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TOWARDS DISCOVERING THE ROLE OF FORMAL AND INFORMAL INSTITUTIONS IN TAX GAP ANALYSES IN SOUTH AFRICA

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Paper presented at the Biannual Conference of the Economic Society of South Africa
Cape Town, 3 September 2015

1. INTRODUCTION

One of the challenges of the post-apartheid government in South Africa was to inculcate that democratic constitutional rights imply citizen's responsibility with regard to tax compliance. Before the constitutional change of 1994 various factors threatened tax compliance: in the business community exchange controls were circumvented; the anti-apartheid slogan "no taxation without representation" eroded the personal and small business income tax bases or hampered their development; and the country's integration into international trade and financial markets opened its economic borders for tax leakage. Resurgence of compliance problems occurred in recent times when poor delivery of public services incentivised tax disobedience of some sort and, more specifically, resulted in non-payment of rates and taxes at local government level.

Recently there has been increasing international concern about tax base erosion (see the OECD's (2013) report). In a comparative study of tax compliance, Gordon and Li (2009) concluded that developing countries, when applying similar tax rates as developed countries, on average collect one third less tax revenue (as a percentage of GDP). Even during trying times after the international financial crisis, the IMF, the OECD, the UN and the World Bank, who collectively advised developing countries on how to improve tax compliance (IMF et al, 2011: 10), stated that "(t)he vicious circle of low tax morale and compliance - which reduces the lifeblood for funding public services - needs to be broken".

This raises the question: what drives high tax compliance? This paper aims: (1) to assess the methods to measure tax gaps and the factors influencing tax compliance, through a literature review; (2) to identify the various forms in which tax noncompliance manifested in South Africa since 1994, and document the policy measures to combat and enable it, respectively; and (3) to suggest the feasibility of and requirements for the calculation of the tax gap in South Africa and of undertaking regression analyses of the possible impact of identified explanatory factors (also interpreted where applicable as formal and informal institutions) on the observed compliance trends.

2. TAX GAP ANALYSES

The tax gap is defined as the "difference between the amount of tax that should, in theory, be collected … against what is actually collected." (HM Revenue & Customs, 2014a: 4). Ahmed & Rider (2013: 335) refer to the tax gap as those taxes not collected when taxpayers are not complying with the tax system. They indicate that a distinction should be made between tax avoidance (which include activities within the law to reduce or minimise the tax liability) and non-compliance (when taxpayers do not comply with their tax liabilities). It is the latter which causes the tax gap. Toder (2007: 1) refers to the gross tax gap as the

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"difference between tax liability in any year and the amount of tax that is paid voluntary and on time". There are three components to this gap: under-reporting, non-filing and under-payment (i.e. not paying the tax by the due date) (Toder, 2007: 1).

The IMF refers to two factors influencing tax gap definitions, i.e. compliance (the compliance gap), and the impact of policy on revenues (the policy gap) (Toro et al., 2013: 11). The former relates to the gap emanating from non-compliance, whereas the latter arises as a result of policy provisions allowing deductions or exemptions. When determining tax gaps, it is recommended that both the compliance and policy gaps are measured, as the latter provides significant information on foregone tax revenues to policymakers when they are considering changes to the tax regime.

Tax gap methodologies

Tax gap methodology can be categorised into top-down or bottom-up approaches (alternatively, macro or micro approaches).

Rubin (2011: 109) defines the *top-down approach* as determining the tax base from a single estimate; the latter is used to calculate a theoretical tax liability (i.e. how much tax would be collected if all taxpayers complied with tax legislation). The tax gap is the difference between the theoretical tax liability and the total amount of taxes collected. To apply the top down approach, two requirements must be met, i.e. information on the tax base to be verified independent from tax authorities, and an equally independent calculation of theoretical tax liability (Rubin, 2011: 110). The latter may be more complex for direct taxes as information on tax liabilities for individuals are dependent on tax reliefs and allowances, whereas the value or volume of sales would be required for indirect taxes. Despite the advantage of top-down approaches in providing a single estimate and producing more timely estimates, their biggest disadvantage relates to the uncertainty of the estimates (Rubin, 2011: 111).

A further sub-division is made in the case of the macro approaches. Fuest & Riedel (2009: 16) refer to procedures that use macro indicators such as monetary variables, as well as those that use information drawn from national accounts statistics. In the former case, since transactions in the shadow economy are mostly cash-based, the currency demand method econometrically estimates excess currency demand by using explanatory variables such as the average tax rate and a measure indicating the complexity of the tax system – these variables are proxies for changes in the underground economy. A second method is using physical inputs such as electricity to proxy economic activity.

The *bottom-up approach* refers to calculations of the tax gap from estimates of its various components. Rubin (2011: 109) indicates the UK uses data matching, tax information, risk registers and random enquiries to estimate these components. According to Braiotta, et al. (2014), bottom-up approaches are particularly used in instances where the tax gap is estimated by taxpayer type.

Gemmell & Hasseldine (2012: 8) distinguish between *macro and micro approaches* to measure the hidden economy or the tax gap[2]. Macro approaches aim to determine a single estimate of the size of the hidden economy (identifying the hidden income), whereas the micro approaches are geared towards determining the extent of noncompliance. Micro methods entail investigating missing tax or taxpayer income by way of auditing methods

[2] Rubin (2011: 109) mentions that in the case of direct taxes, top-down approaches do not measure taxable income; rather, they estimate aggregate income which includes the shadow economy.

(such as used to be employed in the US). Large and representative samples are required for this technique, which can then be scaled up using appropriate weighting.

Fuest & Riedel (2009: 11) also distinguish between the macro and micro approaches to measure domestic tax gaps, and emphasise that even though the former is less reliable and informative (as it relies primarily on aggregate measures), it may be the more feasible method to apply in developing countries where there is a paucity of micro data. However, they do emphasise the need to move in the direction of applying micro methods, particularly where tax audit information collected by national tax authorities can be employed. This would for example allow the tax gap analysis to be disaggregated into gaps by type of taxpayer (such as individuals and businesses).

Tax gap methodologies: Income taxation

According to Toro, et al. (2013: 15), the HMRC use three estimation techniques to measure the tax gap for noncorporation taxes (i.e. income, national insurance contributions and capital gains tax), namely: random audits, data matching and ad-hoc taxpayer segment models. Random enquiry programmes entail an extensive enquiry into the tax returns of a selected sample; the tax gap of the sample is then elevated to population estimates (HM Revenue & Customs, 2014b). Data matching allows for a comparison of reported income from other (third-party) sources with the aim of identifying undeclared income, as income data from these sources may contain income not reflected in internal sources (HM Revenue & Customs, 2014b). This technique may be more appropriate in instances where it is not possible to undertake random enquiries, such as cases where tax returns are not issued.

Since the availability of data may be a constraint in estimating the gap for direct taxes, Rubin (2011: 110) evaluates the practicality of using the top-down approaches to estimate the tax gap of direct taxes. He emphasises two important considerations in using these approaches: suitable information on the tax base and determining theoretical liability (i.e. how much tax would be paid if there is full compliance with tax laws). The former refers to data that is independent of the tax authorities; if it is not, the data do not provide any new information. Estimating the theoretical liability is more complex in the case of direct taxes as information on tax allowances and tax relief is required.

Rubin (2011: 113-118) discusses three categories of top-down approaches that may be considered in measuring direct tax gaps. First there are methods using national accounts data such as factor incomes, the compensation of employees, mixed income and gross operating surplus. One possible technique is to determine theoretical tax liability from factor income. Another technique entails determining the divergence between factor income and some other income measure.

A second category is to estimate the gap from macro models using a single estimate of income. Rubin (2011) highlights three macro models to determine the shadow economy (and hence potentially the tax gap), namely, monetary, latent variable, and other indicator methods. Monetary methods include taking account of cash in circulation or cash-deposits ratios, whereas the latent variable method uses 'multiple indicator multiple causes', a type of factor analysis to estimate the shadow economy (see Rubin, 2011: 117). Other indicator methods entail using measures of electricity consumptions or labour force measures.

A final category includes identifying discrepancies in labour force measures and direct surveys (Rubin, 2011: 118). The former entails comparing business to household surveys to identify the extent of undeclared workers; this is then used to determine the tax not paid by undeclared workers. Direct individual or household surveys are used as another method employed to obtain information on undeclared income.

Possibilities in estimating the tax gap for direct taxation in South Africa

From the discussion thus far it is evident that bottom-up approaches using micro data are more appropriate to estimate the gap for direct taxes. Data requirements are, however, heavily reliant on statistics produced and made available by tax revenue authorities. For example, in the case of the random enquiry programmes, access to random audits is needed to assess the extent of under declaration by taxpayers and involves a full examination of all documentation pertaining to the selected return (HM Revenue & Customs, 2014b). To the extent that such data are not yet accessible to researchers in South Africa, and taking into account confidentiality requirements (which necessitates anonymised data), alternative methodological approaches would have to be used in the interim.

One alternative is to follow the approach of Ahmed & Rider (2013), who estimate the potential income tax in wages. They used micro-simulation models to estimate the potential tax, and relied on detailed information on the tax bases, as well as a tax calculator (a computer program to assess tax liability). After establishing potential tax revenue, they estimate the tax gap by deducting actual tax collections. For salaried individuals, they use two micro level databases, the Household Integrated Expenditure Survey and the Labour Force Survey (Ahmed & Rider, 2013: 340). In the latter case, the Labour Force Survey contains information on wage income that they used to estimate potential income tax. These estimates are seen as upper bound levels since they do not have accurate information to account for tax credits and exemptions in the system at the individual level. Deducting aggregate estimates for charitable donations from the potential tax liability, they estimate a tax gap of about 0.136 billion US dollars, with a voluntary compliance rate of just over 50% of potential tax collections (Ahmed & Rider, 2013: 342).

3. DRIVERS OF TAX COMPLIANCE

We highlight various themes that receive attention in the literature about tax compliance.

Utility maximizing agents and economic deterrence

The seminal work of Allingham and Sandmo (1972) contained the first attempt to construct a framework to analyse tax compliance. Here, the authors frame tax compliance as a strategic decision, where actors attempt to maximize their utility, choosing the course of action with the highest associated payoff. A taxpayer may either declare his actual income (tax compliance) or may declare less than his actual income (tax evasion). While the former's payoff is known, the latter's payoff is dependent on whether or not the under-declaration is noted by the tax authorities. Should investigation reveal under-declaration, the tax evasion may lead to penalties or jail time, which are intended to serve as a deterrent against tax evasion. Hindriks, Keen and Muthoo (1999) however show that the incentives for tax evasion may be different for different income groups. They argue that lower income groups have little to gain from evading taxes, while for the rich, the converse is true.

