognise them easily.

“General farming” or “Primary production” as activity: This very common "sin" is definitely not complete enough to be accepted by SARS. They want to know exactly WHAT was done with the diesel, and also WHERE it was done, in order to comply with the requirements of the law. The problem with something like "General farming" is that it can easily be abused for any activities that are not necessarily directly related to primary production. SARS uses these two specific examples in their own information sessions to illustrate things that do NOT work. If you continue using these items in spite of this advice, you must expect trouble.

Mixing of activities: The law is interpreted and applied very strictly when mixed activities happen. By way of example: If you have a generator providing power to a pack house on the farm, you are allowed to claim the refund for diesel used by it. If the same generator is also used to supply power to the farmhouse and/or workers' houses, it immediately puts paid to ANY claim for diesel used by it, and there is no escape. SARS simply argues that there is no way of determining with certainty how much diesel was consumed for the pack house, and how much for generating household power. The use of percentages or estimates is NOT accepted. Note: The principle of "no estimates or percentages" applies throughout the administration of the scheme - SARS expects measurements and nothing else.

The 80/20% principle: The fact that only 80% of the eligible litres is allowed for calculation of the refund, has NO relation to anything else in the scheme. The 20% that is not refunded is specifically NOT intended to provide for private usage of diesel. The law simply states that 80% of the diesel used in primary production may be claimed. I suspect (just a guess) that this was maybe intended to provide for those cases where vehicles do actually go on the road while transporting primary products to market.

Outside purchases of diesel: There are two problems with this. Firstly, the typical diesel purchase slip is not a complete VAT invoice as required by the law (the name, address and VAT number of the purchaser typically do not appear on these). The second problem is that SARS has taken a decision in principle that any outside purchases are not accepted for refund claims. You might be able to contest this on legal grounds, but you would need to be prepared to take this as far as a court case. My recommendation would be to fit long-distance tanks to the vehicles involved, or to carry an extra drum of diesel if possible and if this should prove to be worth your while when considering all factors.

Bakkies (and any other vehicles primarily intended to be used on the road): SARS absolutely insists on the use of a logbook for each vehicle that you wish to claim the rebate for. Road vehicles are typically used for multiple purposes, e.g. transporting workers early in the day (for which a diesel rebate may NOT be claimed) and then maybe later to load farming inputs in town, for which the refund may be claimed.

In fact (and VERY important): If a vehicle takes produce to market and then returns empty (or with a ridiculously small load) you may NOT claim for the return trip. The law actually describes this specific situation - ONLY trips carrying primary products to market, and ONLY trips carrying legitimate farming inputs back to the farm, may be claimed. Please also read the previous heading about purchases of diesel en route, and also further on regarding logbooks for road-going vehicles.

It is very clear that SARS is much stricter with road-going vehicles like trucks or bakkies than they would for example be in respect of single-purpose equipment like combine harvesters, or even tractors, where the vehicle hardly ever ventures onto a road. A single entry per day would therefore likely suffice for a harvester, where the same single entry for a truck would probably be questioned by SARS.

You basically have two choices here: Firstly, you may decide to stop claiming the diesel rebate for trucks and/or bakkies. If these vehicles do not consume a substantial portion of your total diesel account, this choice may make sense. Secondly, you have the choice of keeping a logbook, and this then has to comply with SARS' standards. SARS' prescribed format (especially the so-called "diesel usage report" is pretty

complicated, and our advice would be to use a simplified format, and then consolidate this into the prescribed format, possibly by hand, or preferably with a computer system.

Please note that activities like driving around the farm for supervision purposes will not necessarily be accepted for refund by SARS. For example: Where you undertake a trip to deliver seed to a planter, this will be accepted, but if you drive into town on business, this will likely not be accepted. My opinion is that it may still be worth the trouble to claim for bakkies used exclusively in the farming environment, but the farmer or farm manager's double-cab will not be worth the trouble, considering the complexities and disputes that will inevitably arise, as well as the amount of record-keeping that is required.

