

August 31, 2021

Decrypting the risks of ETI Schemes for B-BBEE Skills Development



Employee Tax Incentive (ETI) schemes advertised for purposes of addressing Skills Development and Preferential Procurement[1] on the B-BBEE scorecard are becoming increasingly prevalent.

Are these schemes legal and what are the possible pitfalls that an entity should be aware of before deciding to participate in such a scheme?

In this blog we take an in-depth look into the workings of an abusive ETI scheme and the risks that businesses may be faced with when participating in these schemes.

What is the Employment Tax Incentive programme?

The ETI is an incentive aimed at encouraging employers to hire young work seekers. Employers who participate in this programme will reduce their cost of hiring young people by reducing the amount of Pay-As-You-Earn (PAYE) that they must pay over to SARS, while leaving the wage or salary received by the employee unaffected.

The Employment Tax Incentive Act, 26 of 2013 sets out the requirements for this incentive. However, these requirements fall outside the scope of this article.

The general working of an abusive ETI scheme marketed to entities

There are various ETI schemes in the market. There is not one template used by all the schemes, although these schemes are all marketed under the banner of “gaining financial and B-BBEE benefits”. All the schemes have certain common practices, which can be summarised as follows:

The schemes place a strong emphasis on the legality of an employer’s ETI claim by relying on the definition of remuneration and the justifiable grounds for concluding a fixed-term contract with a potential employee.^[2]

The role players

The **author of the scheme** is the company that approaches other entities (the **employers**) and which recruits young people (the **employees**) to participate in the scheme.

The **employers** are entities covering a broad spectrum of sectors and sizes ranging from multi-national entities to SMMEs. The employer is also the entity that signs a 12-month fixed-term employment contract with the employee.

The **employees** are unemployed South African-born individuals between 18 and 30 years of age and must come from a previously disadvantage background.

The **service provider** is the entity tasked with facilitating the training. In some instances, the service provider and the author of the scheme are the same entity. All schemes claim that their training courses are accredited by the Sector Education and Training Authority (SETA). Some schemes are focused on learnerships, while others offer a 12-month structured bursary or skills programme.

Most of the schemes introduce another entity into the mix. This entity can be described as a host employer (hereinafter referred to as the “**contracting entity**”) as the employees of the employer are subcontracted to this entity.

How these schemes typically operate

The author of the scheme advertises fully paid training courses, with employment offered to individuals who match the scheme’s criteria.

At the same time, the author approaches employers and offer them financial and B-BBEE benefits should they become part of the scheme. The scheme mostly promises recognised Skills Development expenditure at no or limited costs to the employer.

The author of the scheme calculates the number of individuals that an employer must employ to meet the employer’s B-BBEE targets while still benefiting financially from the scheme.

The employer then employs the suggested number of individuals as employees on a 12-month fixed term contract. The employees are placed with the contracting entity or the author of the scheme and never set foot on the premises of the employer and are entirely unknown to the employer. Employees are paid a salary of between R2 000 and R6 000 per month by the employer.

The employer receives a monthly invoice from the service provider or author of the scheme (where the service provider and author of the scheme are the same entity). The invoice indicates the amount to be paid for the training that the employees of the employer receive. The money to be paid is in fact the monthly remuneration of the employees, which is ceded by the employees to the service provider/author of the scheme for their tuition fees.

In exchange for the payment, the author and administrator of the scheme provides the employer with payslips as well as all other relevant pay-roll documentation (Payroll/SDL/UIF reports, etc.). This documentation allows the employer to claim ETI monthly from SARS.

Where the employees are subcontracted to a contracting entity, the employer will provide a counter invoice to the author of the scheme for the labour / student placement. In some instances, the author of the scheme approves a monthly refund/reversal of a certain portion of the amount paid by the employer. The basis of the refund/reversal is unknown.