Nonetheless, this notion that punishment serves as a negative incentive for compliance has since been expanded on in the literature. An example is Park and Hyun (2003) who modify the Allingham and Sandmo's (1972) framework. In their investigation of tax compliance in Korea (using experimental data), they come to the conclusion that taxpayers in Korea tend to have the same degree of tax compliance regardless of their income levels. This indicates that taxpayers may have a utility function characterised with constant relative risk aversion. The results indicate that for policy makers, increasing the fine or penalty rate may be the most effective way to increase tax compliance.

Keeping with the theme of using the threat of punishment as a deterrent against tax evasion, Mohdali, Isa and Yusoff (2014) use survey data of individual taxpayers comprising of self-employed and salary-earning employees to test the effect of the threat of punishment on the attitude, compliance and non-compliance of taxpayers in Malaysia. The surprising result is that the threat of punishment is negatively related to taxpayers' tax compliance. Since Malaysian taxpayers display a high tendency to comply with tax laws voluntarily, the threat of punishment could increase the desire of noncompliance as individuals feel they are being threatened for things (tax evasion) that they have no intention of doing. This tends to suggest that, if tax compliance is already high, excessive punishments for tax evasion may lead to decreased compliance.

The limitations of analyses of the utility-maximizing actions of taxpayers (e.g. Allingham and Sandmo, 1972; Yitzhaki, 1974; Cowell and Gordon, 1988; Park and Hyun, 2003), have led to the development of a subsection in the tax compliance literature attempting to identify the positive incentives that affect tax compliance.

Governance and the tax structure

One such expansion into the determinants of tax compliance has focussed on governance and the tax structure. In this respect, some authors (Cowell and Gordon, 1988; Alm, McClelland and Schulze, 1992; Falkinger, 1995) have considered the effect that public good provision has on tax compliance. Here the prevailing consensus is that citizens are expected to increase their tax compliance if they know that the tax revenue is used productively for the provision of public goods. Levi (1988: 52) refers to this as *quasi-voluntary compliance,* as compliance is dependent on receiving something in return from the government. These studies do however not consider the effect that the quality of public good provision has on tax compliance. Authors like Ali, Fjeldstad and Sjursen (2014) and Fjeldstad and Semboja (2001) have however taken this into account, and have included measures for the satisfaction regarding the quality of the public services provided. Ali, Fjeldstad and Sjursen (2014) show that in Kenya, Tanzania, Uganda and South Africa, tax compliance is likely to increase as citizens become more satisfied with the quality of the public goods being provided. Fjeldstad and Semboja (2001) show that the low levels of compliance in Tanzania seem to be correlated with the decline in quality, or complete absence of public services.

With regard to the tax structure, Das-Gupta, Lahiri and Mookherjee (1995) attempt to identify whether or not tax compliance in India is significantly affected by factors such as the tax structure, inflation, declining assessment intensity and traditional enforcement tools. To measure tax compliance, the authors construct an index of non-corporate income tax compliance[3]. After estimating the various models, they find results largely congruent with economic theory. Inflation has a strong negative effect on compliance and tax receipts, implying that taxpayers may have an incentive to delay their tax payments in periods of high inflation if the taxable amount is not adjusted for inflation – the so-called Tanzi effect. The tax structure, namely tax rates and the exemption limit, both have a significant negative effect on compliance and revenue. Lastly, the authors find that even though enforcement has a significantly negative effect on tax revenue, the effect on compliance is less significant. Furthermore, when testing the joint significance of all of the persecution variables used, the

[3] Defined as the ratio of actual tax income receipts (ITR) to the amount of tax income actually due

authors find that the effect of these variables to be insignificant. The authors also find that increased efficiency[4] of the tax authorities has a significant positive effect on tax compliance.

These results therefore have clear implications for tax policy, namely that the most effective way of increasing tax compliance would be to adjust the tax structure (tax rates and the exemption limit) and improve the efficiency, or the perceived efficiency, of the tax authorities. Furthermore, intensifying the threat of punishment seems to have a limited effect on tax compliance. This therefore implies that in some settings, positive incentives encouraging tax compliance, such as lower tax rates and higher levels of exemption, may be more effective than negative incentives discouraging tax evasion, such as increasing the threat of punishment. These types of studies however assume that all taxpayers, namely individuals and firms, partake in the financial sector. This is a vital assumption, given that firms are only subject to taxes when they make use of the financial sector[5]. However, as shown by Gordon and Li (2009), this need not be the case as firms may choose to avoid the use of the financial sector if the benefits from using the financial sector are outweighed by the costs of tax. In this case, firms can choose to transact only in cash, leaving no paper trail and thereby making their activities difficult for tax authorities to monitor. This means that tax revenues will be lower even though the remaining firms may be compliant. This implies that policy makers attempting to increase their tax revenues cannot only consider policies aimed at improving tax compliance, but need to also consider encouraging participation in the financial sector as well. In this respect, Gordon and Li (2009: 857) argue that by improving the effectiveness and efficiency of the financial sector, more firms will use the services on offer, despite the tax implications of doing so.

Political Legitimacy

Another strand of the tax compliance literature focuses on the political legitimacy of the political institutions. Here, legitimacy can be described as the “belief or trust in the authorities, institutions, and social arrangements to be appropriate, proper, just and work for the common good” (Fjeldstad, Schulz-Herzenberg and Sjursen, 2012: 7). Various authors (Kirchler, Hoelzl and Wahl, 2008; Kastlunger *et al*, 2013; Kogler *et al,* 2013) have examined the view that the degree to which citizens trust their governments is important for tax compliance, with the general consensus being that trust in political institutions is positively correlated with tax compliance.

These studies have traditionally focussed on developed countries, with little attention being paid to developing countries. However, the issue of legitimacy is especially problematic in Africa, given that many countries have struggled to establish a lasting political order post-independence (D’Arcy, 2011; Ali, Fjeldstad and Sjursen, 2014). In this respect Ali, Fjeldstad and Sjursen (2014) find very little evidence that political legitimacy is correlated with tax compliance in Kenya, Tanzania, Uganda and South Africa. The authors do however find evidence to suggest that the corruption[6] of tax officials significantly reduces tax compliance in South African and Uganda. These findings are reinforced by D’Arcy (2011). However, it must be noted that both Ali, Fjeldstad and Sjursen (2014) and D’Arcy (2011) use the same dataset, namely the Afrobarometer surveys, thus it is not surprising to see similar results.

[4] Efficiency refers to ‘Assessment Efficiency’, which the authors calculate as: 1 – Work Disposal Rate (WDR). WDR is calculated as the ratio of tax assessments completed during the year to the number of tax assessments for disposal.

[5] This assumption is important for the argument made by Gordon and Li (2009)

[6] Respondents were asked to rank their level of satisfaction with their respective government’s handling of crime, conflict, terrorism, and corruption ranging from 1 = “very badly” to 4 = “very well”.

Social Factors

It is reasonable to assume that compliance will also be affected by the social interactions of tax payers as well as their perceptions of other tax payers. In this respect, the focus shifts from the impact of formal to informal institutions on tax compliance.

An example of the impact of social factors on tax compliance can be seen in the case of Tanzania, where Fjeldstad and Semboja (2001) show that the larger the observed percentage of people in a community that do not pay taxes, the lower the perceived risk of being caught and prosecuted. In this respect, if a taxpayer knows that the other taxpayers in his/her community do not comply and are very rarely caught, this greatly incentivises him/her not to comply. While this may hold in Tanzania, Ali, Fjeldstad and Sjursen (2014) show that social factors, once again proxied by the perception of other people's compliance, do not affect tax compliance as strongly in other African countries, namely Kenya, Uganda and South Africa.[7] The authors do however show that taxpayers in South Africa and Tanzania are more likely to have an attitude of tax compliance if they perceive that their social, ethnic or cultural group is treated fairly in comparison with other social, ethnic and cultural groups.[8] Thus, in an African context there appears to be some support for the notion that social factors matter when determining tax compliance.

In a developed country context, Wenzel (2005) aims to test the effect that ethics and norms may have on tax compliance. He considers the possibility that taxpayers may act based on their moral beliefs and that these beliefs may be influenced by the social consensus. The author obtains data on these moral beliefs and tax compliance through questionnaires, and uses various two-directional regressions in order to test for the relationship between ethics and norms, and tax compliance. He finds that ethics and social norms do seem to affect tax compliance. However, reverse causality appears to exist as well, with tax compliance affecting social norms and ethics. In this respect, it seems as if tax compliance is consistent with the moral beliefs of taxpayers, with the 'moral' taxpayer more likely to fully declare his/her income. However, given the endogeneity present, it is difficult to establish in which direction the causality flows.

Literature on South Africa

This burgeoning interest in the study of tax compliance has also found its way to South Africa. In 2013, the Davis Tax Committee was established to "assess South Africa's tax policy framework…" (Davis Tax Committee, 2014), a brief inevitably investigating tax compliance as well. Despite this burgeoning interest, limited research has taken place with regard to taxpayer perceptions in South Africa (Oberholzer and Stack, 2014: 251). This is especially troubling given that policy makers have often commented on the low levels of tax compliance in South Africa. This was acknowledged by the then Minister of Finance, Trevor Manuel, as early as 2002, when he said: "The compliance levels in SA are unacceptably low. There are still too many individuals and businesses who should be registered for tax that are not[9]" (Hartley, 2002).

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[7] A possible explanation for this is that the Tanzanian population is relatively more homogenous than the other countries studied. This implies that the reference group for the Tanzanian citizen is more likely to be the whole population, where in the other countries this is less likely to be the case.

[8] Respondents were asked describe the frequency with which they perceived their own ethnic group to be discriminated against where 4 = always and 1 = never.

[9] It must however be noted that it is unclear whether his comments were intended as a mere value judgement - namely that South Africa's tax compliance is low compared to what is expected by policy makers, whether South Africa's tax compliance is objectively low – when, for example compared to other similar economies.

Recently however, two studies have been published considering taxpayer perceptions in South Africa. As mentioned earlier, Ali, Fjeldstad and Sjursen (2014) attempt to study the tax compliance attitude of citizens in Kenya, Tanzania, Uganda and South Africa. They apply a binary logit regression to data from the 5th round of the Afrobarometer survey for 2011-12, regressing the explanatory variables on the binary tax compliance variable (1 if the individual is tax compliant and 0 if the individual displays an attitude of noncompliance). The results for South Africa can be summarised as follows. Respondents are more likely have an attitude of tax compliance if they believe that enforcement will make tax evasion more difficult. Respondents are also more likely to have an attitude of tax compliance if the government improves the provision of certain public services, such as policing. The perception of other people's compliance however has a limited effect on the tax compliance attitudes of the respondents. Political legitimacy however appears to have no effect on tax compliance. Lastly, they find that knowledge about the tax system has a significant impact on tax compliance attitudes in South Africa. If individuals perceive it to be difficult to find out what taxes they need to pay, where they can pay them and how much they need to pay, they are less likely to have an attitude of tax compliance.

