

**A CRITICAL EVALUATION OF THE 1964 PREFERENCIAL AGREEMENT (LABOUR
AGREEMENT) FOR MOZAMBIQUE MINeworkERS IN THE LIGHT OF THE
SOUTH AFRICA – MOZAMBIQUE DTC AND THE SADC TREATY**

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Abstract

In 1964, a labour agreement was signed between the governments of South Africa and Portugal on behalf of its colony, Mozambique, to regulate the migration of Mozambican mineworkers to South African mines. In terms of this agreement the Mozambican mineworkers who received income on the South African mines were exempt from any taxes on their South African source income. Although outdated, the agreement is still in force today and is used by the South African mines to enter into employment contracts with Mozambican mineworkers.

Many countries in the SADC region enter into double taxation agreements for the avoidance of double taxation. The 1964 labour agreement is quite unique as the income received by the Mozambican mineworkers is exempt from tax in South Africa for the duration of the contract (usually up to 18 months) entered into by the Mozambican mineworkers and their South African employers although the source of income is in South Africa. The challenge is whether this agreement should continue as an international agreement and whether it is discriminatory to exempt these mineworkers when compared to other mineworkers in the same position working in South Africa.

The purpose of this study is to examine the application of this labour agreement with reference to the South African Income Tax Act and the double tax agreement with Mozambique. It further questions whether this agreement causes a revenue loss and whether or not such loss is justifiable. It further tests whether this agreement is a tax incentive and whether or not it leads to harmful tax competition in violation of the SADC agreement. Finally, the agreement is assessed in light of the discrimination article in the double tax agreement and based on section 9 of the Constitution of the Republic of South Africa.

The main conclusion is whether the 1964 labour agreement should continue as an international agreement in the present circumstances as the agreement is fairly outdated and subject to various interpretations which will have an effect on revenue loss to the South African fiscus.

Abbreviations

BLS	Means the Republic of Botswana, the Kingdom of Lesotho and the Kingdom of Swaziland
BEPS	Base Erosion and Profit Shifting
DTA / DTC	Double Taxation Agreement / Double Taxation Convention
GDP	Gross Domestic Product
IMF	International Monetary Fund
MoU	Memorandum of Understanding on Co-Operation in Taxation and Related Matters issued by the SADC in 2002
MTC	Model Tax Convention on Income and Capital
NUM	National Union of Mineworkers
OECD	Organisation for Economic Co-operation and Development
SADCC	Southern African Development Coordination Conference
SADC	Southern African Development Community
SAMP	South African Migration Project
SARS	South African Revenue Service
TEBA Ltd	The Employment Bureau of Africa
The Act	Income Tax Act 58 of 1962
The OECD Commentary	The Commentary on the OECD Model Tax Convention on Income and on Capital
UN	United Nations
WENELA	Witwatersrand Native Labour Association

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1. Introduction and Background

The migration of workers from Mozambique to South Africa started before the discovery of diamonds and gold on the mines at Kimberley and the Witwatersrand. The first workers came to Natal to work on the sugar and other estates from the 1850s. With the discovery of diamonds in Kimberly in the 1860s it attracted Mozambican workers to South Africa. It is estimated that there were up to 12000 Mozambicans working in South Africa in 1879.¹

In Mozambique factors such as climate changes, economic conditions and a turbulent political and social environment contributed to the migrant labour system of Mozambican workers to South Africa. With the discovery of gold in the 1880s on the Witwatersrand it accelerated the participation of the Mozambican workers in the migrant labour system.²

A brief review of Portuguese capitalism and colonialism in Mozambique will help to explain Portuguese policy towards the migrant labour system of Mozambican workers to South Africa. Portugal began to occupy Mozambique after the Conference of Berlin (1884-1885). The Portuguese economy was weak and it struggled to control and exploit most of the vast territory of Mozambique. As a result the Portuguese gave up some of their rights to exploit this vast territory to concessionary or monopolistic companies. These companies had the foreign capital. The Niassa Company (northern Mozambique) and the Mozambique Company (in provinces of the centre of the country) were some of the main companies. The foreign capital of these companies was financed by the French, Germans, Belgians and the British. These companies offered work to the local labour on plantations and in their enterprises. The British threatened to occupy Southern Mozambique where the Portuguese had control of the territory. The weakness of Portuguese capital investment and the political instability forced the Portuguese to negotiate agreements with the British as they were dependent on its capital. In this way the Portuguese maintained their investment and local labour in Southern Mozambique.³

¹ Gasper, N. 2006. *The reduction of Mozambican workers in South African Mines, 1975 – 1992: A case study of the consequences for Gaza Province – District of Chibuto*. [Online]. Available.

<http://hdl.handle.net/10539/4839> [16 May 2008] : 16 -34

² ibid footnote 1

³ ibid footnote 1

After the Portuguese effectively took control of Southern Mozambique in 1897 it signed agreements with the South African government to take advantage of the current migrant labour system of Mozambican workers to South Africa.⁴

This was important to the Portuguese colonial regime as it contributed to the economy in Southern Mozambique.⁵

To further their control of the movement of workers from Mozambique to South Africa, the Portuguese government instituted the Regulations for Employment of Native Mozambicans in the South African Republic (Transvaal) in November 1897. As a result of these regulations, the registration and movement of these migrant workers came effectively under the control of the Portuguese colonial officials.⁶

The Anglo- Boer war started in 1899. This had negative effects on the mining industry in South Africa. It resulted in the ceasing of mining activities and the repatriation of thousands of Mozambican mineworkers to Mozambique. In December 1901 the Portuguese colonial government and South Africa signed a treaty called the Modus Vivendi. The Modus Vivendi included agreements in respect of migrant labour, railways and ports, and trade. The length of the contract for Mozambican workers on South African mines was established as 12 months. The Mozambican worker could renew the contract if they wished. Also in 1901 an agreement was signed between the Mozambican authorities and the Witwatersrand Native Labour Association (WENELA). In terms of this agreement WENELA was recognised as the sole recruiter in Mozambique.⁷

A new convention was signed between the colonial government of Mozambique and the government of Transvaal in 1909. It replaced the Modus Vivendi of 1901.⁸

The convention established 12 months as the duration of the contract which is similar to the Modus Vivendi but the issue of re-engagement was revised as stipulated in Article VI of the convention which read as follows:

'No labourer shall be engaged in the first instance for a longer period than one year, but at the end of the first period he may be re-engaged for a further period or periods, but so that such period or periods, together with the first period, shall not, without the special

⁴ ibid footnote 1

⁵ ibid footnote 1

⁶ ibid footnote 1

⁷ ibid footnote 1

⁸ ibid footnote 1

*permission of the Portuguese Curator hereinafter referred to, exceed two years. Any labourer who fails to return to the Province of Mozambique at the expiration of this period of service, including any period of re-engagement, shall, unless he shall have obtained special permission from the Curator, be considered a clandestine immigrant for all the purposes of this Convention.*⁹

The convention of 1909 stipulates that no pressure would be put on the Mozambican workers to renew their contracts.¹⁰

In 1928 the convention was again renewed, now between the government of the Union of South Africa and the Portuguese government. The convention solved some of the problems in previous agreements signed between the two governments in respect of the duration of the contract of the Mozambican workers and deferred pay. In the 1928 convention, 12 months was established as the period of the employment contract and it could be renewed for a further six months. Deferred pay which was voluntary in the previous convention was now seen as compulsory. The deferred pay which was a significant part of the wages of the Mozambican workers would be paid to Mozambique in escudos (their local currency).¹¹

The monopoly achieved by WENELA in recruitment of Mozambican workers was one of the outcomes that came out of the agreements between the two governments. Recruitment by WENELA started in 1902 and ended in the middle of the 1960s. WENELA was only allowed to recruit in the areas of Southern Mozambique.¹²

WENELA's annual recruitment in terms of the convention and subsequent amendments to it was 100 000 workers in 1929, 80 000 workers from 1933 to 1935 (this was due to the depression). Annual recruitment rose to 100 000 workers in 1940 – 1964. After that quotas were fixed at 65 000 workers.¹³

⁹ ibid footnote 1

¹⁰ ibid footnote 1

¹¹ ibid footnote 1

¹² ibid footnote 1

¹³ Clarke, DG. 1977. *State Policy on Foreign African Labour in South Africa: Statutory, Administrative and Contractual Forms.*

available:<http://opendocs.ids.ac.uk/opendocs/bitstream/123456789/1839/DSR6%20Working%20Paper%204%20-%20220766;pdf?sequence=1>

In 1964 a new agreement or labour treaty was made with the government of Portugal on behalf of its colonial dependency (the Province of Mozambique)¹⁴ carrying forward some of the principles from the 1928 Convention. The 1964 Agreement maintained arrangements with WENELA.

The new agreement came into operation on the 1st of January 1965 and stipulated that the number of workers from the province of Mozambique to be employed by the mines in South Africa would be mutually agreed upon between the two governments.¹⁵

1.1 Analysis of Mozambican Mineworkers in South Africa

‘The Mozambican labour component in South African mines was clearly significant in terms of numbers of workers from the beginning of the mining industry to the middle 1970s.’¹⁶

The table below is a comparative analysis of South African and Mozambican workers which shows that national labour clearly dropped while the Mozambican labour component employed in South African mines rose from 1946/47 to the end of the 1950s. The Mozambican workers did not follow South African workers into secondary industry because their contracts were dependent on treaties between South Africa and Mozambique.¹⁷

The Mozambican workers received by mines, 1920 – 1975 (selected by years)

Table 1

	Mozambicans	Total of miners received by mines	(%)
1920	76,370	211,838	36
1928	66,094	200,202	33
1929	60,831	199,704	30
1930	56,258	230,892	33
1932	39,129	210,341	19
1934	50,665	243,212	21

¹⁴ ibid footnote 13

¹⁵ Labour Agreement, No.11/1964

¹⁶ Gasper, N. 2006. *The reduction of Mozambican workers in South African Mines, 1975 – 1992: A case study of the consequences for Gaza Province – District of Chibuto*. [Online]. Available <http://hdl.handle.net/10539/4839> [16 May 2008]: 16 -34

¹⁷ ibid footnote 16

1936	70,092	308,860	23
1942	74,507	310,406	24
1946	74,117	297,231	25
1947	78,308	295,486	27
1949	82,636	328,042	25
1951	89,243	325,834	27
1954	86,103	349,454	25
1959	81,673	425,378	19
1960	79,065	426,951	19
1970	93,773	357,972	26
1973	74,759	352,362	21
1974	86,324	319,974	27
1975	113,484	451,514	25

The table below shows the number of foreign workers from Mozambique, Swaziland, Lesotho and Botswana employed by South African gold, platinum, and coal mines from 1996 – 2011:

Table 2

	Mozambique	Swaziland	Lesotho	Botswana
1996	55,022	14,371	81,357	7,932
1997	55,027	12,960	76,360	7,536
1998	52,011	10,338	60,450	6,223
1999	46,890	9,307	52,436	5,139
2000	44,014	8,160	51,351	4,343
2001	45,254	7,794	49,599	3,651
2002	50,589	8,587	54,390	3,551
2003	52,205	7,885	54,202	4,246
2004	48,099	7,521	48,437	3,923
2005	46,256	6,878	43,693	3,257
2006	46,709	7,124	46,082	2,992
2007	44,879	7,099	45,608	2,845
2008 - 2010	Data missing	Data missing	Data missing	Data missing
2011	52,696	7,567	50,465	4,777

‘During most of the period, there were steep decreases in the number of Swazi, Basotho and Botswana, but there was only a marginal decrease in the number of Mozambicans. A possible explanation for this could be the fact that the BLS bilateral agreements (Swaziland, Lesotho and Botswana) provided for the recruitment of contract labourers subject to the availability of South African labour. The bilateral labour agreement between South Africa and Mozambique however does not contain such a provision.’¹⁸ With the comparison between Lesotho and Mozambique there is a drop of +/- 80 000 to +/-50 000 for Lesotho, but the numbers remaining almost constant with Mozambique.