Where the service provider and author of the scheme are not the same entity, the author of the scheme will also provide an invoice to the employer. This fee is normally dressed up as an administration, recruitment or B-BBEE fee for implementing and administering the scheme or structure, as it is more commonly referred to.

At BEE verification, the author of the scheme and/or service provider provides all the documentation required by the employer to prove their claim under Skills Development. Employees are also coached by the author of the scheme regarding their answers to a verification agent's questions when interviewed for Employment Equity and/or Skills Development.

What are the risks faced with when participating in an ETI scheme?

Firstly, it is important to note that all the relevant documentation needed to claim the monthly ETI from SARS, as well as all the documentation required for verification, can be provided by the employer. The author of the scheme makes sure of this. It is the documents that are omitted by the employer that disguise the true nature of the scheme, i.e. the counter invoice or refund/reversal in certain instances, the document confirming the cession of an employee's salary, etc.

The monthly payments to an employee are disguised as two different things depending on the legislation applicable. For B-BBEE purposes, employers claim their employees' monthly salary as Skills Development expenditure, and they use the invoice received from the service provider, together with their payment of the invoice, to support this claim. The payment to the service provider is in fact the employee's monthly salary, or a portion thereof, which is ceded to the service provider as tuition fees in terms of the employee's employment contract. The employees, not the employer, therefore pay the tuition fees. The employer consequently has no claim in terms of Skills Development expenditure. From an ETI perspective, the employer claims the same amount that he unlawfully claims as Skills Development expenditure, now as a monthly salary in order to qualify for the ETI incentive. One payment cannot be two different things depending on how the wind blows.

In instances where the training that an employee received is a learnership, the scheme opens itself to double dipping, which is not allowed in terms of B-BBEE legislation.^[3]

The training courses on offer through these ETI schemes are all basic NQF[4] level 1 – 4 training courses, such as NC: New Venture Creation[5] and a certificate in Hygiene and Cleaning,[6] to name but a few. The contents of these courses are very basic, and it is not clear how an individual who achieves a qualification in one of these training courses will, by completing the course alone, be able to find a decent job that provides a sustainable income. Most of the training courses on offer do not constitute a decent contribution to Skills Development and the B-BBEE objectives listed thereunder.

The skills transferred in terms of “work readiness” training that the employees receive under an ETI scheme is questionable. In most instances, these employees are further outsourced to entities as sales reps to sell insurance products, funeral policies or airtime. The employees are completely reliant on themselves and their ability to sell the contracting entity’s products. It is therefore highly doubtful whether the employee is trained or receives the necessary work experience to enter a decent job or profession. From an ETI perspective, it is highly unlikely that this type of operation serves as justifiable grounds for a fixed -term employment contract, one of the requirements to qualify for the ETI.

The ETI schemes all pitch a monthly incentive of R1 000 per employee. There is a risk to this approach as the value of the ETI that an employer can claim depends on the value of the monthly remuneration paid to an employee. The hours that an employee works during a month also plays a role and because the employees are not working at the premises of the employer, the employer must blindly accept the information they are being provided by the author of the scheme. No due diligence can take place on the side of the employer to make sure that the correct amount is claimed for ETI purposes

The number of students that the authors of these schemes advise employers to take up is always very high and, in most cases, more than the current workforce of the employer. As these employees are outsourced, the employer runs the risk of changing the nature of their business from whatever it is that they are doing, to that of a labour broker. This has consequences on various levels for an employer, some of which relate to the B-BBEE Codes applicable to the verification of the employer.

Vast numbers of young people trained through the ETI schemes, with the limited number of basic courses provided by the service providers, flood the business market and render the education received by the employees “cheap” and worthless to some degree.

The authors of these schemes all claim to have legal opinions from advocates and other legal practitioners which confirm the legality of their operations. The problem is that all the paperwork can be provided, whether it is requested for the ETI programme or whether it is requested for B-BBEE. When one compartmentalises the different areas of the scheme, it all looks legit, but if you put everything together and compare it with the spirit in which the scheme operates and you look at it from a social justice point of view, the picture suddenly changes.