Contractors: You are free to make use of contractors to do work for you, e.g. soil preparation or harvesting. The contract you enter into must be a so-called "dry contract", in other words, the contractor does not use his own diesel, but uses diesel you supply from your bulk tank. Furthermore, you need to deal with the contractor's vehicles exactly as you would with your own, listing each vehicle separately in your system, and issuing diesel individually per vehicle. If the contractor receives diesel from you into a mobile bowser, he must still keep a log per vehicle, which he must provide to you periodically and at the end of the contract.

Hour meters/odometers: As far as I could determine, SARS does not have fixed rules about these. The test will remain whether you have "reasonable and proper records". I suspect that, because something like a generator or other small equipment is not equipped with these meters from new, it would be unreasonable of SARS to require this. This also means that if your tractor's hour meter is out of order, you would be expected to do something about it, unless the tractor is used for a very simple purpose like pumping water, where the usage may be determined in some other way, e.g. it runs for three hours every day.

Fabrication of logbooks: SARS is very much aware that people "wake up" to not having adequate logbooks, when they are confronted with a notice that they are going to be audited, and that they then tend to fabricate a logbook, simply because they never had one to begin with. This is viewed in a very serious light and may lead to prosecution, particularly if SARS is of the opinion that the fiscus is being deliberately defrauded. This is also why the logbook (even if handwritten) must always fit into the bigger picture of the total farming activity.

In conclusion: SARS will ONLY allow you to pass an audit if they are under the impression that you are keeping "reasonable and proper records", and that you are compliant with all legislative requirements. This means that your actions and records must be above suspicion, and that you must avoid all the things that they can be easily identified as transgressions.

SARS' Schedule 6 definition of a logbook: I have quoted it verbatim from the original document. It encompasses the legal basis that SARS will use to judge your logbook:

"Logbooks" means systematic written tabulated statements with columns in which are regularly entered periodic (hourly, daily, weekly or monthly) records of all activities and occurrences that impact on the validity of refund claims. Logbooks should indicate a full audit trail of distillate fuel for which refunds are claimed, from purchase to use thereof. Storage logbooks should reflect details of distillate fuel purchases, source thereof, how dispersed/disposed and purpose of disposal. Logbooks on distillate fuel use should contain details on source of fuel, date, place and purpose of utilisation, equipment fuelled, eligible or non-eligible operations performed and records of fuel consumed by any such machine, vehicle, device, or system. Logbook entries must be substantiated by the required source documentation and appropriate additional information that include manufacture specification of equipment, particulars of operator, intensity of use (e.g. distance, duration, route, speed, rate) and other incidents, facts and observations relevant to the measurement of eligible diesel use.

In short, this means that the logbook entries must be complete enough to objectively prove to SARS that the diesel was correctly used in the primary production process.

Periodic dip-stick readings: SARS requires that you take periodic dip-stick readings, and as an absolute minimum, at the start and end of each VAT period, so once every two months or once a month. The purpose of the dip-stick reading is to create a fixed reference point for comparing the logbook results to. In other words, by way of example: The logbook entries imply that the system contains say 1310 litres. The dip-stick reading should confirm that this is indeed correct, or if not, it will show up either an unexplained gain or loss of diesel. Our recommendation is that you take additional dip-stick readings with each delivery of diesel to the farm (preferably a "before" and "after" reading). We have experience of situations where people order a certain amount of diesel, but what ends up in the bulk tank is then substantially less than what appears on the delivery note, because the tanker driver is operating his own little scheme, selling diesel that he obtains in this fashion.

WHAT DOES AN AUDIT LOOK LIKE?

In the following paragraphs I will discuss the various types of correspondence SARS uses when an audit is under way. It is absolutely important to respect this correspondence by reading and understanding it in the first place, and then secondly to respond fully and accurately to any requests that SARS may make in these letters. If you fail to do this, it is 100% certain that SARS will continue the steps regardless. The chances of this process ending in a favourable result for you are pretty close to zero.