1.2 The 1964 labour agreement

The 1964 agreement stipulates that the recruitment of workers in Mozambique would only be undertaken by an organisation or organisations duly approved by the Authority of the Province of Mozambique and of the Republic of South Africa.¹⁹

‘Three recruitment agencies – Albano Domingos (ALGOS), Agência de Trabalhadores para a África do Sul (ATAS) and Companhia Angariadora de Mão de Obra Nacional (CAMON) – were allowed to recruit in Mozambique through the agreement of 1964; however, unlike WENELA, these new recruitment agencies were licensed to supply labour to mines not affiliated to the Chamber of Mines and to other economic sectors such as agriculture.’²⁰

‘The employment contracts of the Mozambican mineworkers provided provisions relating to the rights and obligations between the recruiting organisation representing the workers and the affiliated mines.’²¹ The employment contracts were entered into for a period of twelve months (313 shifts worked), but the workers were entitled to enter into new contracts, or to extend or to renew their contracts for a period or periods not exceeding six months. The maximum period of service was to not exceed eighteen months. The period of the employment contract was calculated from the date the worker arrives at the place of employment, and the period of extension or of renewal from

¹⁸ Truen, S. & Chisadza, S. 2012. *The South Africa – SADC Remittance Channel*. [Online]. Available: <http://www.finmark.org.za/blog/publication/the-south-africa-sadc-remittance-channel-2/> [February 2012]

¹⁹ Labour Agreement, No.11/1964

²⁰ Gasper, N. 2006. The reduction of Mozambican workers in South African Mines, 1975 – 1992: A case study of the consequences for Gaza Province – District of Chibuto. [Online]. Available. <http://hdl.handle.net/10539/4839> [16 May 2008]: 16 -34

²¹ ibid footnote 20

the day following the one on which the previous contract expired, even if the further contract was signed on a subsequent date.²² These implications remain as the agreement remains in force.

In some instances the Mozambican mineworkers may enter into employment contracts with extensions beyond eighteen months due to the poor drafting of the 1964 labour agreement. It can be said that these employment contracts will fall outside the scope of the 1964 labour agreement.

The 1964 agreement provides certain provisions for compensation in the event of occupational injury and extended employment contracts with the approval of both the Delegate of the Institute of Labour and the South African authorities.²³

The Institute of Labour provides protection and assistance to the Mozambican mineworkers in South Africa.²⁴ The Institute of Labour is still in operation and has its offices in Johannesburg. The Labour Delegate still oversees the interests of Mozambican mineworkers on South African mines.²⁵

1.3 Bilateral treaties

The first democratic government of South Africa in 1994 inherited a series of bilateral labour agreements governing mine migration with the governments of Mozambique, Lesotho, Botswana, Swaziland and Malawi. These treaties gave the South African mining industry privileged recruiting access to non-South African labour outside the terms of the Aliens Control Act (now repealed).²⁶ Under the new Immigration Act, 2002, the mineworkers working under bilateral treaties would not be affected when applying their trade in South Africa.²⁷

Through the economic power of the mining industry it was able to persuade the governments of the day to give them special dispensations to operate their system outside the normal immigration rules and regulations. As a result, the South African government signed a series of bilateral labour treaties

²² Labour Agreement, No.11/1964

²³ Clarke, DG. 1977. *State Policy on Foreign African Labour in South Africa: Statutory, Administrative and Contractual Forms*. available:<http://opendocs.ids.ac.uk/opendocs/bitstream/123456789/1839/DSR6%20Working%20Paper%204%20-%20220766;pdf?sequence=1>

²⁴ ibid footnote 22

²⁵ Panapress..available: <http://www.panapress.com/Mozambique-sacks-Labour-Rep-in-South-Africa--13-574980-17-lang2-index.html>

²⁶ Crush, J. 1997. *Contract Migration to South Africa: Past Present and Future*. available: <http://www.queesu.ca/samp/transform/Crush.htm>

²⁷ Zwane, T.2014. *SA New Immigration Laws: Here's what you need to know*. available: <http://samigration.com/blog/sa-new-immigration-laws-heres-what-you-need-to-know/>

with the major supplier States. The treaties, although still in force, are all old agreements dating, in their current form, back to the 1960s and early 1970s. The treaties set the terms and conditions of access by contract workers (mainly miners) to the South African labour market. The employment contracts for mineworkers from Mozambique, Lesotho, Botswana, Swaziland and Malawi are subject to the conditions laid out in these treaties.

‘The treaties specify a series of conditions and obligations on the part of both South Africa and the source countries on the following issues:²⁸

- recruitment - including right to recruit, length of contract, length of time between contracts, quotas, payment of recruiting fees, the need for written contracts, and provision of facilities for recruiting and processing contracts;
- contracts - including identification of employer and employee, home address of recruit, place of employment, contract length, minimum wage, food and in-kind provision by employer, transport to and from work, and written contracts;
- remittances and deferred pay - provision for compulsory deduction of a proportion of wages and transfer to the home country;
- taxation - exempting contract workers from paying tax in South Africa;
- documentation - including valid contracts, passports and vaccination certificates; endorsement in passport to show purpose and period of entry; employment record books;
- unemployment insurance;
- length of agreements; and
- appointment of labour officials to be stationed in South Africa. The labour offices are nominally responsible for inter alia "protecting the interests of workers", registration of undocumented workers, transfer of money, providing information on conditions of employment; and consulting with the South African government on repatriation of sick or destitute workers.²⁹

‘The Malawi agreement appears to have lapsed since the expulsion of Malawian miners from the industry in 1986.’³⁰ ‘The treaty with Mozambique was actually signed by the Portuguese colonial government. There is no official bilateral [labour] treaty between South Africa and Zimbabwe.’³¹ ‘In

²⁸ ibid footnote 26

²⁹ Crush, J. 1997. *Contract Migration to South Africa: Past Present and Future*. available: <http://www.queensu.ca/samp/transform/Crush.htm>

³⁰ Samp. N.D. 2005. *Southern African Migration Programme*. available: <http://www.queensu.ca/samp/sampresources/policy.html>

³¹ ibid footnote 29

other words no similar agreements existed with Zimbabwe.’ ‘Another reason was that Zimbabwe was always an episodic supplier of migrant labour to South Africa with numbers fluctuating over time. The Mugabe government then withdrew its workers at independence in 1981.’³² The treaties with Botswana, Lesotho and Swaziland are still in operation.

Contract migration to South Africa through bilateral labour treaties is governed by legislation. The Immigration Act of 2002 (as amended in 2004) which replaced the Aliens Control Act of 1991 recognised these bilateral labour treaties. Through these treaties access is granted to unskilled labour from neighbouring states.³³ Under the Labour Relations Act No.66 of 1995 these workers are recognised as employees regardless of the form of their employment contracts.

Section 200A of the Labour Relations Act No. 66 of 1995 list several factors³⁴ that should be present for a person to be an employee. Most of these factors will apply to these workers.

The 1964 labour treaty between South Africa and Mozambique makes provision to minimize the financial costs of migration to South Africa. This includes the exemption of Mozambican mineworkers to pay South African taxes.³⁵

Following South Africa’s transition into democracy, the 1964 labour treaty and similar labour treaties with BLS states are still in operation today to regulate the migration of mineworkers to South Africa.³⁶ The provisions contained in the 1964 labour agreement poses several questions as to its relevance as an international agreement in South Africa today which are briefly explained as follows:

- Its status as an international agreement should be established in the current South African legal system.

³² ibid footnote 29

³³ Truen, S. & Chisadza, S. 2012. *The South Africa – SADC Remittance Channel*. [Online]. Available: <http://www.finmark.org.za/blog/publication/the-south-africa-sadc-remittance-channel-2/> [February 2012]

³⁴ List of factors: (a) the manner in which the person works is subject to the control or direction of another person; (b) the person’s hours of work are subject to the control or direction of another person; (c) in the case of a person who works for an organisation, the person forms part of that organisation; (d) the person has worked for that other person for an average of at least 40 hours per month over the last three months; (e) the person is economically dependent on the other person for whom he or she works or renders services; (f) the person is provided with tools of trade or work equipment by the other person; or (g) the person only works for or renders services to one person

³⁵ Reference: BAMU, PH.2014. An Analysis of SADC Migration Instruments in Light of ILO and UN Principles on Labour Migration. Available: http://www.ilo.org/wcmsp5/groups/public/---africa/---ro-addis_ababa/---ilo-pretoria/documents/meetingdocument/wcms_239819.pdf

³⁶ ibid footnote 35

- Whether the labour agreement overrides or prevents the application of the current DTC between South Africa and Mozambique removing the South African taxing right over South African source income.
- Whether discrimination between nationals of South Africa and Mozambique in terms of the current Constitution of South Africa, 1996 and Article 24 of the OECD MTC arises.
- Whether there is any revenue loss to South Africa due to the exemption of taxes provision in this agreement.
- Whether the exemption for taxes provision can be considered to be a tax incentive that might lead to harmful tax competition in the SADC region.

An important distinction to be made is between Mozambican mineworkers that entered into contracts for the first time (maximum of 18 months) and those that regularly renew their contracts (above 18 months). It is important to establish in which country the Mozambican mineworkers are resident for tax purposes. This will have a bearing on the correct taxation of these mineworkers. Furthermore, the Mozambican mineworkers have to be a resident of either Mozambique or South Africa to make use of the treaty benefits as per the DTC between South Africa and Mozambique. In respect of Mozambique the right to tax will be determined on residence of the Mozambican mineworkers. In respect of South Africa it would have a source claim for taxing these mineworkers and, if the mineworkers were also resident, a further claim based on residence.

The South African Income Tax Act established two tests in the determination of residence for individuals. These are the 'ordinarily resident' and the 'physical presence' tests which will be discussed later. Article 4 of the OECD MTC stipulates that residence should be determined in accordance with domestic laws of the Contracting States. If it is established that the Mozambican mineworker is a resident of both South Africa and Mozambique then the tie-breaker tests should be applied to establish residence of the Mozambican mineworker to either of these countries for tax purposes. This will be discussed later.

In the event that both Mozambique and South Africa tax the Mozambican mineworkers on their South African source income then the tax sparing clauses as stipulated in paragraph 2 of Article 22 of the DTC between the two countries should be taken into account. This is necessary to establish whether there are any schemes between the two countries for the promotion of economic development. If this is the case then both South Africa and Mozambique may grant reductions or exemptions on taxes paid for foreign investors such as the Mozambican mineworkers which are

applying their trade in South Africa. It should further be established whether the 1964 labour agreement may be seen as a scheme for the promotion of economic development between the two countries.

2. Research and Objectives

This dissertation has as its principle aim to provide a critical evaluation of the 1964 preferential agreement (labour agreement) for Mozambique mineworkers in the light of the South Africa – Mozambique DTC and the SADC treaty. The dissertation will test whether SARS has applied this labour agreement correctly in the context of the SADC treaty and its founding objectives of forging links to create a genuine and equitable regional integration and the harmonisation of fiscal policies in relation to tax related matters between Member States. The dissertation will also examine the exemption granted from income tax in South Africa through this labour agreement and the effective provision in the Income Tax Act 58 of 1962 (namely section 10(1)(c)(v)). Finally it will assess whether this agreement would create discrimination of the sort disallowed by the DTC network of South Africa.

To achieve these aims, the following objectives must be met, namely:

- To establish the status of this labour agreement in relation to the DTC between South Africa and Mozambique and the Constitution of the Republic of South Africa, 1996.
- To assess whether such an agreement could be classified as harmful tax competition in terms of the treaty of the South African Development Community (SADC) States and therefore a violation of that treaty.
- The monetary impact of the tax incentive will also be considered in light of the current tax threshold in South Africa against the remuneration received by the Mozambican workers to assess whether or not, in the absence of the labour treaty, such amounts paid would be taxable in South Africa. This will assess the relevance of the tax incentive against the South Africa – Mozambique DTC.
- If the tax incentive remains taxable in the absence of the labour agreement, it is then necessary to assess whether this labour tax incentive would be in violation of the non - discrimination article of the South Africa – Mozambique DTC on the basis of nationality.

