REPORT NO. 694

REVIEW OF REBATE ITEM 311.18/63.09/01.04 ("WIPING RAGS REBATE")

The International Trade Administration Commission of South Africa herewith presents **Report No. 694: Review of rebate item 311.18/63.09/01.04 ("wiping rags rebate")**

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AYABONGA CAWE

CHIEF COMMISSIONER

PRETORIA

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GLOSSARY – LIST OF ACRONYMS

Acronym	Description
AfCFTA	African Continental Free Trade Area
EFTA	European Free Trade Agreement
EU	European Union
FOB	Free-On-Board
GATT	General Agreement on Tariffs and Trade
ITAC	The International Trade Administration Commission of South Africa
Mercosur	Common Market of the South
R-CTFL	Retail, Clothing, Textiles, Leather and Footwear
SACU	Southern African Customs Union
SADC	Southern African Development Community
SARS	South African Revenue Service
Stats SA	Statistics South Africa
The Directive	Policy Directive
The dtic	The Department of Trade, Industry and Competition
The Minister	The Minister of Trade, Industry and Competition
WTO	World Trade Organisation

REPUBLIC OF SOUTH AFRICA

INTERNATIONAL TRADE ADMINISTRATION COMMISSION OF SOUTH AFRICA

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REVIEW OF REBATE ITEM 311.18/63.09/01.04 (“WIPING RAGS REBATE”)

Synopsis

The International Trade Administration Commission of South Africa (the “Commission” or “ITAC”) received a policy directive (the “Directive”) from the Minister of Trade, Industry and Competition (the “Minister”) to review, amongst others, rebate item 311.18/63.09/01.04 as part of the implementation of the Retail-Clothing, Textile, Footwear, Leather (“R-CTFL”) Masterplan, where one of the Four Key Action Points under Commitment 4 of this Masterplan, is to review the rebate provisions with regard to the importation of second-hand clothing. The Directive was also based on concerns which were raised by the Intergovernmental Illicit Economy Trade Task Team, about the potential abuse and/or misuse of the aforementioned rebate item, its contribution to illicit trade and the detrimental and negative effect this may have on the domestic clothing and textile industry and the fact that this rebate provision has not been reviewed for an extended period of time.

During its deliberations and in arriving at its recommendation, the Commission considered the information at its disposal, including comments received during the investigation period as well as oral representations.

The Commission found that:

a) Despite many attempts by ITAC, the South African Revenue Service (“SARS”) and industry to design better conditions and safeguards for this rebate over the years, and efforts by ITAC and SARS to monitor this rebate item, it continues to be abused and mis-used by some firms. However, there are legitimate importers who are running *bona fide* businesses and are compliant with regulations and rebate permit conditions.

b) From an industrial policy point of view, the risk is that second hand clothing (and perhaps even new clothing) finds its way into the South African market, using this rebate item, which has a detrimental effect on the local CTFL manufacturing and retail sectors. Furthermore, illegal imports of second hand and worn clothing also threaten to undermine the objectives of the R-CTFL Masterplan and the nearly 70 000 new manufacturing jobs which the plan seeks to create. Such illegal imports put massive pressure on manufacturers and jobs by distorting prices to levels against which legitimate manufacturers cannot compete.

c) From an administrative point of view, the subject rebate item creates an administrative burden for SARS and ITAC as the goods are imported in compressed bales, making it very difficult to verify what type of products are actually imported. For instance, the outer part of the bales may contain appropriate worn clothing suitable for manufacturing wiping rags but other impermissible clothing is hidden in the middle. Even if the illicit goods are detained or seized by Customs, the only inevitable result is storage costs. Should the rebate item be maintained, SARS proposes additional control measures such as having importers code printed on outer bales on all sides, that garments must be de-faced prior to baling, that collars, buttons and accessories must be removed and garment cut in half, etc.

d) Second hand/used clothing can be sourced within the Republic. The dtic has a number of projects currently under way to support the circular economy and avoid confiscated or seized clothing being dumped in landfill sites but to rather use it in the economy as raw material for manufacturers of various products such as wiping rags, cleaning cloths, insolation, stuffing, animal blankets, etc. Therefore, alternative arrangements should be made for those *bona fide* manufacturers of wiping rags and cleaning cloths to make use of local waste material that is suitable for their needs.

e) Regarding the Republic of Botswana, the Kingdom of Eswatini, the Kingdom of Lesotho and the Republic of Namibia ("BELN") countries, import statistics obtained from the South African Revenue Service ("SARS") show that these countries export appreciable volumes of already "cut-up rags" to South Africa under HS 6310.90. This points to the need for tighter boarder control, policing and monitoring of used clothing and already cut-up rags from the BELN countries.

f) There is a disparity and mismatch in the level of imports of worn clothing under tariff heading 63.09 recorded by SARS into South Africa and exports from foreign suppliers.

Imports of second hand clothing recorded by SARS are significantly higher than exports of second hand clothing recorded by foreign suppliers, thus corroborating comments from stakeholders that the subject rebate item is possibly being used as a conduit to import other types of clothing (including new clothing). This, together with other considerations, suggests that the costs associated with the subject rebate item may very well outweigh the associated benefits.

The Commission concluded that the facts submitted support a strong case that the rebate provision concerned requires termination in the very near future and not over an extended period. A two-year phase out period for rebate item 311.18/63.09/01.04 to the Customs and Excise Act, 1964 (Act No. 91 of 1964) is deemed reasonable. Although, a phase-down of one year might actually be warranted, two years will allow businesses time to repurpose.

In light of the foregoing, the Commission recommended the following:

a) Maintain rebate item 311.18/63.09/01.04 (“wiping rags rebate”) and phase it out over the next 2 years to allow the industry to re-purpose their operations over this period of time to avoid immediate job losses.
b) A 2-year phase-out period for the rebate item be effective from the date of implementation by SARS through a publication in the Government Gazette.
c) The proposed amended guidelines, rules and conditions for rebate item 311.18/63.09/01.04, which would be applicable during the phasing out period be confirmed through a publication in the Government Gazette.

