SCHOOL OF ACCOUNTANCY

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A research report submitted to the Faculty of Commerce, Law and Management in partial fulfilment of the requirements for the degree of Master of Commerce specializing in Taxation

A critical analysis and comparative study on the tax burden of South African individual taxpayers from the 2003 to 2019 tax years.

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DECLARATION

I, Kethabile Ndlovu, declare that “A critical analysis and comparative study on the tax burden of South African individual taxpayers from 2003 to 2019 tax years” is my own original work and it has not been presented to the institution before. To the best of my knowledge, all the necessary guidelines and standards in terms of referencing have been followed and all the sources used have been properly acknowledged.

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I dedicate this study to everyone who has not had it easy - keep pushing. All glory and honour to Our Father!

ABSTRACT

A critical analysis and comparative study on the tax burden of South African individual taxpayers from 2003 to 2019 tax years

Personal income tax (PIT) is the largest source of tax revenue collected by the South African Revenue Service (SARS) and it has accounted for an average of 35% of the total tax revenue between the 2003 and 2019 years of assessment (SARS, 2010 & 2019). South Africa uses a progressive tax system to determine the taxable liability of individuals. In the 2017 tax year the top marginal tax rate for individuals was increased from 41% to 45%, making SARS one of the highest taxing authorities in the world (Trading Economics, 2019b). The contribution of PIT to total tax revenue seems to be growing steadily in the period under review, as compared to the contributions made from corporate income tax (CIT) and value-added tax (VAT) (SARS, 2019a).

In a country characterised by high unemployment rate, social inequalities, political instability, job cuts, recurring recessionary phases, labour unrest, declining foreign investments and widening national debt, the habit of using tax revenue to fund government spending and to support the fiscal policy becomes inevitable and the only readily available option. Since PIT is the main contributor to tax revenue, this raises the question: “is the tax borne by individuals reasonable and is the dependence on PIT as the main source of revenue a sustainable and effective way to improve the social and economic challenges faced by South Africa?”

The purpose of this study is, firstly, to determine whether South African individuals carry a heavy tax burden as compared to taxpayers in other countries with similar economic and social models, using different quantitative methods. This paper will analyse the tax years from 2003 to 2019. This study will underline the effects that dramatic changes in the economy or tax system, such as the

global financial crisis in 2008 and the adoption of the Tax Administration Act (TAA) in 2011, had on PIT levels. Secondly, the study will seek to highlight the economic and social impacts of taxing individuals too heavily. Lastly, the study will recommend the best possible tax policies and reforms that are successful in other countries that could possibly be implemented in South Africa to curb the tax burden borne by individuals.

Key words:

personal income tax, tax liability, tax burden, marginal tax rates, tax revenue to gross domestic product (tax-to-GDP) ratio, tax reforms and policies, individual taxpayers, progressive tax system, year of assessment, nominal vs real GDP, tax year, tax base

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CHAPTER 1: INTRODUCTION

According to the World Bank study conducted in 2006 on the effective tax burden in South Africa, it was stated that South Africa as a developing country has one of the highest tax-to-GDP ratios as compared to its counterparts, namely Zambia, Kenya, Uganda, Tanzania, and that it is more in line with middle-income countries, namely Australia, Canada, India, and New Zealand, which demonstrates the reliance of using taxes to fund government expenditure (World Bank, 2006). Another article also stated that South Africa has one of the highest PIT burdens in the world. A more worrying trend is South Africa's tax-to-GDP ratio, which is fast approaching 30% and was at 28.6% in 2019, far higher than the global average of 15%, and even higher than the Eurozone's rate of 19% (Business Tech, 2018b). For the purposes of this study, PIT burden is defined as the amount of tax carried by individual taxpayers in proportion to their total income or earnings in a particular tax year. In simple terms, how much of the money earned by a South African taxpayer goes towards PIT, and in comparable terms, is the individual worse or better off in comparison to other individuals around the globe?

For several years now in South Africa, PIT remains the largest contributor to the total tax collection; remuneration forms a large portion of the taxable income used to calculate PIT and a progressive tax system is used to determine taxes due by individuals (SARS, 2018). In 2007 the global financial crisis started looming and then in 2008 the negative effects of it were apparent, which resulted in a full-blown global recession in 2009. South Africa was not spared from the aftermath. As a result, the need for governments around the world to impose a larger tax burden on corporates and individuals was unavoidable. As at December 2019, the South African government supports over 17 000 000 grant recipients (SASSA, 2019), with the national debt standing at $70 836 million (Trading Economics, 2019a), the unemployment rate at an alarming 29.1% and recurring mass retrenchments in many fields – the need for tax revenue is ever increasing to meet government and public spending. The list of the financial difficulties faced by South Africa is endless and far more complex, however, only a few of the

economic challenges are mentioned here as they have a more direct impact on the PIT levels.

The increase in the national debt and the ever-increasing need to supply social grants requires more revenue collection. Moreover, the rapid and large-scale job losses influence the increase in the unemployment rate, which will in turn have a negative impact on the tax base to be utilised by SARS for PIT collection. The outcome is that fewer taxpayers will be responsible for the largest part of the total tax revenue to be collected. As a result of the financial setbacks the country faces, increasing the tax rates as well as enlarging the tax base for PIT seems to be the simplest and most obvious choices for the National Treasury. This is seen in the following tax reforms introduced in South Africa over the years: the increase of the top marginal tax rate from 41% to 45% in the 2017 tax year; a proposal to tax foreign employment income; the introduction of capital gains tax (CGT) in 2001; and changing from source-based to resident-based taxation, to mention a few. This raises the question of whether the tax burden placed on individuals is too heavy and whether the design of the PIT system is fair to individual South African taxpayers. Furthermore, what would the best possible reforms be to increase the tax base, keep the minimum and maximum marginal tax rates at a fairer level and collect the revenue needed by the government? All these decisions have to be made jointly by SARS and National Treasury as indicated below:

> The National Treasury is responsible for the tax policy framework and it works closely with SARS to ensure that tax policy and tax administration are well aligned. Section 12(1) of the Public Finance Management Act (1999) (PFMA) requires that: “The South African Revenue Service must promptly deposit into a Revenue Fund all taxes, levies, duties, fees and other moneys collected by it for that Revenue Fund, in accordance with a framework determined by the National Treasury (National Treasury, 2008a).

Taxes are not only essential for revenue-raising purposes, but can also be used to alleviate income inequality, improve economic stability and influence the allocation of resources (Steenekamp, 2007). Therefore, it is important to have a PIT system that will raise the much-needed revenue while promoting fairness, eradicating social inequalities and encouraging economic growth. In order for a developing country like South Africa to improve the economy, attract foreign investments and strengthen international trade, the need to simplify the tax

system and to reduce the tax burden on both individuals and companies becomes of paramount importance. Steenekamp (2012a) remarked that the imperative to reduce poverty levels in developing countries, including South Africa, requires not less but more public expenditure and probably higher tax levels. National Treasury and other tax policy-makers have a challenging task at hand in terms of keeping the tax burden on individuals at a fair and acceptable level and on the other hand ensuring that SARS is able to raise the much-needed tax revenue.

Tanzi (2004) noted that the “two work horses” that must carry the tax burden in a modern world are VAT and PIT. In this study, the focus will firstly be to determine the proportion of PIT to the total tax revenue collection over the 2003 to 2019 tax years. The purpose of this measure is to analyse the trend of PIT collection over the years and establish if tax on individuals is indeed the biggest “work horse” in South Africa. This study will focus primarily on the tax periods from 2003 to 2019 for comparative analysis because of the limited data available from various sources utilized.

Secondly, the study will analyse if the PIT progressivity from 2003 to 2019 is in line with average earnings and the average inflation rate. The aim is to establish if the salaries that account for the majority of the taxable income of individuals are keeping up with the annual changes made to the tax brackets, deductions and rebates, and that the possibility of the tax creep is reduced at all cost. Tax creep occurs when an individual’s annual salary is only adjusted for inflation and, consequently, the taxable income increase exposes the individual to a higher tax bracket, resulting in an increased effective tax liability with no real growth on the salary.

Thirdly, an international comparison will be undertaken to see how the tax profile of individual South African taxpayers measure with that of other countries’ taxpayers. The selected countries that will be included are some from the Southern African Development Community (SADC), Brazil, Russia, India and China (the other BRICS countries) and some Organisation for Economic Co-operation and Development (OECD) countries.

The 16 countries selected in this study to compare South Africa against are: Botswana, the Democratic Republic of Congo (DRC), Mauritius, Mozambique, and Zambia (SADC countries); Brazil, Russia, India and China (BRICS countries); Australia, United Kingdom (UK) and United States of America (USA) from the OECD group; and Algeria, Egypt, Kenya and Nigeria (fastest developing countries in Africa). It should be noted that there is no scientific basis on which the countries were selected, however, the selection of countries is mainly based on the following broad reasons:

- How influential or developed the country is, based on its economic standing; South Africa is an emerging economy so it is imperative to compare its tax performance to that of other emerging countries and to benchmark it against advanced economies in the world. This will give us an idea of whether South African individuals are overtaxed or not.
- Countries with similar bases of taxation for individuals are considered. For instance, if residents are taxed on their worldwide income or a progressive system is adopted, self-assessment for submission of tax returns is allowed, or the tax revenue is mainly supported by PIT revenue like in the case of South Africa.
- Countries that share a particular interest in a co-operative or belong in an organisation of some sort with South Africa are included. For example, South Africa is part of BRICS and SADC and is a key partner in the OECD so some of these countries will form part of this study for analysis purposes.
- How similar the social and economic model or status of the country is to that of South Africa – South Africa has a high youth unemployment rate and its economy used to be supported mainly by primary sectors due to the wealth of mineral resources and favourable agricultural conditions. However, there was a structural shift of the economy in the early 1990s from primary to tertiary sectors, which comprises manufacturing, wholesale and retail trade, financial services, transport, mining, agriculture and tourism (Brand South Africa, 2018). Most of the BRICS countries have seen a similar shift in their economy, therefore it is necessary to include them in this study.

The BRICS countries are fundamentally part of the Group of Twenty, commonly known as the G20. G20 is an international forum for the governments and central bank governors from 19 countries and the European Union. The promotion of economic growth, stabilisation and structural reforms have been central to the mandate of the G20, which is similar to the National Development Plan of South Africa in many respects. The inclusion of the BRICS countries in the G20 reinforces the imperative to include the BRICS countries as part of this study for the international comparative analysis. The objectives of the G20 are outlined below:

> The objectives of the G20 are: a) Policy coordination between its members in order to achieve global economic stability, sustainable growth; b) To promote financial regulations that reduce risks and prevent future financial crises; and c) To create a new international financial architecture (Ministry of External Affrairs - India, 2012).

The selection of SADC countries will be limited to Botswana, the Democratic Republic of Congo (DRC), Mauritius, Mozambique, and Zambia. Other SADC countries are excluded, as they have incomparable population sizes, vastly unparalleled economic resources or different tax structures to that of South Africa. It is important to benchmark South Africa against countries with similar economic, social and/or political models and, consequently, oil-producing nations will be treated with caution for comparative purposes. This is to ensure that the study maintains the necessary accuracy and validity of results that will be obtained from the comparative analysis.

Although not part of SADC, but listed in the top ten developed countries in Africa by Business Tech (2018a) and the United Nations Development Programme (UNDP) (2019) based on their GDP growth and Human Development Index (HDI) in 2019, Algeria, Egypt, Kenya and Nigeria will be included as part of the research to allow for greater scope and measurability of the results. HDI is a statistical tool used by the United Nations (UN) to measure the changes in development levels over time and to compare the development levels of different countries (United Nations, 2019). Not only do these countries have the fastest growing economies in Africa, but the taxation of individuals in Algeria, Egypt and Nigeria is also closely related to the taxation model of South Africa. Resident individuals are

taxed on their worldwide income and non-residents are taxed on income earned from a source within the respective country. Only Kenya uses the source-based taxation model for residents and non-residents. Nevertheless, all of these four developed African countries make use of either remuneration or employment income in the determination of taxable income of an individual and the terms are widely defined like in the case of South Africa. Moreover, all of these countries use progressive rates in determining the tax liability of the individuals. Both Algeria and Nigeria are the biggest oil and gas producers in the African continent and, as such, the taxation system is more elaborate and centralised on the taxation of these industries. These emerging African countries also have shared interests in various trade agreements and international affiliations, including the UN, the World Trade Organisation (WTO), the Common Market for Eastern and Southern Africa (COMESA), and the African Growth and Opportunity Act (AGOA) (Deloitte, 2018).

Moreover, the benchmarking of South Africa against other developed African nations will either corroborate or contradict any contentions as claimed in prior studies. Steenekamp conducted various researches on the tax levels of South Africa, and in one of the studies the following assertions were made regarding the tax burden of South Africa compared to other developing countries forming part of the SADC:

> The level of taxation in South Africa (26.3% of GDP) is much higher than that of its SADC partners. When the tax burden of a more diverse group of 13 developing countries (least developed countries – LDCs) (21.3% of GDP) is compared to the overall tax burden in South Africa, a similar picture emerges – South Africa exhibits a higher tax burden than most of the sample of developing countries (Steenekamp, 2012b).

According to the OECD website (2018), in 2007, South Africa became one of the five key partners (along with Brazil, China, India and Indonesia) to be added to the OECD list. The OECD seeks to address pressing policy issues such as taxation, competition policy and governance by cooperating with various governments, citizens and policy-makers of the member countries (OECD, 2018). As a result of South Africa's addition to the OECD community, it is imperative to also analyse the PIT levels of South Africa against the OECD countries' ideal PIT

levels and averages in order to draw an informed and unbiased conclusion on the tax burden of South African individuals. In the OECD comparison to South African PIT levels, there will be a specific focus on Australia, the United Kingdom (UK) and the United States of America (USA). These three OECD member countries are considered to be amongst the most developed nations in the world based on their GDP growth and HDI. The goal of any country is to eventually be regarded as a developed country, hence it is crucial to benchmark South Africa as an emerging country against some of the already advanced economies. The purpose of the international comparison is also to assess the tax reforms and policies that are implemented in other countries and are actually effective and efficient in meeting the fiscal needs of these countries without burdening individual taxpayers and that can possibly be adopted in South Africa.

This study will rely on pre-existing statistical and numerical data collected from various sources that will be adapted or re-measured and interpreted to draw conclusions on the tax burden of South African individuals. The study will thus mainly be quantitative in design, although qualitative techniques will be used to interpret the data. As the popular saying goes, “numbers do not lie”, hence the quantitative analysis is key to assessing the tax burden of individual taxpayers, using different data available to measure the assumed tax burden. The study will then conclude after reviewing and critically analysing the quantitative results obtained in this study, with the focus being on 2003 to 2019 and paying close attention to how the economic meltdown affected the PIT levels in the post-2008 tax years.

BACKGROUND

South Africa has come a long way in trying to improve the tax system by implementing different tax policies and tax reforms, however, the process is an ongoing one because tax reforms and policies need to be reviewed and revised constantly to ensure their relevance and effectiveness in any given economic climate. Over the years, several Ministers of Finance had been tasked with the mandate to appoint various tax commissions to look into the structure of the

South African tax system and identify ways to improve it. In 1986, the Margo Commission published a report which focused on how to restore the tax base, eliminate tax erosion and leakages, simplify the tax structure, and, more relevant to this research, how to redistribute the overall tax burden to make it fairer, easier and more acceptable (Margo Commission, 1987). The Margo Commission made several recommendations in an attempt to improve the tax structure for low-wage earners. What the Margo Commission failed to address was the question of fairness in the tax burden carried by individual taxpayers and how the recommendations made in the report would address the excessive tax burden skewed towards individuals.

The Katz Commission was appointed in 1994 to further research how to best increase the tax base. The Katz Commission's fifth report on 'Basing the South African income tax system on source or residence principle' made recommendations on whether to increase the tax base of the South African tax revenue by taxing the taxpayers on a residence basis instead of a source basis (Katz Commission, 1995). This study will further bring to attention the sound and effective recommendations made by different tax commissions and tax experts that South Africa may consider to lessen the PIT burden and to concurrently improve economic growth and income redistribution.

Most of the research done to assess the tax levels as well as tax reforms in recent years has been focused on corporate income tax (CIT) levels rather than individual taxpayers. This has been in a quest to improve the economy by bettering the conditions of the business environment in developing countries and creating a less burdensome tax administration for ease of business in South Africa. Steenekamp (2007), however, conducted research that went beyond company income taxes in the study titled "Tax performance in South Africa: a comparative study" which broadly analysed corporate taxes, personal taxes, import taxes and taxes on property, by using a statistical measure to determine whether tax levels are high or low in South Africa relative to other countries. The conclusion of the study was that South Africa uses PIT and CIT more intensively as compared to other tax categories, as well as more than the twenty-nine

countries analysed (Steenekamp, 2007). More relevant to this study will be an in-depth analysis on PIT levels rather than other tax categories. This study will also expand on other components that directly affect PIT levels, such as average earnings, average inflation over the years, and annual changes made to the progressive tax system brackets used to calculate PIT.

In another study titled “Taxing the rich at higher rates in South Africa”, Steenekamp (2012b) reiterated that the tax burden of South African individual taxpayers is already high when compared to a selection of emerging and developed countries and there is no room to stretch the tax base for PIT collections any further. The researcher deduced that the tax composition of South Africa as a developing country is notably similar to the structure of developed countries as opposed to emerging countries and the PIT share generally exceeds that of most developed countries. The focus of that study was dedicated to the rich taxpayers, which were classified as the group with the top one percent of the income share in South Africa (Steenekamp, 2012b). This classification disregards and undermines the reality that South Africa is characterised by high-income inequality and it is a developing country with only a few high income-earning taxpayers. The focus on rich taxpayers does not reflect the tax burden of South African individuals holistically nor realistically, as it only focuses on the top marginal tax bracket.