It should be noted that the 1964 labour agreement between South Africa and Portugal regulating foreign migrant labour from Mozambique to South Africa impacts areas other than taxation. This

dissertation although highlighting the deficiencies on the application of this agreement in practice with respect to taxation does not conclude on how this agreement should be applied with respect to such other areas of Government or whether it should be continued or discontinued with respect to those other areas.

3. The current legal status of the 1964 labour agreement

The 1964 labour agreement's status within the current South African legal system must first be determined. This analysis is necessary as the agreement was entered into during the apartheid government, prior to South Africa's current Constitution and entered into with a colonial power on behalf of its colony. These factors all necessitate a review of the legal status of this international agreement in South Africa.

3.1 Succession of treaties

'The transition from apartheid to democracy did not involve any change in the statehood of South Africa but simply a change of government. Consequently, as a matter of international law, it was unnecessary to provide for succession to treaties as a new government automatically succeeds to the rights and obligations of its predecessor. Despite this, the Interim Constitution contained a clause providing for succession to treaties 'unless provided otherwise by an Act of Parliament'. This clause, which gave to Parliament the power to terminate treaties unilaterally, was strongly criticized by academic writers as being contrary to the procedures for termination prescribed by the 1969 Vienna Convention on the Law of Treaties.³⁷ The 1996 Constitution remedies this 'lapse' by providing that:

'The Republic is bound by international agreements which were binding on the Republic when the Constitution took effect' (Section 231(4)).

Therefore agreements/ treaties in force prior to the Constitution were brought across and remained effective. This would include the 1964 labour agreement between South Africa and Mozambique. There were no other agreements for the avoidance of double taxation with respect to taxes on income between South Africa and Portugal and South Africa and Mozambique prior to 1994, apart

³⁷ Dugard, J.2010. International Law: A South African Perspective: Cape Town: Juta and Company Ltd:55 -59

from the 1957 agreement for the avoidance of double tax on income from the business of air and sea transport.³⁸

The 1964 labour agreement (no. 11/1964 – treaty series) had been approved in Parliament and published in the Government Gazette.³⁹

3.2 The constitution – Section 231

Section 231 of the Constitution of the Republic of South Africa, 1996 refers to the current process for the approval of treaties and their enactment into law. The authority to negotiate and sign international agreements is the responsibility of the executive which consists of the president and the cabinet. Agreements are only binding if they are approved by the National executive of Provinces as well as the National Assembly in parliament.

Previously the Republic of South Africa Constitution Act, 1961 that pre-dates the current Constitution gave the State President the power to enter into and ratify international conventions, treaties and agreements in terms of section 7(g) of that Constitution.

It is submitted that the 1964 labour agreement did not follow the same steps for ratification as stipulated in section 231(2) of the Constitution.

3.3 The constitution: Section 232 & 233

The South African common law which is a blend of Roman-Dutch and English common law adopts the monist approach to customary international law.⁴⁰ In States with a monist system, international law does not need to be translated into national law. The act of ratifying an international treaty immediately incorporates that international law into national law. The International Criminal Court Statute, therefore, can be directly applied and adjudicated in national courts. “Monist systems” do differ in their approach.

- Under some Constitutions direct incorporation of international obligations into the domestic law occur on ratification.

³⁸ Proclamation 324, *Government Gazette* 5962 of 25 October 1957

³⁹ Confirmed from the resources at the SARS Library for research purposes as the agreement in its current format was approved in Parliament.

⁴⁰ Dugard, J.2010. *International Law: A South African Perspective*: Cape Town: Juta and Company Ltd: 55 -56

- In other States direct incorporation occurs only for self – executing treaties.⁴¹

‘Customary international law is part of South African law and courts are required to ‘ascertain and administer’ rules of customary international law without the need for proof of law – as occurs in the case of foreign law. As a species of common law, customary international law is, however, subordinate to all forms of legislation. The relationship between customary international law and municipal law described above was affirmed by South African courts on many occasions before 1993.’⁴²

The customary international law is given constitutional endorsement by section 232 of the 1996 Constitution which, in language substantially similar to the Interim Constitution,⁴³ provides that: *‘Customary international law is law in the Republic unless it is inconsistent with the Constitution or an Act of Parliament.’*

‘There can be little doubt that the “constitutionalisation” of this rule gives it additional weight. Moreover, customary international law is no longer subject to subordinate legislation. Only a provision of the Constitution or an Act of Parliament that is clearly inconsistent with customary international law will trump it.’⁴⁴

This is emphasized by section 233 of the Constitution, which provides that:

‘When interpreting any legislation, every court must prefer any reasonable interpretation of the legislation that is consistent with international law over any alternative interpretation that is inconsistent with international law.’

It is submitted that the 1964 labour agreement between South Africa and Portugal is a source of international law and is consistent with domestic legislation as stipulated in section 10(1)(c)(v) of the Act.

As indicated previously in section 233 of the Constitution, the Act should be interpreted in a way that is consistent with South Africa’s double tax treaties, being a source of international law, unless this interpretation is unreasonable. Therefore, a court will be compelled to interpret the Act in such

⁴¹ The Peace and Justice Initiative: Towards Universal Implementation of the ICC Statute. Available: <http://www.peacejusticeinitiative.org/implementation-resources/dualist-and-monist>

⁴² ibid footnote 40

⁴³ Dugard, J.2010. International Law: A South African Perspective: Cape Town: Juta and Company Ltd: 55 -56

⁴⁴ ibid footnote 43

a way that taxation is limited in accordance with a treaty, unless this interpretation is unreasonable. In the *CSARS v Tradehold* case (132/11) (2012) ZASCA 61 a similar conclusion was reached where the DTA was relevant and took precedence over domestic rules where a conflict arose between the two.

3.4 Enactment of the agreement by domestic law

The 'income' of the Mozambican mineworker, as defined in section 1, is the amount of his gross income remaining after the deduction of any amounts exempt from normal tax for any year or period of assessment.⁴⁵

Exemptions can be divided in two broad terms namely partial exemptions and absolute exemptions. The salary received by the Mozambican worker will fall under the former (partial exemptions) as it is assumed that only the salary will be exempt from normal tax although the taxpayer may receive other forms of income that will be taxable. Under section 10(1) (c) of the Income Tax Act salaries (and amounts for services rendered, referred to as emoluments) payable to certain persons are exempt from normal tax in respect of:

- 'a subject of a foreign state who is temporarily employed in South Africa, provided that the exemption is authorised by an agreement entered into by the governments of the foreign state and South Africa (s10(1)(c)(v)).'⁴⁶

The Explanatory Memorandum to Act No. 88 of 1965 introduces amendments to the then section 10 of the principal Act which stipulates the following:

'Paragraph (a) introduces an exemption from tax in respect of certain foreign workers who are temporarily employed in the Republic, if such exemption is provided for in an international agreement.'

From the above it is clarified that the term 'subject' refers to 'certain foreign workers'. This term can be applied to the Mozambican mineworkers who are temporarily employed in South Africa and not foreign workers in general. Since the 1964 labour agreement came into force on the 1st of January 1965 it is submitted that the Act was amended to make provision for certain foreign workers such as the Mozambican mineworkers for the exemption from tax in South Africa. The term 'agreement' refers to an 'international agreement' which can be applied to the 1964 labour agreement between

⁴⁵ Stiglingh, M., Koekemoer, AD., Van Schalkwyk, L., Wilcocks, JS. & de Swart, RD. 2013. *Silke: South African Income Tax*. South Africa: LexisNexis.

⁴⁶ *ibid* footnote 45

South Africa and Mozambique which is a source of international law. The exemption from tax is certainly provided for in the 1964 labour agreement.

4. The implications of and interaction of the 1964 labour agreement with the South Africa-Mozambique DTC distributive rules

The 1964 labour agreement's main objective will be determined in relation to the South Africa – Mozambique DTC as reflected in its preamble or title on the 'avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income'. This analysis is necessary to determine the nature of the income earned by the Mozambican workers, to allocate the right to tax the income either to the country of residence firstly and then to the country of source and to give relief for foreign taxes payable by the Mozambican workers in the elimination of double taxation. These factors are necessary to establish whether the 1964 labour agreement is in conflict with provisions as laid down in the South Africa – Mozambique DTC.

4.1 Right to tax the remuneration either to the country of residence (Mozambique) or the country of source (South Africa)

South African domestic law defines 'gross income', in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident, as or in the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within or deemed to be within the Republic.

South Africa had a source basis of taxation prior to the year 2001. Amounts were only subject to tax in South Africa if they were from a source within the Republic. The residence of the taxpayer was irrelevant. As from 1 January 2001 the source basis of taxation was replaced by residence basis for years of assessment commencing after that date.

A resident is defined in section 1 of the Act as either a person who is 'ordinarily resident' in South Africa. In other words, South Africa is his or her true home or, in the case of a person not ordinarily resident, who has spent a certain number of days in South Africa, i.e. more than 91 days in total in each of the current and previous five tax years and more than 915 days in total during the previous five tax years.

For a non-resident, only receipts derived from sources within the Republic are subject to tax in South Africa.

Section 9(2) of the Act contains deemed source rules in respect of various categories of income. As there is no specific deemed source rules for services rendered in South Africa by non-residents, the deemed source of services rendered can be linked to section 9(2)(i) of the Act that deals with pensions and annuities received or accrued in respect of services rendered within South Africa. Although this section refers to pensions partly received or accrued in South Africa for services rendered, it can be linked to the income received or accrued by the Mozambican mineworkers for services rendered in South Africa in respect of the 1964 labour agreement.

The Mozambican mineworkers that entered into contracts for the first time will not be classified as tax residents as they do not meet the requirements of being physically present in South Africa as discussed above. The length of their agreement is for 12 months with an option to extend it to a further 6 months after which they have to return to Mozambique, should the terms of the labour agreement be strictly applied.

The source of their income will be the services rendered which is located in South Africa. The income will be included in 'gross income' as defined in section 1 of the Act.

In terms of the Mozambican domestic law a resident is subject to tax on worldwide income with unilateral relief available for any foreign tax paid. A non-resident is taxable only on Mozambique source income.⁴⁷

Juridical double taxation which is the imposition of comparable taxes by two tax jurisdictions namely South Africa and Mozambique may arise on the same taxpayer in respect of the same income.

In respect of the Mozambican mineworker working in South Africa for 12 months with an option to extend it to a further 6 months there might be a source-residence conflict between the two States. The individual may be taxed in Mozambique on its worldwide income and South Africa may tax the same individual at source under its domestic law.

⁴⁷ Musviba, N. South African Tax Guide: Taxation Made Easy. Available: <http://www.sataxguide.co.za/mozambique-taxes-overview/>

The OECD Commentary on Article 15(1) indicates that the general rule as to the taxation of income from employment (other than pensions) is that such income is taxable in the State where the employment is actually exercised. Employment is exercised in the place where the employee is physically present when performing the activities for which the employment income is paid.

The OECD Commentary states further that the condition provided by the Article for taxation by the State of source is that the salaries, wages or other similar remuneration be derived from the exercise of employment in that State. This applies regardless of when that income may be paid to, credited to or otherwise definitely acquired by the employee.

The exception in paragraph 2 of Article 14 of the DTC between South Africa and Mozambique will not apply to the Mozambican mineworkers as they exceed the 183 day rule and their remuneration is paid by an employer (i.e. South African mines) which is a resident in South Africa. The general rule in paragraph 1 will therefore apply as of day one. The Mozambican mineworkers should therefore be taxed in South Africa on a source basis and their income will be included in 'gross income' as defined in section 1 of the Act and in terms of the DTC.

