

Filling the fiscal basket: Quantifying tax revenues from customer loyalty programmes

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Acknowledgements: Some of the sections of this work are based on the mini dissertations of the first two authors which were submitted in accordance with the requirements for the degree Master of Commerce in Taxation at the University of Pretoria in 2022.

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Abstract

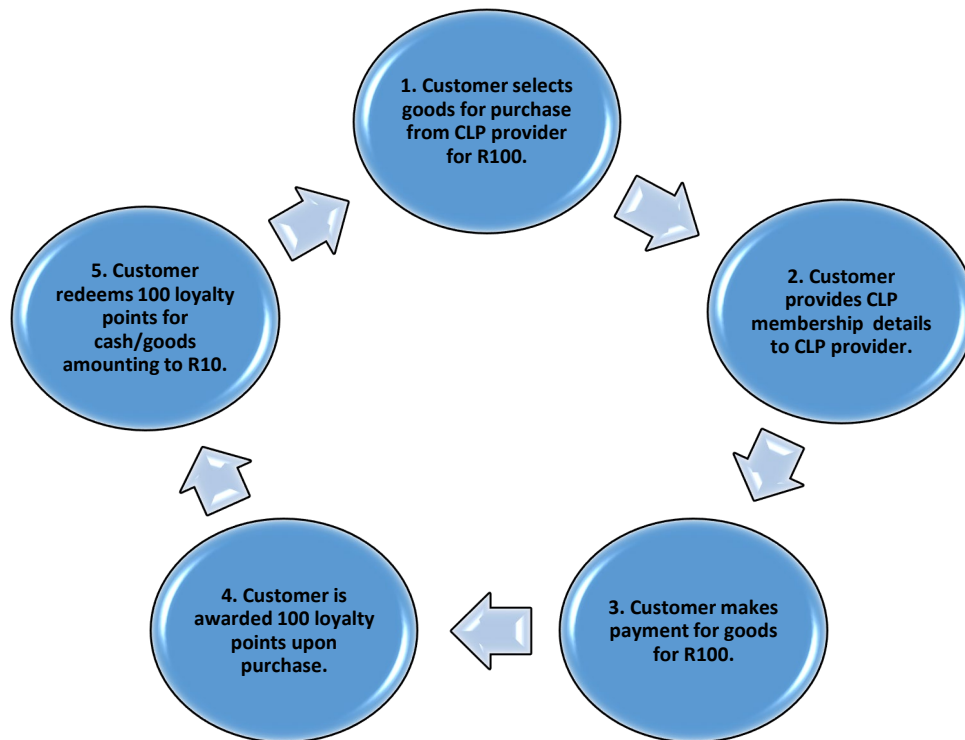
The South African government is experiencing a significant shortfall in tax revenue, and recent research has identified customer loyalty programmes (CLPs) as a potential revenue stream. Despite the popularity of these programmes, which are used by 73% of economically active South Africans, no tax is currently imposed on the rewards received by their customers, resulting in the loss of much-needed tax revenue. This paper quantifies the tax revenue that could have been generated by South Africa's three most-used CLPs over a five-year period (2018–2022) to determine if a tax on CLP rewards is a viable revenue stream for the fiscus. The longitudinal instrumental case study employed demonstrates that the fiscus could have conservatively collected R1 140 753 042 in total tax revenue from the three CLPs if a tax had been imposed on CLP rewards, as proposed in this paper. This paper highlights the significant revenue potential of taxing CLP rewards, and it provides valuable insights for policymakers who seek to address the country's revenue challenges. The findings reveal the magnitude of potential contributions to tax revenue in the form of CLPs. Given the impetus behind CLPs, their exponential growth rate and their increasing importance as a marketing strategy, this paper proposes a re-evaluation by policymakers of the taxation of CLP rewards.

Keywords: Customer Loyalty Programmes, Revenue recognition, Withholding tax, Loyalty rewards.

1. Introduction

Customer Loyalty Programmes (CLPs) are reward systems that provide financial or non-financial benefits to customers to incentivise them to remain loyal (Breugelmans, et al., 2015, pp. 128-129). CLPs have become prevalent across a broad range of industries globally and South Africa is no exception: in 2022, 73% of economically active citizens were making use of CLPs (Burnstone & Olivier, 2018, p. 3; Cromhout, 2022, p. 6). Typically, customers select goods to purchase and, upon payment, presents their CLP membership identification (usually in the form of a loyalty card) which earns them CLP rewards (points or similar benefits) based on the value of the purchase. Customers may usually redeem these rewards in future or use them against future purchases. Figure 1 illustrates the typical operation of a CLP transaction and redemption cycle.

Figure 1: Operation of a CLP transaction



Source: Authors' own.

The illustration provided in Figure 1 is representative of typical CLPs in operation in the retail sector in South Africa, but may be distinguished from programmes that merely provide upfront discounts or vouchers rather than an accumulation of rewards that may be redeemed in future. The focus of this paper is therefore limited to those CLPs in the retail sector that allow customers to accumulate rewards for redemption at a future date, that have become commonplace.

Even though CLPs are becoming more commonplace, research indicates that the South African fiscus has not overtly addressed how CLP rewards are treated from a tax perspective (Odendaal & Pidduck, 2014, p. 10; Pidduck & Odendaal, 2013, p. 1521; Pidduck, et al., 2019, p. 627). Nevertheless, some commentators have proposed that a specific tax on CLP rewards in the hand of customers that could increase tax revenues in South Africa (Odendaal & Pidduck, 2014, p. 10; Pidduck, et al., 2019; Swanepoel & Pidduck, 2020), arguing that while businesses are able to reduce their taxable income by the costs associated with providing CLP rewards to customers, there is no corresponding taxation of these CLP rewards in the hands of customers (Swanepoel & Pidduck, 2020, p. 76).