The audit or inspection is initiated by means of a "Letter of engagement" which is your notice that SARS is going to audit you. It typically begins with a request for two months' worth of records, or it can also start with a direct request for two years' worth of records. It may include a site visit, or it can be limited to a desk audit of the documentation you provide. You may request that this audit be postponed, for example, if you are in the middle of a busy time on the farm such as harvesting or planting, or if there are personal circumstances which can potentially justify a postponement. Our experience is that SARS is quite reasonable in this respect.

Our advice is that your best chance for a relatively painless experience is located in this stage. **It is most definitely in your interest to deal with this initial request to the best of your abilities, to convince the auditor that your record-keeping is so good that it is not worth continuing with the investigation.**

If the inspector is not satisfied with the initial data sample, the next step will be to request a full two years' worth of data. The inspector is NOT allowed ANY discretion in this respect, as it is prescribed like this in the law. So, if you do not pay adequate attention to the initial request, you are most definitely creating additional work for yourself. Remember that the inspector who does the initial investigation is also by far the easiest person to convince that your records are up to standard. **The minute the process is out of his hands, you are going to deal with people who know their law really well and who will probably work to stricter standards, possibly also because they have less direct knowledge of the circumstances and characteristics of your specific farming operation. Remember that SARS' appeals committee will ONLY change the auditor's findings if they are of the opinion that the auditor (and his immediate seniors) did not do their work correctly. This means that there must be definitely WRONG decisions that have the potential to be successfully challenged in court before you will have a chance to get the results overturned.**

When the audit has been completed, you will be sent a "Letter of intent to assess" or a "Letter of findings" in which SARS will spell out its intentions, and which accords you the opportunity to dispute the findings, mainly by providing more complete information, or by pointing out specific factual errors. This letter will typically allow fourteen working days in which you can lodge an objection or provide more information. Please note that if you do not respond within the period allowed, SARS will automatically continue implementing the steps as set out in its letter without any further notice.

During this period, you are also entitled to enter into discussions with the auditor and/or his seniors to try and sway their opinion. In most cases this is your last chance to sort out the problem in a non-confrontational way. If the inspector did indeed make any errors of fact or moved outside the guidelines,

his seniors will most certainly want to correct this before it reflects on their performance. In any case, the letters and notices sent to you are typically co-signed by the inspector's team leader, meaning that the latter probably agrees with the content.

The last step in the process is typically a “**Letter of demand**” or “**Letter of assessment**” if the audit results in your claim being refused partly or fully. If you fail to respond to this letter as may be requested, SARS will continue with further steps, which may include holding back other funds which may be due to you (for example, a VAT refund), or they may go as far as taking funds directly from your bank account. After this, they may also take more conventional debt-recovery steps in terms of the law.

The law makes provision for further formal objection and appeal, and the procedure is described in Article 77A of the law. When you start moving on this level, we recommend that you get professional help before doing anything. There is a prescribed limit of thirty days for submitting formal documents in this regard. If you miss this window, your remaining options are ADR (Alternative dispute resolution) or possibly legal action (effectively taking SARS to court). I recommend that, LONG before you get to this unhappy stage, you rather make the necessary effort with the initial record-keeping - undoubtedly this is an effort involving time and trouble, but this is way more controllable and less trouble than a court case would be.

IN CONCLUSION

Depending on the extent and intensity of your farming operation (e.g. intensive cultivation of crops versus an extensive game farm) you need to take a decision in principle if you are going to claim a diesel refund. There are specific risks if you do this (SARS refuses the claim and/or levies a penalty against you). It is not an easy process to arrive at a successful rebate claim, and it most likely involves cost (even if it only lays claim to some of your time).