On the other hand instances may exist where Mozambican mineworkers regularly renew their contracts and claim relief under the 1964 labour agreement due to the poor drafting of the agreement. In these instances such workers may be regarded as being resident in South Africa through application of the physical presence test. The Mozambican mineworkers' regularly renewing contracts are likely be present in South Africa for more than 91 days in total in each of the current and previous five tax years and more than 915 days in total during the previous five tax years. The Mozambican mineworkers would not be 'ordinarily resident' in South Africa as they would in all likelihood return to Mozambique if they decide not to renew their contracts. The Mozambican mineworkers will therefore be considered as residents for tax purposes in South Africa.

For tax purposes an individual is resident in Mozambique if he/she resides in the country for more than 180 days in a tax year or has a permanent residence in Mozambique at 31 December.⁴⁸

As can be seen from the domestic laws of both South Africa and Mozambique, the Mozambican mineworker may be a tax resident in both States.

⁴⁸ *ibid* footnote 47

In terms Article 4 of the DTC between South Africa and Mozambique the definition of resident should firstly be determined in accordance with the domestic laws of both countries. Where dual residence occurs, the tie –breaker clause is applied. Under the tie- breaker clause certain tests are applied to determine in which country the dual resident is regarded as a resident for the purposes of the DTC between South Africa and Mozambique.

The first test to apply for residence is whether the Mozambican mineworker has a permanent home in either South Africa or Mozambique and in which country the Mozambican mineworker’s personal and economic relations are closer, which is referred as the ‘centre of vital interests’. As the Mozambican mineworker’s stay in South Africa is not of a short term nature as they will be regularly renewing their contracts, it is submitted that the mineworkers will have a permanent home in South Africa. In Mozambique, the mineworkers’ family will be resident in that country which will indicate that the mineworkers in most cases will have a permanent home when they return from South Africa. The Mozambican mineworkers therefore have a permanent home in both countries.

In the so-called Pavarotti Italian court case an indication was given of what is meant by the term ‘centre of vital interests’. The Tax Court decided that the real estate interest located in and outside of Italy and the current accounts and securities deposited in Italian banks was indicative of the taxpayer’s main centre of economic interest.⁴⁹ As will be discussed later in more detail the Mozambican mineworkers are compelled in terms of their contract to defer 60% of their earnings in South Africa to a central bank in Mozambique. This may provide an indication that Mozambique is their ‘centre of vital interest’. The money will mainly be used in Mozambique after their return from South Africa. The Mozambican mineworker’s main centre of economic interest will be in Mozambique as stated in the above Italian course case.

If the above was considered decisive, the Mozambican mineworkers would be resident for tax purposes in Mozambique. However, the ‘centre of vital interests’ determination is clouded by the establishment of the Mozambican mineworkers’ personal interests. In decisions of the Swiss Federal Court⁵⁰ the individual’s family ties took precedence over other economic ties.⁵¹ Following such a view, the Mozambican mineworkers’ family ties would be in Mozambique. However, it is submitted that should uncertainty remain after this test, the remaining tie-breaker rules would be consulted.

⁴⁹ Oliver, L., and Honiball, M. 2011. *International Tax: A South African Perspective*. Cape Town: Siber Ink: 34 -35

⁵⁰ Avery Jones et al ‘Dual residence of Individuals: The Meaning of the Expressions in the OECD Model Convention II’ 1981 British Tax Review 107

⁵¹ Ibid footnote 49

The second test of the tie – breaker clause refers to habitual abode. It is submitted that in this instance, there is little difference from the test of a ‘permanent home’. The contract duration may require what could be termed a habitual abode. It is submitted that the Mozambican mineworkers may have a habitual abode in South Africa and therefore closer ties to South Africa. Whenever they decide to return back to Mozambique their habitual abode will be in Mozambique and they would then have closer ties to that State. However, the Mozambican mineworkers may have a habitual abode in both States.

The third test will give a clear indication as to which country the Mozambican mineworkers will be resident for tax purposes. This test will refer to the nationality of the mineworkers to either South Africa or Mozambique. The 1964 labour agreement refers to Portuguese workers from Mozambique. Therefore, it refers to nationality. As nationality refers to citizenship of a particular country, the Mozambican mineworkers will be a national of Mozambique for the duration of their contracts in South Africa.

This nationality basis would appear conclusive to determine residency under the DTC in the absence of a result in the earlier tests. This determined residence would therefore also apply for the tax purposes of the Mozambican mineworkers in establishing the effects of the terms of the 1964 labour agreement.

It is submitted that most tests would appear to indicate that Mozambican mineworkers that regularly renew their contracts will remain resident of Mozambique for tax purposes.

4.2 Is the treaty even relevant to the earnings contemplated- Is there any revenue loss to South Africa

‘Deferment of wages is compulsory for Mozambique mineworkers, having been negotiated between the government of South Africa and the government of Mozambique (then the Government of Portugal). All Mozambique mineworkers, irrespective of which recruiting organisation was involved

in their recruitment are subjected to the rules as contained in the agreements between the respective governments.⁵²

TEBA Ltd, as the largest approved agent for the collection of compulsory deferred pay for mineworkers recruited from Lesotho and Mozambique, was required in terms of the Deferred Pay Act (Act No.18 of 1974) and the Mozambique inter government agreement to receive deferred pay monies monthly from member mines/contractors and to pay over these monies to the respective governments. In terms of the Lesotho Deferred Pay Act (Act No.18 of 1974), Lesotho mineworkers based in South Africa defer 30% of their gross earnings to Lesotho via Teba Bank (now rebranded as Ubank) for 10 months per 12 month contract.⁵³

‘Mozambique mineworkers are compelled to defer 60% of net earnings, via TEBA Ltd, to the central bank of Mozambique for 6 months of their 12 month contract, or 12 of their 18 month contract. Mozambique mineworkers cannot access their deferred wages until the end of their contracts whilst Lesotho mineworkers can access deferred wages monthly. TEBA Ltd provides this service to its shareholders and clients in return for an administrative fee of 1.5%, based on the collections. The amount collected from mineworkers in 2005 was approximately R660 000 000.’⁵⁴

In respect of the Mozambican mineworkers the Central Bank of Mozambique estimates that total mineworkers’ remittances amounted to US\$72.1m in 2010 (R526,5m).⁵⁵

No figures are available on the possible loss of revenue to the South African fiscus caused by the exemption in terms of the 1964 labour agreement. However, it is evident that the amounts considered are not inconsequential and it appears that a revenue loss of some form does occur as a result of the application of this agreement.

Two important factors will be examined in relation to the possible revenue loss. The first is how the South African mines are treating these mineworkers for tax purposes on their South African source income. Secondly, how SARS is treating these mineworkers for tax purposes and whether SARS is interpreting the 1964 labour agreement correctly to the different types of Mozambican

⁵² Samp. N.D. 2005. *Southern African Migration Programme*. available:
<http://www.queensu.ca/samp/sampresources/policy.html>

⁵³ Truen, S. & Chisadza, S. 2012. *The South Africa – SADC Remittance Channel*. [Online]. Available:
<http://www.finmark.org.za/blog/publication/the-south-africa-sadc-remittance-channel-2/> [February 2012]

⁵⁴ ibid footnote 51

⁵⁵ ibid footnote 52

mineworkers that make use of this agreement for the exemption of taxes on their South African source income. These factors are important as they will give an indication of whether any revenue loss to South Africa occurs.

It is submitted that Mozambican mineworkers that regularly renew their contracts are likely to be skilled mineworkers and in some cases be specialised in their fields. In such cases most workers would be earning a salary which is above the annual tax threshold. Those that enter into contracts for the first time would in most cases be earning a salary that is below the annual tax threshold. In the cases where the salary is below the tax threshold, there is no revenue loss as there is no amount on which tax would ordinarily be collected.

If it is assumed that the South African mines employing workers from Mozambique are applying the exemption in terms of the 1964 agreement read with the Income Tax Act and that such exemption is being applied to those regularly returning workers earning salaries above the threshold, a potential revenue loss clearly exists as the exemption is taking place at source and the taxing rights in terms of the DTC cannot then be exercised by South Africa.

If the exemption is being incorrectly applied and the 1964 agreement only applies to the first contract, it is submitted that the subsequent years of assessment may have resulted in tax in South Africa on this South African source income. In such a case, the revenue loss to SARS may have been substantial. SARS in such instances may return to previous assessments and issue revised assessments for these mineworkers in terms of section 99 of the Tax Administration Act 28 of 2011. For section 99 to apply SARS should consider whether the full amount of tax chargeable was not assessed due to fraud, misrepresentation or non-disclosure of material facts. It is submitted that the exemption of taxes provision in the 1964 labour agreement was applied incorrectly by the Mozambican mineworkers. It is a practice generally prevailing by the Mozambican mineworkers that when entering into contracts in terms of the 1964 labour agreement, the income earned in South Africa will be exempt from any taxes. It is further submitted that there was no misrepresentation or non-disclosure of material facts. This is based on the opinion of the Mozambican mineworkers that the content of the statement they had made in their previous tax returns was in respect of the exemption of taxes provision in the 1964 labour agreement. It is further submitted that there was no direct link between the misrepresentation or non-disclosure of material facts and the Mozambican mineworkers paying too little tax in the previous years of assessment. SARS can therefore only go back three years since the date of the original assessment.

Should the exemption have been incorrectly applied by the mines, the first instance of recovery by SARS would be the recovery of the PAYE that should have been deducted in the previous years from the South African mines in terms of paragraph 5 of the Fourth Schedule to the Income Tax Act.

If the contracts of the Mozambican mineworkers are not renewable beyond the 18 months in terms of the 1964 labour agreement, in other words there is no renewal of contracts, then the issues are minimised as the DTC rules between South Africa and Mozambique would then apply and the domestic exemption would not. This would leave South Africa able to tax on a source basis with no loss to the fiscus. As I previously indicated the renewals of contracts are possible in the South African mines and this remains a key flaw of the 1964 labour agreement.

It is submitted that SARS should request to clarify the application of the exemption by protocol to the 1964 labour agreement as negotiated by Government, specifically as regards the Mozambican mineworkers that regularly renew their employment contracts.

The prevention of the revenue loss and effective base erosion caused by this agreement and its application should be addressed. Such correction would also be in line with the anti-BEPS proposals from the OECD in relation to treaty abuse. Whether the 1964 agreement is justifiable in the current BEPS environment needs to be addressed by Government.

4.3 Article 22 of the DTC between South Africa and Mozambique on the elimination of double taxation

Article XXVI of the 1964 labour agreement between South Africa and Portugal stipulates the following:

*'Portuguese workers whose employment in the Republic of South Africa is regulated by the provisions of this Agreement shall not be liable for any direct taxes payable in South Africa. The Province of Mozambique shall not collect any levies or taxes from the workers for the signing of contracts, medical examinations, departures from or entry into the Province of Mozambique'*⁵⁶

⁵⁶ Labour Agreement, No.11/1964

From the above it can be concluded that the Mozambican mineworkers are not subject to South African taxes, but it appears that there is no objection to the levying of Mozambican tax.⁵⁷ The agreement seems more far reaching, applying to all direct taxes in South Africa (i.e. income tax, employee's tax etc.).

In the event that double taxation may arise then paragraph 1(a)(i) of Article 22 of the DTC should be applied. This article states the following:

*'In Mozambique, where a resident of Mozambique derives income which, in accordance with the provisions of this Convention may be taxed in South Africa, Mozambique shall allow as a deduction from the tax on income of that resident an amount equal to the South African tax paid. Such deduction shall not, however, exceed that part of the tax on income, as computed before the deduction is given, which is attributable to the income which may be taxed in South Africa.'*⁵⁸

The above paragraph follows the so – called 'ordinary credit method' where Mozambique as the State of residence allows as a deduction from its own tax an amount equal to the tax paid in South Africa in respect of the Mozambican mineworkers.⁵⁹

The above paragraph further stipulates that South Africa may, but not necessarily tax the income of the Mozambican mineworkers. In the event that South Africa chooses not to, would leave the taxation open to Mozambique.