Notwithstanding the above, the proposals for the introduction of a mechanism for a tax on CLP rewards in the hands of customers remain. Such proposals do not stray far from measures that have been taken to introduce other taxes, such as additional wealth taxes, that indicate that there is an appetite for additional revenue streams to fund government expenditure (Changole, 2022). The National Treasury (2021a, p. 39) has established that, as of 2020, an increase in tax of up to R40 billion would be needed to stabilise public debt and the economy and a tax on CLP rewards could contribute significantly towards bridging this gap.

Limited published research exists on the taxation of CLP rewards, however Swanepoel and Pidduck (2020) argue that CLP rewards in the hands of customers comply with the

definition of gross income and could therefore be subject to normal taxation in the hands of the customer in South Africa. Their analysis concludes that the fiscus could tax CLP rewards in the hands of customers but propose amendments to the legislation to address specific components of the gross income definition for administrative ease such as those related to timing due to complexities in the manner in which different CLPs operate and the manner in which customers participate in these CLPs (Swanepoel & Pidduck, 2020, p.98).

On this basis, the main purpose of this paper is to determine if a tax on CLP rewards is a viable revenue stream for the fiscus. Even so, the paper provides a discussion of the merits of taxing CLP rewards, including whether CLP rewards in the hands of customers comply with the definition of gross income in the context of the tax code. In doing so, this paper quantifies the tax revenue that could possibly be generated by a sample of CLPs over a five-year period. Previous research has relied on the accounting disclosures presented in the annual financial statements of selected companies that offer CLPs in an attempt to quantify the value of CLP rewards for selected CLPs (Odendaal & Pidduck, 2014, pp. 10-11); however, the values (deferred revenues) used in such studies were based on what is now an outdated reporting interpretation: International Financial Reporting Interpretation Committee 13: *Customer Loyalty Programmes* (IFRIC 13) (International Financial Reporting Standards Foundation, 2022). Commencing on 1 January 2018, IFRIC 13 and its related standards were superseded by International Financial Reporting Standards 15: *Revenue from Contracts with Customers* (IFRS 15) (International Accounting Standards Board [IASB], 2021). IFRS 15 requires companies to implement a five-step approach to recognise, measure and present revenue and deferred revenue received from a customer (Deloitte Touche Tohmatsu Limited, 2016, pp. 2-3; Dili, 2017, p. 1; IASB, 2021). It also provides the users of financial statements with more relevant and reliable information on revenue than its predecessor, as well as more information on CLP rewards, which can now be used by researchers to more reliably quantify the tax revenue that could be collected from CLPs. This paper, therefore, departs from previous research by using accounting disclosures in accordance with IFRS 15. This paper further departs from previous research with the use of a longitudinal approach as discussed in part three.

The paper consists of six parts. Following this introduction, part two includes a description of the operation of the CLPs selected in this paper. The methodology and research design employed is described in part three. Detail for understanding the taxation and accounting treatment of CLPs in South Africa is presented in part four. Finally, the method of tax collection and quantification of the potential tax revenue from selected CLPs are described in part five, followed by the presentation of the findings and conclusions in part six.

2. Understanding the CLPs in this paper

It is beneficial at this point to understand the typical operation of the CLPs in this paper.

Clicks ClubCard, Pick n Pay Smart Shopper and Dis-Chem Benefit are well-established CLPs that are on the list of the top five most-used CLPs in South Africa (Cromhout, 2022, p. 31). All three operate similarly to that illustrated in Figure 1 (refer section 1 above), with minor differences in how CLP rewards are earned, converted to rand values and redeemed (refer Table

1 below). Clicks ClubCard customers earn 1 point for each R5 spent, and 1 point is equal to R0,10 (Clicks Retailers (Pty) Limited [Clicks], 2022); Pick n Pay Smart Shopper customers earn 1 point for each R2 spent, and 100 points are equivalent to R1 (Pick n Pay Stores Limited [Pick n Pay], 2022b); and Dis-Chem Benefit customers earn 1.5% of their qualifying purchases as Benefits (Dis-Chem Pharmacies Limited [Dis-Chem], n.d.-a). For redemption, Clicks ClubCard customers need a 50-point, or R5, balance (Clicks, 2022); Pick n Pay Smart Shopper customers need a 500-point, or R5, balance (Pick n Pay, 2022d); but Dis-Chem Benefit customers do not need a minimum balance (Dis-Chem, n.d.-b). For all three CLPs, the redemption of rewards includes the option for customers to utilise the rewards (in the form of CLP points or other benefits) to reduce their amount owing on a future purchase. While none of these CLPs allow rewards to be exchanged for cash, Pick n Pay Smart Shopper customers have the option to use their CLP points to purchase vouchers at third parties with whom CLP providers have agreements in place or to donate the points to a list of charities (Pick n Pay, 2022c, 2022d).

Table 1: Comparison of selected CLPs

	Clicks ClubCard	Pick n Pay Smart Shopper	Dis-Chem Benefit
CLP points earned for spending	R5 spending for 1 point	R2 spending for 1 point	1.5% of purchases received as a Benefit
Rand value of a CLP point	10 points = R1	100 points = R1	N/A ²
Rewards earned at third parties	Yes	Yes	Yes
CLP point balance needed to redeem	Yes: 50 points	Yes: 500 points	No
Conversion into cash	No	No	No
Redemption at third parties	No	Yes	No
Donation of rewards	No	Yes	No
Expiration of rewards	Yes, after 12 months	Yes, after 12 months	Yes, after 12 months

Source: compiled from Clicks, n.d.; Dis-Chem, n.d.-b; Pick n Pay, 2022d.

3. Methodology and research design

A qualitative research paradigm was implemented through the use of multiple longitudinal instrumental case studies (Creswell & Creswell, 2018, pp. 13-14; Yin, 2018, p. 51). A multiple case study is defined as a manner in which a researcher can study and contextualise the happenings of a real-life phenomenon through the examination and exploration of a limited number of events from which generalisations can be made (Yin, 2018, p. 51). This design was chosen to help make generalisations and identify patterns across the topic for investigation. It is argued that the industry-specific cases form a small part of a larger system and provide the researchers with insights into the system as a whole (Gomm et al., 2000, pp. 99). Replication through pattern-matching helps the researchers to support previous findings and, as such, increases the credibility of the study.