Steenekamp (2012a) also researched the impact of PIT reforms since 1994 on the tax structure and its scope to meet the challenges of rising needs and equity. The study looked into different tax reforms that are employed globally that can be adopted in South Africa in the post-apartheid era. Of particular interest in this research was the finding that South Africa’s usage of direct taxes as a percentage of total tax revenue increased in importance between the 1993/94 and 2010/11 tax years (Steenekamp, 2012a). The research concluded that the total tax burden on individuals appeared to be the same after the global financial crisis as compared to pre-apartheid years, however, the study established that the PIT base in South Africa remained intensively taxed in all those years when compared with other developing countries (Steenekamp, 2012a).

Similarly to the views shared by Steenekamp, an online article titled “Personal income tax buoyancy has run its course” stated that South Africa’s PIT burden had risen from 8.3% of GDP in 2010/11 to 9.8% in 2017/18, proving the dependency on PIT (Money Martketing, 2018). Furthermore, the article suggested that the below-inflation adjustments to the tax brackets over the years has resulted in an increase in the tax burden on individuals coupled with an increase in the effective CGT rates, which represents the progressive nature of the South African tax system (Money Martketing, 2018).

In contrast to what Steenekamp had concluded, in the “Third Interim Report of the Commission of Inquiry into certain aspects of the tax structures of South Africa”, the Katz Commission discussed that the tax-to-GDP ratio of South Africa is in line with other comparable developing countries on a per capita income basis (Katz Commission, 1994). It seems that there are two contrasting views concerning the tax burden on South African individuals as concluded in past studies, and this study therefore serves as an important tool to objectively analyse the PIT levels over a 17-year period to support or disregard the views held in the past.

In 2014, Stander conducted a study titled “The tax base of South African individuals: an international comparison” in order to have a thorough understanding of whether the South African tax base is geared towards taxing individual taxpayers as opposed to other tax bases when compared with India, the USA and the UK (Stander, 2014). The study highlighted the similarities and differences in the basis for taxing individuals in the countries mentioned, with the aim of identifying the improvements to be adopted in South Africa (Stander, 2014). The study was qualitative or descriptive in its analysis and did not quantify the tax burden of individuals in South Africa in order to have a holistic, measurable and clear view of what the tax base of South Africa looks like.

Although much research has been devoted to the tax levels in South Africa, little is known in terms of how the South African PIT burden compares to some of its

neighbouring countries, BRICS countries and other developing countries throughout the years, especially after the global financial crisis. The prior studies conducted focused on the tax burden of South Africa broadly without addressing the core factors that affect PIT levels in South Africa. Moreover, past research mainly compared the South African tax system to that of OECD countries and disregarded the inherent economic, political and social differences presented by these countries.

This study will scrutinise the tax burden carried by individual South African taxpayers. In addition, it assesses the fairness of the PIT system for taxpayers and sustainability of SARS relying on PIT as the main revenue stream for the government. Moreover, this study will consider the possible improvements that can be brought about to lessen the tax burden for individuals, broaden the tax base, and still raise the much-needed tax revenue in this prolonged shaky economic climate that the country finds itself in especially after the 2008 global financial crisis. The fairness of the tax system will be measured by benchmarking South African PIT levels against other emerging markets, assessing how the South African PIT system compares or contrasts with that of its peers, and comparing annual salary growth to the progressivity of the tax tables. Sustainability will be determined by reviewing the tax buoyancy of South Africa to see if the increases in tax levels encourage economic growth.

RESEARCH PROBLEM

The total tax revenue collected by SARS has grown tremendously during the period reviewed in this study, namely from the 2003 to 2019 tax years. There has been an exponential growth of 356% in the tax revenue collection, from R282 210 million in 2003 to R1 287 690 million in 2019. For the first time in the 2003 tax year, SARS surpassed the R100 million mark for PIT collection and PIT accounted for 31.3% of the total tax revenue collected in that year (SARS, 2019a). Then the global financial crisis occurred in 2008 and the PIT contribution as a total of tax revenue dropped slightly to 29.5%. Prior to that, the largest part of the South Africa tax revenue was made up of PIT, followed by CIT, then VAT

(SARS, 2018). After 2008, the pressure on various governments around the world including that of South Africa to raise taxes became compelling and inescapable, and PIT remained the most easily accessible source of tax.

South Africa has an emerging economy and it is a country characterised by high income inequality, an ever-increasing unemployment rate and inflationary pressures. One would assume that these economic challenges mentioned here would have a direct impact on tax revenue collected by SARS annually, however, it is almost shocking to see that SARS was able to double the total revenue collection from R282 210 million in the 2003 tax year to R625 100 million in the 2009 tax year and, for the first time in the 2016 tax year, exceeded the trillion-rand revenue target (SARS, 2018). The revenue authority continues to raise the much-needed revenue, and PIT is still the biggest source of the revenue collected annually and on average accounts for about 35% of the total tax revenue since the global economic crisis took place and continues to rise each year (SARS, 2018). Clearly, PIT is fundamental to the tax structure of South Africa as a developing country. On the other hand, even after the 2008 global financial crisis South Africa has not been able to improve the economic factors that one would assume have a direct impact on PIT levels. These economic factors are: the rise in the unemployment rate, below-inflation salary increases, a tight job market, workforce interruptions due to strikes, low or no bonus payments, increases in household expenditure due to inflation and so on. This raises the question of whether or not the tax burden on South African individuals is perhaps too heavy.

The objective of this study is to explore the tax burden carried by individual taxpayers in South Africa by using an international benchmarking and comparative data analysis. Furthermore, the study will review the PIT levels for the 17-year period between 2003 and 2019 to see if the tax imposed on individuals is fair, reasonable and sustainable given the income-earning disparity and inflationary pressures faced by South Africa. The study will also determine whether the current tax policies employed by the tax administrator are progressive and effective in addressing the inherent economic and social challenges present in South Africa and what the best tax reforms are that the

Minister of Finance can introduce without digging deeper into individual taxpayers' pockets.

Various economists have asserted that individual South African taxpayers are taxed higher when compared to taxpayers from other developing countries and, in some instances, even higher than those from developed countries. Mike Schussler, a distinguished economist in South Africa, has on numerous occasions pointed out that South African taxpayers are taxed "to the max" (Business Tech, 2018b). According to Schussler, South Africa had the seventh highest total tax-to-GDP ratio out of a list of 72 countries, signifying that individual South African taxpayers carry one of the highest PIT burdens in the world (Business Tech, 2018b). Even more worrying is that SA also has a higher tax burden than that of the USA, Switzerland, South Korea, Australia and Israel, which are all developed economies (Business Live, 2019). In support of the assertion that South Africans are taxed heavily, Phillip Burger, an economics lecturer, cautioned that South Africa is indeed highly taxed for an emerging market (Business Live, 2019). According to data from Trading Economics (2019b), South Africa's highest PIT rate of 45% is the twenty-second highest in the world as of December 2019. This study will test the widely accepted hypothesis that South Africans are taxed too much as compared to their international counterparts, highlight the possible consequences of this, and recommend the best possible reforms to the PIT system.

RESEARCH QUESTIONS

The central question in this study is: "Are South African individuals taxed too much?" In order to further explore the primary research question, the following imperative sub-questions will need to be answered:

- How much tax revenue has been collected from 2003 to 2019, and how important is the contribution of PIT to South Africa?

- Are individual South African taxpayers able to keep up with the tax burden placed on them over the years?
- How do South African PIT levels benchmark against their international counterparts, including BRICS and some SADC and OECD countries?
- What conclusions can be drawn about the PIT burden of South Africa from the quantitative analysis, and are there any tax reforms and policies that can be implemented in South Africa?

PURPOSE STATEMENT

The primary purpose of this study is to establish the tax burden carried by individual South African taxpayers over the period 2003 to 2019 and to understand how South African PIT levels compare with some other developing and developed countries, to answer the question: “Is the tax burden placed on South African individuals in line with that of their international counterparts?”

Of paramount importance to this study is the international comparison that will identify various tax structures that are successfully working in other countries that can be implemented in South Africa to enhance the effectiveness and progressiveness of the tax system as well as to improve the fairness of the tax system for individual taxpayers. Tax reforms can be regarded as effective and progressive if they can alleviate the tax burden on individuals, improve the tax buoyancy and encourage tax compliance. An international comparison will be done to analyse how South Africa benchmarks against these countries with similar economic and social outlooks. The international comparison will serve as an important tool to assess the South African tax system and it will highlight the similarities and differences in the PIT systems of the countries compared.

This study will analyse the tax burden in South Africa, particularly focusing on PIT levels in relation to the average-income growth and the top marginal rates of different countries. In addition, this paper will look at the fairness of the tax rates progression (bracket adjustments), comparing them to the average inflation rate as well as the tax-to-GDP ratio.

METHODOLOGY AND DATA

This study seeks to establish the tax levels of individual South African taxpayers over the tax years of 2003 to 2019. The time-period selected on the study for comparative purposes is based on the information accessible from various sources. The research methodology utilised in the study will be both quantitative and qualitative in nature, therefore a mixed approach is used. A quantitative study focuses on gathering numerical data and generalising it across groups of people to explain a particular phenomenon (USC Libraries, 2019). In contrast, a qualitative study focuses on the qualities of entities and on processes and meanings that are not experimentally examined or measured in terms of quantity, amount, intensity, or frequency (USC Libraries, 2019).

The descriptive analysis will be employed in the study to elaborate on what constitutes the tax burden on individuals, how does the PIT burden of South Africa influence the economy, and what informs the design of the tax structure. Information derived from the descriptive analysis will form a critical basis of the possible reforms and tax policies that can be adopted in South Africa to assist in growing the economy while simultaneously alleviating the tax burden borne by individual taxpayers.

A research approach whereby the researcher collects and analyses both quantitative and qualitative data within the same study is referred to as the “mixed method”. The study will mainly be quantitative in nature and the methodology used will be mixed in order to achieve a critical and comparative analysis of the PIT levels in South Africa and other countries. Concurrently, a descriptive analysis will be used to interpret the quantitative data contained in the study and to draw a conclusion on the tax levels of South African individuals over the period analysed. Consequently, it can be concluded with utmost certainty that the research methodology utilised in the study will be the mixed method and the study is time-series based. The data to be used will comprise the following:

- Budget speeches from various years,
- Tax statistics reports compiled by the National Treasury and SARS,
- Tax reports of the Margo, Katz and Davis Tax Committees,
- Statistics from other sources, such as StatsSA, OECD, World Bank, International Monetary Fund (IMF), Trading Economics etc.,
- Prior research,
- Journal articles,
- Newspaper articles,
- Internet sources,
- Electronic databases, and
- Books.

Some of the statistical tools used to measure and analyse the data collected include the following methods: percentages, ratios, growth rates, unweighted averages, changes in percentages and year-on-year comparisons.

ASSUMPTIONS AND LIMITATIONS

The study is a comparative analysis of the South African PIT levels for the period 2003 to 2019, and the following assumptions will be upheld throughout this study:

- The countries selected present a similar PIT structure to that of South Africa.
- The sixteen countries (excluding South Africa) used for international comparative analysis are limited to the following:
  - BRICS countries, namely Brazil, Russia, India and China,
  - SADC countries, namely Botswana, the DRC, Mauritius, Mozambique and Zambia,
  - OECD member states, namely Australia, the UK and the USA,
  - The fastest developing countries in Africa, which are Algeria, Egypt, Kenya and Nigeria.
- The data and statistics used from external sources are assumed to be correct, valid and accurate at the time of those studies.

- Information and data needed to successfully carry out this study is readily available and the latest data is used in some instances
- In some instances, original calculations are done to determine the tax levels and the calculations are assumed to be accurate and valid estimates.
- The tax revenue data used in the study will be a representative of the tax collected by the national government, instead of lower tiers of government authorities such as local and provincial governments.
- The study is limited to PIT levels, with the emphasis being on the period under review which is 2003 - 2019

CHAPTER OUTLINE

Chapter 1: Introduction

This chapter primarily contains the research proposal. It will introduce the background of the study, research problem and research questions and state the knowledge gap this study aims to close. The chapter will expand on the literature review, the objectives to be achieved by the study and the methods to be employed in the study to achieve these objectives.

Chapter 2: PIT levels in SA from 2003 to 2019

This chapter will examine how much PIT contributed to the total tax revenue collected by SARS during the 17 tax years examined. This will show that individuals carry a greater tax burden in South Africa than companies. The total population versus registered taxpayers versus taxpaying individuals will be compared over the period under review. In addition, the breakdown of what makes up the taxable income when calculating PIT will be determined. The tax buoyancy over the period 2003 to 2019 will be analysed here. The chapter will also explore what the consensus is about the personal tax burden of South Africa from different tax experts.

Chapter 3: PIT progressivity compared to average earnings over the 2003 – 2019 tax years

This chapter will seek to answer the question: “Are salaries keeping up with the tax rates’ progressivity?” To answer this, the study will use the average annual inflation rates to see if the PIT rebates, thresholds and the low and top marginal tax brackets are adjusted accordingly for inflation. The impact of PIT on income and wealth equity is also discussed here. Furthermore, the possible consequences of relying on tax revenue and in particular, PIT are discussed here.

Chapter 4: An international comparison

This fundamental chapter will compare the tax-to-GDP ratio of South Africa to some SADC, BRICS and OECD countries to see how South Africa PIT levels measure with that of other countries. In addition, this chapter will compare the South African maximum (45%) marginal PIT rate on an international level. Furthermore, this chapter will make reference to the distinctive features of the PIT models of other countries.

Chapter 5: Alternative PIT reforms

This chapter will seek to highlight significant changes that have been made to the income tax on individuals over the years and the impact thereof on the progressivity of the PIT regime. The changes will be explored as contained in the budget speeches by the National Treasury as well as SARS documents from 2003 to 2019. Additionally, this chapter will conclude on the various tax policies and recommendations that have been made by various tax commissions, experts, boards and professionals that may possibly help curb the weighty tax burden placed on individual South African taxpayers.

Chapter 6: Conclusion

In the last chapter, an answer to the research question (“Are South African individuals taxed too much?”) will be formulated based on the findings outlined in the chapters above. The key results of the quantitative analysis in the preceding chapters will be summarised and concluding remarks on the study will be made.

CHAPTER 2: PIT LEVELS IN SA FROM 2003 TO 2019

The central question that this study is seeking to answer is “are South African individual taxpayers taxed too much?” To bring us closer to uncovering an answer to this question, this chapter will look into the PIT levels in South Africa from 2003 to 2019. Tax revenue is a necessary economic tool and very central to the fiscal policies of many countries, especially for a developing country like South Africa which relies mainly on tax revenue to fund its ever-increasing and burdensome government expenditure. The aim of this chapter is to answer the following research question: how much tax revenue has been collected from 2003 to 2019 and how important is the contribution of PIT to South Africa?

The purpose of this chapter is to break down the weightings of the different sources that accounted for the tax revenue from the 2003 to 2019 tax years. In addition, the chapter will explore the composition of PIT in more detail and analyse how it has changed over the years. The chapter will also compare the maximum marginal tax rate of South Africa to that of other comparable countries, to benchmark the PIT burden of South Africans. PIT will be defined and the components that make up PIT will be outlined clearly in this chapter. The objective is to establish how much PIT contributed to the total tax revenue by comparing the proportion of PIT and other taxes to the total tax revenue collected over the period analysed. The chapter will also outline how many people are registered for tax and what percentage of the population is actually responsible for the payment of PIT. In addition, prior literature on the tax burden of South African taxpayers will be explored in this chapter to get a perspective of what the general view is about the tax imposed on individual South African taxpayers.

Different countries use taxes for various purposes. Taxes are used to raise revenue to fund government services, to encourage or discourage certain types of behaviour, to correct market imperfections and to change the distribution of income or wealth (Bird & Zolt, 2005). Tax is the South African government’s main source of income and is levied under the *Income Tax Act 58 of 1962* (hereafter referred to as ‘the Tax Act’) on the taxable income of persons such as companies,

trusts and natural persons (SARS, 2019b). Taxes are traditionally classified as direct (PIT, CIT and other income and capital taxes) or indirect (VAT, excise duties and consumption taxes, and other taxes on products and production) (Szarowská, 2014). Generally, the first group allows greater redistribution as it is impractical to introduce progressivity in indirect taxes. This study will refer to the other taxes found in the Tax Act for comparative purposes, but will particularly focus on PIT. For the purpose of this study, PIT refers to the normal tax that is paid by natural persons on their taxable income using a sliding scale to determine the tax payable, and a natural person refers to any individual human being. The PIT system in South Africa is progressive in the sense that as an individual's taxable income increases, so does the tax they have to pay on it. As a result, the wealthy are taxed more on their income and those whose taxable income grows due to annual salary increases will most likely ascend to the next bracket on the progressive tax table, and are thus taxed at a higher statutory tax rate. This is what makes the South African PIT structure progressive.

PIT is particularly important for a developing country like South Africa, as it can be used to raise substantial revenue to finance the state as the engine of development and, moreover, to redistribute income and wealth (Bird & Zolt, 2005). Steenekamp (2012a) also concurs that PIT serves the purpose of not only raising revenue, but is also important in ensuring that equity objectives are maintained. The World Bank also agrees that the mandate of taxing authorities is to raise revenue to finance the government, in order to allocate human and financial resources of a country accordingly, and PIT plays a pivotal role in the revenue structure (World Bank, 2006). The most important advantage of PIT is its use to improve on fairness in terms of progressivity of taxation (Jordaan & Schoeman, 2018). In the same vein, Szarowská (2014) further explained that the importance of income tax on individuals is not only in its ability to financially contribute to the government revenue goals (on average, PIT is the second most important source of tax revenues in line with Eurostat tax classification), but also to have an influence on government policies and goals, such as economic growth, wealth and income distribution, the country's competitiveness, functional labour markets and fiscal federalism at the same time. Likewise, Tanzi (2004) agrees

that PIT can serve the objective of raising revenues and subsequently that of equity redistribution. The equity objective can only be met if the country generates significant revenue and if this revenue comes mostly from the taxes levied on upper deciles of the income distribution (Tanzi, 2004).