On the positive side, there are, potentially, substantial amounts involved. For example, if your farm uses (just?) R1 000 000 worth of diesel per year, and if you further use only half of this on eligible activities, your claim will be around R90 000 - this is probably more than you would need to pay somebody to deal with the issue even on a full-time basis. The involvement of such a person would probably also reduce the incidence of diesel theft, so the process can be justified pretty easily purely on financial grounds.

SARS has indicated that they have only issued fines in isolated cases to date, so punitive measures have generally been limited to the amount of the claim. The risk you previously ran was therefore limited. SARS has also indicated that this state of affairs will probably change in the future, meaning that you may be penalised depending on the seriousness of your transgression. Obviously, SARS will try and establish your intention with the claim. Mere negligence will be less serious than a purposeful misrepresentation of facts, which really amounts to fraud.

The clear warning here is that you must understand that it is no longer worth taking a chance and then trying to explain later - the risk is simply becoming too real.

Our recommendation is to fully consider whether you still want to claim the refund. If yes, you will then need to take definite steps to ensure that you visibly comply with the law. In short, this means that the SARS inspector can clearly see that your records are up to standard, and that the law is not being ignored or evaded. Remember that SARS is continually blocking leaks, so you can expect their application of the law to become stricter over time.

How does the Africlock diesel system help me?

To begin with, you need to understand that the Africlock system is NOT a magic wand. Merely implementing the system does NOT guarantee that all future refund claims will be successful. In the same way that possession of a computer and printer does not guarantee that you will be a successful writer, we cannot guarantee that your use of the Africlock system will have a perfect result. Our point of departure is that the correct use of the Africlock system (hardware and software, or software on its own) dramatically improves the probability of success, and vice versa: Not using our system (or something similar) reduces the probability of success.

Please also note that, at the time of writing, SARS has not accredited or approved ANY electronic system. This applies to Africlock, and it applies to all other systems as well. Even VIP Payroll, which is certainly the best-known payroll in the country, is not approved in this fashion. SARS' argument is that what you DO in the system must comply with the law, and that the mere use of some or other system is no guarantee that everything that has been entered into the system is suddenly above suspicion. By way of example: If a tax invoice for diesel purchased is captured into Africlock, the mere fact of the record being visible in Africlock is NOT proof that the invoice has been captured accurately (or even that the invoice actually exists). The proof remains the existence of the actual piece of paper, because this document has an audit trail that can be followed. Hence, Africlock records will be accepted by SARS if they form an integral part of a complete process of building "reasonable and proper records", and fit into the complete picture of your farming operation that the inspector builds.

The Africlock system plays a definite role in the establishment of "reasonable and proper records" because it creates a central repository for data, and then has the ability to present the data in the format that SARS requires. SARS' prescribed formats of logbooks (both the current set on their website and the new suggested formats presented in their early 2016 information sessions) are definitely not simple or easy to complete and maintain, and I will go as far as to say that it is completely impossible to do unless you keep it up on a daily basis, in line with that day's events on the farm.

The Africlock hardware (the box that we erect outside on your bulk diesel tank) keeps track of diesel dispensed from the bulk tank to individual vehicles or equipment items. It contains all the data required to produce the SARS "Storage and dispensing logbook". Where a tractor, which starts out with a full tank in the morning, goes to plough a specific field and then returns to the store and is refuelled, the SARS "Usage logbook" would likely also contain only a single entry, and you would be able to make the argument that Africlock has adequate data. However, there are obviously more complicated situations, e.g. a truck that drives to town with no load, and returns with a load of fertiliser. In this case, the "Usage logbook" would have a minimum of two entries to fully describe the situation in order to comply with the legal requirement. In this situation, you would need to enter the additional data into Africlock on the screens provided for this purpose.

You can purchase the Africlock software separately and use it on its own. Especially where the extent of your farming operation does not justify the purchase of the hardware, this would offer you an alternative means to create "reasonable and proper records".

We are of the opinion that, without the use of a computer, it is just about impossible to create the SARS "Storage and dispensing logbook" and the "Usage logbook" in the required formats.