² Dis-Chem Benefit does not use a point system: 1.5% of purchases in Rand are given as Benefits in Rand.

The data used were in the form of financial information from annual financial statements, which were analysed to obtain the deferred revenue used as a basis to quantify the potential tax revenue from a tax on CLP rewards as proposed in this paper. A longitudinal multiple-case study was applied in selecting which CLPs to use in quantifying the tax revenues from 2018 to 2022. The starting point used was financial statements prepared for the financial year ending in 2018 because this was when the appropriate IFRS disclosures were first implemented.

3.1 Selection of CLPs

South Africa's 25 most-used CLPs, per the 2022 Truth & BrandMapp Loyalty Whitepaper (Cromhout, 2022), were used as the population from which the sample for this paper was selected. Purposeful maximal sampling (Creswell, 2015, p. 205; Patton, 2015) was employed to select the programmes that more than 50% of respondents from this population used. Purposeful maximal sampling is a method where a sample is selected that shows different perspectives of a problem that is chosen in order to meet the requirements needed to answer the research problem (Creswell, 2015, p. 205). The initial sample selected led to the identification of five loyalty programmes whose terms and conditions were inspected, analysed and assessed to determine which loyalty programmes provided upfront discounts or vouchers to customers rather than an accumulation of rewards. All loyalty programmes that provided an upfront discount or voucher were excluded from the scope of this paper as these were not CLP rewards that could be redeemed in future or used to reduce the amount owing on future purchases; these were Checkers Xtra Savings and Woolworths WRewards. The CLPs analysed for this paper were Clicks ClubCard, Pick n Pay Smart Shopper and Dis-Chem Benefit.

4. Understanding the tax and accounting treatment of CLPs in South Africa

It is beneficial to understand both the tax and accounting treatment of CLPs in South Africa before quantifying the tax revenue that could have been generated by the CLPs selected in part five.

4.1 Understanding the taxation of CLPs

The departure point in determining whether an amount could be subject to normal taxation in South Africa is the gross income definition given in the Income Tax Act No. 58 of 1962 (the Income Tax Act). Previous research has argued that CLP rewards qualify as gross income in the hands of the customer (Swanepoel & Pidduck, 2020, p. 97). Swanepoel and Pidduck (2020, pp. 93-96) identified complexities surrounding the timing of the accrual of CLP rewards and whether these rewards are capital or revenue in nature; these complexities, as they relate to the three CLPs discussed in this paper, are discussed below.

One complexity relates to the ownership of CLP rewards. The terms and conditions of all three CLPs indicate that the CLP provider remains the owner of the physical membership card (Clicks, n.d.; Dis-Chem, n.d.-b; Pick n Pay, 2022d); however, CLP rewards may be earned in all three CLPs without presenting a physical card, by providing a cell phone number or identity

number, and it is therefore argued that the ownership of the physical CLP card is separate from the ownership of the CLP rewards earned (Swanepoel & Pidduck, 2020, p. 91). Consequently, since the customer is considered the owner of the CLP rewards, the accrual and receipt of CLP rewards take place when the CLP rewards are earned, which is before the time of redemption for goods and services.

A second complexity lies in the redemption of CLP rewards. The recent case of *Clicks Retailers (Pty) Limited v CSARS* (2021) confirms the viewpoint of Swanepoel and Pidduck (2020, p. 92) that the CLP provider is obliged to provide the customer with CLP rewards when these are first accumulated in accordance with the terms and conditions. Therefore, an argument can be made that accrual to the customer takes place at the first point of sale and not upon the later election of redemption by the customer. Pick n Pay Smart Shopper and Clicks ClubCard customers must have a R5 balance to redeem their CLP rewards, while no limitation is imposed on Dis-Chem Benefit customers (Clicks, n.d.; Dis-Chem, n.d.-b; Pick n Pay, 2022d). Although customers are not entitled to redeem their CLP rewards at the time when they are earned, the views of the judiciary expressed in *Clicks Retailers (Pty) Limited v CSARS* (2021) indicates that accrual would still occur, as the provider is obligated to allocate the rewards to the customer immediately and not only when the rewards are redeemed by the customer. The R5 sub-minimum required by Pick n Pay Smart Shopper and Clicks ClubCard is thus immaterial for the purposes of this paper and is not considered further.

A third complexity is found in the customer's ability to donate CLP rewards. Pick n Pay Smart Shopper allows the donation of CLP rewards (Pick n Pay, 2022c), and the precedent set in *CIR v Witwatersrand Association of Racing Clubs* (1960) applies. The case indicates that where there is no written contractual obligation to donate, the amounts are first beneficially received by the donor (the CLP customer in this instance); therefore, Pick n Pay Smart Shopper points accrue to the customer, as the customer is not able to cede points before the beneficial receipt (Swanepoel & Pidduck, 2020, p. 92).

The fourth complexity lies in the uncertainty created by the loss, theft and expiry of CLP rewards. For all three CLPs considered, CLP rewards expire after 12 months if they are not redeemed (Clicks, n.d.; Dis-Chem, n.d.-b; Pick n Pay, 2022d), but since accrual takes place before loss, theft or expiry can occur, it is submitted that a 12-month expiry does not affect initial accrual.

Despite these complexities it is submitted that it would be appropriate to tax CLP rewards in the hands of customers. Several special inclusions which often override areas of complexity or uncertainty can be found in the gross income definition in section 1 of the Income Tax Act therefore it would not be an unprecedented departure.

In conclusion, an amount is accrued to or received by CLP customers in the form of CLP rewards that can easily be converted to a Rand value in the Pick n Pay Smart Shopper, Clicks ClubCard and Dis-Chem Benefit CLPs. Notwithstanding the uncertainty regarding when CLP rewards accrue or if they are of a capital or revenue nature, it is assumed for the purpose of this paper that the amounts are taxable in the hands of the customer at the initial point of sale, as concluded by Swanepoel and Pidduck (2020:96).