According to paragraph 2 of the same article it states the following:

*'For the purposes of paragraph 1 of this Article, the terms "Mozambican tax paid" and "South African tax paid" shall be deemed to include the amount of tax which would have been paid in Mozambique or South Africa, as the case may be, but for an exemption or reduction granted in accordance with laws which establish schemes for the promotion of economic development in Mozambique or South Africa, as the case may be, such schemes having been mutually agreed by the competent authorities of the Contracting States as qualifying for the purposes of this paragraph'*⁶⁰

⁵⁷ Plender, R. 1987. *International migration law*. AD Dordrecht, the Netherlands: Martinus Nijhoff Publishers

⁵⁸ Article 22 of the DTC

⁵⁹ Oliver, L., and Honiball, M. 2011. *International Tax: A South African Perspective*. Cape Town: Siber Ink: 441 - 460

⁶⁰ ibid footnote 57

The above paragraph contains a reciprocal tax sparing clause. This means that tax residents from either South Africa or Mozambique could benefit from the provision in each case, should each country have reductions or exemptions for foreign investors. The DTC with Mozambique specifically provides that the schemes to promote economic development must be mutually agreed by the competent authorities of the Contracting States as qualifying for the purposes of this paragraph. No list of such agreed schemes have been made public, that is not to say that such schemes do not exist, merely that their existence is not in the public domain.⁶¹

‘The bilateral treaties licensed the mining industry to pursue its own private recruiting in neighbouring countries. The mines (through TEBA) had complete control over who they would recruit and where. On the supplier side, the treaties contained provisions to ensure that some of the benefits of migration flowed back home and to make it impossible for migrants to ever become permanent residents of South Africa. In that respect, they were prototypical bilateral agreements.’⁶²

‘The advantages of the migrant labour system of recruitment were that it benefited both the South African economy and colonial state of Mozambique. It assured an organised and cheaper source of labour for South African mines and contributed to the stability and profitability of this sector. In terms of benefits for the colonial State of Mozambique, this system brought vitally important revenue from recruiting, licence and passport fees.’⁶³

‘It also allowed for the higher taxes levied on Mozambicans in southern Mozambique. There was in addition revenue from customs dues from goods that these workers brought home from South Africa; income from railways freights and transit duties on commodities passing through Lourenço Marques from and to the Transvaal. Additionally deferred payment, established in 1928, benefited the colonial economy twofold. Firstly, the state received the deferred payment of migrant workers in pounds or in gold but it paid the migrant workers in local currency (Escudos), which allowed the State to accumulate foreign currency. Secondly, the fact that the migrant workers were paid in local

⁶¹ Oliver, L., and Honiball, M. 2011. *International Tax: A South African Perspective*. Cape Town: Siber Ink: 466 - 470

⁶² Maja, B. & Nakanyana, S. 2007. *Labour migration and South Africa: Towards a fairer deal for migrants in the South African economy*. [Online]. Available: <http://www.labour.gov.za>

⁶³ Gasper, N. 2006. The reduction of Mozambican workers in South African Mines, 1975 – 1992: A case study of the consequences for Gaza Province – District of Chibuto. [Online]. Available. <http://hdl.handle.net/10539/4839> [16 May 2008]: 16 -34

currency in Mozambique led to the growth of the local market which was dominated by Portuguese commodities, or at least goods sold by Portuguese traders, such as wine, clothes, shoes and so on.⁶⁴

‘The opportunities of employment in southern Mozambique were clearly limited and dependent on plantations and public services where the wages were low and the work conditions were poor; thus, workers and their families benefited significantly from the system of migrant labour because it allowed them to obtain higher income in the mines.’⁶⁵

It is submitted that the 1964 labour agreement may be seen as a scheme for the promotion of economic development for both South Africa and Mozambique and the tax sparing clause in paragraph 2 of Article 22 in such a case may therefore be applied to both States.

In the event that South Africa does not levy the tax through the exemption being applied then, as stipulated in paragraph 2 of the above article, the tax that would have been levied may still reduce the Mozambican tax leading to double non- taxation. This can be illustrated as follows:

Assume that South Africa has a tax rate of 30% and Mozambique has a tax rate of 40%. The Mozambican mineworker earns income of R1 000 in South Africa. The Mozambican mineworker’s tax position in each country is as follows:

South Africa

Income sourced in South Africa	<u>1 000</u>
Tax payable in South Africa	<u>R0</u>

Mozambique

Worldwide income	<u>1 000</u>
Tax on worldwide income (40% x R1 000)	400
Less: foreign tax credit (tax otherwise payable in South African tax that would otherwise have been levied)	<u>(300)</u>
Tax payable in Mozambique	<u>100</u>

Due to the tax sparing provision in the DTC between the two countries, the Mozambican mineworker will only pay 100 in income tax in Mozambique. This will lead to double non- taxation of 300 in both South Africa and Mozambique.

⁶⁴ ibid footnote 62

⁶⁵ ibid footnote 62

'The OECD Committee of Fiscal Affairs concluded that tax sparing provisions should only be considered with regards to countries where the economic level is considerably below to that of OECD Member States. They also state that adopting these provisions will minimize the potential for abuse of such provisions in respect of lost revenue to both the country of residence and the country of source. This will ensure that the provisions apply exclusively to genuine investments aimed at developing the source State.'⁶⁶

This is particularly true in the case of South Africa as the organised and cheap source of labour to South African mines contributed to the stability and profitability of this sector in South Africa.

4.4 Conclusion

The definition of 'gross income' as defined in section 1 of the Act includes remuneration earned by non-residents from a source or deemed source within the Republic. The source of the income of the Mozambican mineworkers will be the services rendered which is located in South Africa by applying the deemed source rules in terms of section 9(2) of the Act.

South Africa therefore has the right to tax the income earned by the Mozambican mineworkers according to its domestic law. In addition, Article 14 of the DTC between South Africa and Mozambique gives South Africa the right to tax the income earned by the Mozambican mineworkers.

If the 1964 labour agreement is strictly applied the Mozambican mineworkers that entered into contracts for the first time would not be taxed in South Africa and there would be a revenue loss to South Africa if their earnings are above the annual tax threshold.

There may be a substantial revenue loss to South Africa in respect of the Mozambican mineworkers that regularly renew their contracts in terms of the 1964 labour agreement as their earnings in most cases would be above the annual tax threshold.

⁶⁶ Holmes, K. 2007. International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation. Amsterdam: IBFD Publications BV: 109

Paragraph 2 of article 22 of the DTC provides a tax sparing provision if it is established that a scheme for the promotion of economic development exists between the two countries. The 1964 labour agreement between the two countries as discussed above appears to be such an arrangement.

5. Does the 1964 labour agreement conflict with other legislation?

The 1964 Labour Agreement will be analysed to determine whether it is in conflict with the Immigration Act No. 13 of 2000 instituted by South Africa including the Constitution of South Africa, 1996. This is necessary to establish whether this agreement will invoke any discrimination clauses.

The Immigration Act (No 13 of 2002) deals with immigration and migration. It repeals the Aliens Control Act of 1991 as well as the Aliens Control Amendment Act (No. 76 of 1995) and regulates the admission of people to South Africa and their right to live and work here. The Act uses a licensing fee to manage the process of allowing foreigners to work and live in South Africa. It also regulates the movement of migrant workers in certain sectors such as mine working and agricultural work.⁶⁷

The Constitution of South Africa, 1996 was approved by the Constitutional Court on 4 December 1996 and took effect on 4 February 1997. The Constitution was as a result of some detailed negotiations on the part of government with an awareness of the injustices of the past. It is widely considered to be the most progressive constitution in the world, with a Bill of Rights second to none.⁶⁸

5.1 Constitution of the Republic of South Africa, 1996

It should first be established whether constitutional law applies to all persons in South Africa, irrespective of whether they are citizens or aliens.⁶⁹

The present Constitution does not contain any direct reference to application to all persons in South Africa irrespective if they are citizens of another country. Therefore, these provisions should be

⁶⁷ Citizenship Immigrants and Migrants. [Online]. Available:

<http://www.paralegaladvise.org.za/docs/chap02.html>

⁶⁸ South Africa.info. 2015. The Constitution of South Africa. [Online]. Available:

<http://www.southafrica.info/about/democracy/constitution.htm#.VRaG3I105jp>

⁶⁹ Rautenbach, IM., and Malherbe, EFJ. 2009. *Constitutional Law*. Pietermaritzburg: Interpak Books: 70

determined on the principles of international law. It is submitted that Mozambican mineworkers working in South Africa are afforded the same Constitutional rights as citizens while in South Africa.⁷⁰

Attention has previously been drawn to the potentially unconstitutional aspects of the 1964 labour agreement, such as compulsory deferred pay. The agreement raises the question of discrimination as envisaged in section 9 of the Bill of Rights which contains the provisions of equality. The following aspects in the 1964 labour agreement may be seen as discrimination in relation to the Mozambican mineworkers, South Africans (mineworkers and normal citizens), mineworkers of neighbouring States like Lesotho, Swaziland and Botswana which entered into similar agreements and workers who obtained work permits under the Aliens Control Act (now repealed):

a) Compulsory deferred pay and remittances

In respect of the Mozambican mineworkers the aspect of compulsory deferred pay and remittances on remuneration received in South Africa should be analysed. This requirement is stated in Article XVIII of the 1964 labour agreement. 'There is considerable debate about the deferred pay system. On the South African side, neither the Chamber of Mines⁷¹ nor the NUM appear to be in favour of this system. Others argue that the system violates the basic rights of a person as contained in the Constitution to earn and spend their money where they wish.'⁷²

b) Permanent residence

Workers from the Southern African region seeking legal access to South Africa were subject to a dual system of control known as the 'two gates' policy. The two gates were (a) the Aliens Control Act of 1991 (now repealed) and (b) various bilateral labour agreements between South Africa and the neighbouring States of Mozambique, Botswana, Lesotho, Swaziland and Malawi. Under the new Immigration Act, 2002, the mineworkers working under bilateral treaties would not be affected when applying their trade in South Africa. The Labour Market Commission, which is a commission to investigate the Development of a Comprehensive Labour Market Policy, argues that the 'two gates' policy, still in application to persons prior to the repeal of the Aliens Control Act, is discriminatory. It discriminates against those Mozambican mineworkers who remain perpetual contract workers under the 1964 labour agreement and are denied the right to more permanent residence and

⁷⁰ ibid footnote 68

⁷¹ The Chamber of Mines were in favour of the continuation of the treaties but not in respect of the compulsory deferred pay and remittances which they view as discrimination.

⁷² Crush, J. 1997. *Contract Migration to South Africa: Past Present and Future*. available: <http://www.queesu.ca/samp/transform/Crush.htm>

employment, as envisaged by South African immigration legislation.⁷³ Furthermore, these mineworkers cannot bring their families with them under the 1964 labour agreement.

c) Compensation and unemployment insurance

'The bilateral treaties do not provide adequately for compensation and unemployment insurance, and the provisions that do exist are out of date. In relation to compensation, migrant workers are generally covered by South African legislation, namely by the Compensation for Occupational Injuries and Diseases Act No. 130 of 1993 (COIDA) and the Occupational Diseases in Mines and Works Act No. 208 of 1993. Compensation in terms of COIDA is often made through TEBA (now an independent company with labour processing, financial and modest development functions) except in relation to Mozambique where it is paid to the Mozambican labour delegate. There is a great deal of dissatisfaction among Mozambican miners relating to the system of compensation. They claim that they either do not receive the money due to them or that they receive only part of it.'⁷⁴

d) Employment contracts

'Employee contracts governed by the treaties are also outmoded and contrary to international requirements insofar as they do not contain details of the occupation the miner will be engaged in nor the remuneration he will receive. Newly recruited workers only receive these details when they arrive at the mine.'⁷⁵

It might be possible that the employment contracts might infringe on the rights of the Mozambican mineworker to fair labour practices as envisaged in section 23 of the Bill of Rights. The Mozambican mineworker may not have certain labour rights in respect of the right to collective bargaining and to join a trade union.

e) Policy of job preference

'The policy of job preference for nationals is also reflected in the bilateral treaties. 'The Lesotho, Botswana and Swaziland treaties provide that recruitment of labour is subject to the availability of South African labour.'⁷⁶ While there is no such provision in the Mozambique agreement, it nevertheless provides that the number of workers to be recruited will be mutually agreed upon by

⁷³ ibid footnote 52

⁷⁴ *Restructuring the South African Labour Market: Report of the Presidential Commission to Investigate labour Market Policy*. [Online]. Available: <http://www.polity.org.za/polity/govdocs/commissions/fintoc.html> [June 1996]

⁷⁵ Ibid footnote 73

⁷⁶ ibid footnote 73

the two governments, thus in fact allowing for the operation of a regulated quota system.⁷⁷ The South African mineworkers may be discriminated against due to the fact job preference would first be given to Mozambican mineworkers.

f) Exemption from direct taxes

Exemption from direct taxes in South Africa which is applicable to Mozambican mineworkers for a maximum period of 18 months as stated in the provision of Article XXVI of the 1964 labour agreement.⁷⁸ The South African mineworkers and indeed all citizens of South Africa are discriminated against by virtue of the exemption from Income Tax applicable to Mozambican mineworkers.