2. BACKGROUND

Directive to review rebate item 311.18/63.09/01.04 ("wiping rags rebate")

2.1. The Minister ITAC in terms of Section 16(1)(d)(i) of the International Trade Administration Act, No. 71 of 2002 to conduct a review of, amongst others, rebate item 311.18/63.09/01.04 ("wiping rags rebate") to the Customs and Excise Act, No.91 of 1964 ('the Customs and Excise Act').

2.2. As indicated by the Minister, this Directive followed concerns which were raised by the Intergovernmental Illicit Economy Trade Task Team, about the potential abuse and/or misuse of the aforementioned rebate item, its contribution to illicit trade and the detrimental effect this may have on the domestic clothing and textile industry. It was further considered that the subject rebate item has not recently been reviewed.

2.3. In addition, one of the Four Key Action Points under Commitment 4 of the R-CTFL Masterplan, is to review the rebate provision with regard to the importation of second-hand clothing.

2.4. The Department of Trade, Industry and Competition ("**the dtic**") participates in the Intergovernmental Illicit Economy Trade Task Team together with ITAC, SARS and National Treasury ("NT"). The Task Team focuses on practical actions to combat illicit trade in a range of products including metals, gold, tobacco, clothing, textiles and footwear.

2.5. The Directive was published as Notice 625 of 2021 in *Government Gazette* Number 45352, on 22 October 2021, for interested parties to comment. Due to the limited comments received, the Commission decided that stakeholders should be afforded a second opportunity to comment through a second publication notice, being Notice 841 of 2022 in *Government Gazette* Number 45930, on 18 February 2022, which notice served to highlight and clarify the various possible outcomes of the review.

3. REBATE ITEM - TARIFF POSITION & PRODUCT DESCRIPTION

3.1. Section 75 of the Customs and Excise Act, read with Schedule 3, provides that certain imported goods that are subject to customs duties may benefit from a rebate against those duties.

3.2. In terms of the Import Control Regulations, second-hand or used goods (including worn clothing) may not be imported except under an import permit issued in terms of Section 6 of the ITA Act.

3.3. ITAC administers numerous rebate items, including the second hand clothing-related rebate item – the “wiping rags rebate”. Imports under this rebate item are subject to import control and rebate permits issued by ITAC.

3.4. The current tariff structure for worn clothing is depicted in Table 1 below. Worn clothing used for the manufacture of wiping rags is classifiable under tariff subheading 6309.00.17. The tariff subheading currently attracts an ordinary customs duty of 60 per cent *ad valorem* or R25 per kilogram under General, European Union/United Kingdom (“EU/UK”), the European Free Trade Association (“ETFA”), the Southern African Development Community (“SADC”), Mercosur and the African Continental Free Trade Area (“AfCFTA”) columns.

Table 1: Current tariff position of worn clothing

Tariff heading	**Tariff sub heading**	**Description**	**Statistical unit**	**Rate of duty**					
				General	EU/UK	EFTA	SADC	Mercosur	AfCFTA
63.09	6309.00.17	Other worn clothing	Kg	60% or 2500c/kg	60% or 2500c/kg	60% or 2500c/kg	60% or 2500c/kg	60% or 2500c/kg	60% or 2500c/kg

Source: SARS

3.5. The details of the rebate item under review are depicted in Table 2 below.

Table 2: Details of the rebate item under review

	'Wiping rags rebate'
Rebate item	311.18/63.09/01.04 in Schedule 3, Part 1 to the Customs and Excise Act, 1964
Implemented	15 April 1990
Rebate detail	"Worn clothing and other worn articles of textile materials containing 35 per cent or more by mass of cotton fibres (excluding brassieres, girdles, corsets, braces, suspenders, garters, jackets, blazers, jerseys, pullovers, cardigans, overcoats, car-coats, raincoats, anoraks, ski-jackets, duffle-coats, mantles, parkas, swimwear, socks and similar clothing articles) at such times, in such quantities and subject to such conditions as the International Trade Administration Commission may allow by specific permit for the manufacture of wiping rags and cleaning cloths".
Product	Wiping rags and cleaning cloths are manufactured from the duty-rebated imports of worn clothing with a cotton content exceeding 35%. These rags and cloths are used in the mining, printing, construction, service, transport, retail, furniture, oil and engineering industries, as well as government institutions.
Purpose	To afford employment creation and support the industry manufacturing wiping rags and cleaning cloths by increasing its competitiveness *vis-à-vis* imported goods through the lowering of production costs.
Extent of Rebate	Full rebate of customs duty on worn clothing and worn textiles with a cotton content exceeding 35% - the main inputs for manufacturing wiping rags and cleaning cloths. **NB:** The rebate is subject to quantity control by linking it to an applicant's production capacity. This is vital since there is a danger that any excess quantity that is imported and not used in the manufacturing process will enter the domestic clothing market, thereby achieving the very negative impact that the rebated import duty seeks to avoid in the first place.
Participation in rebate	In 2015, 22 firms were issued with wiping rags rebate permits with a total volume of 27 269 300 kg. In 2021, 32 firms participated under the rebate system with rebate permits issued to the tune of 23 983 333 kg worth of worn clothing.
Permit validity period	12 months or less from date of issue of permit

Source: ITAC

4. POLICY CONSIDERATIONS

4.1. In terms of the relevant provisions of the ITA Act, the Commission has broad discretion to grant, amend, revoke or refuse an import permit. ITAC will generally not grant an import permit for second-hand or used goods, particularly for clothing. This is so because South Africa, as a general policy stance, is of the view that the importation of used goods should be limited. This is done to protect the domestic clothing manufacturing industry from an influx of imported, cheap second-hand clothing. It assists in preserving, stimulating and encouraging the expansion of the domestic industry, and preserving and creating much needed employment therein.

4.2. ITAC, accordingly, will generally not issue an import permit for the importation of second-hand clothing, except if it is for a specific and circumscribed purpose that the executive arm of Government has carved out (in terms of the rebate) and if the facts considered by ITAC support the issuing of a such a permit.