These results therefore imply that there is scope for improving the attitudes regarding tax compliance in South Africa. This could be achieved via a combination of improving the enforcement of taxes, improving the government's performance in terms of the provision of public services, and improving the efficiency and clarity of the tax paying process thereby increasing individuals' knowledge about the tax system.

Oberholzer and Stack (2014) also conduct an investigation into the perceptions of South African taxpayers on taxation issues. Given that there is no standardised scale to measure tax perceptions, the authors employ an extensive literature review to construct a questionnaire of 23 questions, each related to a specific section of the tax compliance literature. This allows them to test the responses received from South African taxpayers against what economic theory predicts. The questions include issues such as the age, gender, race, language, education, income and employment status of the respondents. The questionnaire also poses questions about the respondent's support of the government, whether or not they are registered with the South African Revenue Services (SARS), perceptions about the future of South Africa and their view on income inequality. The authors target taxpayers in the Tshwane metropolitan area and make use of an external independent company to carry out the data collection process. The results of the questionnaire indicate that South African respondents generally display tax compliance attitudes much in line with what has already been discussed in earlier subsections above.[10]

4. TAX LEAKAGES (NON-COMPLIANCE) IN SOUTH AFRICA AND POLICY RESPONSES

Forms of tax leakages

The standard textbook distinction is between tax avoidance (which is legal) and tax evasion (which is illegal) (see Section 2). Tax avoidance is the result of intended allowances (IMF: policy gap – see above) and unintended loopholes (IMF: compliance gap). The latter originates in poor or inconsistent tax laws and regulations and their enforcement by the revenue authority. Tax evasion is related to factors such as the following:

[10] The full results of the study are far to in depth to be included here.

- Taxpayers' assessment of the risk equation, that is, the ratio between the benefit of not paying tax and the probability of being caught and the associated cost (fine or jail sentence) (see Keen Kim and Varsano, 2006).
- The legitimacy of the ruling government and citizens' view about their taxpayers' responsibilities.
- The general view about honesty in complying with legal obligations, as held by individuals or groups of individuals in society and which reflects different cultural norms and values.
- The efficiency of government services, that is, the benefits received from paying tax (an interpretation that is complicated when the ability-to-pay approach to taxation is in force and taxpayers attempt to individualise expected benefits as if a benefit approach applies).

Policy measures pertaining to tax base broadening and compliance

An important context for our analysis of tax compliance in South Africa is the attempt by the fiscal authorities to both broaden the tax base by taxing untaxed or hard-to-tax subjects or groups, and stem leakages from the expanding tax base. This section gives an overview of these efforts since 1994 .Annexures A and B contain an outline of identified base broadening and base reduction measure, respectively, from 1994 to 2015, arranged by type of tax or tax benefit.[11] Where available, money values of the measures are provided – most of the time pertaining to the year of introduction.[12]

Governments obviously have – or should have! – a vested interest in a tax system that generates income while complying with allocative and administrative efficiency and fairness. After 1994, the focus initially was on "… improving the tax administrative capacity of the South African Revenue Services (to enhance tax compliance and thus revenue collections), in order to ensure essential base-line support for future reforms. Subsequent tax reforms, such as simplifying the tax system, broadening the tax base and reduce tax rates, have supported other policy initiatives of government ensuring a stable, neutral, efficient and equitable tax regime" (National Treasury, 2007: 2). These tax imperatives remain in the forefront of the fiscal mind, as the following statement demonstrates (National Treasury, 2004: 93): "The low effective tax rates in specific sectors of the economy have continued to act as a catalyst for discussions between SARS and these sectors to understand the causes of the low rates and to collaborate in addressing them. As an example, the banking sector has agreed to look into its effective tax rate following g discussions with SARS. Discussions with this and other sectors have yielded fruitful results but much remains to be done."

We distinguish three concepts: enhanced compliance, base broadening (narrowing) and tax rate increases. (a) Enhanced compliance refers to compliance with tax laws and regulations, given the tax base and existing rates. It is about ensuring that the tax burden is distributed as officially intended, given the existing tax base and tax payers, and that any tax gap, i.e. the difference between the potential and actual revenue yield, is reduced. (b) Base broadening (narrowing) is about expanding (shrinking) the tax base (arguably in varying degrees of equity) in terms of the Haig-Simons definition of tax liability on the basis of purchasing

[11] This table was compiled from data in another table which the authors constructed. The latter presents all the relevant tax measures chronologically, but is too long for publication.

[12] See National Treasury (2004: 79) for a quantification of tax relief measures from 1994/95 to 2003/04. The table includes an amount of R62.0m for "Adjustments to personal income tax rate structure". This is a seriously misleading statement, as most of the tax relief was to eliminate or reduce bracket creep; in other words, to avoid increases in the real tax burden because of the inflation of taxable personal income.

power. This allows for country-specific choices of the nature of fairness and the expansion of the tax base to include hitherto untaxed or partially taxed groups as well as to establish new taxes. Our classification of tax measures also include the identification of measures that in- or unintentionally encourage or facilitate non-compliance and that erode the tax base, as well as measures aimed at protecting the existing tax base. The latter includes the adjustment of monetary thresholds to maintain the real value of the tax yield. (c) Tax rate increases are about higher rates intended to increase the real revenue yield and/or to change the distributional incidence of the tax burden. In the third column of the table in Annexure A we use the information to infer the formal or informal institution (in the new institutional sense of the word) that informed the tax measure. For example, three of the policy measures with regard to the broadening of the personal income tax base (Table A-1 of Annexure A), have been interpreted as necessary because of tax rules that enabled tax avoidance. Invariably some of the interpretations may be questioned. Annexure B was easier to compile: it contains the formal tax rules that unambiguously resulted in base reduction. Table 1 provides a summary of the measures in the annexures, categorised with regard to the most important taxes and type of institution (formal and informal). This table should be seen as a first attempt of identifying institutions, especially as more work is required regarding informal institutions.

There are ambiguous trends as well. Some tax measures may amount to an increase in the real tax burden by stealth, such as when fiscal drag is not fully eliminated with respect to personal income tax or, more generally, when monetary thresholds are not indexed. Furthermore, it is necessary to distinguish between static and dynamic effects. The introduction of the graduate corporate income tax schedule to incentivise small and medium sized enterprises, for example, could in the static sense of the word be viewed as an erosion of the corporate tax base. Dynamically speaking, this very step may be a credible way of facilitating the movement from the informal into the formal sector of the economy and thus expanding the tax base over time. Taxation and tax expenditures (i.e. subsidies) aimed at addressing negative and positive externalities (i.e. Pigouvian measures) also entail some ambiguity. The essence of a Pigouvian tax is that it is supposed to reduce consumption of the particular good or service to a societal optimal level. When the particular tax becomes a luctrative money spinner for the National Treasury, such as is the case with so-called sin taxes, the fiscal authorities develop a vested interest in maximising its revenue yield and it becomes virtually impossible to distinguish between the internalisation of the negative externality and measures (and an undisclosed motive) of revenue enhancement. In the latter case the measure also embodies elements of tax base broadening. We therefore register such alleged Pigouvian taxes and tax subsidies as well, at least to register that they have a meaningful impact on revenue yield (whether as an increase or a decrease, i.e. cost, for the fiscus).

Another complicating factor from a classification point of view is when a particular tax has explicit equity features, such as the tax treatment of medical scheme contributions, where the aim is to relieve the burden on the poor and simultaneously cap the allowance at a certain income level. A case in point is the replacement of the deductibility of medical scheme contributions in terms of the progressive tax system, with a lump-sum tax credit. The former resulted in a progressive tax benefit; the latter amounts to a regressive tax benefit. The replacement step is on the one hand an increased benefit for lower-income groups and thus a reduction of the tax base; on the other hand, a protection of the tax base with regard to higher income groups. This ambiguity results in having to classify such a measure – and others similarly – as both a base broadening and base narrowing step.

One also gets the impression that over the years, many of the obvious methods to improve compliance, i.e. those with relatively big revenue implications, were addressed. The following statement by National Treasury (2004: 74) resonates with this observation: "As the tax system approaches an appropriate structure, reflecting enhanced efficiency and fairness, the net incremental benefits from further improvements become more modest." The type of changes in recent years tends to be more sectoral or micro in nature, reflecting fine-tuning of the particular tax type. Also, occasionally notice is given of issues that are being investigated, such as when the following issues with obvious tax compliance implications are reported as matters for tax research (National treasury, 2012: 59): taxation of financial instruments (including derivatives); long-term insurance companies – review of the taxation, accounting and regulatory practices of the four-fund system; and taxation of income from capital (interest income, dividends, capital gains, rental) to be reviewed to ensure greater equity and minimise opportunities for tax arbitrage. We tried to steer away from announcements of intent and to record measures as and when they were actually implemented, although here and there we did register intention, especially in recent years to ensure they are on the radar while realising that implementation still lies ahead. In various cases the tax change was announced without an estimate of the revenue implication, reflecting ignorance, or belief that it is the right thing to do, e.g. switching from a source to a residence tax base, or when an estimate of the increase in the number of small businesses that register will probably at best be a wild and useless guess.

Another category of change that occurs from time to time, is the ironing out of inconsistencies, often unintended, that are discovered retrospectively and that enable avoidance with horizontal inequity (uneven playing fields) and compliance discrepancies as a result. A case in point is the reintroduction of an excise duty on computer monitors (National Treasury, 2011: 71), when it was discovered that they were used as televisions, thus putting the users tax wise in a better position than the owners of televisions (which were subject to excise duties).

The extent to which these requirements are met thus depends on both the institutional arrangements surrounding the collection and use of taxes and the nature and structure of the tax system. We will trace the context with regard to these two aspects.