It is evident from a wealth of literature that taxes are important for the fiscal development, and PIT in particular is more important for an emerging economy like South Africa. This chapter will focus on the trend analysis of total tax revenue and further show the composition of South African tax revenue over the 17 tax years. A scrutiny of the growth rate of PIT from 2003 to 2019 in relation to the three main revenue contributors (VAT, CIT and PIT) will be undertaken. Table 1 below depicts the total tax revenue collected as well as the year-on-year percentage growth from the 2003 to 2019 tax years. Tax collection has been on a steady growth since the 2003 to 2019 tax years, except in the 2010 tax year. Notably, the tax revenue performance was at its highest peak in the 2007 tax year just before the economic turmoil struck. The substantial revenue growth in 2005 to 2007 was due to the robust economic growth experienced in those years. Economic growth is represented by an increase in GDP. During the 2007 budget speech, the then Minister of Finance, Trevor Manuel, had positively remarked that the economy had grown more strongly in 2006 than was anticipated and the robust growth was expected to average 5% per year over the next three years (National Treasury, 2007). The generation of new jobs, broadened consumer base and rapid growth in investment contributed immensely to the robust 5% GDP (National Treasury, 2007).

It was not long after the South African economy grew by an average of 5% from 2003 to 2007 when uncertainty in the global market started looming. The severe turbulence in the housing market in North America came with disruptions that rapidly affected the global landscape and, in turn, slowed the growth prospects worldwide (National Treasury, 2009a). The decline in revenue collected in the 2010 tax year can be attributed to the global financial crisis that took place in late 2007 right through to late 2009. Recessionary effects such as rising inflation, higher oil prices and wide-scale job losses negatively affected the tax revenue collection in South Africa as evidenced by the sharp decline in the total tax

revenue collected, which resulted in a negative percentage growth thereof. Although the economic outlook in South Africa has not returned to its former glory years of averaging 5% per annum before the global meltdown, the domestic economy managed to stabilise due to strong commodity prices, low interest rates and faster global growth (National Treasury, 2011). Consequently, the global economy recovery resulted in an improvement in the tax revenue collection as evidenced by the moderate growth from the 2011 to 2019 tax years shown in Table 1 below. The increase in tax revenue has been mostly attributed to a combination of factors, including inflation, high economic growth, high commodity prices, improvements in tax administration and tax compliance (SARS, 2010). The highlight of the post-global economy crisis years has been the revenue collection surpassing R1 trillion from the 2016 tax year onwards.

Tax years	Total revenue (million)	Percentage change year-on-year
2002/03	R282 210	11.9%
2003/04	R302 508	7.2%
2004/05	R354 980	17.3%
2005/06	R417 334	17.6%
2006/07	R495 515	18.7%
2007/08	R572 871	15.6%
2008/09	R625 100	9.1%
2009/10	R598 705	-4.2%
2010/11	R674 183	12.6%
2011/12	R742 650	10.2%
2012/13	R813 826	9.6%
2013/14	R900 015	10.6%
2014/15	R986 295	9.6%
2015/16	R1 069 983	8.5%
2016/17	R1 144 081	6.9%
2017/18	R1 216 464	6.3%
2018/19	R1 287 690	5.9%

Table 1: Total revenue collected (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

The study will now focus on the composition of tax revenue in order to understand how PIT contributes to the whole tax structure in relation to other tax categories. The combined revenue contribution of PIT, VAT and CIT has been accounting for over 80% of the total tax revenue of South Africa in the years under review, as illustrated in Figure 1 below. The fuel levy, excise and customs duties account for around 11% and other taxes, including dividends tax (formerly known as secondary tax on companies or STC), account for the remainder of around 9%. For this reason, the comparative analysis of PIT will only be benchmarked against the other main revenue streams, these being CIT and VAT.

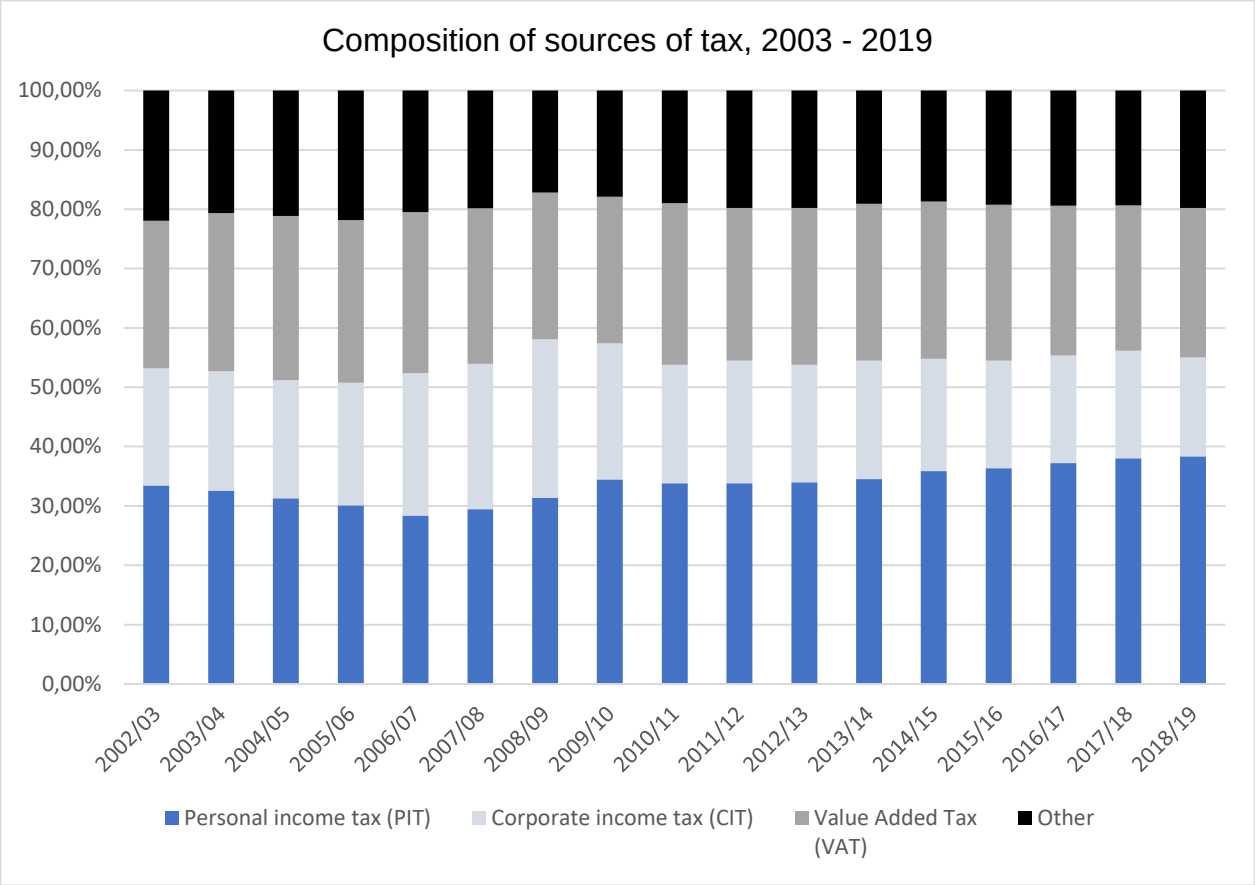

Figure 1: Composition of sources of tax (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

Figures 2a and 2b below depict the trends of PIT, CIT and VAT as part of the total revenue collected from 2003 to 2019. Figure 2a contrasts the composition of main sources of tax collected in 2015 and 2019 tax year - which is the latest available information from SARS. For several years now, tax revenue growth in South Africa has mainly been supported by PIT as evidenced by Figures 2a and

2b below. There has been an increase in the PIT contribution from 33.4% in 2003 to 38.3% in 2019, and PIT remains the main portion of tax revenue compared to other direct taxes, such as CIT and dividends tax. The positive growth in PIT can be ascribed to a combination of things, including the tax register, tax rate increases, above-inflation adjustments to salaries, upward social mobility of taxpayers as well as greater tax compliance (SARS, 2018). VAT tends to be the main contributor in comparison to other indirect taxes, including custom duties, excise taxes and the fuel levy.

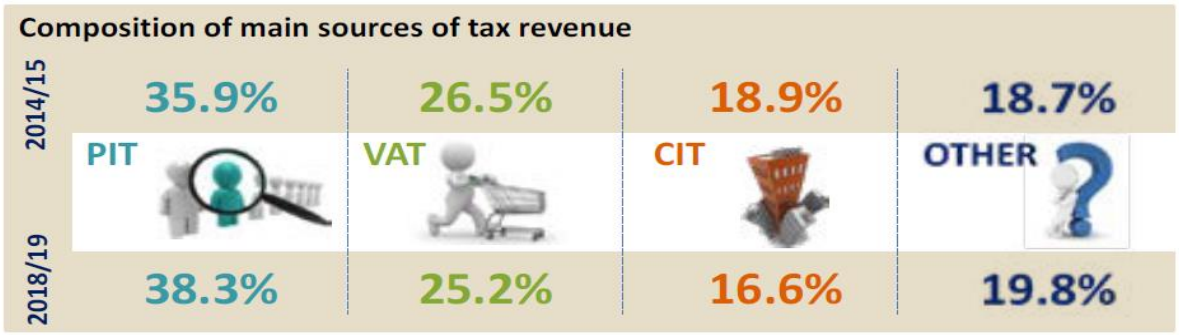

Figure 2a: Composition of main sources of tax revenue, 2015 vs 2019 (adapted from: SARS, 2019a)

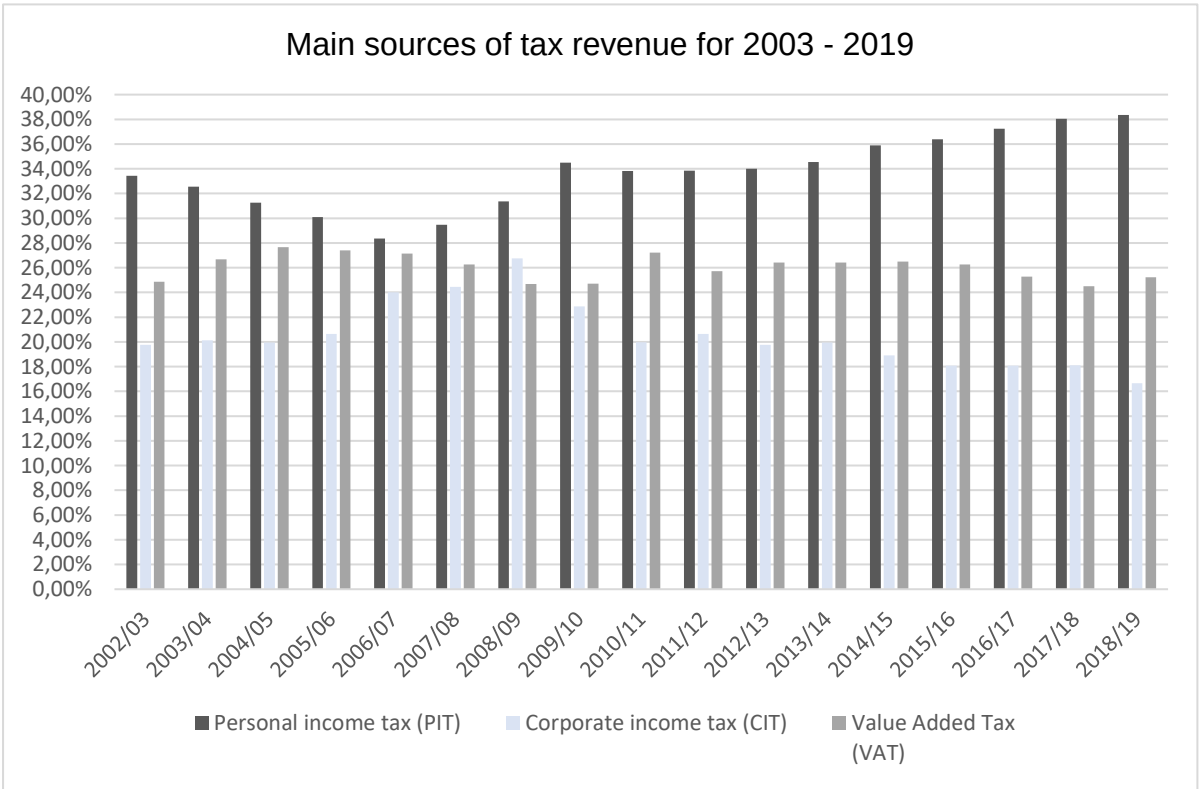

Figure 2b: Main sources of tax revenue, 2003-2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

On average, PIT has been constituting 35% of the total tax revenue from 2003 to 2019. In the tax year ended 2007, the PIT contribution was at its lowest level at 28.4%. This was partly due to the moderate PIT cuts and the elimination of the retirement fund tax (National Treasury, 2007). Figure 3 below shows the breakdown of taxes collected by the government from the latest national statistics available at the time of this study. PIT had again outperformed other taxes and contributed over a third of the tax pie in 2018 as shown in Figure 3 below.

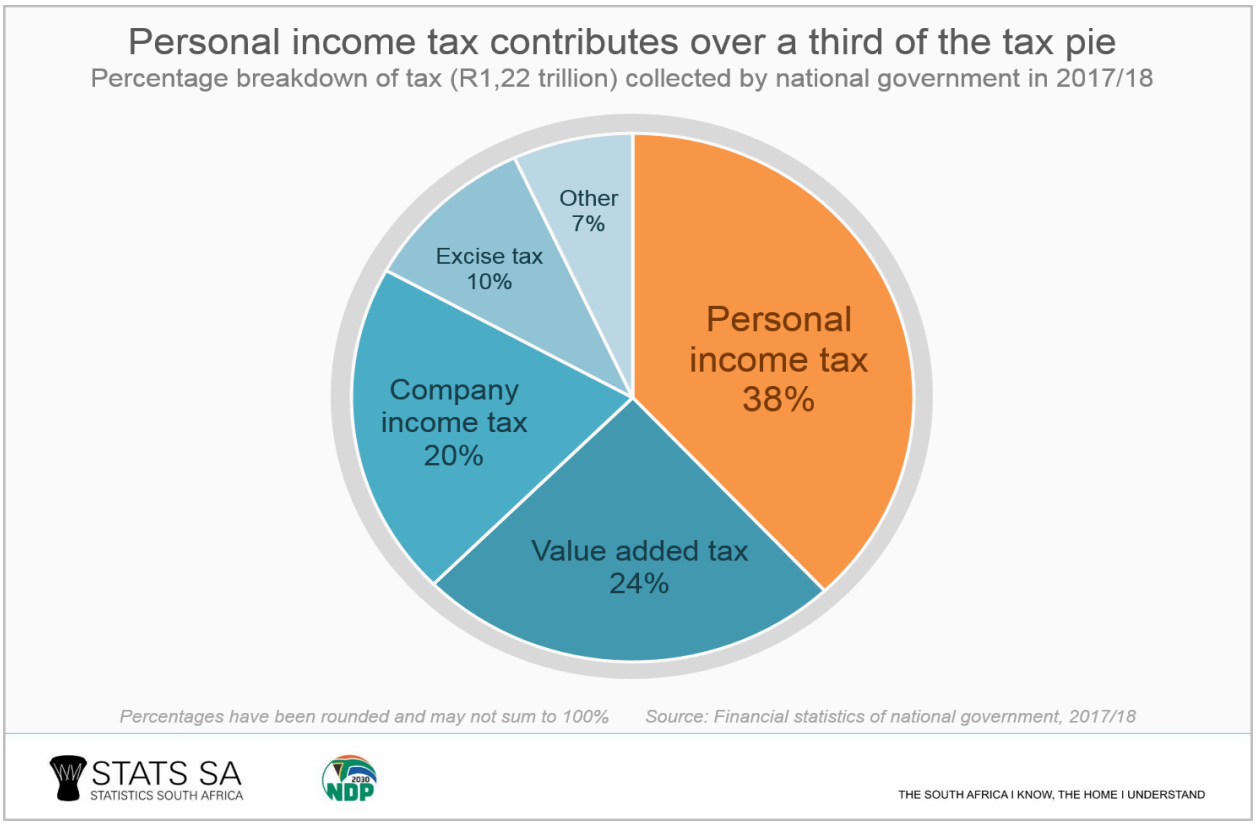

Figure 3: Tax contribution pie chart for 2017/18 (Stats SA, 2019)

Moreover, there was a continual increase in the individuals registered for PIT from the 2003 tax year onwards, however, for the first time in the 2007 tax year, the percentage of year-on-year growth had declined from 10.6% in 2002/2003 to around 6.9% in 2006/2007 (National Treasury, 2008a). Changes in tax policy between 2006/07 and 2008/09 included significant PIT relief, through adjustments to the PIT brackets and the addition of primary and secondary rebate thresholds (National Treasury, 2009b). PIT contribution has been at its highest level at 38.3% in the 2019 tax year. The contributing factor to the growth was the significant rise in the number of registered individuals from 21 million to 22 million

in the year ended March 2019 (SARS, 2019a). SARS made the following statement regarding the recent improvement in the tax registration:

> SARS continued to broaden the tax base and expand its taxpayer and trader register through the pillars of the compliance model, namely: education, service and enforcement programmes. The growth of the tax register is influenced by socio-economic conditions, tax policy and legislative amendments. SARS has increased registration compliance by introducing bulk registration at places of employment and providing an online facility that enables employers to register staff when submitting their monthly Pay-As-You-Earn (PAYE) returns (SARS, 2018).