5. PERMIT CONDITIONS AND EVIDENCE OF MISUSE AND/OR ABUSE

5.1. Where goods are subject to import control and are to be imported under rebate, ITAC requires that a rebate permit be sought first and thereafter an import permit. ITAC spends a considerable amount of time, energy and resources investigating whether a particular applicant qualifies for a rebate permit and, if so, on what terms and conditions.

5.2. Rebate and import permits are only issued for a limited duration (12 months or less) – i.e. so that an importer is required to submit regular applications for the rebate and, on each occasion, to satisfy ITAC that granting the rebate would achieve the objective of the rebate at that point in time. During this process, applicants who received previous rebate permits also have to demonstrate their compliance with all of the Customs and Excise Act rules, guidelines and permit conditions. In other words, the applicant must demonstrate that its previous permit was used strictly for the purpose for which it was granted.

5.3. The rebate item concerned are subject to conditions to ensure that their respective objectives are achieved. One important condition is proper record keeping of imported goods. It requires permit holders to keep various verifiable records (such as import volumes, production and sales volumes etc.) to allow ITAC to monitor the use of this rebate item.

5.4. In order to ensure compliance with the permit conditions, ITAC conducts periodic verifications of permit holders. ITAC verifications, which were conducted during the period 2013-2018, with the aim of establishing the level of compliance of permit holders, have found that substandard recordkeeping is prevalent amongst holders of permits for wiping rags.

5.5. Information obtained through verifications indicated that transgressions included, amongst others, the transfer of the benefits of permits to persons or entities not named in the permits and the importation of other items/clothing under rebate, which are not suitable for the manufacture of wiping rags.

5.6. ITAC exposed additional misuse of permits during these verifications, such as –

a) **Mis-declaration of imported goods**
ITAC investigated numerous cases of mis-declaration where unsuitable worn or new clothing items were imported under the wiping rags rebate. Articles described as track suits, sweat shirts, denim, sleepwear, plain blouses, skirts and sweaters have also been found in imported consignments under this rebate item.

b) **Fraudulent documentation**
ITAC found that applicants have submitted forged permits to SARS to clear consignments of worn clothing.

6. MARKET AND TRADE ANALYSIS

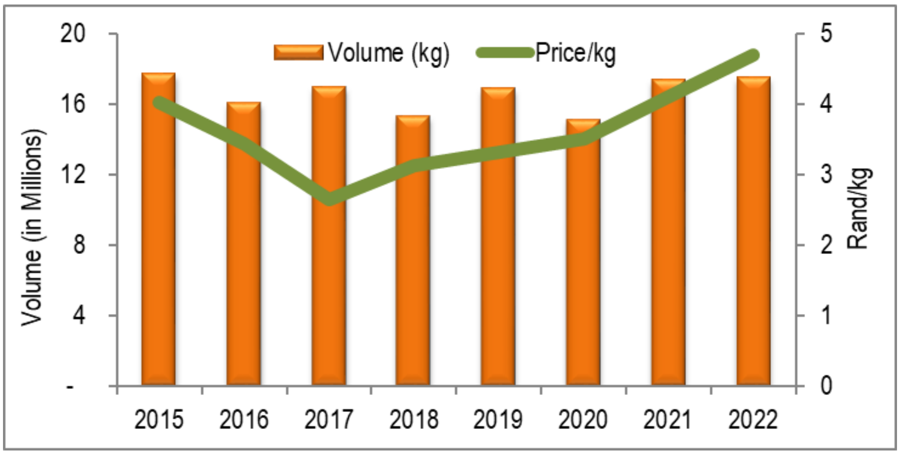
6.1. In 2020, 24 firms participated under the wiping rags rebate provision with a total volume of imported worn clothing amounting to 15 059 909 kg to the value of R52.8 million and at an average F.O.B price of R3.5/kg. In 2022, import volumes increased to 17 528 253 kg with a total value of R82.3 million. The top five (5) importers under the wiping rags rebate accounted for 63% of total import volumes at an average import price of R4.64/kg. Further analysis of import data shows that the majority of imports of worn clothing originate from Pakistan, followed by the Netherlands and the United Arab Emirates ("UAE"), collectively accounting for 70% of total imports in 2022.

6.2. Imports under rebate item 311.18/63.09/01.04 are only subject to quantity control measures by linking imports to an applicant's production capacity, which is determined by the number of cutting machines and employees.

6.3. According to import statistics obtained from SARS, import volumes have been relatively stable over the period 2015-2022, fluctuating between 15 and 17 million kilograms. Imports originated mainly from Pakistan, the Netherlands, the UAE, the United States of America ("USA") and Italy, in that order. These aforementioned countries accounted for an average of approximately 80% of the subject imports during the period 2015-2022. It should be noted that Pakistan only accounted for less than 10% in 2012 while UAE accounted for 0% of total imports. However, by 2022, imports from Pakistan accounted for 29% while imports from the UAE accounted for almost 23% of all imports.

6.4. In terms of prices, Figure 1 below indicated that FOB prices of worn clothing used for the manufacture of wiping rags have been trending upwards since 2017, with prices increasing, on average, by 78% between 2017 and 2022. This may partly be attributed to a weaker Rand/Dollar exchange rate over the period concerned.

Figure 1: Import trends of wiping rags



Source: SARS Trade Statistics

6.5. A closer look at the import statistics indicates an anomaly in the volume of imports of worn clothing under tariff heading 63.09 recorded by SARS compared to the volume of exports from foreign suppliers. According to trade statistics obtained from SARS, South Africa imported 5 400 521 kg worth of worn clothing in 2020 from Pakistan. However, trade data from TradeMap indicates that Pakistan only exported 900 000 kg to South Africa. Similarly, SARS statistics shows that South Africa imported 1 220 753 kg of worn clothing from the USA while TradeMap data shows that the USA only exported 264 000 kg in 2020. With respect to the UAE, SARS data shows that South Africa imported 2 594 903 kg of worn clothing while TradeMap indicates that the UAE did not export any worn clothing to South Africa.