5.2 The Immigration Act No.13, 2002

‘In the past the South African immigration policy has been described as having ‘two gates’ which is a dual system of control for foreign workers. Under the Aliens Control Act, immigration and temporary residence is governed by statute. However, exemption clauses in the Act allow for bilateral treaties with neighbouring states which govern the entry of contract workers, primarily in the mining and commercial agriculture sectors.’⁷⁹

In respect of the South African Immigration Act it was therefore proposed to continue the system of exemptions. In effect this would mean that the 1964 labour agreement in respect of the Mozambican mineworkers continues and the contract labour system remains outside legislative control in this instance.⁸⁰

6. Is the 1964 labour agreement a harmful tax practice as contemplated in the SADC treaty

The 1964 labour agreement will be analysed to determine whether the exemption of taxes on income received by the Mozambican mineworkers in South Africa can be seen as harmful transactions as contemplated in the SADC treaty. This is necessary to establish whether the

⁷⁷ ibid footnote 73

⁷⁸ Labour Agreement, No.11/1964

⁷⁹ SAMP. N.D. 2005. *Southern African Migration Programme*. available:

<http://www.queensu.ca/samp/sampresources/policy.html>

⁸⁰ ibid footnote 78

agreement is in contravention of any of the permissible types of tax incentives provided in the Memorandum of Understanding on Co-Operation in Taxation and Related Matters (MoU) issued by the Southern African Development Community (SADC).

6.1 Is the 1964 labour agreement a tax incentive?

‘Many countries, developed and developing alike, offer various incentives in the hope of attracting investors and fostering economic growth. Yet there is strong evidence⁸¹ that calls into question the effectiveness of some tax incentives for investment, including in particular tax free zones and tax holidays. Indeed, ineffective tax incentives are no compensation for or alternative to a poor investment climate and may actually damage a developing country’s revenue base, eroding resources for the real drivers of investment decisions - infrastructure, education and security.’⁸²

‘Tax base erosion due to tax incentives is compounded by the lack of transparency and clarity in the provision, administration, and governance of tax incentives. The granting of tax incentives for investment is often done outside of a country’s tax laws and administration, sometimes under multiple pieces of legislation. The design and administration of tax incentives may be the responsibility of several different Ministries (e.g., finance, trade, investment). Where various Ministries are involved, they may not coordinate their incentive measures (tax and non-tax) with each other or the national revenue authority, with the result that incentives may overlap, be

⁸¹ Strong evidence on effectiveness of incentives: (a) Incentives ranked 11th out of 12 location factors in a survey of 7000 firms in 19 African countries. (UNIDO 2011); (b) In South East Europe investors indicate that rather than encouraging Foreign Direct Investment (FDI), special tax incentives either were not taken into account or operated to discourage investment – provisions were difficult to track, understand or comply with and/or invited corrupt behaviour on the part of tax officials, tending to increase project costs and uncertainty (OECD 2007); (c) In 1980 no low-income Sub-Saharan African country had tax free zones, 50 percent did so by 2005; in 1980 about 40 percent offered tax holidays, by 2005 over 80 percent did so (IMF 2009a); (d) Forgone tax revenues ranged between 9.5 and 16 percent of GDP per year in the Eastern Caribbean Currency Union over 2001-2003, while the effect of tax incentive regimes on foreign direct investment appeared to be very modest (IMF 2008), (e) A study of 40 Latin American, Caribbean and African countries for the period 1985–2004 showed that there is no effect on total investment or economic growth due to tax incentives (IMF 2009b); (f) Prior to 2006 Mauritius had an extensive set of tax incentives. A major tax reform was undertaken in 2006 which included the removal of most tax holidays, exemptions and investment tax credits. FDI and Corporate Income Tax revenue experienced strong growth since the reforms (IMF 2011); (g) The design and administration of tax incentives may be the responsibility of several different Ministries (e.g., finance, trade, investment). Where various Ministries are involved, they may not coordinate their incentive measures (tax and non-tax) with each other or the national revenue authority, with the result that incentives may overlap, be inconsistent, or even work at cross-purposes & (i) Morocco is the only MENA country to elaborate a Tax Expenditure Report, which has been integrated into the government’s budget process (OECD 2008).

⁸² Organisation for Economic Cooperation and Development ("OECD"). 2003. Draft Principles to Enhance the Transparency and Governance of Tax Incentives in Developing Countries. [Online]. Available: <http://www.oecd.org/ctp/tax-global/transparency-and-governance-principles.pdf>

inconsistent, or even work at cross-purposes. Administrative discretion in the management of incentives can seriously increase the risk of corruption and rent seeking.⁸³

6.2 Definition of tax incentives

‘The Business Dictionary (2011) defines a tax incentive as ‘the deduction, exclusion, or exemption from a tax liability offered as an enticement to engage in a specified activity (such as investment in capital goods for a certain period’. The MoU issued by the SADC defines tax incentives as ‘fiscal measures that are used to attract local or foreign investment capital to certain economic activities or particular areas in a country.’

The above can also apply to individuals. Tax sparing can also be linked to the granting of tax incentives to foreign investors, particularly in regard to the promotion of economic development in the source State.⁸⁴ Tax sparing can also apply to foreign individuals in the source State.

‘The fundamental purpose of taxation is to raise revenue effectively, through measures that suit each country’s circumstances and administrative capacity. In fulfilling the revenue function, a well-designed tax system should be efficient in minimizing the distortionary impact on resource allocation, and equitable in its impact on different groups in society.’⁸⁵

According to the SADC Memorandum of Understanding on Taxation (2002), tax incentives are ‘fiscal measures that are used to attract local or foreign investment capital to certain economic activities or particular areas in a country.’ This definition excludes ‘general tax incentives’ that apply to all investments.⁸⁶

Zee, Stotsky and Ley (2002) adopt a similar definition in a recent review of this topic. They claim that ‘any tax provision that is applicable to all investment projects does not constitute a tax incentive.’ This definition excludes ‘general tax incentives’, such as accelerated depreciation that applies to all investments.⁸⁷

⁸³ ibid footnote 81

⁸⁴ Oliver, L., and Honiball, M. 2011. International Tax: A South African Perspective. Cape Town: Siber Ink: 466 - 470

⁸⁵ Bolnick, B. 2004. Effectiveness and Economic Impact of Tax Incentives in the SADC Region. Available :http://pdf.usiad.gov/pdf_docs/PNACY929.pdf [February 2004]

⁸⁶ ibid footnote 84

⁸⁷ ibid footnote 84

6.3 Memorandum of understanding on the co-operation in taxation and related matters - SADC

In 2002 the Southern African Development Community (SADC) issued the Memorandum of Understanding on Co-Operation in Taxation and Related Matters (MoU) to its fifteen member states. In terms of the MoU the member States agreed on steps to be taken to co-operate in taxation matters and to harmonise the tax regimes of the member States in accordance with Articles 21 and 22 of the Treaty of the Southern African Development Community (Treaty).

Article 4(1) of the MoU stipulates that member States will endeavour to achieve a common approach to the treatment and application of tax incentives and will, amongst other things, ensure that tax incentives are provided for only in tax legislation.

Article 4 of the MoU provides the following tax incentives:

- a) investment allowances in addition to full depreciation allowances;
- b) an investment tax credit where a certain percentage of the acquisition cost is deducted in addition to normal depreciation deductions, from the tax liability;
- c) the full cost of acquisition of the asset is allowed as a deduction from the taxable profits of the year in which the investment was made;
- d) accelerated depreciation allowances;
- e) declining balance depreciation allowances;
- f) tax privileged export processing or enterprise zones; and
- g) tax holidays.

The above incentives can be seen as focussing more on investment tax incentives operating through company income tax although some can also apply to individuals.

6.4 Tax incentive – Exemption from normal tax for Mozambican mineworkers

The 1964 Labour agreement can be seen as focussing more on individual tax incentives than on corporate tax incentives. There are no incentives in the hope of attracting investors and fostering economic growth as in the case of corporate tax incentives. The Mozambican mineworkers are

provided tax incentives in the form of exemptions from income tax on remuneration for a maximum of 18 months of their contract.

There is a form of tax base erosion due to the tax incentives provided to the Mozambican mineworkers as there could be a lack of transparency and clarity in the provision, administration and governance of the tax incentive provided to the mineworkers. Although the 1964 labour agreement is given effect in terms of s 10(1)(c)(v) of the Act which exempts the mineworkers from normal tax on income there is clearly a lack of transparency and clarity due to the tax incentive. The 1964 labour agreement is not well known to SARS and other government departments and the South African public in general.

The agreement is not always readily assessable to SARS and other government departments e.g. the labour department that have to keep statistical data with regards to immigration and working permits. There are no up to date figures available on the revenue loss to the fiscus as a result of the income not taxed. Revenue losses in total remittances which includes compulsory and voluntary deferment of wages is not readily available. Therefore, the tax incentives provided to the Mozambican mineworkers are not always collected and reported which will certainly have an effect on reliability of adequate analysis that can be provided to government on the analysis of their costs and benefits in a national context to support government decision –making.

6.5 Restricting tax incentives to particular taxpayers – Mozambican mineworkers

South Africa imposes tax on a residence basis and tax non-residents on a source basis. Therefore the exemption on any tax payable on income received by the Mozambican workers in South Africa is clearly a tax incentive. This is often a clear indication that South Africa is engaged in harmful tax competition as stipulated in Article 4(3)(a) of the MoU. The Article lists a number of instances which are evidence of harmful tax competition. This includes “ring fencing” of a regime from the domestic economy in favour of non-resident taxpayers which is applicable in the case of the Mozambican mineworkers. The Mozambican mineworkers that are incorporated into this regime enjoy the benefit of the infrastructure of South Africa which provides the preferential tax regime, without necessarily incurring the cost of the infrastructure.⁸⁸

⁸⁸ Organisation for Economic Cooperation and Development ("OECD"). 1998. *Harmful Tax Competition: An Emerging Global Issue*. [Online]. Available. <http://www.oecd.org/dataoecd/33/0/1904176.pdf> [22 June 2011]

'The fundamental purpose of taxation is to mobilize revenue to finance the provision of public goods and services through the government budget. Therefore, *the core principle of taxation is that the tax system should be an effective instrument for raising revenue*. While fulfilling the revenue function, taxes also have a pervasive influence on economic decisions of individuals and businesses, and on social equity. Hence, the tax system should be structured to achieve the appropriate level of revenue as efficiently and fairly as possible. In short, a well-designed tax system should be:⁸⁹

- **Effective** in raising revenue;
- **Efficient** in its effect on resource allocation decisions of households and businesses; and
- **Equitable** in its impact on different groups in society'.