It must be noted that although there is a school of thought that supports the taxation of CLP rewards based on accounting values, it is not followed in this paper (Schon, 2005, p. 146). Accounting values for CLP rewards issued are presented after taking into account various

estimates of future usage, whereas this paper proposes the taxation of all rewards earned and not just those that are expected to be redeemed. In addition to this, the recognition and disclosure prescribed by IFRS 15 require judgement, and it is evident from the financial statements of the three CLPs studied in this paper that these requirements are not comparable across the board. The details of the accounting treatment are discussed below.

4.2 Understanding the accounting treatment

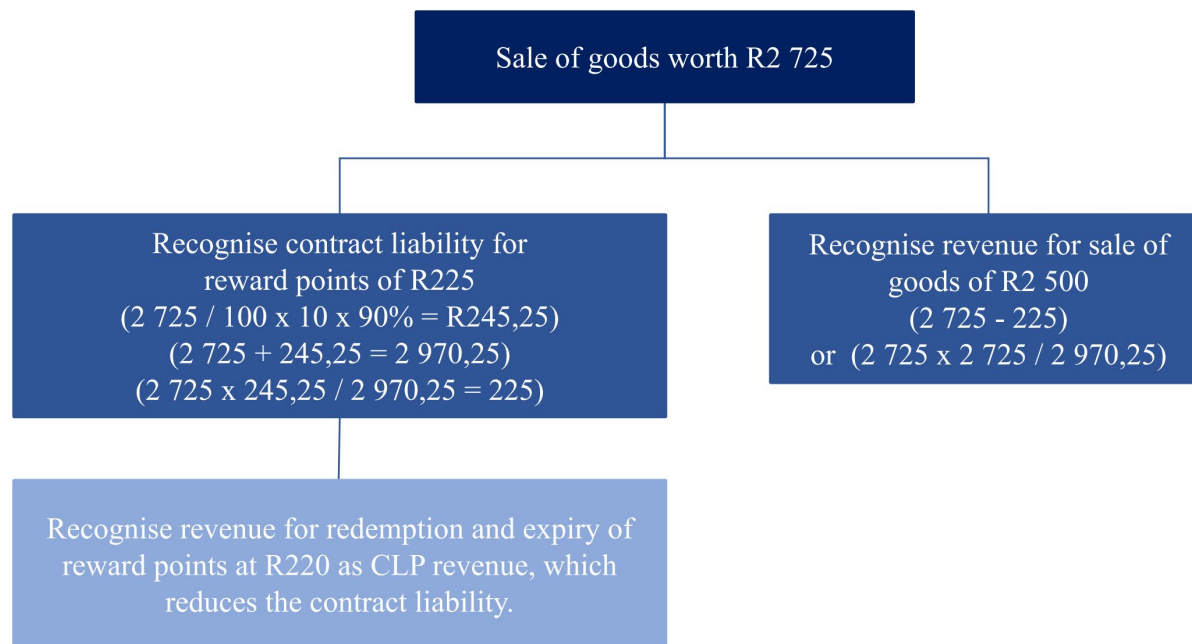
The accounting treatment of CLP rewards is prescribed by IFRS 15, which mandates that revenue from CLP rewards must be recognised and disclosed separately (IASB, 2021, paras B39-B89). This was not the case in the previous accounting standard, IFRIC 13. To summarise, IFRS 15 indicates that the sale of goods to and the earning of CLP rewards by the customer are two separate performance obligations in the hands of the CLP provider (IASB, 2021, para. B40). The transaction price is considered the full price of goods sold and must be allocated between the two performance obligations: the sale of goods and the CLP rewards awarded to the customer (IASB, 2021, para. B42). Revenue relating to the sale of goods may be recognised at the time of the sale, but the portion of revenue allocated to CLP rewards must be recognised as a “contract liability” (IASB, 2021, para. 31), which is the liability that is created when an entity has an obligation to transfer goods or services to a customer for which payment has already been received (IASB, 2021, p. A931). The contract liability becomes revenue in the hands of the CLP provider at a future date, either upon redemption by the customer or expiry of the rewards, and the value of the revenue relating to the CLP rewards is based on the provider’s expectation of how much of the CLP rewards will be exercised or redeemed during the financial year. This expectation is determined by each CLP provider by analysing past redemption rates of CLP rewards to predict future redemption rates; however, IFRS 15 does not provide detailed guidance on how this estimate must be made (IASB, 2021, para. B46). A short example is provided below to aid in explaining how the contract liability is recognised for the awarding of CLP rewards.

Example 1

Company A operates a CLP where customers obtain 10 reward points for each R100 spent, and each CLP reward point is valued at R1. At the start of its current financial year, Company A has an opening balance of R200 for its contract liability. During the financial year, customers participating in the CLP purchase R2 725 worth of goods. It is expected, based on Company A’s past experience, that only 90% of CLP reward points earned will be redeemed in future. During the current financial year, R220 is recognised as revenue due to the redemption and expiry of CLP reward points (Figure 2), and the reconciliation of movement in the contract liability leads to a closing balance of R205 (Table 2).

The allocation of revenue during the current financial year may be illustrated as follows:

Figure 1: Illustration of IFRS 15 revenue allocation



Source: Authors' own.

The disclosure to be made, as required by IFRS 15, for the above company would be as follows:

Table 2: Reconciliation of movement in the contract liability account of Company A

Reconciliation of movement in the contract liability account	Rand '000
A Opening balance of the contract liability	200
B Plus CLP reward points earned in the current year that are expected to be utilised	225
C Less revenue recognised from CLP reward points (reward points redeemed or utilised and expired)	(220)
D Equals closing balance of the contract liability	205

Source: Authors' own.