Conclusion

The ETI schemes described above are currently being used as a means to achieve another purpose – for an employer to generate a monthly income stream by way of the ETI programme while *earning points on the Skills Development B-BBEE scorecard* without spending any of the employer's own money.

Although the B-BBEE Commission has been silent on these practices and the impact they have on achieving the Skills Development goals set out in the B-BBEE Codes, SARS and National Treasury have taken a stance in curbing the abuse of the ETI programme. The 2021 Budget Review proposed amendments to the definition of “employee” in the ETI Act. As a result, the proposed amendments have been included in the Draft Taxation Laws Amendment Bill that was published for public comment. The proposed amendments suggest that the substance over legal form must be considered when an employer's claim for ETI is assessed. The amendments also propose that the changes must be applied retrospectively as from 1 March 2021. As a further elaboration, SARS made a tax ruling in a private matter which excludes any student from the definition of an “employee” in terms of the ETI Act. The private ruling^[7] then went on to confirm that an employer is not entitled to claim ETI in respect of any of the students enrolled in ETI schemes that operate on the basis described earlier in this article. Although the ruling is only binding between SARS and the parties involved in the application, the ruling was published for general information, which is an indication, and maybe even a warning, to other parties that engage in the same type of practices.

The question an employer must therefore ask themselves when they are confronted by marketers of these type of schemes is whether the reward is worth the risk.

*SERR Synergy assist businesses with the development and implementation of B-BBEE strategies by taking all the B-BBEE scorecard elements into consideration. We have compiled a very unique training product that focuses on Fourth Industrial Revolution (4IR) skills whereby businesses can benefit from various **training and skills development programmes**.*

About the Author: Danel Gous is a Law graduate from the University of Potchefstroom for Christian Higher Education. She also obtained her Master's Degree in Import and Export Law at the North-West University, Potchefstroom. Danel is an admitted High Court attorney, conveyancer and notary with more than ten years legal practice experience. She joined SERR Synergy's B-BBEE Department in 2016 where she currently holds the position of Senior Project Manager.

[1] There are certain risks that an entity that participates in an ETI scheme faces in terms of Preferential Procurement as B-BBEE element, but this article will only focus on the risk in terms of the ETI Act and Skills Development as B-BBEE element.

[2] The following is of importance: (i) Remuneration is widely defined in paragraph 1 of the Fourth Schedule to the Income Tax Act, 58 of 1962, to include all payments and amounts payable, in cash or otherwise, whether or not for services rendered and includes salaries, wages, leave pay, bonuses, gratuities, commission, overtime pay and other amounts paid for services rendered as well as allowances and advances; and (ii) Section 198B (4) of the Amended Labour Relations Act, 66 of 1995 stating: "*Without limiting the generality of subsection (3), the conclusion of a fixed term contract will be justified if the employee-...(c) is a **student or recent graduate who is employed for the purpose of being trained or gaining work experience in order to enter a job or profession.***" (own emphasis).

[3] The employer can provide the correct paperwork to claim the Skills Development expenditure (the ceded salary in the form of the service provider's invoice), as well as the salary itself as captured on an employer's payroll. It is in fact the same thing dressed up differently by way of providing different documentation. One cannot determine by looking at the paperwork alone that it refers to the same thing.

[4] NQF stands for National Qualification Framework and is defined as *“the system that records the credits assigned to each level of learning achievement in a formal way to ensure that the skills and knowledge that have been learnt are recognised throughout the country”*. The NQF consists of 10 levels. Level 1 – 4 equate to grade 9 to 12 or vocational training (high school grades). Levels 5 to 7 are college diplomas and technical qualifications, and levels 8 to 10 are university degrees.

[5] NQF level 2 qualification.

[6] NQF level 1 qualification.

[7] Binding Private Ruling: BPR 367

©SERR Synergy, www.serr.co.za