'An effective tax system is one that satisfies revenue requirements, given the desired scope and size of government and the availability of non-tax financing. In dynamic terms, an effective tax system should be elastic, in the sense that revenue rises naturally with GDP without requiring frequent ad hoc measures. An effective tax system must be consistent with a country's administrative capacity. Even the best tax code can produce poor results if it is not well administered. The introduction of special investment incentives inherently complicates tax administration and creates loopholes through which companies and wealthy taxpayers avoid or evade other tax obligations. These are serious problems worldwide, but the costs are especially high in countries with weak tax administration and critical revenue constraints. Under these conditions, simplicity is a cardinal principal.'⁹⁰

'Many SADC countries face a critical need to enhance tax collections (relative to GDP) in order to finance urgent demands for public services, including those essential to economic growth and social welfare, such as education, health, public security, legal and judicial systems, and economic infrastructure. Therefore, the revenue effect of tax incentives is a central concern. In countries with adequate fiscal resources, revenue risks may not be a major issue; but in countries where revenue performance is precarious, such policies may be highly imprudent.'⁹¹

SARS might assess the Mozambican mineworkers according to the DTC between South Africa and Mozambique. This may result in objections from the Mozambican mineworkers who insist that they should not be taxed in South Africa according to the 1964 labour agreement. The above problem can be due to an administrative capacity in the organisation, in that revenue authority staff might be

⁸⁹ Bolnick, B. 2004. *Effectiveness and Economic Impact of Tax Incentives in the SADC Region*. Available :http://pdf.usiad.gov/pdf_docs/PNACY929.pdf [February 2004]

⁹⁰ Bolnick, B. 2004. *Effectiveness and Economic Impact of Tax Incentives in the SADC Region*. Available :http://pdf.usiad.gov/pdf_docs/PNACY929.pdf [February 2004]

⁹¹ ibid footnote 89

unaware of the 1964 agreement and how it should be implemented. It can also be said that the agreement will have an impact on revenue loss which in turn will affect urgent demands for the finance of public services in both a South African and a Mozambican context.

‘Efficiency is especially important for poor countries that can least afford economic losses due to avoidable resource misallocation. To minimize efficiency losses, most tax reform programs in developing countries aim to apply a moderate tax rate to a broad tax base. To the extent that special incentives shrink the tax base, revenue targets can only be achieved with higher tax rates on other activities or persons that remain chargeable.’⁹²

The 1964 agreement stipulates that the mineworkers would not be liable for any direct taxes payable in South Africa on income received. This will have an effect that tax rates would increase on other activities and residents of South Africa.

‘The concept of tax equity is endlessly debated. Yet there is widespread agreement that an equitable tax system should:⁹³

- Minimize the tax burden on the poor;
- Collect more from the rich than from those with lower incomes (vertical equity);
- Avoid excessive tax rates and arbitrary impositions all around; and
- Provide relatively uniform and non-discriminatory treatment of taxpayers with similar economic circumstances in terms of ability to pay (horizontal equity)’.

‘Equity issues are often neglected in deliberations about tax incentives, but they surely bear consideration as a matter of principle, and also because perceptions of unfairness can undermine the political sustainability of an incentive program. Investment incentives directly reduce the tax burden on income earned by relatively wealthy investors. As a result other taxpayers may bear a greater tax burden.’⁹⁴

The tax incentive to Mozambique workers is discriminatory towards South African mineworkers with similar economic circumstances and South African residents which are not employed in the mining sector. It can be said that the tax incentive is discriminatory towards the mine workers from

⁹² ibid footnote 89

⁹³ Bolnick, B. 2004. *Effectiveness and Economic Impact of Tax Incentives in the SADC Region*. Available :http://pdf.usiad.gov/pdf_docs/PNACY929.pdf [February 2004]

⁹⁴ ibid footnote 92

Botswana, Lesotho and Swaziland with similar economic circumstances. The workers from these countries shall be liable to pay taxes levied upon them by their respective Governments. 'The South African authorities shall endeavour to ensure that the employers of such workers deduct such taxes at the rates prescribed by the Botswana, Lesotho and Swaziland authorities from the wages of their employees and remit any monies so deducted to appropriate authorities of these countries according to the labour agreements with these countries.'⁹⁵

6.6 Regional integration of Mozambique in the SADC

'The mining industry in South Africa can be seen as the most important factor in the process of regional integration. From its inception, in the last third of the nineteenth century, this sector has needed large numbers of workers many of whom were recruited from different parts of Southern Africa. Mozambican workers were part of this process from the beginning and constituted a major segment within the migrant work force.'⁹⁶

'This massive presence of Mozambican workers in the South African mining industry was important to the Mozambican economy. There were agreements concerning the supply of Mozambican workers to South African mines between the two States from the late nineteenth century. The system of deferred pay and the complementary accords about ports and railways conferred substantial advantages on the Mozambican State and economy. On the other hand, wage labour on the South African mines constituted a significant source of income for Mozambicans, especially in the rural areas of Southern Mozambique.'⁹⁷

6.7 Options for co-operation

As stated in the MoU, the Member States are determined to take such steps as are necessary to maximise the co-operation of the Member States in taxation matters.

⁹⁵ Labour Agreement, No.1/1973, No.3/1973 & No.3/1986,

⁹⁶ Gasper, N. 2006. *The reduction of Mozambican workers in South African Mines, 1975 – 1992: A case study of the consequences for Gaza Province – District of Chibuto*. [Online]. Available. <http://mobile.wiredspace.wts.ac.za/handle/10539/483> [16 May 2008]: 16 -34

⁹⁷ Gasper, N. 2006. *The reduction of Mozambican workers in South African Mines, 1975 – 1992: A case study of the consequences for Gaza Province – District of Chibuto*. [Online]. Available. <http://mobile.wiredspace.wts.ac.za/handle/10539/483> [16 May 2008]: 16 -34

‘A well designed agreement on tax co-operation can be a win-win strategy for all Member States.’ Such an agreement will have a particular importance for the poorest Member States like Mozambique, which most need to attract additional investment. ‘Since the entire SADC community has an interest in helping the poorest members to develop, there is a widespread acceptance that a viable agreement should include special consideration for these States, allowing them more latitude in structuring their incentive programs.’⁹⁸

This would come back to the tax sparing provisions as discussed previously. Such an agreement between the Member States will contain tax sparing provisions for schemes for the promotion of economic development for the poorest members like Mozambique.

This agreement read together with any DTA’s between the Member States and Mozambique may also contain such tax sparing provisions. As the workers from these Member States apply their trade in Mozambique in respect of genuine investments in developing Mozambique in line with their incentives programs this will lead to the non-taxation of their income in Mozambique as the source State. If such agreement can be seen as a reciprocal tax sparing provision for any of the Member States in respect of the same incentive programs the same workers will also not be taxed in these States. This will lead to double non-taxation of the same income of these workers between the Member States and Mozambique.

6.8 Conclusion

The 1964 bilateral labour agreement between South Africa and Mozambique appears to be in default of Article 21 and 22 of the SADC treaty which seeks co-operation of Member States in taxation matters and to harmonise the tax regimes. As stated previously mineworkers from Swaziland, Botswana and Lesotho are treated differently on taxes levied upon them compared to Mozambican workers in similar circumstances. Although it can be argued that the mineworkers from these States appear to be exempt from any taxes on income received in South Africa. According to the labour agreements of these States the Government of South Africa has the obligation to deduct taxes from these mineworkers and remit it to Governments of their respective States.

⁹⁸ Bolnick, B. 2004. Effectiveness and Economic Impact of Tax Incentives in the SADC Region. Available :http://pdf.usiad.gov/pdf_docs/PNACY929.pdf [February 2004]

In case of the Mozambican labour agreement no such provision exists and it only states that the Mozambican mineworkers will be exempt from any taxes in South Africa. There is no uniform agreement on matters of tax incentives to particular taxpayers in the SADC Member States which in this instance are in respect to the tax incentives provided to the Mozambican mineworkers which in terms of Article 4(3)(a) of the MoU is evidence of harmful tax competition.

On the other hand cognisance should be taken of the fact that the main objective of the SADC treaty is to seek regional integration of Member States in Southern Africa especially the poorest members like Mozambique.

In some way the 1964 labour agreement between South Africa and Portugal goes a long way in achieving that objective. In not taxing the income of the Mozambique workers in South Africa, it would help attract investment in Mozambique which will have a significant impact on the Mozambican economy and society as a whole.

7. Does the 1964 labour agreement violate the non-discrimination article of the South Africa – Mozambique DTC based on nationality?

An analysis of the 1964 labour agreement will be done to identify whether the Mozambican mineworkers as nationals are treated on equal terms with nationals of South Africa, Botswana, Lesotho and Swaziland which are in similar circumstances and whether the taxes that are imposed on the Mozambican mineworkers are not more burdensome than their South African, Botswana, Lesotho and Swaziland counterparts. This is necessary to establish whether the 1964 labour agreement is in contravention of Article 24 of both the OECD and UN MTC.

‘The general principle of non-discrimination in the treatment of a country’s citizens is often enshrined in the country’s constitutional law or human rights legislation. In the taxation context, discrimination can be regarded as the unfavourable treatment of a taxpayer in comparison with another taxpayer or category of taxpayers in respect of the same taxable item(s) and in the same circumstances.’⁹⁹

“Discrimination” has been broadly defined as:

⁹⁹ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV: 400 -401

‘the equal treatment of different cases or the unequal treatment of comparable cases. In an international tax context discrimination most often takes the form of different treatment of taxpayers whose situations are comparable except in respect of a characteristic such a nationality.’¹⁰⁰

‘Article 24 of the OECD model DTA contains a non-discrimination clause that prevents partner states from discriminating between its nationals and enterprises and those nationals of other states in applying the provisions of the DTA between the two states.’¹⁰¹

‘On closer analysis of the non-discrimination clause, it might indicate infringement on the right of equality of our nationals/citizens as enshrined in section 9 of the Constitution of the Republic of South Africa, 1996. However, non-discrimination and equality differ completely. In fact infringement on the right to equality might be justified but discrimination cannot be justified.’¹⁰²

Neither of the OECD and UN MTCs provide a definition for ‘discrimination’ or ‘non-discrimination’. Article 24 of the OECD MTC does not guarantee fair or equitable tax treatment of Mozambican nationals of the Contracting State (Mozambique) but merely ensures that these nationals are not treated more harshly in terms of taxing their income than the nationals of the other Contracting State (South Africa). As a result the basic fairness of the South African tax system cannot be questioned.¹⁰³

Article 24 of both the OECD and UN MTCs apply to every kind of taxes between nationals and enterprises and not just those mentioned under the tax treaty. It will therefore, cover taxes like Pay as You Earn, Value-Added Tax and the Skills Development Levy

7.1 Article 24 of the OECD MTC

The non-discrimination rule in Article 24 (1) of the OECD model DTA states:

‘Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than

¹⁰⁰ ibid footnote 98

¹⁰¹ ibid footnote 98

¹⁰² Oliver, L., and Honiball, M. 2011. *International Tax: A South African Perspective*. Cape Town: Siber Ink: 486 - 487

¹⁰³ Oliver, L., and Honiball, M. 2011. *International Tax: A South African Perspective*. Cape Town: Siber Ink: 486 – 487

*the taxation and connected requirements to which nationals of that other State in the same circumstances in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provision of Article 1 also apply to persons who are not residents of one or both of the contracting State.*¹⁰⁴

‘The non-discrimination principle embodied in Article 24(1) therefore turns on the nationality of a taxpayer and not the taxpayer’s residence.’¹⁰⁵

Insofar as Article 24 is concerned, South Africa can legitimately discriminate between residents and non-residents of South Africa (who may be residents of Mozambique). But South Africa cannot discriminate between its nationals and nationals of Mozambique who are in the same circumstances as its nationals. Article 24(1) tells us that, in evaluating the circumstances of two taxpayers (one a national of Mozambique) and the other (a national of South Africa), we must take into account especially the circumstances of each national’s residence.¹⁰⁶