Based on the example above, the financial statements of CLP providers were analysed to obtain the equivalent value of CLP reward points earned in the current year that are expected to be utilised (B: R225 in the example above). It is necessary to calculate this value because, according to IFRS 15, companies are only required to disclose the opening and closing balances of the deferred revenue (A and D in the example above) and the revenue recognised (C in the example above). The value of B can be calculated as D plus C less A.

As discussed in 4.1, prior research has argued that CLP rewards issued to customers could be taxed as gross income in some circumstances (Swanepoel & Pidduck, 2020). If this is accepted as correct, the most accurate basis for the taxable amounts would be the value of CLP rewards issued to the customer (R272,50 in the example, being $2\,725 / 100 \times 10$), as that is the amount that meets the gross income definition found in section 1 of the Income Tax Act.

However, companies are not required to disclose the CLP rewards issued to customers separately in their financial statements, which means it is necessary to estimate this value. To calculate the value of CLP rewards issued (or the closest estimate thereof), the CLP reward points earned that are expected to be utilized (B: R225 in the example above) must be divided by the redemption rate (90% in the example above), which produces an estimate of R250 in the given example. The calculation of the value of CLP rewards issued for the CLPs selected for this study is included below.

4.3 Calculation of CLP rewards issued

The authors envisioned using disclosures of the reconciliation of the contract liability and value of CLP rewards issued, as mandated by IFRS 15, to quantify the tax revenues on CLP rewards to customers. However, disclosures were found to be disparate; the intricacies of the quantification of CLP rewards issued for each CLP selected are outlined below.

4.3.1 Clicks ClubCard

Clicks’s integrated annual reports from 2018 to 2022 provide the percentages of total revenue related to Clicks ClubCard customers (Clicks Group Limited [Clicks Group], 2018b, p. 34; 2019b, p. 49; 2020b, p. 50; 2021b, p. 48; 2022b, p. 46). Therefore, it was possible to calculate the value of revenue from sales to Clicks ClubCard customers by multiplying these percentages with the total value of revenue for Clicks in each year. As has been noted previously, the terms and conditions of Clicks ClubCard state that for every R5 that a ClubCard customer spends at Clicks, the customer will receive one CLP point, which is valued at R0,10. Therefore, to calculate the value of CLP points issued, the value of revenue in the financial statements was multiplied by the percentages disclosed in the integrated annual reports (Clicks Group, 2018a, p. 31; 2018b, p. 34; 2019a, p. 31; 2019b, p. 49; 2020a, p. 50; 2020b, p. 33; 2021a, p. 33; 2021b, p. 48; 2022a, p. 38; 2022b, p. 46). This amount was then divided by R5 to quantify the number of CLP points issued and then multiplied by R0,10 to quantify the value of the CLP points issued in each year which ranges from R478 361 430 in 2018 to R681 700 300 in 2022 (Table 3).

Table 3: Value of points issued by Clicks ClubCard, based on revenue attributed to CLP customers

	2018	2019	2020	2021	2022
Revenue (R'000)	30 981 958,00	33 376 010,00	36 102 951,00	39 982 414,00	42 500 019,00
Percentage of revenue attributed to CLP customers	77,20%	77,60%	78,20%	80,20%	80,20%

Revenue from CLP customers (R '000)	23 918 561,02	25 899 783,76	28 232 507,68	32 065 896,03	34 085 015,24
Calculation to get to the value of CLP points issued	/R5 x R0,1	/R5 x R0,1	/R5 x R0,1	/R5 x R0,1	/R5 x R0,1
Value of CLP points issued (R '000)	478 361,43	517 995,68	564 650,15	641 317,92	681 700,30

Source: Compiled and calculated based on data from Clicks Group (2018a, p. 31); (2018b, p. 34); (2019a, p. 31); (2019b, p. 49); (2020a, p. 50); (2020b, p. 33); (2021a, p. 33); (2021b, p. 48); (2022a, p. 38); (2022b, p. 46).

The total value of CLP points issued that could have been taxed over the five-year period from 2018 to 2022 for Clicks ClubCard is R2 884 025 486. The value of CLP points issued by Clicks ClubCard is considered conservative due to the participation of CLP partners where customers may earn additional CLP points for purchases at these reward partners, that would not be included in the revenue for Clicks's integrated annual reports.

4.3.2 *Pick n Pay Smart Shopper*

Pick n Pay discloses the opening and closing balance (rows A and E of Table 4) of deferred revenue (the contract liability), and although the company does not disclose the total value of revenue recognised from the Smart Shopper CLP separately, it does disclose the total actual value of revenue recognised for three deferred revenue items (row C of Table 4). Pick n Pay's financial statements identify the three deferred revenue items as prepaid gift card liability, Smart Shopper loyalty programme liability and refund liability (Pick n Pay, 2019, p. 70; 2020, p. 78; 2021a, p. 78; 2022a, p. 80). To determine the value of revenue recognised that relates to the Smart Shopper liability (row B of Table 4), the percentage of the Smart Shopper liability that relates to total deferred revenue was calculated using the closing balances of these liabilities (row D of Table 4). Then, except for 2018, each year's percentage was applied to the following year's total revenue recognised as deferred revenue to calculate the value attributable to the Smart Shopper liability (row B of Table 4); this method was followed because deferred revenue is recognised as revenue in a subsequent year, meaning that the closing balance of deferred revenue will become revenue recognised in the future. Finally, to determine 2018's revenue an average percentage of the values determined for 2019 to 2022 was used, as 2017's financial statements were prepared prior to the implementation of IFRS 15.