The number of registered individuals include any natural person and for the purpose of this study, the definition of registered individuals will be limited to taxpayers who were potentially assessed for normal tax excluding special trusts. The number of registered individuals is considered at the date of 31 March of every year and, by definition, registered individuals are classified as active taxpayers; this excludes cases of deceased estates, or where a taxpayer's status is in suspense or dormant, the taxpayer is insolvent, their address is unknown, or they are inactive (SARS, 2018). Income tax on persons and individuals is the government's main source of income and, on average, around 95.5% of taxes on persons and individuals is from PAYE (National Treasury, 2008b). Table 2 below shows the total registered individual taxpayers from 2003 to 2019 and the year-on-year percentage change over the period. The year-on-year percentage change is the change in the figure of the current year compared with the figure in the previous year expressed as a percentage. Data on registered individuals was not available for the tax years prior to 2002. The primary objective of SARS is to grow the tax register and in so doing reduce the tax gap. The level of growth is influenced by economic conditions, tax policy, legislative amendments, tax-base broadening activities (ensuring that those entities not registered for tax are registered) and the overall compliance climate (SARS, 2011).

Tax year	Registered individuals	Percentage change year-on-year
2002/03	3 415 432	Not available
2003/04	3 777 005	10.6%
2004/05	4 115 293	9.0%
2005/06	4 476 261	8.8%

Tax year	Registered individuals	Percentage change year-on-year
2006/07	4 764 105	6.4%
2007/08	5 204 805	9.3%
2008/09	5 540 646	6.5%
2009/10	5 920 612	6.9%
2010/11	10 346 175	74.7%
2011/12	13 703 717	32.5%
2012/13	15 418 920	12.5%
2013/14	16 779 711	8.8%
2014/15	18 185 538	8.4%
2015/16	19 075 270	4.9%
2016/17	19 980 110	4.7%
2017/18	21 104 375	5.6%
2018/19	22 170 513	5.1%

Table 2: Registered individuals, 2003-2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

The tax registry for individuals has seen a positive year-on-year growth from the 2002/3 to 2018/19 tax year. By contrast, the number of companies registered for income tax has decreased from 3.2 million in 2017/18 to 2.0 million in 2018/19 (SARS, 2019a). There has been a dramatic escalation on individuals' registrations over the period analysed. The total registry indicated just over 3.4 million in 2003 and increased dramatically by over 549%, translating to just over 22 million people being registered in the tax year ended 2019. The most notable spike in tax registration is seen in the 2010/11 tax year (see Figure 4 below). There was an exponential year-on-year growth of 74.7% in the number of registered individual taxpayers from the 2010 to 2011 tax year (Table 2 above). This was primarily due to the introduction of the employer filing system that was made available in 2010 which required all individuals issued with an employee tax certificate (commonly known as an IRP5) to be registered, regardless of how much they earn (SARS, 2011). This implied that not every registered taxpayer was actually being assessed for PIT and actually paying any income tax, however, this had a positive outcome for SARS as the chances of collection and

better administration of taxes improved. The effect of the widespread tax registration translated into sustainable growth in the PIT collection from the 2011 to 2019 tax years (see Figures 2a and 2b above). The then Minister of Finance, Pravin Gordhan, had noted in the 2011 national budget speech that tax revenue had finally recovered after the global financial crisis. PIT as well as VAT receipts and customs duties had increased strongly compared to CIT revenue, which was still suffering from the effects of the 2009 recession on company profits (National Treasury, 2011).

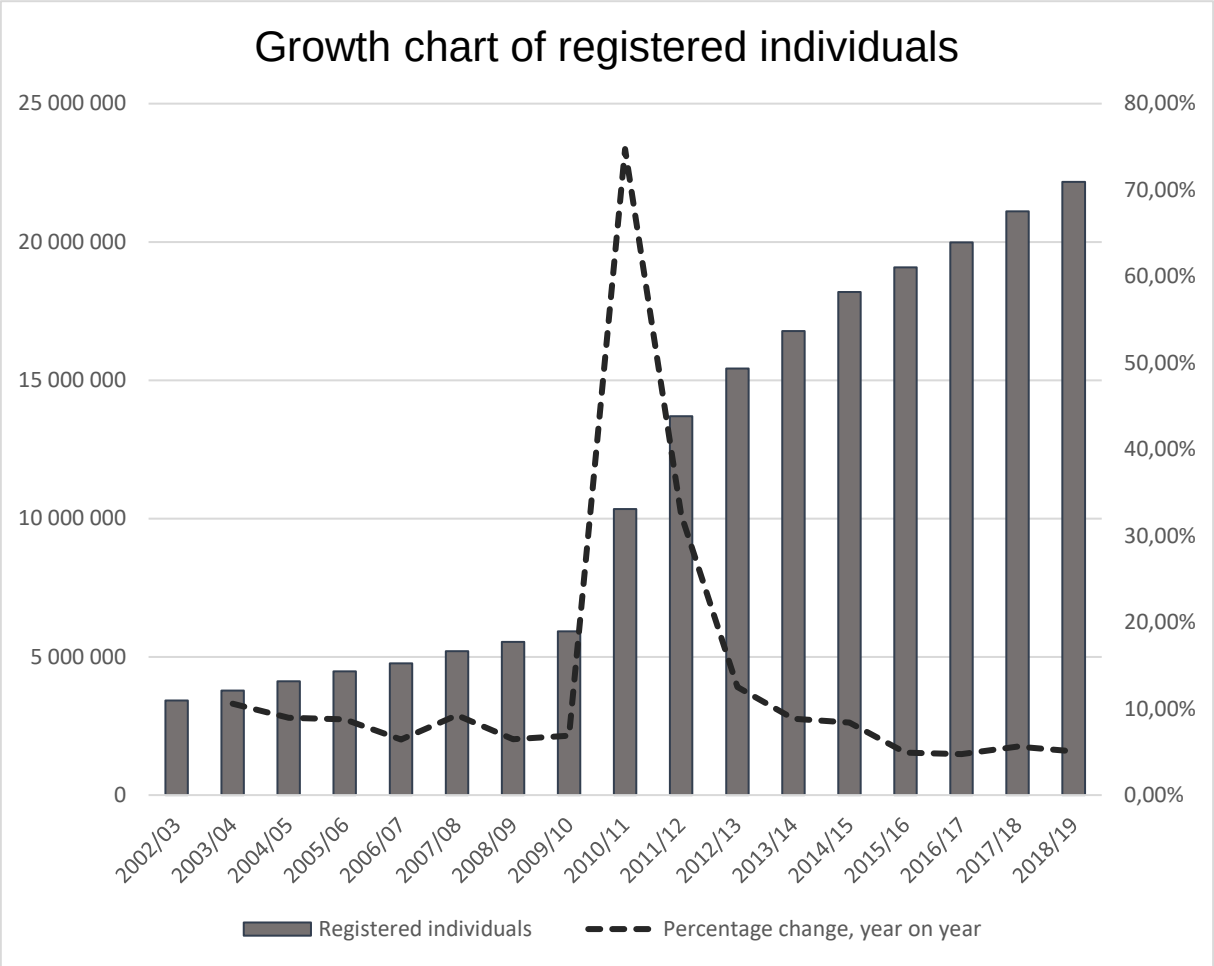

Figure 4: Growth chart of registered individuals, 2003-2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

The Katz Commission was tasked with the delicate but important job of trying to find the right balance in a form of PIT reforms that would successfully reduce the overall tax burden and concurrently strive to grow the tax base, and effectively raise the highly needed revenue to fund the government's financial goals. In

reducing the tax burden, the recommendations were centred around broadening the tax register, keeping the tax rates as low as possible, reducing the number of tax brackets and simplifying the tax structure in order to build on tax morality and compliance (Katz Commission, 1994). In almost every annual budget speech, the various Ministers of Finance emphasise that the strategic objective in growing the revenue collection lies in broadening the South African tax base by growing the number of registered taxpayers. The consistent growth in the number of registered individuals was influenced by improvements in socio-economic conditions, tax policy and legislation. The introduction of bulk registration at places of employment ensured that compliance was enhanced and that it was easier for employers to submit PAYE returns (SARS, 2019a).

Tax year	Registered individuals	Assessed individuals	Percentage assessed
2002/03	3 415 432	3 352 190	98.15%
2003/04	3 777 005	3 542 006	93.78%
2004/05	4 115 293	3 605 378	87.61%
2005/06	4 476 261	3 215 192	71.83%
2006/07	4 764 105	4 318 512	90.65%
2007/08	5 204 805	4 645 657	89.26%
2008/09	5 540 646	5 076 863	91.63%
2009/10	5 920 612	5 532 652	93.45%
2010/11	10 346 175	6 084 907	58.81%
2011/12	13 703 717	6 359 048	46.43%
2012/13	15 418 920	6 103 488	39.58%
2013/14	16 779 711	5 991 934	35.71%
2014/15	18 185 538	5 672 322	31.19%
2015/16	19 075 270	5 365 552	28.13%
2016/17	19 980 110	4 898 565	24.52%
2017/18	21 104 375	4 917 029	23.30%
2018/19	22 170 513	Not available	Not available

Table 3: Registered vs assessed individuals, 2003-2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

The efforts put in by SARS to grow the tax registry have been impressive and could potentially assist in growing the tax base, however, one should be mindful that not all registered taxpayers actually bear the tax burden. Even more worrying is that the South African population stood at over 58.78 million in 2019 and, with the tax registration that was at 22 million (see Table 3 above), this implied that about 37% of taxpayers fund the state resources. The picture becomes even bleaker when the number of assessed taxpayers who submitted tax returns and were potentially charged for a tax liability is compared with the South African population. When the narrow view is considered, it becomes apparent that the actual number of taxpayers who are in reality carrying the tax burden in South Africa are only a fragment of registered taxpayers and could imaginably be strained. The number of registered taxpayers was at its highest level in the 2019 tax year at just over 22 million, however, only 23.3% of the registered individuals were assessed. A call for concern was that the number of social grants recipients was at a staggering 17 million as at December 2018 and, in the very same year, only 4.9 million taxpayers actually paid PIT which translates to a mere 28.8% of individual taxpayers carrying the tax burden to maintain the social mandate of the government. Although the highest number of registered taxpayers was recorded in 2019, it is shocking to see that the lowest number of taxpayers was actually assessed in the very same year when the tax periods between 2003 to 2019 are scrutinised. From the 2010 to the 2019 tax years, the number of assessed individuals has been on a downward spiral, although there has been a substantial growth in the number of registered individuals. Steenekamp (2007) noted that the ability of people to pay taxes, and in particular their willingness to pay, is dependent on the types of government services provided and how well the government can curb corruption. If taxpayers feel that the government meets their needs, their willingness to comply with the tax authority and adhere to the tax administration grows.

One of the common measures that can be used to quantify the tax burden carried by the taxpayers is the tax-to-GDP ratio. Steenekamp (2007) indicates that when taxes are analysed, it is important to present tax levels and compositions as ratios to GDP. The reason is that tax-to-GDP, also known as the tax ratio, provides an

indication of the size of the government sector as well as the tax burden imposed on taxpayers and some indication on whether a country can raise more taxes without burdening its taxpayers. Thus, the tax ratio and in particular the PIT-to-GDP ratio will be a fundamental measure of the tax burden of individual South African taxpayers. The tax-to-GDP ratio is represented in nominal and real GDP, and the difference is defined below.

> GDP is the total market value of all goods and services provided by a country during a certain time usually measured over every quarter or year. GDP is mainly used to ascertain the economic growth, purchasing power, and overall economic health of a nation using real and nominal terms. Nominal GDP takes price changes, money supply, inflation and changing interest rates into account when calculating GDP. Real GDP uses nominal GDP after it has been adjusted for inflation or deflation by comparing and converting prices to a base year's prices. By adjusting for price changes, the final number won't reflect false increases or decreases in GDP due to fluctuation in prices, and it is a more accurate representation of a country's economic activity (MasterClass, 2019).

The nominal GDP is commonly used to aggregate the contribution made by taxes to the government fiscus, as changes to the tax-to-GDP ratio are driven by the relative changes in nominal tax revenue and GDP. If the growth in tax revenue over a consecutive period is more than that of the total GDP, then the tax ratio will increase. Consequently, if the increase in GDP is more than the increase in the tax revenue, then the tax ratio will decline. This implies that the tax-to-GDP ratio does not necessarily mean that the amount of tax revenue has increased in nominal or even in real terms, as the tax ratio can be influenced by either changes in tax revenue or GDP (OECD, 2018b). An ideal tax-to-GDP ratio differs for each country depending on whether it is an emerging or developed country. A country analysis of tax-to-GDP ratios will be discussed in detail later in this study to measure how South Africa is performing compared to its counterparts and developed countries. It is believed that for a country to become developed, it needs to collect 25-30% in taxes to GDP (Bird, 2008). The 25% threshold is deemed sufficient to scale up infrastructure spending. However, Bird (2008) warns that the aim to increase tax revenue through more vigorous collection efforts in developing economies is naïve, and developing countries should rather focus on other revenue-maximising efforts, such as broadening the tax base (especially on consumption taxes), reducing tax rates on income taxes, and improving tax administration.

The IMF and OECD believe that the tax-to-GDP ratio matters as it can give a clear indication of the direction that tax policy and administration need to take in any given country, and it can then be measured against economic growth and development (ACCA Global, 2018). Research conducted by the IMF suggests that a tax-to-GDP ratio of above 15% creates a conducive environment for investment and development, as it means that there is sufficient tax revenue collected in order to invest in infrastructure and education, for example, and this can have a massive effect on an economy (ACCA Global, 2018). Table 4 below thus illustrates the main sources of tax revenue contribution to GDP from the 2002/3 to 2018/19 tax years. The tax-to-GDP ratio of South Africa has been above the 15% recommended by IMF when the focus is in nominal terms, and only in real terms does the tax ratio reach 15% in the 2005 tax year. The base year used for the real GDP is adjusted or fixed for inflation based on the 2010 constant prices as provided by the South African Reserve Bank (SARB), as those are the most up-to-date statistics available on the Statistics South Africa (StatsSA) website at the time of this study.

Tax years	(PIT)	(CIT)	(STC/ DT)	(VAT)	Indirect taxes (other)	Tax to nominal GDP	Tax to real GDP at 2010 prices
2002/03	7.4%	4.4%	0.5%	5.5%	4.4%	22.2%	13.2%
2003/04	7.4%	4.6%	0.5%	6.1%	4.2%	22.7%	13.5%
2004/05	7.6%	4.8%	0.5%	6.7%	4.6%	24.2%	15.0%
2005/06	7.7%	5.2%	0.7%	7.0%	4.8%	25.4%	16.8%
2006/07	7.5%	6.3%	0.8%	7.1%	4.6%	26.3%	18.9%
2007/08	7.9%	6.6%	1.0%	7.0%	4.3%	26.8%	21.2%
2008/09	8.6%	7.3%	0.9%	6.8%	3.8%	27.5%	23.4%
2009/10	8.3%	5.5%	0.6%	5.9%	3.7%	24.0%	21.8%
2010/11	8.4%	4.9%	0.6%	6.7%	4.1%	24.7%	23.8%
2011/12	8.6%	5.2%	0.7%	6.5%	4.3%	25.3%	25.6%
2012/13	8.7%	5.1%	0.6%	6.8%	4.4%	25.6%	27.4%
2013/14	9.1%	5.3%	0.5%	7.0%	4.5%	26.4%	29.7%
2014/15	9.8%	5.1%	0.6%	7.2%	4.5%	27.2%	32.2%

Tax years	(PIT)	(CIT)	(STC/ DT)	(VAT)	Indirect taxes (other)	Tax to nominal GDP	Tax to real GDP at 2010 prices
2015/16	10.0%	5.0%	0.6%	7.2%	4.7%	27.5%	34.8%
2016/17	10.2%	5.0%	0.7%	6.9%	4.6%	27.4%	36.7%
2017/18	10.7%	5.1%	0.6%	6.9%	4.8%	28.0%	38.7%
2018/19	11.0%	4.8%	0.7%	7.2%	5.0%	28.6%	40.8%

Table 4: Main sources of tax-to-GDP, 2003-2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a) (Stats SA, 2019) and own calculations

The tax-to-GDP ratio in nominal terms has been growing continually from 2003 at 22.2% until 2009 at 27.5%. Then in the 2010 tax year, the tax ratio nominally declined to 24%. This trend follows a similar pattern as that of the revenue collections, as there was a decline of 4.2% in the tax revenue (see Table 1 above) from the 2009 to 2010 tax year. This was due to the recession of 2008, which disrupted SARS' ability to collect maximum revenue due especially by companies in the succeeding years. The highest tax-to-GDP ratio in nominal terms was at 28.6% for the year ended in 2019. The tax ratio in nominal terms was higher than the tax ratio in real terms from the 2003 to 2011 tax years, however, the real GDP rose at an even quicker rate from 2012 and reached a maximum of 40.8% in 2019.