Therefore, discrimination on the grounds of nationality exists only where nationality, and nothing else, is the decisive criterion for the taxpayer being treated less favourably under South Africa’s domestic law. Conversely, if South Africa treats a national of Mozambique less favourably than its own nationals for reasons other than nationality (i.e. the criterion warranting the different tax treatment is one other than nationality), there is no violation of Article 24 (1) of the OECD model DTA. Hence, one particular circumstance that does not fall under Article 24 (1) is less favourable treatment of non-residents of South Africa, even if they are nationals of Mozambique. Thus only nationals of South Africa who are resident in Mozambique (being in the same circumstances as the taxpayers in question who are not nationals of South Africa) are the basis of comparison.¹⁰⁷

For example, under Article 24 (1) there is no discrimination in its tax treatment if South Africa taxes the income of non-residents at a higher rate than the income of residents of South Africa. This is because Article 24(1) requires non-discriminatory treatment of nationals of the two states in like circumstances.¹⁰⁸

¹⁰⁴ Article 24 (1) of the OECD MTC

¹⁰⁵ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV: 401 – 402

¹⁰⁶ *ibid* footnote 104

¹⁰⁷ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV: 401 - 402

¹⁰⁸ *ibid* footnote 106

Therefore, a national of Mozambique who is a non-resident of South Africa must be treated in the same way as a national of South Africa who is a non-resident of South Africa and also a resident of Mozambique. Since the tax law of South Africa, which imposes a higher tax rate on non-residents of South Africa, applies equally to non-residents who are nationals of Mozambique and to non-residents who are nationals of another Country, both nationals are treated in the same way.¹⁰⁹

According to Article 1 of the OECD MTC the provisions of the DTA would only apply to a resident of a contracting State. Therefore, for Article 24(1) to operate it should refer to nationals. Therefore, Article 24(1) should override Article 1 in that respect. In its definition, Article 24(1) does that.¹¹⁰

‘Both the OECD and UN MTCs define the term ‘national’ in Article 3 as:

- (i) any individual possessing the nationality or citizenship of that Contracting State; and
- (ii) any legal person, partnership or association deriving its status as such from the laws in force in that Contracting State.’¹¹¹

Therefore, the concept of nationality will be defined according to the contracting State’s domestic law. In respect of individuals that will be the law that defines nationality or citizenships.¹¹²

Therefore, the question should be asked whether the tax laws of a contracting State discriminates between two persons solely on the basis that one is a national and the other person is a non-national. For example, under the domestic law of South Africa, nationals are given an allowance if they reside in a specific geographic area, non-nationals of Mozambique should qualify for the same relief provided that they reside in the same area.¹¹³

7.2 Non-discrimination – South African mineworkers, BLS & Mozambican mineworkers

Article 24(1) specifies that the tax and its related requirements imposed by South Africa on nationals of Mozambique cannot be ‘other or more burdensome than’ that imposed on South Africa’s own nationals in the same circumstances as Mozambique’s nationals. In so far as the imposition of tax is

¹⁰⁹ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV: 402 – 403

¹¹⁰ *ibid* footnote 108

¹¹¹ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV: 402 – 403

¹¹² *ibid* footnote 110

¹¹³ *ibid* footnote 110

concerned this means first that the tax imposed on the Mozambique nationals must be the same tax to which South African nationals are subjected.¹¹⁴

In respect of the Mozambique mineworkers they are not subject to any direct taxes on income earned in South Africa for a maximum period of 18 months. The South African mine workers will be taxed on their income for this period if they are above the annual tax threshold.

The Mozambican mineworkers tax liability is therefore not more burdensome than that of South African mineworkers in the same position.

The mineworkers from Swaziland, Botswana and Lesotho are treated differently on taxes levied upon them compared to Mozambican mineworkers in the same circumstances. It can be argued that the mineworkers from these States appear to be exempt from any taxes on income received in South Africa due to the fact that the labour agreements of these States stipulate that the Government of South Africa has the obligation to deduct taxes from these mineworkers and remit it to Governments of their respective States. In case of the Mozambican labour agreement no such provision exists and it only stipulates that the Mozambican mineworkers will be exempt from any taxes in South Africa. It is submitted that there is no discrimination between mineworkers from these States and mineworkers from Mozambique. The tax liability of mineworkers from Swaziland, Botswana and Lesotho is also not more burdensome than that of the South African mineworkers in the same position.

Article 24(1) further stipulates that nationals of South Africa who are residents of Mozambique (being in the same circumstances as the Mozambican mineworkers who are not nationals of South Africa and are also residents of Mozambique) are the basis of comparison.¹¹⁵

According to the OECD commentary on Article 24(1) the underlying question is whether two persons who are residents of the same State are being treated differently solely by reason of having a different nationality.

¹¹⁴ *ibid* footnote 110

¹¹⁵ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV:402 -403

As both the South African mineworkers and Mozambican mineworkers are residents of Mozambique, it is submitted that the South African mineworkers are treated differently solely by having a different nationality.

This is based on the fact that the 1964 labour agreement is only applicable to Mozambican mineworkers and the exemption on any direct taxes payable in South Africa is only available to the Mozambican mineworkers. In giving relief from any direct taxes to the Mozambican mineworkers, South Africa distinguishes between its own nationals resident in Mozambique and the Mozambican mineworkers resident in Mozambique. The same treatment is therefore not afforded to its nationals that reside in Mozambique.

This would amount to discrimination against the South African mineworkers that are resident in Mozambique unless South Africa extend to the South African mineworkers the same treatment afforded to the Mozambican mineworkers.

It further stipulates that Article 24(1) is not restricted to nationals who are solely residents of a Contracting State, but on the contrary, extends to all nationals of each Contracting State, whether or not they be residents of one of them. In other words, all nationals of a Contracting State are entitled to invoke the benefit of this provision as against the other Contracting State. This holds well, in particular, for nationals of the Contracting States who are not residents of either of them but of a third State.¹¹⁶

This can be applied to mineworkers from the BLS (Botswana, Lesotho & Swaziland) or any other mineworker which is a national of their State of origin but is resident in Mozambique. These mineworkers are therefore entitled to invoke the discrimination clause in Article 24(1) against the other Contracting State which is South Africa. Unless the same treatment is afforded to these mineworkers by South Africa as stipulated in the 1964 labour agreement, this would amount to discrimination against the mineworkers resident in Mozambique.

¹¹⁶ Holmes, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV:402 -403

8. Conclusion

The 1964 labour agreement between South Africa and Portugal is quite unique in a sense that the income received by the Mozambican mineworkers are exempt from tax in South Africa for the duration of the contract (usually up to maximum of 18 months) entered into by the Mozambican mineworkers and their South African employers although the source of the income is in South Africa.

‘The DTC between South Africa and Mozambique cannot impose tax where the income is not subject to tax under domestic legislation. As a result, even where a treaty does give South Africa the right to tax the income from the Mozambique workers in respect of employment in South Africa the exemption provided for in domestic law renders this right ineffective.’¹¹⁷

There would be a revenue loss to South Africa in respect of the Mozambican mineworkers that regularly renew their contracts as they will make use of the exemption provision in the 1964 labour agreement. In most cases these workers will be earning a salary that is above the annual tax threshold. In respect of the Mozambican mineworkers that entered into contracts for the first time there would be no revenue loss to South Africa as their earnings in most cases would not be above the annual tax threshold.

In the event that there is double taxation as a result of the 1964 labour agreement between the two countries the tax sparing clause makes provision that the tax residents of each country could benefit from this provision should each country have reductions or exemptions for foreign investors. The 1964 labour agreement is seen as a scheme for the promotion of economic development for both South Africa and Mozambique and the tax sparing clause can be applied to both countries. This may lead to double non-taxation of the South African source income in both countries.

Article 4(3)(b) of the MoU stipulates that member states of the SADC will endeavour to avoid ‘introducing tax legislation that prejudices another Member State’s economic policies, activities, or the regional mobility of goods, services, capital or labour. It is clear that article 4(3)(b) refers to the

¹¹⁷ Oliver, L., and Honiball, M. 2011. *International Tax: A South African Perspective*. Cape Town: Siber Ink: 441 - 460

harmful effects of tax competition'. It is submitted that the 1964 agreement which is given effect in terms of section 10(1)(c)(v) of the Act, prejudices the other Member States within the SADC region.

Mineworkers from Mozambique will prefer to apply their services in the mining sector of South Africa due to the favourable position of their income being exempt from income tax for the duration of their contract. They would not in all likelihood apply their services in other Member States of the SADC region where their income would be taxed. The other Member States suffer a significant detriment as a result thereof and would be prejudiced. In this instance there will be harmful tax competition.

The 'ring-fencing' of a regime from the domestic economy in favour of non-resident taxpayers is often a clear indication that a country is engaged in harmful tax competition. Taxpayers that are incorporated into the regime enjoy the benefit of the infrastructure of the country providing the preferential tax regime, without necessarily incurring the cost of the infrastructure. This can be applied to the 1964 agreement. The agreement can be classified as 'regimes that restrict the benefits to non-resident taxpayers',¹¹⁸ which in this instance is the Mozambican mineworkers. This kind of ring-fencing is included in article 4(3)(a) of the MoU. The effect of ring-fencing is that taxpayers are relieved from the burden of paying taxes (usually at a relatively high rate) in the country of residence.¹¹⁹ In this instance the income of the Mozambican mineworkers is exempt from income tax for the duration of their contracts.

The 1964 bilateral labour agreement between South Africa and Mozambique appears to be in default of Article 21 and 22 of the SADC treaty which seeks co-operation of Member States in taxation matters and to harmonise the tax regimes in the SADC region. There is no uniform agreement on matters of tax incentives to particular taxpayers in the SADC Member States. This is due to the tax incentives provided to the Mozambican mineworkers. In terms of sub - article 3(a) of article 4 of the MoU this is evidence of harmful tax competition.

On the other hand it should be noted that the main objective of the SADC treaty is to seek regional integration of Member States in Southern Africa especially the poorest members like Mozambique. In some way the 1964 labour agreement between South Africa and Portugal goes a long way in

¹¹⁸ Organisation for Economic Cooperation and Development ("OECD"). 1998. *Harmful Tax Competition: An Emerging Global Issue*. [Online]. Available. <http://www.oecd.org/dataoecd/33/0/1904176.pdf> [22 June 2011]

¹¹⁹ Legwaila, T. 2010. *The Suitability of the South African Corporate Tax Regime for the Use of South African Resident Intermediary Holding Companies*. [Online]. Available: <http://upetd.up.ac.za/thesis/available/etd-05222010-170510/unrestricted/00front.pdf> [24

achieving that objective as it would help attract investment in Mozambique which will have a significant impact on the Mozambican economy.

Article 24(1) of the OECD MTC is identical to Article 23(1) of the DTC between South Africa and Mozambique on non-discrimination of nationals. The Mozambican workers do not carry a heavier tax burden than the South African nationals due to no taxes being levied by South Africa for a maximum of 18 months. The non-discrimination article therefore does not apply. There would be no discrimination between mineworkers from Swaziland, Botswana and Lesotho and mineworkers from Mozambique. The tax liability of mineworkers from these states is also not more burdensome than that of the South African mineworkers in the same position. There would be discrimination against the South African mineworkers that are resident in Mozambique as the 1964 labour agreement only refers to Mozambican mineworkers.

It is submitted that the 1964 labour agreement will fall short on the unconstitutional aspects of the Constitution of the Republic of South Africa of 1996. As stated previously the Bill of Rights applies to Mozambican mineworkers that are resident in South Africa. The unconstitutional aspects relates to the compulsory deferred pay which compels the workers to defer 60% of net earnings to a central bank of Mozambique and exemption from taxes in South Africa compared to South African workers in general. The agreement raises the question of discrimination as envisaged in section 9 of the Bill of Rights which contains the provisions of equality.

It is submitted that SARS should provide a clear interpretation of the 1964 labour agreement. This is important as it would give a clear indication whether the Mozambican mineworkers that regularly renew their employment contracts can make use of the exemption of taxes provision in this agreement. Due to the current BEPS environment worldwide this would even become more important as the revenue loss to South Africa would become more substantial in the long run.

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