6.6. Wiping rags and cleaning cloths can be imported already cut, either sorted or unsorted and are classifiable under tariff subheadings 6310.10 (sorted rags) and 6310.90 (other). An examination of data on imports of already cut-up wiping rags and cleaning cloths classifiable under tariff subheading 6310.90, shows that these “imports” originate mainly from the Kingdoms of Lesotho (“Lesotho”) and Eswatini, and have accounted for approximately 95% of total imports over the period 2019-2021. It should be noted that “imports” from Lesotho accounted for less than 1% in 2010, but by 2021 accounted for close to 60% of total imports. On the other hand, imports of already cut-up wiping rags classifiable under tariff subheading 6310.10 originate mainly from Mozambique followed by Pakistan and Eswatini, collectively accounting for 93% of total import volumes. Similar to Lesotho, imports from Mozambique accounted for less than 1% of imports in 2010, but by 2021 accounted for approximately 61% of total imports.

6.7. Import data at the Commission’s disposal, indicated that already cut-up wiping rags classifiable under tariff subheading 6310.90 (unsorted) were imported into South Africa at an average FOB price of R1/kg from Lesotho and R2.52/kg from Eswatini during the period 2019-2021. On the other hand, already cut-up wiping rags classifiable under tariff subheading 6310.10 (sorted) were imported at an average FOB price of R7/kg from Mozambique, R4/kg from Pakistan and R1/kg from Eswatini, during the period 2019-2021.

6.8. Information at the Commission's disposal indicates that existing participating firms under the wiping rags rebate also import already cut-up wiping rags under tariff subheading 6310.10 (sorted). The risk or loophole this creates is that it makes it difficult for Customs and ITAC to distinguish wiping rags manufactured from imported worn clothing particularly if they get mixed with already cut-up wiping rags. As such, there is a high possibility that imported worn clothing could be removed to the rebate store without being cut into wiping rags and the volume replaced with already cut-up wiping rags. This may partly explain the proliferation of worn clothing in the local market.

7. COMMENTS RECEIVED: INITIAL PUBLICATION

7.1. ITAC developed a questionnaire to solicit input and data from interested parties on, *inter alia*, pricing, volume of imports, production and sales, as well as customer lists, employment and investment. This data was requested in order to understand, amongst others, the demand and supply conditions in the market and the financial position of the industry.

7.2. Requests for comments were sent to 24 firms participating under rebate item 311.18/63.09/01.04.

7.3. Comments were received from the following eight (8) firms that utilise the wiping rags rebate, namely:

a) Disclose All Trade and Invest (Pty) Ltd;
b) Lesclo International (Pty) Ltd;
c) Black Italia Trading Enterprise CC;
d) Ian Farrell Import and Export CC;
e) Multifibres (Pty) Ltd;
f) Sarkodie and Son Import and Export;
g) Fatty Saikou Import and Export (Pty) Ltd;
h) Mpili Mining & Logistics (Pty) Ltd.

COMMENTS RECEIVED FROM WIPING RAGS REBATE USERS

7.4. **Disclose All Trade and Invest (Pty) Ltd**, objected to the review on the basis that they are a small business and the Covid-19 pandemic has caused disruptions in trading conditions. It was submitted that the status quo be retained given that they managed to survive the difficulties posed by the two pandemic years.

7.5. **Lesclo International (Pty) Ltd** opposed the review and indicated that they have created employment and provided a valuable product at a cheaper price to consumers.

7.6. **Black Italia Trading Enterprise CC ("Black Italia")** opposed the review and indicated that South Africa and its customs area do not produce enough rag material to supply the demand, hence importing is the only viable option for local suppliers. Black Italia stated that they commenced full production in January 2020 and produced for three months before the pandemic and lock down commenced.

Black Italia indicated that it employs permanent and part-time employees. It submitted that the removal of the rebate provision will result in an increase in the cost of importing as well as overhead costs and this will result in the business being unprofitable or ceasing to exist all together. Black Italia further stated their business is fairly new and are yet to break-even in their two years of active production, subsequently increasing the tariff or withdrawal of the rebate on imported used clothing will be detrimental to their success.

7.7. **Ian Farrell Import and Export CC**, neither supports nor opposes the review, on the basis that the request for the review is from a high authority, which is trying to eliminate illegal trade in worn clothing. It submitted that ITAC has a good system of controls in place regarding the rebate facility. However, should ITAC decide to withdraw the rebate item, which provides for the importation of worn clothes to be cut into rags and cleaning cloths, it will have to continue supplying the rags and cloths by importing finished products. This will result in a high rate of unemployment.

7.8. Ian Farrell Import and Export CC stated that the problem lies with SARS not being able to police the products coming in from SA's neighbouring countries. They also raised their concern based on high shipping costs, which are as great as or even greater for some products than the cost of input materials. They stated that the availability of raw material is subject to supply and demand. Prices for raw material have increased by 25% for 2021, as a result of freight rate increases. However, they stated that should freight costs decrease, they anticipate a decrease in cleaning cloth prices going forward.

7.9. **Multifibres (Pty) Ltd ("Multifibres")** opposed the review based on capital investment made, employment created, promotion of entrepreneurship, job retention and creation. They further indicated that South Africa requires more entrepreneurs to ensure real growth. Large companies and large corporates do not employ as many people but that it is small companies like Multifibres that employs more people.

7.10. **Sarkodie and Son Import and Export** supported the review in terms of retaining the wiping rags rebate, based on the opportunity provided by the Government to become an entrepreneur through the utilisation of the rebate item concerned and create employment.

7.11. **Mpili Mining & Logistics Pty Ltd ("Mpili")** is a family business that has been in operation for 9 years, and specializes in bond stores, customs and excise consultation as well as manufacturing textiles and supply of cleaning equipment and cleaning products thus providing diverse services to clients.

Mpili objected to the review as they are unclear on what the amendment of the tariff would entail due to the current economic climate and effects of the pandemic on businesses. Small manufacturing companies are in the process of recovering, and further restrictions to permits would cause further negative outcomes affecting the industry and increase unemployment.

7.12. **Fatty Saikou Import and export (Pty) Ltd**, neither supported nor objected to the review. However, it indicated that should the rebate be withdrawn there will be job losses.