The PIT-to-GDP ratio constitutes the largest portion in the total tax-to-GDP ratio from the 2003 to 2019 tax years. Moreover, the PIT to GDP ratio has been growing constantly since 2003 and there was a slight dip of 0.3% (see Table 4) from the 2009 to 2010 tax years. The CIT-to-GDP ratio took the hardest knock after the recession as it moved from 7.3% in 2009 to 5.5% in 2010 and it has been challenging to get the CIT-to-GDP ratio to its former glory, as it only averaged 5.1% after the recession (see Table 4). The continued slack in CIT contribution is a result of low production in the face of continued power outages, several labour unrests and a general decline in the economic climate. When compared to other tax types, PIT was the least tainted by the negative after-effects of the economic and financial crisis in 2008. However, the PIT contribution

has been slower when compared to the exponential addition of the individual taxpayers to the tax register since the 2011 tax year. There was year-on-year growth of 74.7% in the tax registrations in 2011, but the effect of this in substantially growing the PIT contribution as would have been expected had not been evident. Various economists had attributed this to negative effects in the economy, such as lower bonus payments, moderate wage settlements, little to no increase in salaries, continued job losses in various sectors and a stabilisation of overall public service employment (National Treasury, 2018).

The PIT-to-GDP ratio was over 7% from 2003 to 2008 and gradually increased over the years until it reached 11% in the 2019 tax year. Jordaan and Schoeman (2018) indicate that for economic growth to be optimal, South Africa's PIT-to-GDP ratio should not exceed 6.7%. Based on this assertion by Jordaan and Schoeman, South Africa's PIT-to-GDP ratio has not been at the optimal level to encourage economic growth as the ratio has been well above the recommended optimal level of 6.7%, from a minimum of 7.4% in 2003 to 11% in 2019 (see Table 4 above). The same sentiments were shared in an online article by PwC, titled "Tax reform needed to promote economy" which stated that the South African tax system is not doing enough to enhance economic growth, hence a comprehensive tax reform is needed. The reasons cited were the heavy reliance as well as high tax rates on CIT and PIT, which deters economic growth (PwC, 2014). Steenekamp (2012b) observed that contributions from personal taxes (35.7%) were usually more than double the share of income tax on companies (15.4%) in developed countries, because CIT is an easier source to exploit than PIT, and, consequently, the share of company tax far exceeds that of tax payable by individuals in most countries. Unlike other developing countries, South Africa displays a different pattern in terms of the reliance placed on taxing individuals when the contribution of taxes is calculated on the country's GDP. The contribution made by the income tax from individuals to the country's GDP ratio is actually over double (11%) the income tax from corporate taxes (4.8%) and this pattern remained constant during the period analysed in this study. Another study that investigated the use of PIT for redistributive proposes found that in developed countries, PIT revenues are about 8-10% of GDP and only about 1-2% in

developing countries, while the difference is far worse in some regions with high inequality (Bird & Zolt, 2005). Again, South Africa follows the regime of developed countries, which begs the question of whether the burden placed on South African individuals is too heavy.

Tax buoyancy or tax elasticity is an indicator used to measure the efficiency, effectiveness and responsiveness of the tax levels and policies that have been employed by policy-makers in encouraging economic growth (Steenekamp, 2007). For instance, if the tax policies implemented have been successful in growing the tax revenue base, this will yield a positive outcome for tax revenue growth and, as a result, the tax buoyancy ratio will be above one. Tax buoyancy is calculated as a ratio of percentage growth in tax revenues to growth in nominal GDP for a given year, and if a country attains a value of one in any given year, then the economy is growing in proportion to the level of taxation. Taxes can give an indication of the health of the economy through the tax-to-GDP ratio, and the revenue buoyancy represents the resultant impact which tax has on growing the economy. A buoyancy ratio greater than unity (one) over the long term supports the sustainability of fiscal policy (National Treasury, 2018). Table 5 and Figure 5 below indicate how the average and annual tax buoyancy in South Africa performed over the 2003 to 2019 tax years. The tax buoyancy ratios presented below are calculated using net tax revenues (total tax revenue less Southern African Customs Union [SACU] payments) for the main budget, as reported by National Treasury and SARS (2019) and extracted from the Tax Statistics issued annually (Steenekamp, 2007).

Tax buoyancy	2002 – 2003	2003 – 2004	2004 – 2005	2005 – 2006	2006 – 2007	2007 – 2008	2008 – 2009	2009 – 2010	2010 – 2011	2011 – 2012	2012 – 2013	2013 – 2014	2014 – 2015	2015 – 2016	2016 – 2017	2017 – 2018	2018 – 2019
Annual	0,74	0,85	1,55	1,54	1,38	1,15	0,83	-0,71	1,18	1,13	1,22	1,20	1,38	1,26	0,97	1,00	1,23
Average	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05	1,05

Table 5: Tax revenue buoyancy, 2003 – 2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

The growth rates have varied significantly from year to year. The year-on-year elasticities varied between a low of 0.74 and a high of 1.55, with the exception of an absolute negative growth of -0.71 experienced in the 2010 tax year (see Figure 5 below). This is not shocking, as South Africa, like many countries, was still recovering from the severe consequences of the economic meltdown that occurred in 2008. Recovery has been promising and steady in the years succeeding the global financial crisis, with both tax and economic growth levels above a buoyancy of one. Between 2010/11 and 2015/16, tax revenue grew faster than the economy and, as a result of the large tax increases in 2015/16, this trend was expected to continue. However, tax revenue growth subsequently slowed down in the 2016/17 tax year, effectively matching the pace of economic growth (National Treasury, 2018). The tax buoyancy was suddenly below unity since 2017 and just at exactly unity in the 2018 tax year, due to the technical recession that was imminent from the 2017 tax year.

Moreover, the other major reason for the sudden slow pace in the tax buoyancy was the shift in the dividend withholding tax revenue from the previous year, as some taxpayers aimed to avoid paying the higher rate of 20% that was introduced in the 2017 budget speech (National Treasury, 2018). Higher VAT refunds compared to those of the previous years and slower growth in company taxes also contributed to the decline in the tax growth. Additionally, the decrease in the demand for wage workers severely affected PIT, and a weaker consumer outlook coupled with weaker import growth resulted in large shortfalls of VAT and custom duties. Much of the performance of the tax buoyancy is influenced by the changes in the PIT contribution and expectedly so, as personal taxes account for a major share of the South African tax structure.

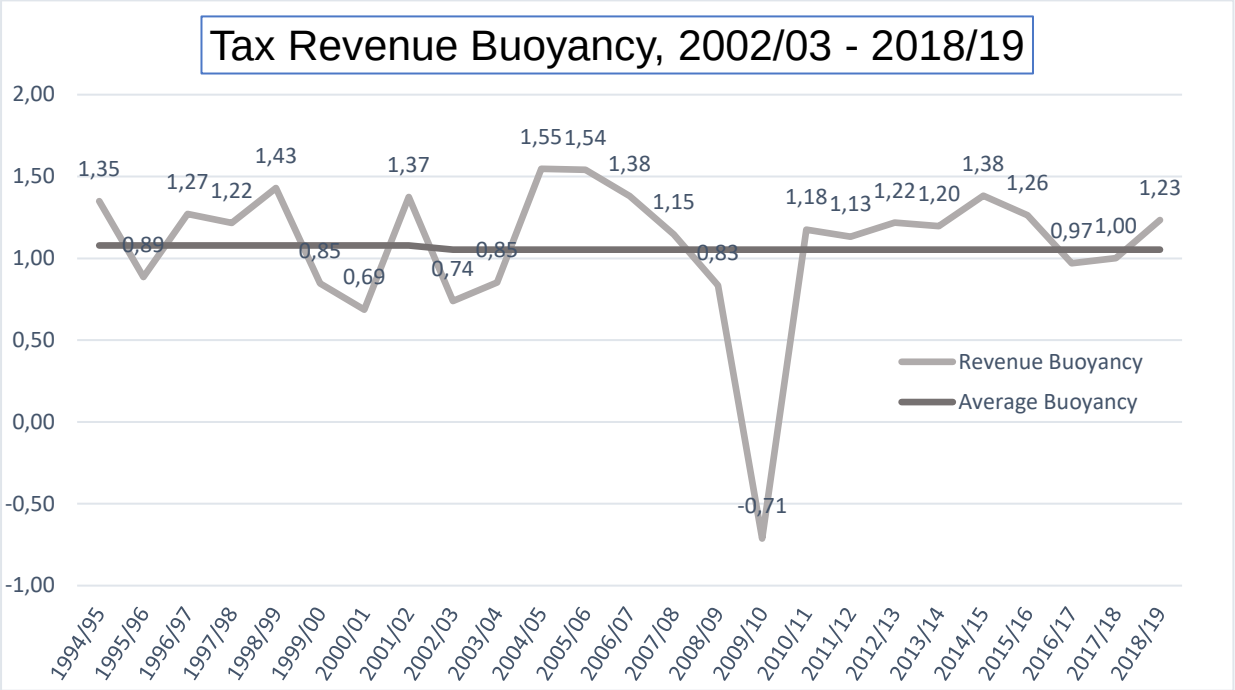

Figure 5: Tax revenue buoyancy 2003 – 2019. (SARS, 2019a)

The revenue buoyancy ratio fell short of attaining the desired ratio of above one in 5 out of 17 tax years analysed between 2003 and 2019, but the tax revenue has been able to make a meaningful contribution to the South African economy in most of the years reviewed. However, growth in the total tax revenue did not correlate with the economic growth in the 2017 and 2018 tax years, and, as a result, the tax elasticity was at 0.97 and 1 respectively and declined below the long-term average of 1.05 for the period under review. This can be attributed to the technical recession that loomed in 2016. The technical recession resulted in lower than expected collections in taxes on income and profits, subdued VAT and PIT growth levels due to lower wage settlements and an increasing unemployment rate (SARS, 2018). When the period is extended and sub-Saharan African countries are included in an extensive buoyancy analysis, South Africa is ranked eighth, with an average buoyancy of 1.29, indicating that revenues have on average been growing faster than the economy (Steenekamp, 2007). This finding further validates the importance of taxes to the economic growth and how intensively the South African government depends on the usage of taxes to aid the economy. According to SARS (2018), during the recessionary phases the growth in tax revenues is usually higher than the growth in the

economy, putting pressure on revenue collection. Revenue growth in South Africa is mainly supported by PIT, and policy changes to PIT can influence the overall direction of the tax buoyancy in relation to the growth of the economy.

Schussler is of the view that the tax burden placed on individuals in South Africa is amongst one of the highest in the world (Business Live, 2019). The economist stated that the country was situated at number twelve amongst the most-taxed countries in the world, according to the database obtained from the International Centre for Tax and Development (ICTD) (Business Live, 2019). Steenekamp (2012b) supports this claim, stating in numerous studies that the average tax burden to GDP of South Africa is higher than some of the developed and developing countries, and the share of PIT generally exceeds that of developing and least developed countries. In comparative terms, South Africa seems to be exhibiting too much reliance on PIT, and this further substantiates the claim that South African individuals carry a heavy tax burden as compared to other developing countries and that individual taxpayers are exploited far more than corporates. Further exploitation might have detrimental consequences for revenue growth and economic stimulation. Moreover, taxpayers' compliance levels and tolerance will be put to the test if the tax burden on individuals becomes heavier and unbearable over time. Bird and Zolt (2005) have put forward that if potential taxpayers perceive that their preferences are properly represented and delivered by political institutions and consider the government to be resourceful rather than wasteful, they may be more willing to tolerate higher levels of taxation and to comply with their tax obligations.

CHAPTER 3: PIT PROGRESSIVITY COMPARED TO AVERAGE EARNINGS OVER THE 2003 TO 2019 TAX YEARS

According to SARS (2018), PIT is the normal tax that is paid on an individual's taxable income. An individual's taxable income is determined once the gross income has been calculated and all the applicable exemptions, deductions and allowances have been taken into account. Remuneration, business income, trust income, director's fees, investment income, annuities and pension income are some of the many incomes an individual may receive and thus are included in their taxable income (SARS, 2019b). This chapter seeks to answer the following questions: were individual South African taxpayers able to keep up with the tax burden placed on them over the years analysed, and are the PIT levels fair? The answers to these questions will be revealed by determining what type of earnings PIT is mainly made up of and whether the inflationary changes in earnings are taken into account when the progressivity of the income tax structure is outlined by the Minister of Finance annually. One of the advantages of PIT is the use of it to improve on fairness in terms of progressivity of tax and encouraging growth (Jordaan & Schoeman, 2018). Additionally, when the PIT structure is progressive enough and the PIT levels are set at the right measure, the potential to expand the tax base and thus grow the tax revenue without immensely burdening individuals increases. Some of the different reforms and policies to the PIT structure that were implemented over the years by policy-makers will be broadly referred to in this chapter.

It is widely believed by tax experts that the PIT system plays a pivotal role in the tax system of a developing economy such as South Africa, as it can be used to do the following:

- Firstly, to redistribute income equitably to reduce the levels of income and wealth inequality;

- Secondly, to allocate the tax burden in a manner considered to be politically fair;
- Thirdly, to raise the maximum amount of revenue to fund the state's resources, given the various economic and political constraints, and;
- Finally, to alleviate poverty through pro-poor tax policies that seek to free the poor from some of their tax burden (Bird & Zolt, 2005).

Steenekamp (2012a) has pointed out that South Africa is a country known to be associated with high levels of unemployment, large social and income inequalities, and minimal foreign direct investment, therefore a PIT system that mitigates these social and economic challenges is of utmost importance as it can help to stabilise the economic growth rates over time. The goal of tax reforms should be to promote economic growth and to build a sustainable revenue base for government, without compromising the equity and fairness of the system (PwC, 2014). The right PIT structure will not only raise the much-needed revenue, but will also encourage economic growth and income equality, and will lift employment. Governments have therefore been on a quest to find alternative PIT reforms that can achieve the economic and social goals of their countries. This may be possible if the focus of the tax structure is shifted towards taxes that have the least negative impact on economic growth, investment and employment while at the same time reducing reliance on taxes (which distorts incentives to work and invest) (PwC, 2014). The OECD also shares the same sentiments that the best tax policy options for promoting economic growth when measured as GDP per capita are those that will have a smaller negative impact and influence on economic decisions of individuals and corporates (OECD, 2010).

The best tax policy options for promoting economic growth has been ranked by the OECD from least to most distortionary, and they are (in the following order): recurrent taxes on immovable property, then consumption taxes and other property taxes as well as environmentally-related taxes, PIT and, lastly, CIT (OECD, 2010). The OECD believes that the less disruptive the taxes are to the participants of the economy, the more the taxes should be utilised as sources to fund the tax budget of the country and, in this case, wealth taxes should be

focused on rather than taxes on companies. Different measures or methods can be used to establish the impact of taxes on the overall economy and the assumed tax burden of taxpayers.

Slow economic growth remains a challenge to be thoroughly explored by policy-makers and the ability of taxes to significantly help in this regard remains questionable. The National Treasury (2018) noted that economic growth is far too low to reduce alarmingly high unemployment rates and inequality in South Africa. In several studies, including the previously mentioned one titled “Taxing the rich at higher rates”, it had been asserted that South Africa is a developing country characterised by large income and taxable income inequality, hence it is necessary to exploit taxes more equitably and efficiently for developmental and redistributive purposes. Steenekamp (2012b) indicates that in the 2010 tax year, 47% of the total taxable income was derived from the 10% of the highest earning individuals and approximately 18% came from the very rich taxpayers represented by 1% of the South African population, which suggests that the very rich incur most of the tax burden. However, tax breaks or deductions for high-income earners such as dividend exemption, pensions, medical aid, interest exemption, retirement funds and capital gains that low-income earners cannot afford ensure that the majority of income earned by high-income earners eventually escapes the tax net. This further exacerbates the unequal tax burden distribution and income inequality in South Africa. As it had been noted earlier, taxes not only have the ability to encourage economic growth, but through correct tax reforms and redistribution of the tax burden, taxes can be used to address economic challenges including income inequality.

Many developing countries like South Africa have extremely unequal distributions of income and wealth (Bird & Zolt, 2005). The Gini coefficient is a common measure that can be used to estimate the extent of income and wealth inequality in a country. The closer the Gini coefficient is to zero, the more equal the income or the wealth distribution is, and the closer the measure moves to unity, the more unequal the income distribution is in a country. Bird and Zolt (2005) indicate that around the year 2000, the Gini coefficient of Latin America was 0.522 compared

to 0.412 in Asia, and only 0.342 in the developed OECD countries. StatsSA conducts a survey every five years focusing on the income and expenditure of South African households on national and provincial levels. The information obtained through this survey is weighted according to the population census figures in order to represent all households in South Africa (StatsSA, 2018). The latest survey was conducted between 2014 and 2015 and the survey pointed out the following regarding income and wealth distribution in South Africa:

> The Gini coefficient for household income stood at 0.63 in 2015 and South Africa is the most unequal country by any measure possible. This study reveals that labour market incomes are the largest contributor to inequality in South Africa, contributing more than 90% of the overall Gini coefficient between 2006 and 2015. Of even greater concern is that South Africa's wealth inequality is at 0.9, which is higher than the income inequality coefficient, but even more worrying is that the coefficient is more than the world's wealth inequality. The share of household wealth held by the top 10% in the distribution was 71%, while the bottom 60% held 7% of the net wealth. Similar statistics for OECD countries suggest that, on average, the top 10% of the wealthiest households own 50% of total wealth, while the bottom 60% own only 13% (StatsSA, 2017).

Because of the unequal wealth distribution in South Africa, the Davis Tax Committee was tasked with the enormous responsibility of identifying feasible, efficient and fair ways of increasing the tax base by way of introducing more avenues to tax wealthy individuals in a quest to primarily reduce the wealth inequality (Davis Tax Committee, 2018). The committee examined the overall tax base and tax burden and the possible appropriate tax mix for South Africa (Black, Calitz & Steenekamp, 2015). This request was made in pursuit of maintaining vertical equity. Vertical equity refers to a principle of taxation that holds that different taxpayers should be treated differently for PIT by ensuring that taxpayers with more income and/or capital pay more tax (National Treasury, 2019). The South African tax system has estate duty, donations tax, dividends tax and transfer duty that are regarded as taxes more applicable to wealthy taxpayers. The two major PIT reforms to be implemented in South Africa were the change from a source- to residence-based income tax system as well as the introduction of CGT in 2001. CGT is regarded by many as a wealth tax as well. With the majority of the new taxes, the aim is mostly to potentially raise more revenue from these new taxes, however, the introduction of CGT in South Africa was also to build on the income and wealth equality (horizontal and vertical equity) goals of the government. However, the problem with CGT is that it is only triggered when

a deemed disposal or disposal of an asset takes place. Consequently, taxpayers can choose to hold on to their assets as a strategy to avoid or evade CGT, move income into investments that will attract lower CGT, or simply conceal the income by shifting it offshore.