Table 1: Summary of tax measures, by tax type and formal and informal institution

(Δ = change)

Type of Tax	Institution	Improved compliance	Base broadening	Base narrowing	Higher rates (real terms), tax replacements
Personal income tax	Formal (tax rule Δ)	1. Tax avoidance reduced	1. Horizontal inequity reduced 2. Monetary values adjusted: base protection)	1. Vertical inequity reduced 2. Pigouvian tax subsidy	
Corporate income tax	Formal (tax rule Δ)	2. Tax incentive or avoidance opportunity (loophole) withdrawn	3. New tax (SMEs, dynamic view) 4. Monetary values adjusted: base protection)	3. Pigouvian tax subsidy, selective industrial development (MIDP, IDZs, biofuels, youth subsidy and others) 4. Graduate corporate rate (static) 5. Accelerated depreciation allowances 6. Abolition of tax 7. Legimitising nonliability	1. Non-neutral tax replacement

Table 1: Summary of tax measures, by tax type and formal and informal institution

(Δ = change)

Type of Tax	Institution	Improved compliance	Base broadening	Base narrowing	Higher rates (real terms), tax replacements
Tax incentives (general)		3. Market based solution to negative externalities		8. Pigouvian subsidies: education, dona-tions, conservation, car manufactur-ing, emissions reduction, energy efficiency	Δ
Capital gains tax	Formal (tax rule Δ)	4. Tax avoidance reduced	5. New tax	9. Differential	2. Rate increases
VAT	Formal (tax rule Δ)		6. Differential (withdrawal of zero-rating)	10. Differential (zero-rating)	
			7. Extension vendor registration		
Excise taxes & customs duties	Formal (tax rule Δ)	5. Reinstate duty earlier abolished	8. Pigouvian tax	11. Abolition of taxes	3. Rate increases
			9. New tax luxury goods	12. Pigouvian subsidy (MIDP)	
Levies and user charges	Formal (tax rule Δ)		10. Pigouvian tax		4. Neutral tax replacement
			11. Monetary values adjusted: base protection)		5. Rate increases
					6. New tax
Tax base & Accounting method	Formal (tax rule Δ)	6. Accrual: avoidance reduced			7. Residence tax
Reform of entities and administrative capabilities, and of formal tax rules, regulations and procedures	Formal (tax rule Δ)	7. SARS Administrative efficiency Compliance cost reduced	12. SARS Administrative efficiency Compliance cost reduced		8. SARS Administrative efficiency
		8. Tax amnesty, avoidance prevention and anti-evasion measures	13. Tax amnesty, avoidance prevention and anti-evasion measures		9. Tax amnesty, avoidance prevention and anti-evasion measures
	Informal	9. Administrative efficiency	14. Administrative efficiency		10. Administrative efficiency
		10. Tax education	11. Tax education		

Institutional arrangements

One of the biggest challenges of the post-apartheid government in South Africa was to inculcate that democratic constitutional rights implies imply responsibilities of tax compliance. As mentioned in the introduction, before the constitutional change of 1994 there were a number of factors that threatened tax compliance.

The most important corrective institutional change was the reform of the tax authorities, with the establishment by law of the South African Revenue Service (SARS) as an administratively autonomous organ of the state in terms of South African Revenue Service Act 34 of 1997 (RSA, 1997).

This reform gave them the ability to attract very competent tax experts[13] and to greatly improve communication with and education of the entire tax community. SARS was destined to operate from more than 45 service centres to educate South Africans about their tax obligations in order to improve compliance (National Treasury, 2001: 66), thereby strengthening norms and behaviour of tax responsibility in the democratic state (see bottom row of Table 1). SARS remained aware of the importance of tax compliance education (see, for example, National Treasury, 2004: 92)[14] The educational programme was accompanied by various organisational and process changes to reduce compliance cost, such as e-filing, the collection system known as SITE (Standard Income Tax on Employees)[15] and programmes to promote tax compliance of small business and newly enfranchised citizens (see, for example, National Treasury, 2006: 82; 2008: 56, 63). The latter included simplifying the tax forms and reducing the number of returns that must be filed (National Treasury, 2002: 85). Various measures were put in place to improve compliance (Department of Finance, 2000: 71), such as:

- Strengthening of the anti-avoidance provisions of the Income Tax Act;
- Requiring 'declarations of good standing' before taxpayers can obtain government contracts or permission to invest outside the country;
- Publishing the names of tax offenders;
- Launching of a multi-pronged programme to reduce value-added tax and customs fraud, including reducing the number of international border posts; and
- Introduction of a fraud hotline.

The fiscal authorities faced the challenge of ensuring that the Income Tax Act conformed to the Interim and Final Constitutions (National Treasury, 2007: 10). To the effect education and tax reform measures and enforcement measures went hand in hand. Gradually, SARS's tone also became more assertive.[16] Intrinsic to all of this is taxpayer integrity, on which the Government relies for improved compliance results (National Treasury, 2006: 82) – a clear recognition of the importance of informal institutions (i.e. norms of behaviour) in the new institutional economics sense of the word.

In our summary tabulation of the base broadening measures and new tax incentives (Table 1, as derived from Annexures A and B) we inferred that the following factors were instrumental in tax leakage, which was why rectifying measures were taken: tax rules enabling avoidance or evasion, inefficient administration (including compliance procedures and practices), tax measures to internalise negative externalities, and poor or incomplete registration of taxpayers in hard-to-tax groups (notably the informal sector, small and medium-sized businesses and the financial sector).

[13] The establishment of a high profile tax office in Sandton to better service the corporate sector is a case in point.
[14] It is stated that SARS will build on its successful 2003 filing season by launching an intensive taxpayer education campaign in 2004.
[15] Subsequently terminated when its usefulness was overtaken by the functionality of e-filing.
[16] This is evident from the following (National Treasury, 2002: 69: "SARS … has introduced a new assertiveness in its approach to compliance with the tax and customs laws." Various administrative steps were listed (National Treasury, 2002: 69-70).

The following measures established new base reduction measures: various tax incentives, which were informed by arguments related to positive externalities, equity and ability-to-pay considerations and, in general, a preference for government intervention sometimes based on dubious arguments.

Tax reforms

The major base broadening tax reforms constituted the introduction of a tax for small business, the subjection of financial services to value-added tax (VAT), the shift from a source to a residence-based tax dispensation, the introduction of a capital gains tax (recognised for its role to reduce corporate income tax leakages), reduction in import duties in terms of the membership of the World Trade Organisation (WTO), using excise tax to build an element of progressiveness into the tax system.[17] The introduction of a graduate corporate tax structure, as stated earlier, may in the long run turn out to be base broadening as well.

A worrisome feature has been the persistence and increased number of base draining tax incentives, especially without evidence of their cost-benefit advantages. The huge tax benefit afforded to the development of the motor industry and, more recently, selective tax incentives supportive of certain industrial sectors or subsectors (including urban and industrial development zones) are cases in point. The tendency to fall back on tax incentives go against the view expressed by the Katz Commission (see National Treasury, 2007: 12): "In recent years, Government has focussed its efforts to minimise on the use of selective tax incentives, thereby providing scope for reducing the statutory tax rates that are applied to a broad tax base. It is advanced that this is the most appropriate means to promote economic development, rather than relying on selective incentives that erode the tax base, distort investment decisions and complicate the tax legislation and administration."

5. THE WAY FORWARD – FUTURE RESEARCH AVENUES

This study is an exploratory analysis of tax compliance in South Africa, in which we presented a survey of the literature and identified the nature of (non-)compliance in South Africa by cataloguing the inferred institutions (in the new institutional sense of the word) that enable avoidance and evasion (see Table 1) as well as the policy attempts to broaden (shrink) the tax base (see Annexures A and B). Our preliminary findings suggest there are two avenues of future research. One is to estimate the extent to which there is non-compliance in South Africa, particularly in the case of direct taxes. The first best option would be to apply random enquiry programmes, as pursued in the UK and US. This can be done if it is possible to access anonymised data from tax authorities. A starting point could be to determine first estimates using the techniques in Ahmed & Rider (2013), and work towards a more refined estimate as more and better data become available.

A second research path is to explore the factors determining tax compliance. Previous studies (see Oberholzer & Stack (2014) and Fjeldstad et al. (2012) earlier on) have provided some evidence in this regard, and further quantitative analyses can add to the existing literature, particularly with a more expanded sample of taxpayers (Oberholzer & Stack (2014) had a sample of 260 respondents), and investigating the distinct implications of the impact of identifiable formal and informal institutions.

[17] Largely in order to compensate somewhat for the regressiveness of VAT.

6. CONCLUSION

This paper presented an overview of the literature on tax compliance and non-compliance. As in all countries, South Africa implemented many measures since 1994 to broaden the tax base. Many measurers were also implemented that amounted to a narrowing (erosion) of the base and the latter tendency seems to be increasing as evidenced by the rising number of tax incentives. This necessitates a proper understanding of the size and nature of the tax gap, which is a matter for further research, as is an investigation into the formal and informal institutions that impact on compliance.

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ANNEXURE A

CATEGORIES OF BASE BROADENING (IMPROVED COMPLIANCE; REDUCED LEAKAGE; MAINTENANCE OF REAL TAX VALUE))

Table A-1: Personal income tax measures

Tax measure	Details / Comment	Inferred non-compliance feature	Source
1. Curtail fringe benefits	As from 1 May 1995 the value to be placed on any second or subsequent vehicle, not used primarily for business purposes, will be determined at 2,0 per cent per month of the vehicle cost.	Horizontal inequity	DoF, 1994: 5.5
2. Taxation of lump-sum payments on termination of service	Ruling about the effective income tax rate to apply such that tax avoidance is prevented.	Tax rules retrospectively viewed as enabling excessive avoidance opportunities	DoF, 1995: 5.7
3. Limitation placed on various employee deductions	Limited to the following: business travel deduction against car allowance; certain medical expenses; contributions to pension and retirement annuity funds; donations to certain public benefit organisations; specific expenditure against allowances of holders of public office; and wear and tear allowances on equipment.	Tax rules retrospectively viewed as enabling excessive avoidance opportunities	NT, 2002: 83
4. Capping of medical scheme contributions	▪ New regime introduces monthly monetary caps for tax-free medical scheme contributions (with the caps to be adjusted annually) ▪ Taxpayers ⩾65: full deduction for all medical expenses.	Tax rules retrospectively viewed as enabling excessive avoidance opportunities	NT, 2006: 70,73 NT; 2007: 70; 2009: 56, 62
5. Further reforms of the tax treatment of medical scheme contributions	▪ Income tax deductions for medical scheme contributions for taxpayers below 65 years to be converted into tax credits. ▪ Where contributions plus out-of-pocket medical expenses exceed 7.5% of taxable income, they can be claimed as a deduction against taxable income.	No noncompliance; change tax system for equity and fiscal cost reasons; possibly also elements of base narrowing.	NT, 2012: 45
6. Income tax "relief"	▪ Periodic partial or full elimination of fiscal drag ▪ Full elimination is preservation of tax base in real terms; partial elimination is increase in tax base (burden in real terms) by stealth	Protecting income tax base in real terms; sometimes increasing it by stealth	NT, various years; e.g. 2011: 63, 67-68; 2012: 45, 49, 50; 2013: 45, 49;