COMMENTS FROM OTHER STAKEHOLDERS

COMMENTS FROM SACTWU

7.13. SACTWU represents workers in the clothing, textile and leather sectors nationally. It was submitted that these are important labour intensive sectors in the South African economy, employing large numbers of people – the majority of whom are women, and often sole breadwinners located in impoverished parts of the country.

7.14. SACTWU submitted that it has a history of participating in previous reviews and amendments of the subject rebate item and has had concerns for many years. SACTWU remains concerned due to suspected high levels of abuse of this rebate, and given this problem and its disastrous impact on industrialisation and jobs, submitted that this rebate item must be withdrawn.

7.15. In its motivation, SACTWU submitted that at a high level, the kinds of abuse which are likely to occur with imports under this rebate item include, at a minimum, the following:

a) Many garments imported under the wiping rags rebate item 311.18/63.09/01.04 are not further processed into wiping rags and cleaning cloths but are rather sold into the informal and formal wholesale and retail market as second hand clothing, and may even be sold as new clothes.

7.16. SACTWU further submitted that its members regularly and continuously complain about the ubiquitous sale of second hand clothing into the market. Such clothing is openly and widely sold in informal settings like street corners, roadsides and informal markets across the length and breadth of the country, and even in more formal settings like stores and online. It was submitted that, for instance, it is an open secret that all manner of second hand clothing is sold in vast quantities on the streets of Johannesburg central and Marabastad. At various times the industry has complained to SARS about these markets but they continue unabated.

7.17. SACTWU submitted that the illegal trade of second hand clothing has even mushroomed online, on sites like Facebook, Instagram and Gumtree where businesses advertise the sale of bales of imported second hand clothing. The following examples were mentioned:

a) A vendor on Facebook, which calls itself 'Imported Bales', openly offers consumers a vast array of other clothing such as men's t-shirts, ladies t-shirts, children's t-shirts, shirts, hoodies, socks, belts, dresses, blouses, skirts, shorts, tracksuits, leggings, jeans, underwear and footwear which it claims are second-hand clothing imported from places like Canada, Lithuania, the UK, Italy, and Belgium.

b) Large numbers of other vendors of second hand clothing can be easily found on Facebook Marketplace. In some cases, the imported second hand bales have even been sorted so that re-sellers can specialise in re-selling particular brands like H&M, Zara, Cotton On, and Mango.

7.18. SACTWU indicated that customs fraud is rife, and that rebate item 311.18/63.09/01.04 has been abused through mis-declaration, under-invoicing or smuggling to allow second hand clothing or even new clothing to be imported under this rebate code, despite the protection which ITAC has tried to provide. It further submitted that SARS is well aware of this problem. Amongst many other cases, is the detention of several dozen containers of second hand clothing in KwaZulu Natal, and the fact that SARS has also been confronted with second hand clothing imported from the USA, which was misclassified as new clothing.

7.19. SACTWU further submitted that challenges are experienced with the wiping rags rebate item 311.18/63.09/01.04 in that instead of all the imported products being re-purposed for the manufacture of wiping rags and cleaning cloths, leakage is occurring and some of these goods (including undeclared new and counterfeit clothing) are being diverted to the wholesale and retail clothing market.

7.20. According to SACTWU, illegal CTFL imports put untenable strain on the local CTFL manufacturing industry and jobs. These illegal imports also threaten to undermine the R-CTFL Masterplan and the nearly 70 000 new manufacturing jobs which the plan offers to create. SACTWU submitted that such illegal imports put massive pressure on manufacturers and jobs by distorting prices to levels against which legitimate manufacturers cannot compete. But this problem is even more acute with illegally imported worn and used clothing because the price of such clothing is a fraction of the price of new manufactured goods.

7.21. SACTWU concluded that despite many attempts by ITAC, SARS and industry to design better conditions for this rebate over the years, and by ITAC and SARS to monitor this rebate, it is clear that it continues to be abused. Therefore, it does not believe it will be possible to design new and better conditions to finally resolve these problems. It submitted that it is not possible for local manufacturers to compete against illegally imported second hand clothing or illegally imported new clothing that is smuggled into South Africa through the worn clothing rebate provision. The sale of such clothing into a market is a deadly virus for a diverse CTFL manufacturing industry and its jobs: it erodes domestic clothing and textile manufacturing capacities and capabilities and ultimately leads to massive job losses.

7.22. Should there be a need to consider new domestic sources of supply for companies such as those manufacturing cleaning cloths and wiping rags, SACTWU would be prepared to participate in an exploratory process to find alternative sources of supply. This may also assist to remedy some challenges faced by workers in those sectors.

COMMENTS FROM AMSA

7.23. AMSA is a national Federation of regional employer associations. It represents 10 700 employees and 141 companies all of whom are adversely affected by the abuse of this rebate item. In light of the abuse occurring under this rebate item, it was submitted that it should be discontinued.

7.24. Regarding the wiping rags rebate, AMSA submitted that there have been instances reported by SARS Customs to the stakeholders at the SARS Clothing, Textile, Footwear, Leather Industry Forum (“CTFLIF”) of blatant abuse and mis-declaration. It is often used as a conduit for importing new clothing, which then finds its way into the marketplace. It is believed that some of this abuse has even been committed by registered permit holders.

COMMENTS FROM TEXFED

7.25. Texfed submitted that the subject rebate item must be withdrawn in light of the misuse and mis-declaration associated with it.

7.26. Texfed indicated that it is important to note the origin of the items imported under tariff subheading 6309.00.17. In most cases the garments originate as discarded clothing items from developed economies i.e. EU and the USA. However, a large volume, almost 40%, also originates from Pakistan. In this instance, Texfed suspects that a used clothing route is being used to evade the ordinary customs clothing duty of 45% *ad valorem* (i.e. mis-declaration).

7.27. Texfed also submitted that, in terms of prices, on average, 1 425 900 kg of other worn clothing was imported monthly at an average FOB price of R4.06/kg.

8. RE-PUBLICATION - COMMENTS RECEIVED

8.1. During the re-publication period, comments were received from several participating firms under the subject rebate item.