Steenekamp (2012b) noted that the rich earn the proportional share of capital income as they largely hold on to assets that generate capital gains, share options and dividend income. As an alternative to taxing the rich at higher marginal tax rates, Steenekamp concluded that since wealthy taxpayers disproportionately benefit from capital income tax reliefs and tax expenditures, and they can easily shift the tax between different income sources (capital gains, interest, dividends) because of the different tax rates attached to these types of income, it is therefore necessary for National Treasury to reduce these benefits for capital earners and also align tax rates among the different capital incomes to avoid tax shifting (Steenekamp, 2012b). On the other hand, Bird and Zolt (2005) believe that wealth taxes may not necessarily contribute significantly in reducing income and wealth inequality because, firstly, the rich normally accrue capital income which is a form less observable than wages, therefore it is costly and difficult to keep track of and charge the correct tax liability to it. Secondly, those who earn high labour income are more often able to control when they actually receive the income and the type of compensation they want and, as a result, they are more likely to completely evade tax or misrepresent the form or type of income earned. Thirdly, the rich have the resources to invest their money in foreign countries and even stay abroad if they feel that the income tax they pay does not justify the benefits they get from the public sector. According to Bird and Zolt (2005), eradicating inequality in the distribution of wealth and income depends on how the public perceives how well the government addresses social objectives with respect to fairness, social justice, and redistribution. If taxpayers perceive an unfair distribution of tax burdens and that there is widespread misuse of public funds, this may lead to an increase in tax avoidance and evasion (Bird & Zolt, 2005).

Steenekamp (2012b) strongly advised against placing a heavier tax burden on the wealthy individuals in order to curb unequal wealth distribution in South Africa, stating that it may backfire because the rich individuals may choose to reduce their tax burden by working fewer hours in formal employment, reducing their work effort, choosing to retire earlier from paid work, choosing lower-paying careers, choosing to receive fringe benefits over a cash salary, shifting compensation between corporate and personal income, evading tax altogether or simply emigrating. Bird and Zolt (2005) also caution against the use of the PIT regime to greatly influence the redistribution of income in developing countries, because most PIT structures are not progressive enough to alleviate income inequality. The Davis Tax Committee believes that focusing on wealth taxes to grow the PIT base and simultaneously reducing the tax, income and wealth inequality may not be the best solution for South Africa as cited below:

> …a wealth tax is not the only available nor necessarily the best instrument to address the inequities of income and wealth. Other methods of redress include land reform and programmes on the expenditure side of the fiscal budget such as increased access to quality health and education and the provision of infrastructure as well as effective government leading to growth and employment (Davis Tax Committee, 2018).

It was reported in the 2019 Tax Statistics issued by SARS in conjunction with National Treasury that the revenue growth in South Africa had mainly been supported by the increase in PIT contribution as opposed to VAT contribution, which has been on a constant decline, and the CIT contribution, which has shown no significant growth since the global recession in 2008. Evidently, based on the tax statistics of South Africa, the tax burden carried by individual taxpayers has relatively been exceeding that of corporates for several years (see Figures 1 and 2 above). In contrast, a study that looked at the role of PIT in developing countries found that developing countries relied more on corporate taxes rather than taxes on individuals (Bird & Zolt, 2005). It was found that PIT is often three to four times more than CIT when the composition of the tax revenue for developed counties is sampled in the study (Bird & Zolt, 2005). Steenekamp (2012b) also concurs that in developing countries it is much easier to shift the tax burden to corporates than individuals and, as a result, the revenue contribution by companies far exceeds that of tax payable by individuals. It is, however, a different reality when the composition of tax revenue is analysed for South Africa; the country, as a

developing economy, exhibits an abnormal trend as compared with other developing economies, as taxes on individuals or persons far exceeds the tax contributed by companies (as evidenced by Table 4 and Figures 1 or 2 above).

Furthermore, studies show that shifting the tax burden from individuals to companies may not necessarily work because the tax imposed on corporates does not entirely fall on them. Companies can respond to heavy tax rates by raising prices of goods and services, lowering wages of workers or settling for cheap labour and, even worse, by retrenching workers, and the detrimental effects of high company taxes will thus be borne by individual taxpayers (National Treasury, 2018). It is therefore important to scrutinise the sources of PIT revenue in South Africa and how the changes in the PIT model can influence economic growth and income distribution.

Taxes on income and profits (PIT and CIT) were the number one category for tax revenue collected by SARS, followed by domestic taxes on goods and services (VAT), then taxes on international trade and transactions (customs duty) for the years under review (SARS, 2019a). Next, this study will scrutinise who is responsible for the taxes on income and profits. Table 6 below shows what or who contributed to the income and profits by breaking down the total percentage among individuals, companies, secondary tax or dividends tax and retirement funds.

	Taxes on income and profits					
Tax years	Persons and indivi-duals[1]	Compa-nies	Secondary tax on companies or dividends tax[2]	Tax on retirement funds	Other[3]	
2001/02	61,36%	28.75%	4.86%	4.20%	0.82%	100.00%
2002/03	57.32%	33.87%	3.84%	4.25%	0.71%	100.00%
2003/04	57.28%	35.40%	3.57%	2.85%	0.90%	100.00%
2004/05	56.85%	36.26%	3.84%	2.26%	0.80%	100.00%
2005/06	54.44%	37.33%	5.32%	2.07%	0.84%	100.00%
2006/07	50.21%	42.50%	5.46%	1.14%	0.69%	100.00%
2007/08	50.83%	42.20%	6.20%	0.09%	0.69%	100.00%
2008/09	50.89%	43.17%	5.22%	0.67%	0.05%	100.00%
2009/10	57.14%	37.57%	4.31%	0.96%	0.03%	100.00%
2010/11	59.73%	34.98%	4.52%	0.76%	0.01%	100.00%
2011/12	58.70%	35.54%	5.15%	0.61%	0.00%	100.00%
2012/13	60.31%	34.82%	4.32%	0.55%	0.00%	100.00%
2013/14	61.04%	34.95%	3.41%	0.60%	0.00%	100.00%
2014/15	62.83%	32.92%	3.78%	0.47%	0.00%	100.00%
2015/16	63.96%	31.50%	3.94%	0.56%	0.04%	100.00%
2016/17	63.89%	30.76%	4.68%	0.60%	0.07%	100.00%
2017/18	64.77%	30.55%	3.92%	0.67%	0.09%	100.00%
2018/19	66.61%	28.70%	4.05%	0.55%	0.08%	100.00%

Table 6: Taxes on income and profits, 2002-2019 (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

Taxes received from individuals and persons have been the main category supporting taxes derived from income and profits, as seen in Table 6 above. The word person is not limited to a natural person only, but it includes insolvent estate,

[1] Excludes interest on overdue income tax
[2] Dividends tax (DT) replaced STC from 1 April 2012
[3] Includes interest on overdue tax, non-resident shareholders' tax, non-residents' tax on interest, tax on undistributed profits and small business tax amnesty

the estate of a deceased person and any trust. In this study, the term person refers to a natural person. The tax burden carried by companies is still below that of individuals when taxes from income and profits are carefully looked into. The taxes on income and profits from companies was at its maximum level before the 2007 to 2009 tax years due to exchange rate appreciation, a higher demand for commodities as well as higher commodity prices contributing to the growth in taxable income. Then the performance of corporates subsequently declined in 2010 as the effects of the global financial crisis started to take its toll on the taxable income of companies, as there was a lower demand for products and services as well as lower prices for commodities, which had a negative effect on company profitability (SARS, 2010). In fact, taxes from income and profits by companies has been on constant decline from 43.17% in 2009 to the lowest point of 28.70% in 2019. This is not entirely shocking, as it was established earlier that PIT had been carrying the growth in tax revenue of South Africa for several years now. It then becomes imperative to carefully examine what types of income are contributed by individuals or persons from the 2003 to 2019 tax years.

Income tax on individuals comprises three different elements: employees' tax, provisional tax and assessed tax which is paid on final assessment (SARS, 2019a). Table 7 below highlights these three main types of taxes, particularly coming from individuals as they contribute the most to the South African tax burden (see Table 6 above). Of all the taxes contributed by persons and individuals, pay-as-you-earn commonly known as PAYE (also known as employees' tax) accounted for the majority of the tax revenue collected by SARS over the years analysed, as shown in Table 7 below. This is followed by provisional tax received from individuals. Both employees' tax and provisional tax are administered under the Fourth Schedule of the Tax Act. They are not a separate tax; rather, they both use different methods of calculating the tax liability of a person and the applicable tax payable to SARS. The purpose of PAYE is to ensure that an employee's income tax liability calculated on remuneration is settled at the same time that the remuneration is earned and, if applicable, paid over every month to SARS by the employer on behalf of the employee receiving remuneration (SARS, 2019b). On the other hand, provisional tax is levied on

income received by any person other than a company who earns income which is not remuneration nor an allowance/advance as envisaged in section 8(1) of the Act (SARS, 2019b). Simply put, PAYE is borne by wage workers and salaried employees, and can thus be classified as labour income. Consequently, provisional tax is applicable to individuals who earn passive or capital income such as rental, dividends, interest, royalties, capital gains and profits from personal businesses. Subsequently, it follows that the PIT burden, which was the largest contributor to the tax revenue of South Africa from 2003 to 2019, was mainly borne by individuals who are labour income earners.

	Taxes on persons and individuals (R million)				
Tax years	PAYE	Provisional tax	Assessment payments	Refunds	Total
2002/03	R90 388.33	R7 121.41	R3 280.86	-R6 453.92	R94 336.68
2003/04	R94 592.51	R7 132.33	R3 495.03	-R6 724.74	R98 495.13
2004/05	R106 719.20	R7 748.39	R3 725.16	-R7 210.86	R110 981.88
2005/06	R121 025.52	R8 720.07	R4 065.88	-R8 166.13	R125 645.35
2006/07	R133 760.37	R10 370.82	R4 986.81	-R8 539.66	R140 578.35
2007/08	R158 106.17	R12 319.72	R4 796.26	-R6 447.80	R168 774.35
2008/09	R183 695.41	R16 345.96	R6 303.10	-R11 198.76	R195 145.71
2009/10	R192 646.30	R17 200.46	R10 065.23	-R14 766.97	R205 145.02
2010/11	R220 308.33	R15 263.82	R6 829.47	-R15 476.60	R226 925.03
2011/12	R245 612.21	R15 583.28	R6 781.06	-R17 576.92	R250 399.64
2012/13	R270 912.82	R16 935.06	R7 746.63	-R19 772.91	R275 821.60
2013/14	R302 894.85	R19 192.27	R8 883.27	-R20 895.85	R310 074.54
2014/15	R344 522.79	R21 955.90	R9 396.42	-R20 504.27	R355 370.84
2015/16	R376 164.36	R26 101.48	R10 646.95	-R20 747.18	R392 165.61
2016/17	R410 806.89	R28 640.57	R12 718.83	-R22 964.84	R429 201.45
2017/18	R446 274.17	R29 795.85	R16 000.71	-R26 801.34	R465 269.39
2018/19	R477 503.06	R34 934.98	R14 667.86	-R30 510.89	R496 595.02

Table 7: Taxes on persons and individuals (National Treasury, 2008a) (SARS, 2017) (SARS, 2019a)

The determination of remuneration is key to calculating the amount of employees' tax to be withheld by an employer and paid over to SARS on behalf of the employee. Remuneration is defined in paragraph 1 of the Fourth Schedule of the Act and broadly includes salaries, overtime pay, commission pay, annual bonus, allowances and fringe benefits. Of the labour income received by employees, salaries and wages account for the larger part of remuneration on average for any given year, as depicted in Figure 6 below. The second best source of labour income comes from annual payments, such as performance bonuses or thirteenth cheques.

According to the latest Living Conditions Survey (LCS) available at the time of this study, conducted in the October 2015 census by StatsSA, 76.2% of South African households obtained their income from work, and the average income (earned by working) for all households was R100 246 per annum. The survey does not specify how allowances and fringe benefits from employment are accounted for as a source of income, and the assumption is that they form part of salaries and wages (see Figure 6 below). When the survey is broken down further to distinguish the income per decile, it indicates that households in the top four deciles earned 75% or more of their income from work, which was the primary source of income for many households. StatsSA (2017) data indicated that households in the top deciles are less dependent on social grants, however, for the bottom three deciles, income from pensions, social insurance, and family allowances accounted for the largest share (even more than income received from work). Although the South African government has made great strides in growing the economy since 1994 by trying to tackle the high rates of poverty, inequality, and unemployment, these challenges still persist. Poverty remains high for an upper middle-income country, with more than half of the population of South Africa being poor (StatsSA, 2017).

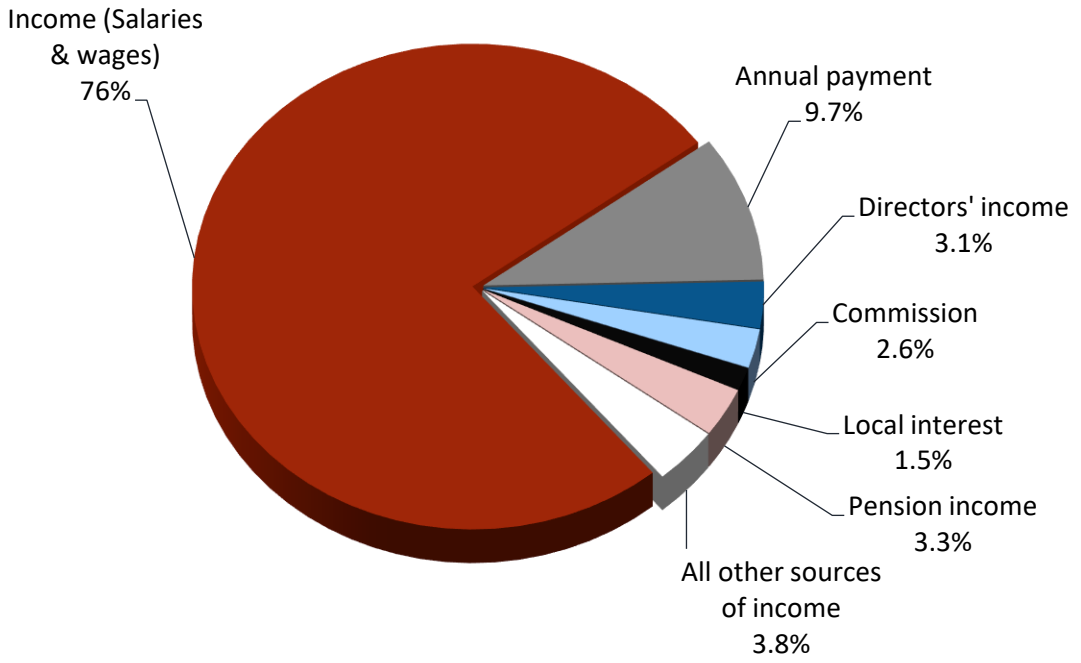

Figure 6: Sources of income/earnings in 2015, (StatsSA, 2017)

A more progressive PIT system is one of the methods that can be used to lessen the unequal income distribution and fairly distribute the tax burden placed on individuals and simultaneously generate more stable and long-term financial resources that are needed to make the economic growth more durable and boost domestic fixed capital formation (Rao & Weller, 2008). This can be achievable, as progressive income taxation tends to affect income inequality by equalising the after-tax income distribution. South African's PIT regime has the ability to improve on the fairness of tax on individuals by using progressivity of the tax schedules (Jordaan & Schoeman, 2018). Steenekamp (2012a) also agrees that measures to redistribute conventionally include social transfers and a progressive income tax system. Accordingly, the amount of tax each person is liable to pay on their taxable income is affected by the progressivity in the tax thresholds levels, rebates and the overall structure of the income tax brackets. Decreased progressivity on the PIT system may consequently lead to many employers and employees negotiating informal arrangements, it may influence individuals to choose to operate in more informal markets, and high PIT rates may influence decisions of where to locate capital investment (Bird & Zolt, 2005). Therefore, it is of vital importance to confirm that the PIT structure is annually adjusted for the

possible fiscal drag or tax bracket creep to maintain progressivity and include more taxpayers in the tax base. Fiscal drag occurs when salaries are adjusted to compensate for the effect of inflation due to time value of money; the taxpayer is then pushed into an income tax bracket where higher rates apply. In this way the individual's effective tax rate is increased, even though the taxpayer's income in real terms may not be increasing (SARS, 2019a).

A progressive PIT system is one that taxes individuals proportionately more with the assumption that their taxable income is relatively higher due to inflation with every tax year that passes by. Adjusting personal income marginal tax rates and income bands is a powerful fiscal policy tool that the government can use to enlarge the tax revenue base depending on the proportionality of the tax regime, however, care should be taken to adjust marginal tax rates until income is maximised and the negative impact on the economy is minimised (Jordaan & Schoeman, 2015). For this reason, a comparison of the inflationary changes to the adjustments of the PIT structure becomes imperative in determining that progressivity is continually maintained, as that will make the PIT system more equitable and efficient.