Table A-2: Fringe benefit tax			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Increase in PAYE withholding rate on motor allowances and fringe benefit on company cars	The deemed private kilometres (i.e. assumed to have been driven for private use) for individuals who receive motor vehicle allowances will be increased to 18 000 p.a., and the monthly taxable fringe benefit of a company car will be increased to 2.5% of the determined value of the vehicle, effective from 1 March 2006.	Tax avoidance rules retrospectively assessed to be too generous (presumably horizontal inequity ***Revenue = R1.37bn***	NT, 2006: 70,73
2. Travel (motor vehicle) allowances	▪ The deemed business kilometre procedure to be scrapped from 2010/11. ▪ Taxpayers who are required to use their personal vehicles for business purposes will still be able to keep a logbook to claim business travelling expenses.	Removing a practice deemed (ex post facto) to have been unjust.	NT, 2009: 63
3. Company car fringe benefits	Car manufacturers that import vehicles calculate the fringe benefit at cost. To align the treatment of company car fringe benefits for all employees (whether or not they work for a vehicle manufacturer), the actual retail market value is to be used in all cases (phased in over 4 years).	Tax rule enabling tax avoidance – now amended	NT, 2014: 49
4. Measures to limit tax avoidance through salary structuring.	▪ Tightening company car fringe benefit rules ▪ Employee deferred compensation and insurance schemes to be taxed fully as fringe benefits on a monthly basis	Tax rule enabling tax avoidance – now amended	NT, 2010: 72, 78
5. Fringe benefit tax: occasional free service	Withdrawal of employers' allowance to provide employees with occasional services to the value of R500 that is not included in the income of the employee.	Tax rule enabling tax avoidance – now amended ***Revenue = R5m***	NT, 2002: 84
6. Bursaries and scholarship for further education	Bursaries and scholarships for further education are under specified conditions exempt from income tax in the hands of employees.	Education as positive externality; rule legitimising nontax liability	NT, 2002: 82
	To simplify matters, bursaries and scholarships for current and future employees to be tax-exempt as long as the employer's funds go directly to tuition and tuition-related expenses, and the employee agrees to repay the employer if the employee fails to fulfil their scholarship or bursary obligations		NT, 2006: 76
	<u>Bursaries to relatives of employees</u>: To facilitate employer- sponsored education and training of the dependants of low-and middle-income workers, it is proposed that this tax-free fringe benefit be increased to R10 000 p.a. for employees earning up to R100 000 p.a.		NT, 2008: 65

Table A-3: Corporate income tax			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. General export incentive scheme	Withdrawal of income tax exemption	Tax rules enabling tax avoidance – now withdrawn	DoF, 1994: 5.5
2. Close corporation income tax	Loopholes closed through various measures (including procedural reforms)	Tax rules enabling avoidance – now withdrawn	NT, 2001: 81
3. Graduate rate structure for SMEs	▪ 15% on first R100 000 taxable income and 30% thereafter ▪ Extended in 2002.	Tax rule (new) to broaden tax base (dynamic view – see Annexure 2, Table 3 for opposite view)	DoF, 2000: 80; NT, 2002: 78.
4. Tax pertaining to cross-border flows	Exemption from tax on income arising in certain designated foreign countries to be repealed, and taxes on company expatriation to be extended to discourage offshore flows	Tax rules enabling avoidance – now withdrawn	NT, 2003: 72, 88
5. Ring-fencing tax base	Losses from secondary trades (e.g. "weekend" businesses) to be ring-fenced to prevent offset of losses against other types of income.	Tax rules enabling avoidance – now withdrawn ***Revenue = R50m***	NT, 2003: 72, 79
6. Protecting company tax base	Income tax exemption for gold share companies and the international headquarters company regime to be eliminate	Tax rules enabling avoidance – now withdrawn	NT, 2003: 72, 90-91
	Various measures to avoid erosion in respect of: restricting debt; taxation of long-term insurers (four funds); unlisted real estate investment trusts; hedge funds; uniform cross-border withholding.	Tax rules enabling avoidance – now withdrawn	NT, 2013: 53-56
	Various steps envisaged to curtail tax leakage via international tax havens	Inadequate tax rules enabling avoidance – now amended	NT, 2005: 90
7. Protection of South Africa's intellectual property (IP) rights tax base	Certain SA companies seek ways to shift this intellectual property offshore as exchange controls are gradually lifted. Measures to remedy the potential loss of IP and the impact on tax revenue collections will be introduced. (At this stage statement of intent)	Tax rules identified as not protective of tax base (risk of base erosion)	NT, 2007: 63, 76
8. Secondary tax on companies (STC) and Dividend withholding tax	Reducing the rate from 12.5% to 10.0% and broadening the base.	Replace company tax on distributed earnings (dividends) with final withholding dividend tax on beneficiaries	NT, 2007: 62, 67, 68
	Second phase of reforms to the STC, culminating in the introduction of a final withholding dividend tax (10% envisaged) at shareholder level in 2009		NT, 2008: 56, 61
	Final set of amendments to support dividends tax reform; final implementation second half of 2010		NT, 2009: 56, 64
	Implementation postponed to 1 April 2012		NT, 2011: 71

	▪ For equity reasons (high-income individuals tend to receive a larger portion of their income in the form of dividends and capital gains) it is proposed that the dividend withholding tax come into effect at 15% – five percentage points higher than the previous secondary tax on companies rate. ▪ Income from capital can be derived as interest income, dividends or capital gains, all of which should be taxed equitably. ▪ Pension funds that are exempt from income tax will receive their dividends tax free.	Replacement tax; revised rates for equity reasons tax neutrality between different forms of capital income ***Net revenue gain = R1.9bn = R7.45bn (loss: abolition of STC) – R5.50bn (dividend withholding tax)***	NT, 2012: 45, 50-51
9. Closure of dividend schemes	Several dividend schemes that undermine the tax base are closed.	Tax rules enabling avoidance – now withdrawn	NT, 2011: 71
10. Square Kilometer Array (SKA): income tax and VAT relief (intent)	SKA is eligible for income-tax exemption under existing public-benefit provisions. Under consideration is providing VAT relief either in the form of a refund mechanism or the zero-rating of consideration received by the project and for imported goods and services *if South Africa were to win the bid.*	Tax rules enabling avoidance because of research and development activity	NT, 2012: 57

Table A-4: Capital gains tax (an income tax on companies and individuals)

Tax measure	Details / Comment	Inferred non-compliance feature	Source
1. Capital gains tax	Introduced 1 October 2001	Tax rules enabling avoidance – now amended; base broadening	NT, 2001: 64
	Increases in the monetary thresholds for capital gains	Tax rules maintaining (more or less) or increasing the real value of legitimised tax deductions	NT, Various years (e.g. NT, 2007: 72; 2011: 71)
	Treating the sale of shares (equities) held for more than three years as capital gains as of 1 October 2007	Tax rules of base broadening	NT, 2007: 62, 68
2. Increase in effective capital gains tax rates	▪ To enhance equity, effective capital gains tax rates to be increased (having been unchanged since introduction). ▪ The inclusion rate for individuals and special trusts will increase to 33.3%, shifting their maximum effective capital gains tax rate to 13.3%. ▪ The inclusion rate for other entities (companies and other trusts) will increase to 66.6%, raising the effective rate for companies to 18.6% and for other trusts to 26.7%. ▪ Will come into effect for the disposal of assets from 1 March 2012. <u>Exemptions for individual capital gains are increased</u>: ▪ Annual exclusion from R20 000 to R30 000 ▪ Exclusion amount on death from R200 000	No noncompliance; tax rates increased [A mix of real tax yield increase and base narrowing at the lower end of the income distribution for equity reasons] ***Revenue = R1.2bn [individuals (R800m); companies (R1.2)]***	NT, 2012: 45, 51

Table A-4: Capital gains tax (an income tax on companies and individuals)			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
	to R300 000 ▪ Primary residence exclusion from R1.5 million to R2 million ▪ Exclusion amount on the disposal of a small business when a person is over age 55 from R900 000 to R1.8 million ▪ Maximum market value of assets allowed for a small business disposal for business owners over 55 years increases from R5 million to R10 million		

Table A-5: Taxation of retirement funds			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Tax introduced (abolished 2007, See Annexure B, Table B-4)	Changes limit the expenses allowable in policyholder funds; change the basis of valuation of liabilities in the policyholder funds to the "financial soundness" basis of valuation; and limit the deductibility of transfers of surpluses from policy holder funds to the corporate fund. (Subject to public hearings by Joint Standing Committee on Finance)	Tax rules of base broadening	DoF, 1996: 2.16

Table A-6: Taxation of trusts			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Tax rate set for trusts	▪ Trusts, other than trusts mentioned below, to be taxed at a flat rate of 40%. ▪ Special trusts and testamentary trusts established for the benefit of minor children to be taxed at the individual tax rates.	Tax rules enabling avoidance through inappropriate use of trusts – now amended ***Revenue = R90m***	NT, 2002: 86
	Reconfirmed		NT, 2013: 49

Table A-7: VAT			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. VAT zero-rating of illuminating paraffin	Introduced poverty alleviation measure	Tax rule for equity or poverty alleviation reasons, countering VAT regressiveness ***Revenue loss = R400m***	NT, 2001: 71, 72
2. Financial services	Elimination of VAT zero-rating of interest earned on loans to non-residents in order to level the playing field.	Tax rules enabling beneficial VAT treatment favouring one economic sector – amended	NT, 2012: 57
3. VAT registration of foreign businesses	All foreign businesses supplying e-books, music and other digital goods and services in South Africa will be required to register as VAT vendors to ensure that the local consumer pay VAT on imported digital goods or services	Tax rules not incorporating all entities into the tax net – amended	NT, 2013: 59

Table A-8: Taxation of gambling			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Introduction of withholding tax (provincial)	All gambling winnings above R25 000, including those from the National Lottery, to be subject to a final 15% withholding tax.	Previously untaxed purchasing power (Haig-Simons)	NT, 2011: 64, 71
2. Introduction of withholding tax (national)	Uniform 1% national levy on top of provincial levies	Previously untaxed purchasing power (Haig-Simons)	NT, 2012: 57

Table A-9: Transfer duties			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Transfer duty rules amended	To prevent avoidance through 'nominee transactions'	Tax avoidance enabled by inadequate formal tax rules ***Revenue = R300m***	NT, 2003: 72