8.2. Comments were received from the following ten (10) firms that utilise the wiping rags rebate, namely:

a) Sarkodie and Son Import and Export;
b) Multifibres (Pty) Ltd;
c) Disclose All Trade and Invest (Pty) Ltd;
d) Fatty Saikou Import and Export (Pty) Ltd;
e) Ian Farrell Import and Export CC;
f) Black Italia Trading Enterprise CC;
g) Zayabeng Projects CC;
h) Tramco (Pty) Ltd;
i) Mings Distributors CC; and
j) Phoenix industrial and Safety Suppliers CC.

8.3. Comments received from **Sarkodie and Son Import and Export,** supported the review, based on the opportunity provided by the Government to become an entrepreneur through the 311.18 rebate item and create employment.

8.4. **Multifibres (Pty) Ltd ("Multifibres"),** stated that should the Commission decide to withdraw the rebate item, the following points should be considered:

a) **Their People.** They have consultations with Trade Unions to undertake regarding retrenchment of affected employees. This will take several months to finalise.

b) **Their Suppliers**. They would want to ensure that all active shipments would be permitted to be customs-cleared before the date the rebate item is cancelled. Average transit times are 4-6 weeks.

c) **Their Contractual Obligations**. They have rental contracts with landlords. We would either need to relocate to smaller premises or sublet available space due to closure of manufacturing processes.

d) **Their Supply Chain**. They will require time to source the appropriate finished goods abroad and set up a supply chain in order to ensure continuity of supply to our clients. We estimate the RSA rag market to be in excess of 800, 000kgs per month (40 x 40ft containers) which is substantial additional capacity for overseas manufacturers to absorb without any planning of notice.

e) **Their Customers**. Import duties and additional US$ labour cost will push the prices of our products up considerably and we would need time and sufficient notice to inform our clients of price increases and /or imminent shortages in supply.

8.5. In their conclusion, Multifibres requested that the Commission be considerate of an appropriate withdrawal period to be at least 4 months from the date of the official notice thereof. This would allow a reasonable amount of time to make the necessary arrangements to remodel our business accordingly. They further requested that all rebate permit holders with permits expiring during a potential withdrawal period be granted an extension on their current rebate permits up to and including the final withdrawal date of the rebate item without having to re-apply for an entire new permit for a short period of time. This way no one company may gain an unfair advantage over another.

8.6. Comment received from **Disclose All Trade and Invest (Pty) Ltd,** stated that if rebate item 311.18 is withdrawn a fair exit period would be at least 10 years, minimum, considering:

a) They have made large capital investments;
b) They provide real jobs with union representation, provident fund, life insurance; all labour laws are adhered to;
c) They are members of National Textile Bargaining Council (NTBC);
d) They are 100% black owned, involved in manufacturing and the Government keeps on saying they need SME's; and
e) One of the reasons for the review is potential abuse or misuse- this is not a reason enough, compliance to the many things is required by ITAC, together with inspection by customs and ITAC, allows enforcement of any abuse or misuse.

8.7. **Fatty Saikou Import and export (Pty) Ltd**, stated that should their business close, the following sectors will be affected:

a) The South African Revenue Service has already been counting its losses as the result of the Corona virus, economic impact, impending joblessness and business closures would hammer revenues even harder.
b) In respect of job losses SME's represents a staggering 98% of business in South Africa. The fact is that the SME's employs between 50-60% of the country's workforce and are responsible for a quarter of job growth in the private sector.
c) Mining sector will be one of the sectors that will be highly affected as they rely on the wiping rags for cleaning in their industrial use.

d) Engineering sector was also benefiting from the supply of wipes, garages and workshops require absorbent cloths to soak up any oil, grease or chemical spills and leaks. Closing of this sector will have a huge impact on their industry.
e) Printing companies also get help from these wipes for cleaning purposes, which help prolong the life of the print heads by making sure they are being thoroughly cleaned and no build ups occur.

8.8. **Ian Farrell Import and Export**, neither support nor opposes the review, on the basis that the request for the review is from the high authority, which is trying to eliminate illegal trade in worn clothing and they fully support the initiative. They believe that ITAC has a good system of controls in place regarding the rebate facility. However, should ITAC decide to withdraw the importation of worn clothes to be cut by them, they will have to continue supplying the cloths through importing finished products. This will result in a high rate of our local unemployment levels.

8.9. Ian Farrell Import and Export stated that the problem lies with SARS not being able to police the products coming in from our neighbouring countries. They also raised their concern based on shipping costs, which are as great as or even greater for some products than the material cost. The raw material is subject to supply and demand and is a very low cost item. Prices have increased by 25% in 2021, brought about by freight rate increases; however, they stated that should the freight cost decrease, they anticipate a decrease in cleaning cloth prices going forward.

8.10. Ian Farrell Import and Export, raised the following concerns:

a) A cut-off date should be the same for all the players, should the rebate be withdrawn;
b) Permits for new players;
c) Duty on cut rags;
d) Moving their product into neighbouring countries;
e) Final determination required as soon as possible in order for them to able to plan their way forward; and
f) An ability or desire of their current supplier to take on additional staff to cut rags.

8.11. **Black Italia Trading Enterprise CC** ("Black Italia") opposed the review and indicated that South Africa and its customs areas do not produce enough rags material to supply the demand. Importing is then the only viable option for local suppliers. Black Italia stated they commenced full production from January 2020 and produced for three months before the pandemic and lock down set in.

8.12. Black Italia employs permanent and part-time employees, and submitted that removing the rebate provision will result in an increase in the cost of importing and overhead costs and that this will result in the business being unprofitable or cease all together. Black Italia further stated their business is young and they are yet to break-even in their two years of active production, subsequently increasing the tariff or withdrawal of the rebate on importation will be detrimental to their success.

8.13. **Zayabeng projects CC**, objects to the review and indicated that the withdrawal of this rebate will dissolve an industry that has been contributing to the economy for more than 20 years. It is not only the company that will be affected, but the workers, as well as other key organisations within the medium to large industry that uses their component as part of their consumables in the process of manufacturing e.g. Motor industry, Mining, Machinery and tooling.