Both StatsSA and SARS have indicated that the main source of income for most South Africans is received from salaries and wages (see Figure 6 and Table 7 above), so it follows that the majority of PIT will be derived from PAYE thus the level of progressivity in the PIT rates will be compared to the changes in the income bands at the minimum and maximum marginal tax rates. Jordaan and Schoeman (2015) admit that changes to marginal rates affect not only the revenue base, but also tax efficiency and the optimum level of taxes that supports economic growth. Like in the majority of studies, they used the micro-simulation (MS) tax model that was constructed to measure the revenue and efficiency of adjustments to marginal tax rates on individual income (Jordaan & Schoeman, 2018). The MS tax model attempts to measure the cumulative tax burden on low-income households as a result of the annual changes to marginal tax rates and income bands. The MS tax model will not be attempted in this study, but the results drawn from other studies that employ this technique will be used to

corroborate the outcome of the methods used in this study. This study will use its own calculations (year-on-year percentage changes or growth rates) to measure the assumed progressivity of the tax schedules for the years 2003 to 2019.

The National Treasury (2018) indicates that the level and rate of growth in remuneration is worrisome as the cost-of-living adjustments consistently exceed the consumer price inflation. This is concerning because most taxpayers in South Africa are salaried employees with inflation-linked salaries and this implies that their expenditure, including their tax liability, could be increasing at a faster rate than their earnings. Section 5(2) of the Income Tax Act states that the rates of tax chargeable in respect of taxable income shall be fixed annually by Parliament unless the Minister of Finance dictates otherwise. Currently, such changes mainly consist of adjustments to tax brackets and thresholds to account for inflation, although since the 2017/2018 budget such adjustments have been minimised, as a result of the widening in the budget deficit (Jordaan & Schoeman, 2018). Assuming that an individual's annual salary is only raised to compensate an employee for the average consumer price inflation per year and the changes to the tax schedule are also adjusted at exactly the inflation rate, the effective tax burden of the individual will remain constant from one year to the next. However, if the adjustments on the tax schedules are below the average rate of inflation, then an individual's tax burden will increase because of the tax bracket creep. The pertinent question is: are the changes to the PIT structure representative of the annual changes to individuals' average earnings? Figure 7 and Table 8 below compare the average annual inflation rate to the growth of the income bands in the lowest and highest tax brackets.

In order for taxpayers to benefit from the progressivity of the tax schedules, the annual changes in percentage of the tax brackets should be in line with or more than the average inflation rate. However, Figure 7 below shows that tax brackets are not always fully adjusted for inflation. In Figure 7, the dotted lines moving above the solid lines show where the income tax brackets are not adjusted for inflation and the tax bracket creep will inevitably affect many low-income taxpayers.

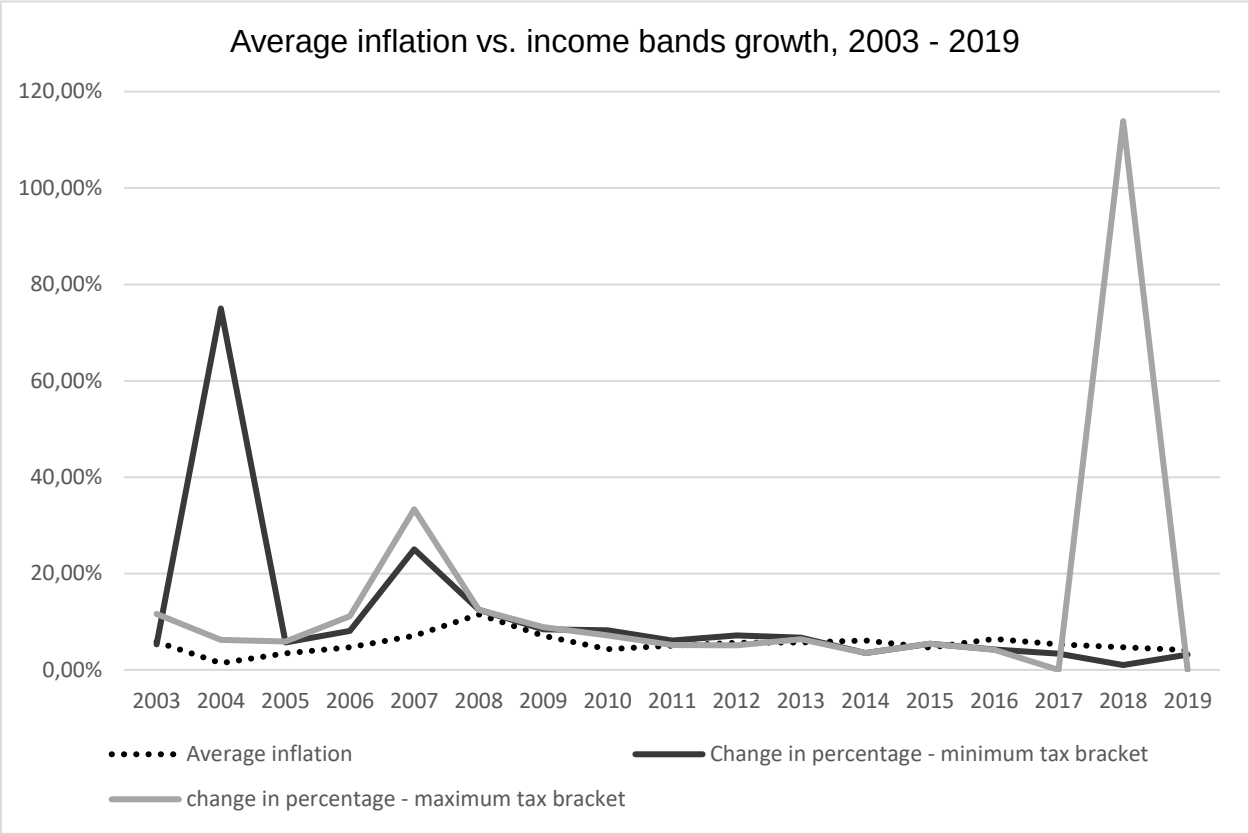

Figure 7: Average inflation vs growth in income bands, 2003-2019 (SARB, 2017) (SARS, 2019a) (Stats SA, 2019) and own calculations.

In the numerous budget speeches presented by the Ministers of Finance over the years, it had been claimed that PIT schedules are fully adjusted to compensate taxpayers for the effects of inflation (National Treasury, 2009b). However, Figure 7 above proves otherwise. Some tax experts have publicly refuted these claims, stating that adjustments to the tax schedules have not always taken into account the time value of money and, in some years, no tax relief had been granted to taxpayers. An online article titled “Minister’s income tax relief an illusion” highlighted that the tax relief of R9.3 billion in the 2014 tax year claimed to have been granted to taxpayers was misleading, since the income tax brackets are not adjusted for inflationary-linked income (IOL, 2014). This meant that taxpayers who received salary increases in line with or above the inflation rate were affected by the fiscal drag and would therefore forfeit a larger portion of their salaries to PAYE than in the prior year. Only individuals who do not receive annual increases in their salaries, meaning becoming poorer each year, are actually less affected

by the progressivity in the income tax bracket. Another article stated that in the 2019 tax year, none of the income tax brackets were adjusted upwards, and all taxpayers who received a pay increase equal to inflation were in fact taking home less money in real (inflation-adjusted) terms than in 2018 (Business Tech, 2019). Seemingly, instead of only allowing for inflationary adjustments, the alignment of income brackets, rebates and thresholds at above-inflation rates could be beneficial; it could improve the efficiency of the income tax regime as more individuals could be included in the tax net (Jordaan & Schoeman, 2018).

In the 2019 budget review speech, the Minister of Finance admitted that due to the tough economic conditions coupled with a growing demand for fiscal commitments such as free higher education and national health insurance, a decision to increase revenue collections by not adjusting for inflation on the income tax brackets was implemented (National Treasury, 2019). Table 8 below shows that the income tax brackets were not fully adjusted for inflation in the 2002/3 tax year, then for a long time the adjustments were in line with the annual average inflation rate until 2012 when the highest bracket adjustment was below inflation. Thereafter, the lowest and highest tax bracket adjustments have been below the annual average inflation in 2014, then there was slight improvement in 2015 and then from 2016 to 2019 the lowest tax bracket was not adjusted for inflation. In the 2017 and 2019 tax years, the top income bands were static in comparison to prior years. National Treasury (2018) argued that in support of progressivity of South Africa's tax system, the top four personal income tax brackets were not adjusted for inflation. The below inflation adjustments are a well-executed strategy for SARS to make up for any shortfall in the budgeted revenue.

Tax years	Average inflation	Minimum marginal rate - taxable income	Change in percentage	Maximum marginal rate - taxable income	Change in percentage
2003	5.8%	R40 000	**5.3%**	R240 000	11.6%
2004	1.4%	R70 000	75.0%	R255 000	6.3%
2005	3.4%	R74 000	5.7%	R270 000	5.9%
2006	4.7%	R80 000	8.1%	R300 000	11.1%
2007	7.1%	R100 000	25.0%	R400 000	33.3%
2008	11.5%	R112 500	12.5%	R450 000	12.5%
2009	7.1%	R122 000	8.4%	R490 000	8.9%
2010	4.3%	R132 000	8.2%	R525 000	7.1%
2011	5.0%	R140 000	6.1%	R552 000	5.1%
2012	5.6%	R150 000	7.1%	R580 000	**5.1%**
2013	5.7%	R160 000	6.7%	R617 000	6.4%
2014	6.1%	R165 600	**3.5%**	R638 600	**3.5%**
2015	4.6%	R174 550	5.4%	R673 100	5.4%
2016	6.4%	R181 900	**4.2%**	R701 300	**4.2%**
2017	5.3%	R188 000	**3.4%**	R701 300	**0.0%**
2018	4.7%	R189 880	**1.0%**	R1 500 000	113.9%
2019	4.1%	R195 850	**3.1%**	R1 500 000	**0.0%**

Table 8: Primary rebates, tax thresholds vs average inflation (SARB, 2017) (National Treasury, 2019) (Stats SA, 2019) and own calculations.

The structure of the income tax schedule, number of tax brackets, applicable marginal rates specified per tax bracket, annual thresholds and the various rebates offered by the PIT system all play an integral part in ensuring the desired progressivity of the system. Tax thresholds ensure that taxpayers who earn income below a certain range are not included in the tax base, while rebates provide a relief by reducing the tax liability in a form of tax credits. Figure 8 below illustrates the changes made to the primary rebate and tax thresholds in relation to the annual average inflation from 2003 to 2019. Ideally, rebates and thresholds should be adjusted upward for inflation, meaning the dotted line representing the average inflation should be below the bar graph for a taxpayer to receive any relief. As seen in Figure 8, thresholds and rebates were always adjusted at the same rate from the 2003 to 2019 tax years. Since 2011, there has been small to

no inflationary adjustments to both rebates and thresholds and this meant that individuals with inflationary increase in their income tax faced a larger tax burden in the latter years (National Treasury, 2019). Governments should be aware that without applying adequate inflationary adjustments the effects of tax bracket creep will be unavoidable, as the tax structure may become less equitable if taxpayers are being pushed into higher tax brackets with no accompanying increase in real income (Sabirianova, Buttrick & Duncan, 2009).

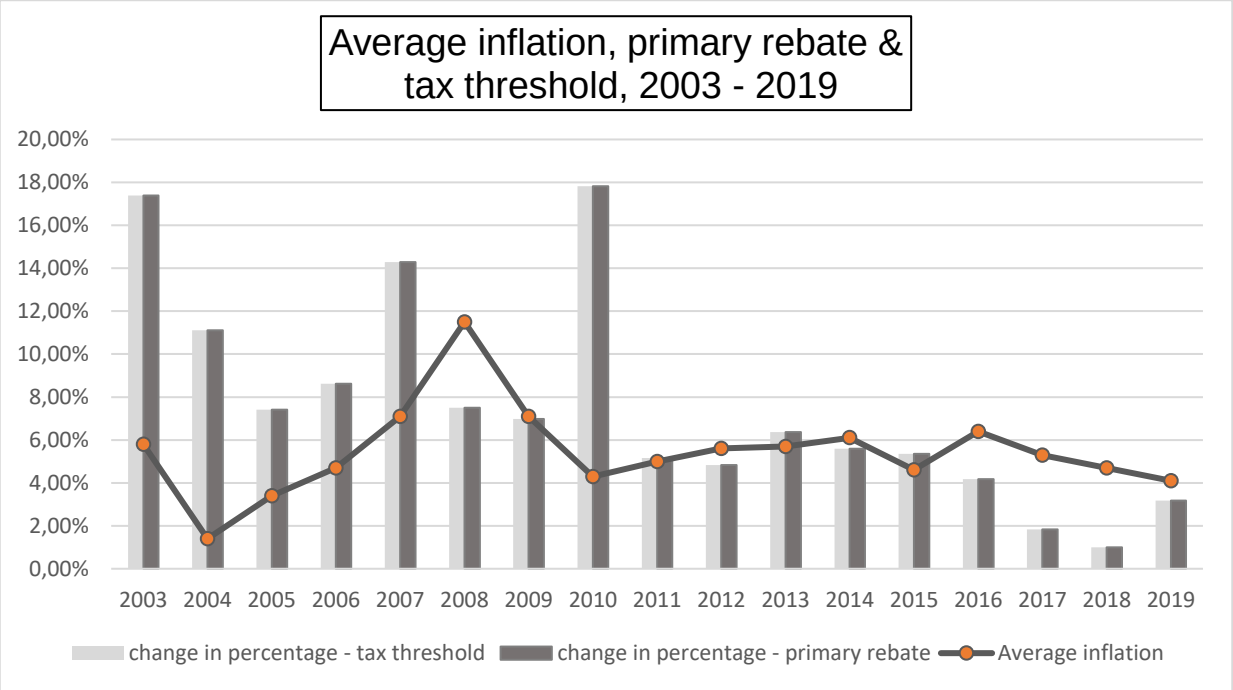

Figure 8: Primary rebates, tax thresholds vs average inflation (SARB, 2017) (National Treasury, 2019) (Stats SA, 2019) and own calculations

When inflation is not factored into the tax schedule, the buying power of individuals decrease, as they tend to cede a relatively larger part of their inflationary-linked salaries to income tax. From the 2017 tax year, there were seven income tax brackets. To clearly illustrate the effect of below-inflation adjustments to the income tax tables for the period under review, Figure 9 below, being the latest available data on the rates of tax for 2017/18 and 2018/19 will be used.

Taxable income (R)	Rates of tax (R) 2018/19 tax year
1 – 195 850	18% of taxable income
195 851 – 305 850	35 253 + 26% of taxable income above 195 850
305 851 – 423 300	63 853 + 31% of taxable income above 305 850
423 301 – 555 600	100 263 + 36% of taxable income above 423 300
555 601 – 708 310	**147 891 + 39% of taxable income above 555 600**
708 311 – 1 500 000	207 448 + 41% of taxable income above 708 310
1 500 001 and above	532 041 + 45% of taxable income above 1 500 000

Taxable income (R)	Rates of tax (R) 2017/18 tax year
1 – 189 880	18% of taxable income
189 881 – 296 540	34 178 + 26% of taxable income above 189 880
296 541 – 410 460	61 910 + 31% of taxable income above 296 540
410 461 – 555 600	**97 225 + 36% of taxable income above 410 460**
555 601 – 708 310	149 475 + 39% of taxable income above 555 600
708 311 – 1 500 000	209 032 + 41% of taxable income above 708 310
1 500 001 and above	533 625 + 45% of taxable income above 1 500 000

Figure 9: Tax schedules for the year ended 2018 and 2019 (National Treasury, 2018)

The tax liability is the amount payable after the applicable tax rebates have been taken into account to reduce the said liability. The primary rebate was R13 635 in 2018 and moved upwards to R14 067 in 2019, which is a 3.1% increase as opposed to 4.1% of the annual average inflationary adjustment. The example below illustrates the effects of the tax creep and the growing tax burden on an individual with a constant real income every year. Assuming that there is an individual under 65 years old, who earns an annual salary of R550 000 which is adjusted yearly for inflation only, how will the below-inflation increase to the tax brackets and primary rebate affect the individual's tax liability if he/she earns no other taxable income and has no allowable deductions in the 2018 and 2019 tax years?

In the 2017/18 tax year, the taxpayer was on the fourth income tax bracket and they would have paid R133 842 on tax [(R97 225 + 36% (550 000 - 410 460)) – R13 635]. Meanwhile, if the taxable income of an individual is fixed for inflation at

an average of 4.1% (Stats SA, 2019) for the 2019 tax year, the taxpayer will jump to the fifth tax bracket and the tax payable will be R140 435 [(R147 891 - R39% (R572 550 - R555 600)) – R14 067]. Due to an inflation-linked increase on the taxpayer's income, he/she ceded an extra R6 593 of their income to SARS in 2019 although their salary had remained constant in real terms and their standard of living is effectively decreased by the unintended increase in the tax burden. Not only has the taxpayer moved to a higher tax bracket, but the effective tax rate has also increased from 25% to 26%. With all things constant, this means that if an individual's salary increases in proportion with or by more than the rise in inflation, the tax liability will increase disproportionately to the taxable income of the individual, resulting in a heavier tax burden.

As mentioned before, above-inflationary growth in salaries have a positive effect on the PIT base and this is because PIT mainly comprises remuneration (salaries), however, to alleviate the tax burden placed on individuals the tax schedules should be adjusted for the effects of inflation. It is imperative to note that adjustments of tax rates might have an impact on tax efficiency, thereby affecting tax morale and tax revenue to be collected (Jordaan & Schoeman, 2015). Rao and Weller (2008) have proposed that a more progressive PIT structure may incidentally affect stability by influencing trends that are associated with less volatility, such as more equal income distribution. It is therefore in the best interest of the tax authorities to keep the tax regime progressive enough to promote equity. Another group of tax experts conclude that in order to make the PIT regime more equitable, the tax-free thresholds should be set equal to the GDP per capita or twice the GDP per capita in the case of developing countries where tax administration is less efficient (Sabirianova Peter, et al., 2009).