Table A-10: Excise taxes			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. More effective levying of excise duties on tobacco, alcoholic beverages & fuel (eventual aim for tobacco: 50% of retail price)	Use of Pigouvian tax argument to change behaviour	Negative externality presumably not adequately internalised – amended ***Revenue (2000) = R650m***	DoF, 2000: 68, 80
	Periodic adjustment to inflation and other increases in pursuit of goals	Negative externality presumably not adequately internalised – further amended; maintenance of pursued internalisation real monetary value	NT, 2009: 67; 2010: 76, 79; 2011: 64, 73; 2012: 45, 56, 57; 2013: 46, 49, 57-58, 60
2. Increase in ad valorem duties	Increase in the maximum nominal ad valorem excise tax rate on passenger cars and light commercial vehicles from 20% to 25%	Tax rule increasing tax rate	NT, 2011: 74
3. Reintroducion of duties	Ad valorem excise duties on monitors (abolished in 2004) to be reinstated at 7% flat rate.	Tax rule removing discrepancy between televisions (that are taxed) and computers (that are used as televisions)	NT, 2011: 74
4. New excise taxes on luxury goods	Ad valorem excise duties to be levied on: aeroplanes and helicopters with a mass exceeding 450kg but not 5 000kg at 7%; motorboats and sailboats longer than 10m at 10%	▪ Not non-compliance; a new tax = base broadening ▪ Probably informed by need to balance regressiveness of VAT	NT, 2012: 58

Table A-11: Levies and user charges (dedicated levies and taxes)			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Replacement of regional services council levies with a provincial fuel levy	No planned change in aggregate tax base	Tax rule change ***Presented as revenue neutral***	NT, 2007: 62
2. Increase of general fuel levy and Road Accident Fund (RAF) levy	Stepping up the utilisation of existing tax bases by rate increases.	Tax rule to protect tax base Higher fuel levy: ***Revenue = R950m***	NT, 2007: 63, 68, 73-74
	Periodic adjustment in monetary values of levies (fuel and RAF)	Tax rule to protect tax base and improve funding of RAF	NT, 2009: 68, 69; 2010: 72, 80; 2011: 75
3. Environmental levy introduced	▪ An environmental levy of about R3 per bulb (between 1 cent and 3 cents per watt) to be	Negative externality hitherto	NT, 2009: 56, 61, 66

Table A-11: Levies and user charges (dedicated levies and taxes)

Tax measure	Details / Comment	Inferred non-compliance feature	Source
	levied on energy-intensive (incandescent) light bulbs at manufacturing level and on imports from 1 October 2009.	not internalised (Pigouvian tax) ***Revenue = R2.78bn***	
4. Increase in the international air passenger departure tax	To increase the international air passenger departure tax of 2005/06 from 120 to R150 per passenger on flights to international destinations and R80 on flights to Southern African Customs Union member states respectively from 1 October 2009.	Fell behind on maintenance (approximately) of real value of revenue yield – tax rule adjusted	NT, 2009: 56, 67
5. Environmental fiscal reform: Vehicle CO2 emissions tax	▪ To introduce a flat rate CO2 emissions tax on new passenger motors (announced in 2009) and commercial vehicles ,effective from 1 September 2010.	New tax: negative externality hitherto not internalised (Pigouvian tax) ***Revenue = R450m***	NT: 2010: 72, 79
	▪ Tax for passenger vehicles to increase from R75 to R90 for every gram of emissions/km above 120 gCO_2/km and, in the case of double cabs, from R100 to R125 for every gram/km in excess of 175 gCO2/km, effective from 1 April 2013.	Negative externality hitherto not adequately (implied value judgement or disguised money-spinner) internalised (Pigouvian tax) ***Revenue = R355m***	NT, 2013: 57, 60

Table A-12: Tax base

Tax measure	Details / Comment	Inferred non-compliance feature	Source
1. From source to residence base: phased introduction of a residence-based income tax	Extension of income tax base to include foreign source investment income. In 2002 it was reported that this had already contributed to base-broadening	Tax rule changing the tax base; base broadening	NT, 2002: 72

Table A-13: Accounting method

Tax measure	Details / Comment	Inferred non-compliance feature	Source
1. Introduction of accrual basis of taxation	Introduced in 1999 to neutralise the unacceptable tax deferral opportunities that existed for taxpayers who acquired option contracts and claimed the full premium or acquisition price as a deduction for tax purposes in the year of acquisition.	Tax rule enabling avoidance – fundamental change	DoF, 2000: 68

Table A-14: Reform of entities and administrative capabilities

Tax measure	Details / Comment	Inferred non-compliance feature	Source
1. Establishment of SARS	Established as administratively autonomous organ of the state in terms of South African Revenue Service Act 34 of 1997	Administrative inefficiency – major institutional reform	RSA (1997)
2. Measures to improve collection efficiency	Pertain to income tax, VAT and customs duty	Administrative inefficiency	NT, 2003: 77
3. Various tax administrative initiatives	Pertain to collection enhancement, service, processing and enforcement	Administrative inefficiency	NT, 2003: 101; NT, 2004: 92-96
4. Small businesses compliance	Significant changes aimed at reducing compliance costs and providing an enabling environment for small businesses	Administrative inefficiency	NT, 2005: 69, 70, 71, 89
5. Broadening the tax base; reducing non-	▪ Enforcing registration for income tax purposes to increase number of people in the tax system ▪ Mobile X-ray scanners and high visibility roving anti-	Administrative inefficiency	NT, 2005: 96-97

Table A-14: Reform of entities and administrative capabilities			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
compliance	smuggling teams ▪ Investigative unit for high net worth individuals to identify undisclosed income ▪ Introducing voluntary disclosure dispensation ▪ Measures to counter abuse of incentive schemes		
6. Modernisation of corporate tax administration	▪ Move to a full self-assessment system explored. ▪ System to be reliant on a number of building blocks, including greater reliance on taxpayer integrity, an advance rulings system to resolve cases of doubt, more clearly defined disclosure requirements, a shift from returns to be assessed to returns of tax owing, e-filing, more consistent interest charges, enhanced risk identification, and well-defined penalty systems for non-disclosure and underdeclarations of income. ▪ The advance tax ruling system will be brought into operation on a phased basis starting in 2006.	▪ Administrative inefficiency ▪ Reliance going forward on taxpayer integrity	NT, 2006: 82
	SARS: three cross-industry areas as focal points for 2007/08, viz. trusts; undervaluation and understatement of stock; and employees' tax	Administrative inefficiency	NT, 2007: 78
7. Cost of compliance: very small business	A simplified tax package for very small businesses with an annual turnover up to R1 million intended to reduce the tax compliance costs for very small businesses, and not necessarily their tax liability	Compliance cost	NT, 2008: 56, 63
8. Voluntary disclosure for taxpayers in default 9. Installed from 1 Nov 2010 to 31 Oct 2011	▪ A defaulting taxpayer will be granted relief provided: - Disclosure is complete - SARS was not aware of default ▪ A penalty would have been imposed had SARS discovered the default in the normal course of business	Tax evasion	NT, 2010: 72, 81
10. Measures to improve compliance (deteriorated during recession) over next three years	▪ Increased digitisation to enable self-service and voluntary compliance ▪ Further modernisation of personal income tax, PAYE, corporate income tax and VAT systems ▪ Modernisation of customs systems ▪ Improved call centres, office operations and payment processes ▪ Enhanced focus on large taxpayers and high net worth individuals	Administrative inefficiency enabling (exploitation of) tax avoidance	NT, 2010: 81
11. To improve tax administration	▪ Pertaining to contributions to pension funds ▪ Streamlining of the base on which contributions to retirement funds and other social security taxes is calculated.	Administrative inefficiency – regulations, procedures amended	NT, 2011: 69
12. Tax administration efficiency regarding compliance	▪ A newly designed case sourcing system will be rolled out to improve internal efficiencies and compliance. ▪ Pertains to tobacco industry, textiles; using dogs and dog handlers and high volume scanners at Durban and Cape Town ports	Administrative inefficiency enabling avoidance and evasion	NT, 2015: 59-60

Table A-15: Reform of formal tax rules, regulations and procedures			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Continued efforts to ensure banking sector pays equitable share of tax	Possible amendments in income tax act mooted: ▪ Clarifying the distinction between capital and ordinary income for the sale of financial instruments ▪ Reviewing the tax rules regarding financial leases ▪ Ensuring the immediate accrual of certain income receipts that are postponed through artificial contingencies.	Inadequate tax rules enabling avoidance	NT, 2001: 80
2. The procedural law pertaining to tax collections will be enhanced to ensure that parties cannot escape their tax obligations	No details provided in 2003 Budget Review	Rules (legal system) enabling avoidance – amended	NT, 2003: 73
3. Measures to improve collection efficiency	Pertain to income tax; VAT; customs duty	Inefficient administrative processes - amended	NT, 2003: 77
4. Tax pertaining to cross-border flows	The current exemption from tax on income arising in certain designated foreign countries will be repealed, and taxes on company expatriation will be extended in order to discourage offshore flows	Tax rules enabling avoidance - amended	NT, 2003: 72, 88
5. Measures to protect company tax base	Losses from secondary trades (e.g. "weekend" businesses) will be ring-fenced in order to prevent losses from being claimed as an offset against other types of income.	Tax rules enabling avoidance - amended ***Revenue = R50m***	NT, 2003: 72,79
	The income tax exemption for gold share companies and the international headquarters company regime will be eliminated	Tax rules enabling avoidance - amended	NT, 2003: 72,90-91
6. Procedures to improve tax collection	Procedural law pertaining to tax collections to be enhanced to ensure that parties cannot escape their tax obligations	Statutory tax procedures enabling avoidance - amended	NT, 2003: 73
7. Anti-avoidance measures	Proposals for overhauling and updating the general anti-avoidance rules in the revenue laws to be tabled during 2005/06 in a discussion document.	Statutory tax procedures enabling avoidance – notice of prospective amendment	NT, 2005: 71
8. Bribes, penalties and other illegal activities	South African tax law to be amended to specifically address bribes, penalties and other forms of illegal activity.	Statutory tax procedures enabling evasion	NT, 2005: 96-97
9. Closure of sophisticated tax loopholes	Cross-border mismatches; Interest cost allocation for finance operations; "Protected cell" companies; Participation preference and guaranteed shares; Cross-border interest exemption; Transfer pricing	Statutory tax procedures enabling avoidance	NT: 2010: 78, 192-3 (Annexure C)

Table A-16: Education of taxpayers			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. Education to improve compliance	▪ Service centres will focus on educating South Africans about their tax obligations to improve compliance. ▪ Previously neglected communities and key players in the cash economy will receive special attention.	▪ Legacy of non-compliance due to pre-1994 political non-representation ▪ Deficient informal institution being addressed	NT, 2001: 66

Table 17: Tax amnesty			
Tax measure	**Details / Comment**	**Inferred non-compliance feature**	**Source**
1. To allow for the repatriation of capital	Intended for those persons who desire to bring back funds but fear the consequences of past illegal acts (Success results with amnesty in NT, 2006: 68)	informal norms of behaviour effecting tax evasion	
2. Tax amnesty for small business	Will allow SARS to waive taxes due by small businesses for years of assessment ending on or before 31 March 2004, where the turnover for the 2005 year of assessment does not exceed R5 million.	Legacy of non-compliance due to pre-1994 political non-representation plus administrative practices resulting in non-registered taxpayers – amended	NT, 2006: 64, 75
	Applications may be made until 31 May 2007		NT, 2007: 78