8.14. **Tramco**, opposed the review and stated the following reasons, amongst others:

a) There are not enough raw materials produced locally for the manufacture of wiping rags;
b) The removal of the rebate item will result in an increase in prices of the wiping rags locally;
c) The removal of this rebate will result in a high percentage of job losses, and a number of the employees have a limited skills set and will struggle to find employment elsewhere;
d) The impact of Covid-19 has been huge on the economy and also to businesses in their industry, the subsequent and continuing shipping crisis has made operating conditions very tough and the timing of this review is not ideal; and

e) The legitimate use of rebate item has no negative effect on the local clothing industry and serves as an important catalyst to create employment and generate investment in manufacturing.

8.15. **Mings Distributors CC**, submitted the following reasons, amongst others, why the rebate provision should be retained:

a) The South African economy requires stimulus and to this end any legal economic activity should be encouraged;
b) The retaining and development of industries will assist in reducing the rate of unemployment;
c) Global warming and other environmental concerns must be addressed urgently. The worn clothing items are detailed in the current rebate encompassing description would, due to being ‘not fit for human consumption’, otherwise be detrimental to the environment by adding to the congestion in landfill sites and polluting the atmosphere whether in the Republic of South Africa or abroad. Instead the rebate permit allows for this waste to be recycled for commercial use whilst simultaneously creating employment and supplying marketable products to the economy;
d) They further submitted that it would be disingenuous were an office of the state to summarily shut down businesses without compensating the affected businesses and ensuring alternative employment for the business owners and their staff particularly in the current economic climate and with the rate of unemployment in the country so high;
e) The Republic of South Africa would be missing an opportunity to align this country with other countries of the world, which are striving to contain pollution; and
f) There is a strong possibility that the discontinuation of the rebate allowance could have the effect of introducing all three of the potential irregularities as are referred to in the motivation for the review.

8.16. **Phoenix Industrial and Safety Suppliers**, submitted the following objections, amongst others:

a) They commenced their business in the safety sector 27 years ago and the supply of rags has become their core business.
b) They have invested their hard earned resources into their factory and it has been challenging to compete against large companies in Gauteng and throughout the country.
c) They have made investment in quality cutting machines, compacting and strapping machines to ensure top quality finished products that we have always been proud to put into the marketplace.
d) Adding duty to used clothing will result in their inability to purchase adequate goods for manufacturing as we do not enjoy credit facilities with their overseas suppliers.

8.17. Comments were also received from industry and associations, namely; Texfed, Pepkor, Kingsgate, ATASA, AMSA and SAAA.

8.18. **Texfed** supports the immediate removal of rebate item 311.18/63.09/01.04. It further submitted that it sees absolutely no reason for recommending a phased removal of this rebate provision as the rebate provision has been abused and have caused immense harm to the clothing and textile industries in South Africa and SACU.

8.19. Texfed indicated that there are literally bales of imported second hand garments everywhere on the streets of South Africa. In a news clip on China City in Johannesburg, in the background one could witness hundreds of bales of second hand clothing that were being sorted and just being put up for resale. Texfed submitted that these bales of second hand clothing should be earmarked for shredding and being recycled as used fibre.

8.20. **The South African Apparel Association ("SAA-A")** is the largest compliant employer association representing the trade and labour market interests of its members in the domestic clothing manufacturing sector. SAA-A submitted that there is wide-spread abuse of this rebate item which pose serious risks to its members and most importantly to the job security of the many thousands of people in their employment.

8.21. SAA-A further indicated that, in respect of rebate item 311.18/63.09/01.04 (worn clothing used for the manufacture of rags and cloths), there have been numerous instances of abuse and mis-declarations reported by SARS Customs in the CTFL Sector Forum. This rebate facility is also abused from time to time as a conduit for importing new clothing items which find their way into the domestic market.

8.22. **The Apparel & Textile Association of South Africa ("ATASA")**, an employer organisation registered with the Department of Labour, representing 62 members with a total of 13 601 employees nationally in the clothing manufacturing and textile industry objected to the existence of the subject rebate provision. ATASA submitted that the abuse of the subject rebate provision results in these goods being under declared and a lot of goods make its way to the retail shelves.

8.23. **AMSA** reiterated its comments, which were provided in the initial publication phase. AMSA submitted that there have been instances reported by SARS Customs to the stakeholders at the SARS Clothing, Textile, Footwear, Leather Industry Forum ("CTFLIF") of blatant abuse and mis-declaration. It is often used as a conduit for importing new clothing, which then finds its way into the marketplace. It is believed that some of this abuse has even been committed by registered permit holders.

8.24. **Pepkor** submitted that it has the largest retail store footprint in Southern Africa with more than 5 470 stores of which approximately 3 000 provide affordable quality apparel (and other) products to millions of South African families. Pepkor supports the withdrawal of the subject rebate provision.

8.25. **Kingsgate Clothing Group ("Kingsgate"**) who is a local manufacturer of various clothing items including jackets and employs a significant number of people directly and indirectly also supports the withdrawal of the rebate provision.

8.26. Pepkor and Kingsgate submitted that at several SARS and CTFL Industry Stakeholders meetings, it has been recorded that there is widespread abuse of the above rebate item. SARS Customs also reported at the CTFL meetings that rebate item 311.18/63.09/01.04 had been abused and many mis-declaration instances occur such as new clothing items being imported as worn clothing.

9. Summary of oral presentations

9.1. Oral representations were presented to the Commission by three interested parties, namely:

a) KWP Law on behalf of Mings Distributors cc;
b) Wiper Fibres cc, Ragman cc, Rag Clean cc, Just Rags cc and Rags 4 Us cc; and
c) Phoenix Industrial and Safety Suppliers cc.

9.2. Oral presentations from the wiping rags manufacturers objected to the withdrawal of the wiping rags rebate citing, amongst others, that there are not sufficient raw materials produced locally to sustain the manufacture of wiping rags. The removal of the rebate item will result in an increase in the local prices of wiping rags and will result in a high percentage of job losses. It was further submitted that there is a strong possibility that the discontinuation of the wiping rags rebate could have the effect of creating an incentive for smuggling of used clothing. Importers under the wiping rags rebate further submitted that the main challenge lies with SARS not being able to police products entering the South African market from neighbouring countries.