The value of the points issued by Smart Shopper which were expected to be utilised was calculated as the opening balance of deferred revenue (row A of Table 4) less the value of revenue recognised (row B of Table 4), less the closing balance of deferred revenue (row E of Table 4). The value of CLP points issued (row F of Table 4) represents the value of CLP points issued less the CLP points that Pick n Pay expects not to be redeemed, which is disclosed in the financial statements in percentage terms as the expected forfeiture rate (Pick n Pay, 2018,

p. 45; 2019, p. 70; 2020, p. 78; 2021a, p. 78; 2022a, p. 80). Expected forfeiture rates may differ for the opening balance, closing balance and revenue recognised; however, only the rates for opening and closing balances are disclosed, and the average of these two rates was used in the calculation. The average expected forfeiture rate so calculated was deducted from 100% to obtain the percentage of points expected to be utilised or redeemed (row G of Table 4). The value of points issued (row F of Table 4) was then divided by the calculated percentage of points expected to be redeemed (row G of Table 4) to calculate the value of total points issued during a given year (row H of Table 4) which ranges from R110 551 090 in 2018 to R164 724 080 in 2022.

Table 4: Value of points issued by Pick n Pay Smart Shopper

	2018	2019	2020	2021	2022
A Smart Shopper deferred revenue opening balance (R '000)	96 900,00	121 300,00	96 900,00	122 900,00	170 600,00
B Less revenue recognised as from CLP reward points (points redeemed or utilised and expired) (R '000)	(70 231,74)	(76 669,53)	(50 908,43)	(91 023,33)	(117 097,37)
C Revenue recognised as deferred revenue (R '000)*	164 900,00	177 800,00	134 600,00	221 300,00	242 500,00
D Percentage of Smart Shopper deferred revenue to total deferred revenue*	42,59%	43,12%	37,82%	41,13%	48,29%
E Less Smart Shopper deferred revenue closing balance (R '000)	(121 300,00)	(96 900,00)	(122 900,00)	(170 600,00)	(189 400,00)
F Equals Rand value of points issued and expected to be utilised (R '000)	94 631,74	52 269,53	76 908,43	138 723,33	135 897,37
G Percentage of points issued adjusted for average expected forfeiture*	85,60%	84,80%	82,50%	83,75%	82,50%
H Value of CLP points issued (R '000)	110 551,09	61 638,60	93 222,34	165 639,79	164 724,08

Source: Authors' own (Pick n Pay, 2018, p. 45; 2019, pp. 43, 70; 2020, pp. 48, 78; 2021a, pp. 47, 78; 2022a, pp. 49, 80).* These rows are used to demonstrate calculations. Row C is multiplied by row D to calculate the value in row B. Similarly, row G is multiplied by row F to calculate row H.

The total value of CLP points issued that could have been taxed over the five-year period from 2018 to 2022 for Pick n Pay Smart Shopper amounts to R595 775 910. As Pick n Pay

does not disclose CLP points issued and redeemed in the same financial year, such CLP points were not factored into the calculation of total CLP points issued for the purposes of this study, as the value thereof is not determinable. Consequently, the value of CLP points issued by Smart Shopper is considered a conservative.

4.3.3 Dis-Chem Benefit

Members of Dis-Chem Benefit earn 1,5 percent of the total Rand value spent in the form of Dis-Chem Benefits (Dis-Chem does not utilise a points system). Dis-Chem provides detailed disclosures regarding its Dis-Chem Benefit programme: the opening balance, closing balance, revenue recognised during the year, and Benefits issued during the year as related to the deferred revenue from Dis-Chem Benefit. The value of Benefits issued as disclosed is presented after removing the Benefits that are not expected to be utilised (as with Pick n Pay Smart Shopper) meaning that the disclosed value is the net amount.

Dis-Chem discloses Benefits that are expected to be redeemed in its financial statements as well as having disclosed its Dis-Chem Benefit redemption rates for each of the years under investigation in this study. The redemption rates ranged between 80% and 90% for 2018, 2019 and 2021, so the midpoint of 85% was used in the calculation (Dis-Chem, 2018, p. 45; 2019, p. 59; 2021a, p. 72); for 2020 and 2022, the range disclosed by Dis-Chem was between 90% and 100%, so the midpoint of 95% was used in the calculation (Dis-Chem, 2020, p. 70; 2022, p. 67). To quantify the value of the CLP points, the expected value of the CLP points to be redeemed, as disclosed, was divided by the midpoint of the disclosed ranges of redemption rates; this calculation provided an estimated value of Benefits that ranges from its lowest (in 2019) at R184 052 940 to its highest (in 2021) at R331 069 410 (Table 5).

Table 5: Value of Benefits issued by Dis-Chem Benefit

	2018	2019	2020	2021	2022
Disclosed value of benefits issued (R '000)	159 749,00	156 445,00	178 662,00	281 409,00	182 479,00
Redemption rate	/ 85%	/ 85%	/ 95%	/ 85%	/95%
Value of benefits issued (R '000)	187 940,00	184 052,94	188 065,26	331 069,41	192 083,16

Source: Authors' own (Dis-Chem, 2018, p. 45; 2019, p. 60; 2020, p. 70; 2021a, p. 72; 2022, p. 67).

The total value of CLP Benefits that could have been taxed over the five-year period from 2018 to 2022 for Dis-Chem Benefit amounts to R1 083 210 774. Dis-Chem does not disclose CLP Benefits issued and redeemed in the same financial year, so these were not factored into the calculation of total CLP Benefits issued for the purposes of this study, as the value thereof is not determinable. Similarly, the value of CLP points issued by its CLP reward partners, where customers may earn additional CLP points for purchases at these reward partners, may

also not be included in the revenue for Dis-Chem. Consequently, the calculated value of CLP Benefits issued by Dis-Chem is considered a conservative.