ANNEXURE B

CATEGORIES OF SYSTEMS-BASED TAX BASE EROSION

Table B-1: Tax incentives (general)

Tax measure	Details / Comment	Inferred tax alleviation feature	Source
1. Bursaries and scholarship for further education	Bursaries and scholarships for further education are under specified conditions exempt from income tax in the hands of employees	Education as positive externality; legitimised nontax liability	NT, 2002: 82
	To simplify matters, bursaries and scholarships for current and future employees will be tax-exempt as long as the employer's funds go directly to tuition and tuition-related expenses, and the employee agrees to repay the employer if the employee fails to fulfil their scholarship or bursary obligations		NT, 2006: 76
	<u>Bursaries to relatives of employees</u>: To facilitate employer- sponsored education and training of the dependants of low-and middle-income workers, it is proposed that this tax-free fringe benefit be increased to R10 000 p.a. for employees earning up to R100 000 p.a.		NT, 2008: 65
2. Learnership incentives	R25 000 deduction will be allowed to an employer when a learnership agreement is signed. Further R25 000 on successful completion	Education as positive externality; legitimised reduced tax liability	NT, 2002: 75
	Amounts increased ***Cost = R80m***		NT, 2006: 76
	Extended for further 5 years		NT, 2011: 72
3. Extension of tax deduction in respect of public benefit organisations	More organisations and activities to benefit	Tax rule legitimising tax avoidance	NT, 2002: 77
4. Increase in threshold for tax deductible donations made to qualifying public benefit organisations to 10 per cent for both individuals and companies	To maintain (more or less) or increase the real value of the benefit	Tax rule legitimising tax avoidance ***Cost = R185m***	Various years, e.g. NT, 2007: 75
5. Biodiversity conservation and management incentive	▪ Landowners will receive an income tax deduction for preserving habitats and biodiversity on their land. ▪ The deduction will cover expenses incurred in developing and implementing an approved conservation management plan under either the National Biodiversity Act (2004) or the Protected Areas Act (2003). ▪ The deductions contemplated would be limited to income derived from the land.	Recognising (ex post facto) and internalising positive externality (Pigouvian tax subsidy)	NT, 2008: 67
6. Certified emission reductions tax incentive	▪ The limitation of not allowing a rollover of donations in excess of 10 per cent of taxable income will be scrapped. ▪ Where land has been owned for many years, the value for the purpose of this incentive should be the lower of the municipal or market value.	Existing benefit extended	NT, 2013: 57
7. Incentives for investments in energy-efficient technologies	Investments by companies in energy-efficient equipment to qualify for an additional allowance of up to 15% on condition that there is documentary proof of the resulting energy efficiencies (after a two- or three-year period), certified by the Energy Efficiency Agency.	Recognising of (ex post facto) and internalising positive externality (Pigouvian tax subsidy)	NT, 2009: 56, 66

8. Making certified emission reduction credits tax exempt or subject to capital gains tax, instead of normal income tax	▪ Income derived from the disposal of primary CERs (certified emission reductions) to be tax-exempt or subject to capital gains tax instead of normal income tax. ▪ Secondary CERs to be classified as trading stock and taxed accordingly	Market-based solution to negative externality	NT, 2009: 56, 66
	In light of the adoption of a second commitment period of the Kyoto Protocol, government proposes to extend the incentive to 31 December 2020.	Existing benefit continued	NT, 2013: 57
9. Fringe benefit (trend reversal)	Where an employer transfers a house to an employee at a price below market value, a taxable fringe benefit is triggered. The fringe benefit tax is often unaffordable for low-income employees. To contribute to a more stable workforce and adequate housing, government proposes to provide fringe-benefit tax relief for lower-income earners in such cases.	Reversal on fringe benefit taxation trend for equity (affordability) reasons	NT, 2013: 50
10. Energy-efficiency savings tax incentive	▪ The energy-efficiency savings tax incentive will be increased from 45 c/kWh to 95 c/kWh and extended to cogeneration projects. ▪ It encourages firms to support a greener economy and complements the proposed carbon tax. Businesses can claim deductions based on energy saved. ▪ In future, this allowance will be funded through a recycling of revenues from the carbon tax. [Example of dedicated tax, almost amounting to a revolving fund]	New incentive to internalise external benefit ***Cost = R150m***	NT, 2015: 53

Table B-2: Individual income tax measures

Tax measure	Details / Comment	Inferred tax alleviation feature	Source
1. Interest income exemption	▪ Increased to R6 000 for taxpayers under 65 and to R10 000 for taxpayers aged over 65 ▪ Monetary values adjusted from time to time	Increase legitimate tax avoidance opportunity	NT, 2002: 80; NT, 2007: 63 and further years
2. Medical cost deductions increased	Individual taxpayers are allowed to deduct medical expenses to the extent they exceed the greater of 5 per cent of taxable income or R1 000. The R1 000 threshold will be removed from 1 March 2002.	Tax rule legitimising medical subsidy ***Cost = R36m***	NT, 2002: 83
3. Reduce and (eventually abolish) the Retirement Fund Tax to protect savings, especially for low-income wage earners	▪ The Retirement Fund Tax is reduced from 25 per cent to 18%. ▪ Cost = R1850m (Based on the argument for tax neutrality vis-à-vis other savings vehicles– articulated by the Katz Commission – NT, 2003: 82)	Tax reduction measure (tax neutrality; equity)	NT, 2003: 71, 72, 79
	Rate reduced from 18% to 9%	Tax reduction measure (tax neutrality; equity)	NT, 2006: 64, 70
	Abolishing the retirement fund tax with effect from 1 March 2007 ▪ Consistent with the shift to the retirement savings taxation model envisaged. ▪ To result in improved returns for	Tax reduction measure (tax neutrality; equity)	NT, 2007: 62, 68, 72

	retirement fund members and a counterpart to the proposed limitations on tax deductibility of retirement fund contributions by high-income individuals. ▪ Cost = R3bn		
4. Tax-free share transfers to employees.	Provision is made for broad-based tax-free share transfers to employees.	Legitimised tax alleviation	NT, 2004: 74, 88-89
5. Capital gains tax on primary residences	People selling their primary residence with a gross value below R2 million will not be liable for capital gains tax.	Legitimised tax alleviation	NT, 2009: 64
6. Taxation of lump sum benefits upon retirement	As from 1 March 2011, government will increase the tax-free lump sum benefit upon retirement from R300 000 to R315 000.	Monetary value of allowance in real terms adjusted (approximately?) for inflation	NT, 2011: 71
7. Rebate for individuals 75 years and older	▪ A third rebate of R2 000 per year is proposed for taxpayers 75 years and older This increases the tax threshold for eligible individuals to R104 261.	New allowance for very old people	NT, 2011: 63, 68
8. Tax-preferred savings accounts	These accounts will have an initial annual contribution limit of R30 000, to be increased regularly in line with inflation, and a lifetime contribution limit of R500 000. contribution Eligible service providers will include banks, asset managers, life insurers and brokerages.	incentive to encourage household savings	NT, 2014: 48
9. To promote greater equity in the income tax system as	▪ Pertaining to contributions to pension funds ▪ Individuals will be allowed to deduct up to 22.5 per cent of their taxable income for contributions to pension, provident and retirement annuity funds. ▪ To ensure greater equity, two thresholds will be established – a minimum annual deduction of R12 000 and an annual maximum of R200 000.	Inequity in income tax rules - amended	NT, 2011: 69
10. Retirement savings reform	Changes to the taxation of contributions to retirement funds in line with the Taxation Laws Amendment Act (2013) will provide additional relief to most retirement fund members and encourage them to save for retirement. Employer contributions are deemed to be a fringe benefit in the hands of the employee. Both employee and employer contributions will be deductible, up to a limit, for income-tax purposes by the employee.	Enabling rules of tax deductibility to encourage retirement provisions	NT, 2014: 48

Table B-3: Corporate income tax measures

Tax measure	Details / Comment	Inferred tax alleviation feature	Source
1. Graduate rate structure for SMEs and micro businesses	▪ 15% on first R100 000 taxable income and 30% thereafter ▪ Extended in 2002.	Tax rule enabling tax avoidance through business organisational design, eroding corporate income tax base (static view)	DoF, 2000: 80; NT, 2002: 78.
	▪ Extension of graduated tax rate of 15 per cent for small business on first R150 000 taxable income ▪ Turnover threshold increased from R1m to	▪ Tax rules legitimising tax deductions ▪ Incentive to	NT, 2002: 78, 85; NT, 2006: 74

	R3mcost R40m ▪ Periodic subsequent adjustment (*inter alia* to adjust for inflation)	promote SMEs	
	▪ Presumptive tax structure for very small businesses	Tax rules legitimising easier tax compliance	NT, 2008: 60
	▪ Small businesses will be exempt from tax on the first R35 000 of income (subsequently increased – see for example next line)	Tax rule legitimising nontax liability	NT, 2005: 70
	▪ Increase in the tax-free threshold for small businesses from R59 750 to R63 556. ▪ Taxable income ceiling for reduced rate increased from R300 000 from R350 000; rate reduced from 10% to 7%. ▪ Taxable income > R350 000: rate = 28%.	Incentive to encourage the growth of small incorporated businesses. Static not necessarily base-broadening; dynamic: possibly	NT, 2012: 53
2. Small business support and tax liability	▪ Provided through an additional deduction for start-up expenses of up to R20 000 and an increase to R5 million in the turnover limit for small businesses.	Tax rules legitimising tax deductions ***Cost = R10m***	NT, 2003: 72, 79, 86
	▪ Increases in the monetary thresholds for qualifying small businesses	Tax rules maintaining (more or less) or increasing the real value of legitimised tax deductions	NT, Various years
	▪ A set of responses to encourage informal businesses to migrate to the formal sector.	Tax rules legitimising nontax liability	NT, 2005: 87
	▪ Incentives to encourage venture capital equity investments in small and medium-sized businesses	Tax rules legitimising nontax liability	NT, 2008: 56, 63-64
3. Accelerated depreciation for small business investment	A simplified 50: 30: 20 tax depreciation regime proposed for nonmanufacturing assets of small businesses.	Tax rules legitimising tax deductions	NT, 2005: 71
	Instead of 20% p.a. over 5 years, full cost of investment may be deducted in the tax year in which the asset is brought into use by the taxpayer for the first time..	Tax rules legitimising tax deductions ***Cost = R40m***	NT, 2001: 82
	Three-year accelerated tax depreciation write-off period for all nonmanufacturing assets for small business	Tax rules legitimising tax deductions ***Cost R1.4bn***	NT, 2005: 86
4. Depreciation allowances for certain airport infrastructure	Tax allowances of 5% pa on a straight-line basis for investment in airport hangars and runways.	Tax rules legitimising tax deductions	NT, 2001: 79
5. Depreciation allowances for private developers	Enhanced allowance will be considered for private developers who improve another party's land, subject to anti-avoidance mechanisms	Tax rules legitimising tax deductions	NT: 2010: 79
6. Accelerated depreciatio n allowance	▪ To complement the strategic investment programme and other initiatives of DTI, an accelerated depreciation allowance is introduced. ▪ New manufacturing assets acquired within three years from 1 March 2002 will be depreciated over 4 years. ▪ 40% of the cost of the asset will be deducted in the first year and 20% for the subsequent 3 years. ▪ Only for taxpayers in respect of assets used directly in their manufacturing businesses.	Tax rules legitimising tax deductions ***Cost = R295m***	NT, 2002: 84-85; 2005: 86
7. Accelerated depreciation	▪ Envisaged to encourage manufacturing investment and job creation	Tax rules legitimising tax deductions	NT, 2002: 68