9.3. Part of the objections to the withdrawal of the wiping rebate revolved around the fact that certain manufacturers of wiping rags have been in existence for decades and have made investments in quality cutting machines, compacting and strapping machines to ensure top quality finished products. The immediate withdrawal of the wiping rags rebate will not afford enough time for the industry to re-organize and re-purpose.

10. SUMMARY OF FINDINGS

10.1. Rebate item 311.18/63.09/01.04 has been in existence since the early 1990s. Despite many attempts by ITAC, SARS and industry to design better conditions and safeguards for this rebate over the years, and efforts by ITAC and SARS to monitor this rebate, it continues to be abused and mis-used by some firms.

10.2. Information at the Commission's disposal indicates that the subject rebate item has been abused through mis-declaration, under-invoicing or smuggling to allow second-hand clothing or even new clothing to be imported under this rebate item. However, there are legitimate importers who are running *bona fide* businesses and are compliant with regulations and rebate permit conditions.

10.3. Information received from interested stakeholders seems to suggest that many garments imported under rebate item 311.18/63.09/01.04 are not further processed into wiping rags and cleaning cloths but are rather sold into the informal and formal wholesale and retail market as second hand clothing, and may even be sold as new clothes.

10.4. From an industrial policy point of view, the risk is that second hand clothing (and perhaps even new clothing) finds its way into the South African market, using this rebate item, which has a detrimental effect on the local CTFL manufacturing and retail sectors. Furthermore, illegal imports of second hand and worn clothing also threaten to undermine the objectives of the R-CTFL Masterplan and the nearly 70 000 new manufacturing jobs which the plan seeks to create. Such illegal imports put massive pressure on manufacturers and jobs by distorting prices to levels against which legitimate manufacturers cannot compete.

10.5. From an administrative point of view, the subject rebate item creates an administrative burden for SARS and ITAC as the goods are imported in compressed bales, making it very difficult to verify what type of products are actually imported. Even if the illicit goods are detained or seized by Customs, the only inevitable result is storage costs. Should the rebate item be maintained, SARS proposes additional control measures such as having importers code printed on outer bales on all sides, that garments must be de-faced prior to baling, that collars, buttons and accessories must be removed and garment cut in half, etc.

10.6. Second hand/used clothing can be sourced within the Republic. The dtic has a number of projects currently under way to support the circular economy and avoid confiscated or seized clothing being dumped in landfill sites but to rather use it in the economy as raw material for manufacturers of various products such as wiping rags cleaning cloths, insolation, stuffing, animal blankets etc. Therefore, alternative arrangements should be made for those *bona fide* manufacturers of wiping rags and cleaning cloths to make use of local waste material that is suitable for their needs.

10.7. The Commission received a very limited number of comments from rebate participants during the initial publication phase. Six (6) comments were received from wiping rag firms representing only 19% of total industry firms participating under the wiping rags rebate. Comments received were largely in favour of retaining the rebate item.

10.8. Comments received from the wiping rag manufacturers cited their objection to the withdrawal of the wiping rags rebate based on, amongst others, that there is not enough raw material produced locally to sustain the manufacture of wiping rags; the removal of the rebate item will result in an increase in prices of the wiping rags locally and will result in a high percentage of job losses. It was further submitted that there is a strong possibility that the discontinuation of the wiping rags rebate could have the effect of creating an incentive for smuggling of used clothing. Importers under the wiping rags rebate further submitted that the problem lies with SARS not being able to police products coming in from neighbouring countries.

10.9. Part of the objections to the withdrawal of the wiping rebate revolved around the fact that certain manufacturers of wiping rags have been in existence for decades and have made investments in quality cutting machines, compacting and strapping machines to ensure top quality finished products. The immediate withdrawal of the wiping rags rebate will not afford enough time for the industry to re-organize and re-purpose.

10.10. In terms of the wiping rags rebate and the BELN countries, import data indicated that these countries export appreciable volumes of already “cut-up rags” to South Africa under HS 6310.90. This points to the need for tighter boarder control, policing and monitoring of used clothing and already cut-up rags.

10.11. Information at the Commission’s disposal indicates that there is a disparity and mismatch in the level of imports of worn clothing under tariff heading 63.09

recorded by SARS into South Africa and exports from foreign suppliers. Imports of second hand clothing recorded by SARS are significantly higher than exports of second hand clothing recorded by foreign suppliers, thus corroborating comments from stakeholders that the subject rebate item is possibly being used as a conduit to import other types of clothing (including new clothing). This, together with other considerations, suggests that the costs associated with the subject rebate item may very well outweigh the associated benefits. The costs in this instance would be the negative impact on industrialization and jobs within the textile and clothing sectors as well as undermining efforts and objectives of the R-CTFL Masterplan. On the other hand, the immediate withdrawal of the rebate item would have a negative impact on legitimate entrepreneurs and manufacturers of wiping rags as well as associated job losses.

10.12. According to information at the Commission's disposal, the rebate provision is being misused (abused). This is not only an administrative burden, but more importantly has a significant adverse impact on a highly sensitive (and diminished) sector of the South African economy. The Commission concluded that the facts submitted support a strong case that the rebate provision concerned requires termination in the very near future and not over an extended period.

10.13. A two-year phase out period for rebate item 311.18/63.09/01.04 to the Customs and Excise Act, 1964 (Act No. 91 of 1964), is deemed reasonable. Although, a phase-down of one year might actually be warranted, two years will allow businesses time to repurpose.

11. RECOMMENDATION

11.1. In light of the foregoing, the Commission recommended the following:

a) Maintain rebate item 311.18/63.09/01.04 ("wiping rags rebate") and phase it out over the next 2 years to allow the industry to re-purpose their operations over this period of time to avoid immediate job losses.
b) A 2-year phase-out period for the rebate item be effective from the date of implementation by SARS through a publication in the Government Gazette.

c) The proposed amended guidelines, rules and conditions for rebate item 311.18/63.09/01.04, which would be applicable during the phasing out period be confirmed through a publication in the Government Gazette.

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