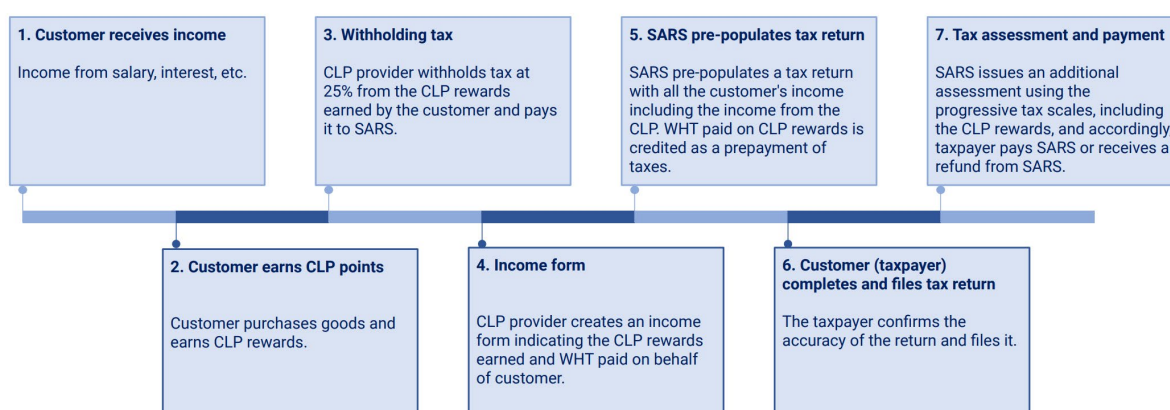
Based on the above calculations outlined in the three sections above, it is evident that customers for these three CLPs are provided with a considerable quantity of CLP rewards, even if these have been calculated on a conservative basis. Consequently, any tax applied to these CLP rewards may contribute to the much-needed tax revenues required by the South African fiscus. A remaining area of concern may be how to collect those taxes without placing an inordinate administrative burden on SARS. The method of collection is discussed below.

5. Method of tax collection for CLPs

5.1 Progressive and withholding tax

Pidduck, et al. (2019, p. 634) propose a withholding tax (WHT), where the WHT serves as a prepayment of taxes, as a solution for taxing CLP rewards. It is submitted that it is appropriate for the customer to bear the tax burden from the receipt of CLP rewards because the benefits accrue to them. A prepayment of taxes in the form of a WHT would rely on current WHT systems in place at SARS and would see the CLP provider withholding an upfront flat tax rate on CLP rewards on behalf of the fiscus. Then, upon assessment of the individual taxpayer, SARS could levy the progressive tax at the rate applicable to the individual based on the progressive tax tables applied in South Africa and apply a credit for any WHT already paid. Whilst the proposal for an initial WHT, serving as a prepayment of individual normal taxes, arguably increases the administrative burden for SARS, it is proposed that this WHT system use automation and existing third-party reporting channels to reduce the administrative costs. Although there are undeniably additional costs to be incurred in taxing CLP rewards in the hands of customers, the premise of this paper is to quantify the revenue for a sample of CLPs in order to go some way in determining if the revenue would outweigh the costs. Similarly, the proposed WHT would require CLP providers to obtain additional personal information from customers in order to facilitate third-party reporting to SARS. Consequently, some additional administrative costs are anticipated for CLP providers should the proposed system be implemented. However, CLP providers already track and report CLP records at the customer level, therefore the administrative burden for CLP provider is not anticipated to be overly onerous.

Figure 2: Outline of the steps for the proposed mechanism for collecting tax on CLPs



Source: Authors' own.

Additional consideration could be given to making the WHT a final tax at a flat rate. Whilst this will have the benefit of decreasing the administrative burden for SARS, it has the disadvantage of making the tax more regressive as it no longer feeds into the individual tax system. A proposed rate of 25% WHT is used for purposes of this paper because it is consistent with the withholding rate for independent contractors. This rate is considered appropriate solution given that SARS and CLP providers will not know at the time of withholding, where CLP customer fall on the 18% to 45% progressive tax table.

5.2 Calculation of tax revenue

The proposed rate of 25% was applied to the value of CLP rewards issued, and the cumulative potential tax revenue from all three CLPs was calculated for each of the five years studied. This calculation revealed that, from 2018 to 2022, the potential total tax revenue collected from the customers of the three CLPs could have amounted to R194 213 131, R190 921 805, R211 484 439, R284 506 781 and R259 626 886, respectively and that the combined tax revenue for this period could have been a formidable R1 140 753 042 (Table 6).

Table 6: Combined tax revenue from selected CLPs at a 25% tax rate

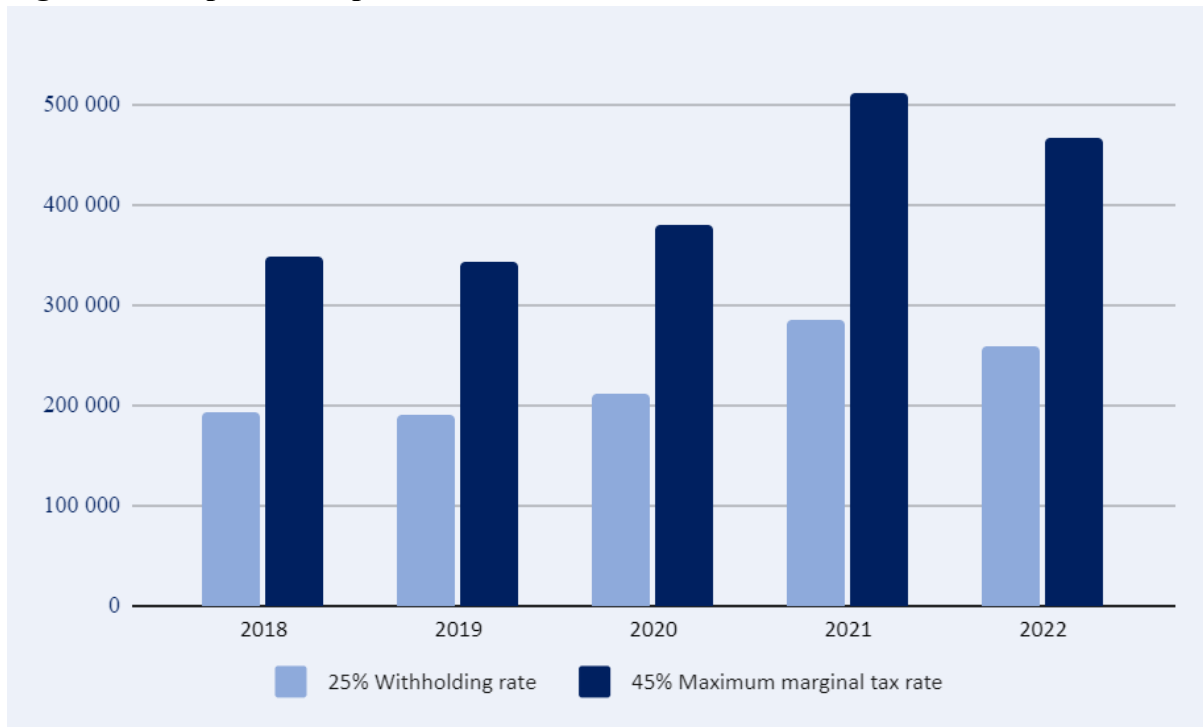
	2018	2019	2020	2021	2022	Total
Clicks ClubCard (R '000)	119 590,36	129 498,92	141 162,54	160 329,48	170 425,08	721 006,37
Pick n Pay Smart Shopper (R '000)	27 637,77	15 409,65	23 305,59	41 409,95	41 181,02	148 943,98
Dis-Chem Benefit (R '000)	46 985,00	46 013,24	47 016,32	82 767,35	48 020,79	270 802,69
Total (R '000)	194 213,13	190 921,80	211 484,44	284 506,78	259 626,89	1 140 753,04