allowances	▪ Tax regime related to depreciation of fixed and moveable assets to be reviewed to ensure greater consistency. ▪ Various interim amendments pertaining to: rail locomotives, wagons and port assets; commercial buildings; environmental capital expenses; corporate reorganisation and BEE transactions	Tax rules legitimising tax deductions and their implement-ation	NT, 2007: 69
8. Accelerated depreciation allowances	▪ Accelerated depreciation allowances for urban development zones, materially addressing urban decay and the supply of affordable housing to the urban poor ▪ 5 year write-off period for investments for refurbishing buildings and 17 year write-off for new commercial and residential buildings	Tax rules legitimising tax deductions ***Cost = R1,3 billion (tax revenue foregone within 4 years)***	NT, 2003: 71, 79
9. Accelerated depreciation allowances	▪ 3-year write-off for renewable energy technology	Tax rules legitimising tax deductions	NT, 2005: 89
10. Accelerated depreciation allowances	▪ Accelerated depreciation allowances for urban development zones ▪ Nine urban development zones approved; prospective extension to seven more zones	Tax rules legitimising tax deductions	NT, 2005: 75
11. Removal of securities taxes on certain warrant transactions	To facilitate the development of warranty market by eliminating certain transaction costs that are absent in many competing markets	Tax rules legitimising tax deductions ***Cost = R80m***	NT, 2002: 93
12. Dividend tax on foreigners removed	The tax on foreign dividends from offshore subsidiaries is removed in order to encourage capital in-flows	Tax rules legitimising tax deductions	NT, 2003: 71, 72
13. Tax benefit for Public benefit organisations	List extended	Tax rules legitimising nontax liability ***Cost = R60m***	NT, 2003: 71, 72, 79
	Threshold increased	Tax rules legitimising nontax liability ***Cost = R160m***	NT, 2006: 79
	▪ Proposed that employers be allowed to deduct donations by employees (within limits) to section 18A organisations in determining employees' tax payments. ▪ To support the activities of PBOs that provide bursaries and loans to needy students, it is proposed that the provision of student loans by PBOs should be included in the list of public benefit activities.	Tax rules legitimi-sing tax allow-ance	NT, 2008: 69, 70
	▪ To allow donations in excess of 10 per cent of taxable income in any given year to be rolled over as allowable deductions in subsequent years.	Existing benefit extended; enables further inroads on potential tax revenue	NT, 2013: 53
14. Financial transaction tax relief for the new issue of company shares	▪ All financial transaction taxes to be eliminated on the issue of shares (while providing appropriate safeguards to ensure that this exemption is not used as a tool to eliminate financial transaction taxes imposed on sales between shareholders). ▪ To take effect 1 Jan 2006.	Tax rules legitimising nontax liability; addresses nonneutrality between debt and equity capital, amounting to removal of tax discrepancy	NT, 2005: 85
15. Research and development expenditure	▪ Deduction for current R&D expenditure increased from 100% to150% ▪ The depreciation allowance for capital expenditure increased from current 40: 20: 20: 20 to 50: 30: 20.	A presumed internalisation of positive externality (Pigouvian)	NT, 2006: 77

16. R5 billion in tax subsidies over the next three years to support the emerging industrial policy	▪ Carefully designed tax incentives that encourage higher levels of investment in labour-intensive or strategic sectors will be considered. ▪ **<u>Note</u>**: it is important to identify clearly where the market failures are, consider the costs and benefits of such actions, and explore alternatives.	Tax rules legitimising nontax liability, reflective of developmental state thinking ***Cost = R1bn (R5bn over 5 years)***	NT, 2008: 56, 60, 62
17. Youth employment subsidy	▪ To support job creation, a youth employment subsidy in the form of a tax credit to be introduced. ▪ t will be administered by SARS through the PAYE system to limit abuse, ensure maximum liquidity and ease business compliance. ▪ Implemented 1 January 2014	New incentive to promote job creation and youth employment; distortion to compensate for, rather than correct, distortions in labour market ***Cost = R5bn over 3 years***	NT, 2011: 72
	▪ Refunds effective from 4th quarter 2014		NT, 2014: 47, 52, 57
18. Industrial Development Zones (IDZs)	▪ To support the objectives of the industrial policy action plan and the New Growth Path, businesses making greenfield and/or brownfield investments qualify for tax relief. ▪ Greenfield investments in IDZs qualify for additional relief. ▪ Government will consider expanding incentives for labour-intensive projects in IDZs.	Tax rules legitimising nontax liability, reflective of developmental state thinking	NT, 2011: 73
19. Tax incentives in special economic zones	In certain special economic zones, the Minister of Finance will authorise the following tax incentives, after consultation with the Minister of Trade and Industry: ▪ A 15% corporate income tax rate for businesses in such areas. ▪ An employment incentive allowing for a tax deduction for employment of workers earning less than R60 000 per year. ▪ An accelerated depreciation allowance for buildings in these areas, based on the existing regime for urban development zones, to encourage developers to invest more in industrial premises.	Tax rules enabling tax reduction, perhaps regional decentralisation argument of positive externality	NT, 2013: 52
20. Biofuels production incentive	▪ It will serve as an "infant industry" support mechanism and will be phased out over an assumed 20-year lifetime of a benchmark plant. ▪ The initial cost of the incentive will be 3.5c/l to 4c/l of petrol or diesel, recovered through a levy included in the monthly price determination.	Tax rule internalising a positive externality; revival of infant industry argument	NT, 2013: 58

Table B-4: Taxation of retirement funds

Tax measure	Details / Comment	Inferred tax alleviation feature	Source
1. Tax abolished (Introduced in 1996 – see Annexure A, Table A-5)	Abolished	Tax rule of base reduction ***Cost = R3bn***	NT, 2007: 68

Table B-5: VAT			
Tax measure	**Details / Comment**	**Inferred tax alleviation feature**	**Source**
1. Zero-rating of paraffin	VAT = 0%	Tax rule reducing VAT base; countering VAT's regressive equity impact, but reducing VAT base ***Cost = R400m***	NT, 2001: 82
2. Zero rating of municipal property rates	VAT = 0%	Tax rule reducing VAT base ***Cost = R1bn***	NT, 2006: 70

Table B-6: Fuel levy			
Tax measure	**Details / Comment**	**Inferred tax alleviation feature**	**Source**
1. Increase in biodiesel fuel tax concession to 40 per cent of the general fuel levy	▪ A review of international practice indicates that to support the industry the rebate should be set at 40% of the general fuel levy. ▪ Given the emerging character of the industry, this is expected to have a limited effect on the fiscus.	Legitimised tax incentive ***Limited cost expected in light of industry's emerging character***	NT, 2006: 80
2. Diesel fuel concession for primary production sector	▪ Tax allowance on basis of non-transport character of fuel as production input	Tax alleviation rules ***Cost = R416.6m***	NT, 2001: 86-87

Table B-7: Excise duties and other indirect taxes			
Tax measure	**Details / Comment**	**Inferred tax alleviation feature**	**Source**
1. Reduced excise duties on passenger vehicles and abolition of duties on computers	To ease their cost for business and personal uses	Tax rules legitimising tax deductions ***Cost = R572m***	NT, 2003: 71, 72, 98
2. Stamp duties abolished	Stamp duties on insurance policies and fixed deposits are abolished.	Tax base reduced ***Cost = R200m***	NT, 2003: 72, 79, 90
	Stamp duties on mortgage bonds and negotiable certificates of deposit are removed	Tax base reduced	NT, 2004: 74, 88-89
	Stamp duties on banking debit entries are abolished	Tax base reduced ***Cost = R350m***	NT, 2005: 70
	Stamp duties on short-term leases (less than five years) to be abolished.	Tax base reduced ***Cost = R90m***	NT, 2007: 76
3. Increases in the monetary thresholds for capital gains, donations tax, transfer duty and estate duty	▪ To maintain (more or less) the real value of the benefit	Tax rule legitimising tax avoidance Cost to adjust table for transfer duties = R4.5bn	Various years (e.g. NT, 2007: 72)

Table B-8: Customs duties			
Tax measure	**Details / Comment**	**Inferred tax alleviation feature**	**Source**
Tariff reductions and rationalisation in ad valorem excise duty rates	Reform customs duties in accordance with the WTO agreement (94/95-99/00)	Tax base reduced	DoF, 1995: 2; 1996: 2.16.2; 2000: 68
Selective abolishment of *ad valorem* excise duties	Ad valorem excise duties on printers, recorded music and some cosmetic products abolished.	Tax base reduced ***Cost = R270m***	NT, 2004: 74, 79
	Ad valorem excise duties on sun protection products and on professional digital cameras are abolished	Tax base reduced ***Cost(*** sun protection products) ***=R10m***	NT, 2005: 70
	Abolish excise duties on products as listed in Annexure C of 2006 Budget Review	Tax base reduced ***Cost = R22m***	NT, 2006: 70, 79, 192 (Table C.5)
	Abolish the ad valorem excise duties on products as listed in Table C.5 in Annexure C of the *Budget review*.	Tax base reduced ***Cost = R85m***	NT, 2007: 73

Table B-9: Transfer duties			
Tax measure	**Details / Comment**	**Inferred tax alleviation feature**	**Source**
Increase in transfer duties thresholds	Property transfer duty thresholds are increased	Tax rule alleviate tax burden in respect of property transfers ***Cost (2011) = R450m***	NT, 2005: 70; 2011: 64, 73