Source: Authors' own.

Whilst collections of R1 140 753 042 over five years might seem trivial when compared to overall personal income tax of R555,5 billion which was collected in the 2021/22 year (National Treasury, 2022, p. 9), the potential revenue from CLPs could still make a marked difference to South Africa's fiscus. To better understand these cumulative results, the potential tax revenue from the three selected CLPs could be compared to the R40 billion that is needed to help stabilise public debt and the economy over the next four years (National Treasury, 2021a, p. 39). The calculated potential tax that could be collected from just these three CLPs in the form of this WHT amounts to 2,85% of this amount. The amount may, in fact, be even larger because higher income earners tend to participate more in CLPs than lower income earners (Cromhout, 2021, p. 12; 2022, p. 6; Cromhout & Netto, 2020, p. 9), making it plausible that the estimates of tax revenues above are conservative as customers of CLPs would be taxed at their marginal income tax rate, which may be up to 20% higher than the WHT rate applied in the calculations given. Consequently, for every 1 percentage point increase in the tax rate it would generate R45 630 122 in tax revenues. Therefore, taxation of CLP rewards at the maximum marginal tax rate of 45% would mean that, from 2018 to 2022, the combined potential total tax revenue that could have been collected from the customers of the three selected CLPs amounts to a formidable R2 053 355 476..

These tax revenues at a maximum marginal rate make it clear by comparison that a drastic increase in tax revenue may be expected at a higher marginal tax rate (Figure 4). It is also possible that figures based on the 45% tax rate are more closely aligned with the actual tax revenues that would be received under the proposed method of taxation than the figures calculated solely based on the proposed WHT rate of 25%.

Figure 3: Comparison of potential tax revenue at different rates



Source: Authors' own.

An approximation of the tax that an average active customer of each CLP would pay is helpful to better understand the potential impact of the proposed tax on the individual customer for each of the CLPs selected for use in this study. During 2021, Pick n Pay had 8.5 million active Smart Shopper customers; Clicks had 9.2 million active ClubCard customers; and Dis-Chem had 5 million active Benefit customers (Clicks Group, 2021b, p. 11; Dis-Chem, 2021b, p. 9; Pick n Pay, 2021b, p. 54). The 2021 tax revenues calculated above were divided by the number of active customers of each CLP, resulting in an estimate of the average value of tax that could have been collected from each active CLP customer assuming an even point distribution among them: the maximum value calculated was just R31.37, which was for Clicks ClubCard customers taxed at a tax rate of 45%. Although each customer is unique, and the tax paid would vary, this information provides an indication of the tax burden on a more granular level, per customer, for each CLP selected for use in this study.

During 2021, an average, active customer of Clicks ClubCard would have paid R17,43; an average, active customer of Pick n Pay Smart Shopper would have paid R4,87; and an average, active customer of Dis-Chem Benefit would have paid R16,55 in tax on their CLP rewards, at a tax rate of 25%. Thus, the impact on the average, individual, active customer would be arguably low. Furthermore, if these customers were all taxed at the maximum marginal rate of 45%, a customer of Clicks ClubCard would have paid R31,37; a customer of Pick n Pay Smart Shopper would have paid R8,77; and a customer of Dis-Chem Benefit would have paid R29,80 in tax on their CLP rewards. Thus, the impact on higher-income customers may also be considered low. Consequently, the tax is unlikely to impact taxpayer behaviour by discouraging participation in CLPs.

6. Conclusion

The implementation of a tax on CLP rewards as outlined in this paper provides a conservative estimate of total tax revenue amounting to R1 140 753 042 that could have been collected from the CLP rewards earned by customers of Clicks ClubCard, Pick n Pay Smart Shopper and Dis-Chem Benefit, in aggregate, for the five financial years 2018 to 2022. This amount applies if these rewards are taxed at a rate of 25%, but at the maximum marginal rate of 45%, the estimate rises to a formidable R2 053 355 476. It should also be noted, however, that this paper only investigates the impact of taxing three of South Africa's CLPs; therefore, a significant increase in tax revenues may be gleaned from the taxation of other CLPs not included in the scope of this paper.

In light of the significant potential contributions to tax revenue from just the three CLPs selected for this study, it is evident that the fiscus may have overlooked a substantial revenue stream that is gaining momentum in South Africa. Given the impetus behind CLPs and their exponential growth rate and increasing importance as a marketing strategy, it may be high time for the fiscus to re-evaluate the taxation of CLP rewards in the hands of customers.

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