Not only has South Africa's PIT burden increased over the years reviewed, as evidenced by the constant growth in the PIT to GDP ratio, but in 2017 the government also added a new top income tax bracket of 45% for those earning above R1.5 million, hence the growth in the highest tax band was at a staggering 113.9%. This was followed by a one percentage point increase in PIT rates that affected all but the lowest income tax bracket in 2015/16, and below-inflation

adjustments to tax brackets from 2015/16 to 2018/19. As a result, the tax burden on individuals has been increasing and this was further exacerbated by the increase in the effective CGT rates, dividends withholding tax rate and lower-than-inflation adjustments to the tax schedules, so the tax relief claimed to be offered to individual taxpayers is essentially non-existent (National Treasury, 2018).

Household income is stretched every time the government decides not to adjust the tax tables and other tax determinants accordingly for inflation and, consequently, individuals are further pressured with an already high PIT burden. The downside of increasing collection of tax revenues through the manipulation of the progressivity of the tax schedules can lead to detrimental consequences such as worsening the uneven income redistribution. Furthermore, the deviation from a progressive income tax system will result in large revenue losses and instead further exacerbate the tax burden of low-income and middle-income taxpayers in the already heavily tax-burdened and highly unequal country (Steenekamp, 2012a). Up to this point, the study has been reviewing the South African individual's tax burden on a micro level and chapter 4 will benchmark South Africa's PIT levels on a more international level.

CHAPTER 4: AN INTERNATIONAL COMPARISON

The world has become intertwined and integrated, and countries are co-existing and have become more dependent on one anther due to globalisation. Globalisation essentially means that a country's dependence on the rest of the world is now very high and what happens in other countries can affect the activities of that country and its people (Tanzi, 2004). Countries are offered opportunities to share resources and to achieve economic growth since the playing fields are widened by the globalised environment. Globalisation forces countries to continuously improve on their tax structures not only for the purpose of maximum tax collection, but also for compliance with the international standards, facilitation of trade and market competitiveness. In open economies, the design of a national tax system will need to consider the design of tax systems in other countries, since countries are increasingly using their tax systems to improve their ability to compete in global markets (OECD, 2010). The downside of globalisation in a developing country like South Africa is that it tends to put pressure on governments to reduce the level of taxation. This is necessary because international tax has generated a significant reduction in the marginal tax rates for PIT and for CIT (Tanzi, 2004).

This key chapter discusses the aspects of different tax structures on an international level and different measures will be used to determine the tax burden of individuals on a cross-country analysis. The aggregate tax burden by a country can be measured by the percentage of tax to GDP and the larger the share of the tax burden, the greater potential the tax system may have to redistribute income through a progressive tax regime (Bird & Zolt, 2005). The comparison of the PIT/tax-to-GDP ratios and maximum marginal tax rate of South Africa to some SADC, BRICS and OECD countries is undertaken. Jordaan & Schoeman (2018) highlight that it is important that countries continuously assess the efficiency of their tax regimes in order to adjust and align accordingly with international trends in this regard within a very competitive tax environment. It is then imperative to not look at South Africa in isolation when the tax burden of individuals is analysed because as a developing country it largely operates on a

global scale. Likewise, this chapter will make reference to the distinctive features of the PIT models of other countries and how to possibly incorporate these in South Africa. There is no scientific basis on which the countries are selected, however, the selection of the specific countries from the SADC region and OECD is based on them having similar PIT regimes to that of South Africa or falling within a similar level or context of economic development. The distinction between developed and developing economies is reflected by per capita income, extent of urbanisation, population size and density, structure and openness of economy and political stability (Steenekamp, 2007). Loosely put, SADC and BRICS countries are widely seen as emerging economies and OECD countries are considered the most developed in the world.

The common observation by tax analysts is that individuals are taxed more intensively in developed countries rather than developing countries. The goal of this chapter is to ascertain this shared observation by benchmarking South Africa's PIT levels against those of other developing countries from the SADC region, BRICS and the already developed countries from the OECD, namely Australia, the US and the UK. Bird and Zolt (2005) believe that PIT plays a much smaller role in developing economies compared to developed ones, as the share of PIT to the total tax revenue is relatively minimal in contrast to income from companies and indirect taxes. The effective scope of PIT in developing countries is much narrower than in developed countries because many forms of tax relief afforded to individuals are disguised as specific exclusions on capital income and exempt income (Bird & Zolt, 2005). Steenekamp (2007) agrees that developing countries generally have to rely more on indirect taxes like customs, excise duty and VAT and thus tend to have difficulty in taxing companies and individuals. However, he found that out of 29 developing countries around the world that were selected in a tax performance study, South Africa's average effective PIT rate far exceeds the mean rate for the sample of countries and the country exploited PIT to the utmost as evidenced by holding the highest extraction rate of 8.94% as compared to an average of 3.44% (Steenekamp, 2007).

More evidence suggests that PIT is under-utilised in developing countries due to the highly uneven income distribution, since richer taxpayers can influence economic and political reforms (Tanzi, 2000). As a result, emerging markets have a constrained tax base and revenue sources available to tax individuals, leading to heavy reliance on indirect taxes. Adding to this, the following issues further prevent developing countries from fully utilising income taxes from individuals:

> Developing countries are often characterised by a large share of agriculture in total output and employment; by large informal sector activities and occupation; by many small establishments; by a small share of wages in total national income; by a small share of total consumer spending made in large and modern establishments. All these characteristics reduce the possibility of relying on certain modern taxes such as personal income taxes and, to a much lesser extent, on value-added taxes. They also reduce possibility of achieving high tax levels (Tanzi, 2000).

Surprisingly, another study on cross-country analysis revealed that South African tax levels on individuals were rather high and deviated from the normal pattern presented by developing countries. The study included 13 developed (DC) and 13 least developed countries (LDC) from around the world and focused on the data series up to 2007 which was compiled from IMF sources (Steenekamp, 2012b). Similarly to this present study, Australia, the UK and the US were amongst the developed countries used for comparison purposes and the least developed countries included were Thailand, Egypt and Hungary, amongst others. The results from the study indicated that taxes on income, profits and capital gains represent the largest portion from which tax revenue is collected by developed countries at over 50% and this pattern is very much alike to that of South Africa, as discussed in the chapter prior to this. On the other hand, taxes on goods and services dominate the sources from which tax revenue is collected in the least developed countries at 52%. This outcome from Steenekamp's study indicated below attests to the findings in chapter 3 of this study that taxes collected from individuals and persons have been the main source of revenue for South Africa for the tax periods from 2003 to 2019.

> In developed countries, income tax on individuals (35.7%) is more than double the share of income tax on companies (15.4%). In developing countries, company tax is an easier source to exploit than personal income tax, and consequently the share of company tax far exceeds that of tax payable by individuals. Trade taxes are insignificant sources of tax revenue in developed countries (0.6%) compared to developing countries (10.9%). When South Africa's tax composition is compared to the sample of DCs and LDCs, the most

> striking observation is that in most respects the South African structure is similar to that of DCs. The South African personal income share generally exceeds that of DCs (in eight out of the 13 countries) (Steenekamp, 2012b).

Another study conducted in 2012 signalled that PIT usually constitutes just below 10% of all tax revenue raised in low-income countries as opposed to an average of over 25% in high-income countries that are part of the OECD (Jordaan & Schoeman, 2018). South Africa is far from meeting the classification of a high-income country because of the social and economic challenges that the country faces, yet it exhibits PIT levels of over 37% on average (see Figure 2) for the period under review – this is considerably higher than the 25% of OECD countries. The South African government seems to be placing a much higher responsibility on individuals than corporates and other possible tax sources to raise revenue. Even more worrying is the fact that the empirical evidence from the various studies suggested that the tax burden carried by individuals in South Africa outpaces that of countries with same level of development as South Africa and, even worse, the OECD countries that are considered to be far developed. This begs the question of whether the tax burden placed on South African individuals is possibly excessive and disproportionate, given the economic and social difficulties the country faces. The subsequent countries were selected, based on the following distinctive features:

Australia

Australia has transformed itself into an internationally competitive, advanced market economy in recent years. It is a member of the OECD and had one of fastest growing economies during the 1990s, a performance due in large part to economic reforms adopted in the 1980s.

Similar to South Africa in terms of taxing individuals, Australia uses a progressive tax scale and makes a distinction among residents, non-residents, residence basis and source basis. Australian tax residents are subject to income tax on their worldwide income, in other words, income from both Australian and foreign sources except for certain foreign income and gains of temporary residents (PwC, 2020). On the other hand, non-residents are taxed only on the taxable income

derived from sources in Australia. Citizenship and nationality of an individual are not definitive in the determination of whether an individual meets the tax residency status in Australia.

United Kingdom

The UK has strong trading power and is one of the pioneers in the financial centre of the world. It has influenced global financial policies through its involvement in the United Nations, OECD, European Union and Commonwealth (PwC, 2020). It should be noted that the UK tax policies and structure might drastically change because of its recent exit from the European Union (also referred to as “Brexit”) on 31 January 2020. The UK has a leading services industry specifically in terms of banking, insurance, and business services and this industry accounts by far for the largest proportion of GDP of the country.

Unlike South Africa, the UK makes reference to resident and domiciled in determining the taxable liability of an individual based on their worldwide income. The UK also uses the progressive tax rate schedule to calculate the taxable income of individuals, meaning the higher your income, the higher your tax liability.

United States of America

The US has the most developed economy in the world based on its 2019 nominal GDP and the US dollar is the most accessible and widely used currency in international transactions (PwC, 2020).

Citizenship is key in the determination of tax residency status of a natural person in the US. Individuals who are considered residents and citizens of the US are taxed on income earned worldwide. Non-resident taxpayers are taxed on their US source income and income effectively connected with a US trade or business (with certain exceptions) (PwC, 2020). Equivalently to South Africa, the US utilises a progressive tax system in taxing individuals. The major differences

between the US and South African tax systems is that in the US an individual's tax bracket is dependent not only on his/her taxable income, but also on the person's filing status: single, married and filing jointly or qualifying widow/widower, married and filing separately, and head of household (PwC, 2020).

In comparison to South Africa, the developed country with the most identical tax structure for individuals appears to be Australia, however, the three OECD member countries above are amongst the leading economies in the world and they all play a pivotal role in the global markets. These countries also have the biggest influence on the foreign economic and tax policies of many developing countries, including South Africa. The comparison of the tax levels of these specific OECD countries to the tax burden of South Africa is therefore of vital importance to this study.

South Africa is a key member of SADC. Some of the objectives of SADC, established in 1992, are to achieve development and economic growth, alleviate poverty, enhance the standard and quality of life of the people of Southern Africa, and support the socially disadvantaged through regional integration (SADC, 2018). SADC countries serve a critical part in benchmarking the PIT levels of South Africa, as they all have aligned developmental plans as envisaged in the objectives above and, presumably, taxes are central to the economic development of such countries. The following SADC countries were selected for these reasons:

Botswana

- Botswana, like South Africa, is considered to be a developed country in Africa and a developing country in the world according to the UNDP.
- Developed countries are measured using the HDI. The data collected is used to rate countries according to life expectancy and health, economic growth, standard of living and education (United Nations, 2019);
- South Africa and Botswana are part of SACU and AGOA;

- Like South Africa, Botswana's major sectors include finance, business services and tourism;
- Botswana operates a source-based system of taxation for residents and non-residents. Unlike South Africa, Botswana refers to the term "citizen" on their tax base, who are subject to tax on their income from foreign sources (Deloitte, 2018);
- South Africa makes a distinction between resident and non-resident for the purpose of taxation.

DRC

- The PIT system is a bit different from that of South Africa as the tax regime mainly focuses on income from employment. Investment income and income from business activities do not form part of taxable income of an individual for personal taxation. Individuals engaged in a business are taxed under the rules governing companies (Deloitte, 2018);
- Progressive tax rates are used to determine taxes due by individuals on employment income and are withheld by the employers and paid over to the taxing authority, so it is similar to the PAYE system used in South Africa;
- The DRC and South Africa both have trade relations with the World Trade Organisation (WTO).

Mauritius

- Although Mauritius has a significantly smaller population than South Africa, both countries are considered developed countries in Africa (United Nations, 2019);
- Mauritius, like South Africa, taxes residents on their worldwide income and non-residents are taxed only on source-based income. However, residence classification is defined differently to South Africa;
- A progressive tax scale is not followed – a flat tax rate of 15% was levied on individuals instead, and the tax rate has changed to 10% in the 2019 tax year;
- Both South Africa and Mauritius are part of COMESA and AGOA;

- Like South Africa, agriculture and tourism are the main economic drivers in Mauritius.

Mozambique

- The tax liability of resident individuals is determined using progressive rates based on their worldwide income, and non-residents are taxed on any income from a source within Mozambique. This is similar to the tax basis of South Africa;
- Unlike South Africa, the income of an individual is taxed under separate schedules for employment, trade and business, capital gains, real estate and other income in Mozambique (Deloitte, 2018);
- Similarly to South Africa, employment income is defined broadly and includes benefits-in-kind;
- Both Mozambique and South Africa have trade relations with AGOA;
- Like in South Africa, Mozambique has a huge agricultural industry.

Zambia

- Unlike South Africa, Zambia operates a source-based tax system;
- However, like South Africa, taxable income for natural persons includes employment income (defined broadly), annuities, business income, investment income and CGT;
- Progressive rates are used to determine the tax liability of an individual, which is similar to how natural persons are taxed in South Africa;
- Both countries are members of trade agreements: COMESA and AGOA (Deloitte, 2018);
- Zambia has a booming copper industry and its major economy drivers include agriculture, mining and tourism, similar to South Africa.

In an attempt to reduce the tax burden levied on individuals, many developed countries had opted to drastically reduce the top marginal tax rates in the tax years from 1980s. The downside of this reform was that the decline in top income

tax rates were not matched by a reduction in the average tax income levied on labour income of an average production worker and, therefore, the majority of lower-income taxpayers did not benefit from this change (OECD, 2010). This was due to the increase in tax thresholds that was aligned with the growth in average earnings, thus there was a minimal reduction of marginal rates in lower tax brackets. Jordaan and Schoeman (2018) mention that if the objective of the tax reform is to reduce the tax burden placed on individuals, it is important to increase the tax thresholds thereby lessening horizontal income inequality and to reduce the number of marginal tax brackets and lower marginal tax rates. The following part of the study will assess how South African PIT levels weigh in against its international counterparts from the 2003 to 2019 tax years. Measures of total tax-to-GDP ratios are routinely used for international comparisons of overall tax burdens.

The fundamental study titled “Global reform of personal income taxation” reached a consensus that the ideal number of tax brackets for developing and developed economies should ideally be set between four to six income tax brackets, thereby making the tax system easier to administer and simpler to understand (Sabirianova Peter, et al., 2009). They justify this by citing that the excessive division of personal income into multiple tax brackets comes with larger administrative and information costs and may create additional incentives for manipulating taxable income to move down the lower income bands (Sabirianova Peter, et al., 2009).

Table 9 below compares the number of tax brackets across the 17 countries selected from BRICS, SADC, OECD and the fastest emerging economies in Africa, being Algeria, Egypt, Kenya and Nigeria. The data used is for the latest year of assessment ended in 2019. The majority of the countries below meet the ideal number of four to six tax brackets required for simplification and maintain the progressivity of the PIT schedules. Along with South Africa, only China and the US are out of this range with seven income bands each. This is concerning because South Africa’s economic development is nowhere near that of the US and China, as both these countries are considered to be competitive market

leaders and global economic influencers. On the other hand, only Mauritius and Russia have single and flat tax rates for taxing individuals. Mauritius applies a flat rate of 10% regardless of the person's tax residency status, as long as the income is derived from sources within Mauritius. Unsurprisingly, Mauritius is ranked first in Africa and twentieth worldwide in terms of a country providing ease of doing business, and the country has attracted considerable foreign investment and has earned one of Africa's highest per capita incomes (PwC, 2020). In Russia, a distinction between residents and non-residents is made and, based on their residency status, individuals are taxed at 13% if resident and 30% if not resident. The decrease in the number of tax brackets, gradual elimination of surtaxes, and the dwindling use of multiple tax schedules, non-standard allowances and tax formulas has moved countries toward simpler PIT structures and thereby improved the collection of taxes from individuals by taxing authorities (Sabirianova Peter, et al., 2009).

Country	Number of tax brackets
Algeria	4
Australia	4
Botswana	4
Brazil	4
China	7
DRC	4
Egypt	5
India	4
Kenya	5
Mauritius	1
Mozambique	5
Nigeria	6
Russia	1
South Africa	7
United Kingdom	4
United States	7

Zambia	4

Table 9: Number of tax brackets – cross country (PwC, 2020)

Most efficient tax policies or reforms involve the reduction of PIT rates, opportunities for broadening the tax base, improved tax collection, simplification and better administration of the tax system (Steenekamp, 2012a). The observation made by Buttrick, Duncan and Peter (2009) indicate that it is advisable that low- to middle-income countries set their maximum marginal income tax rates between 30% to 50% and the minimum marginal income tax rates should be limited to between 10% and 20%. It should be noted that tax policies that focus only on raising PIT rates are proving not to be efficient as they not only discourage and distort economic activity, but they are also ineffective in redistributing wealth and income across developing economies (Bird, 2008). Horizontal inequality may be worsened because only the majority of the less fortunate individuals entangled within the tax system will bear the tax burden, while wealthy individuals explore their options for proper tax planning and take advantage of tax arbitrage. Figure 10 below uses the latest data available to compare the lowest and highest marginal income tax rates of the 17 key countries selected.

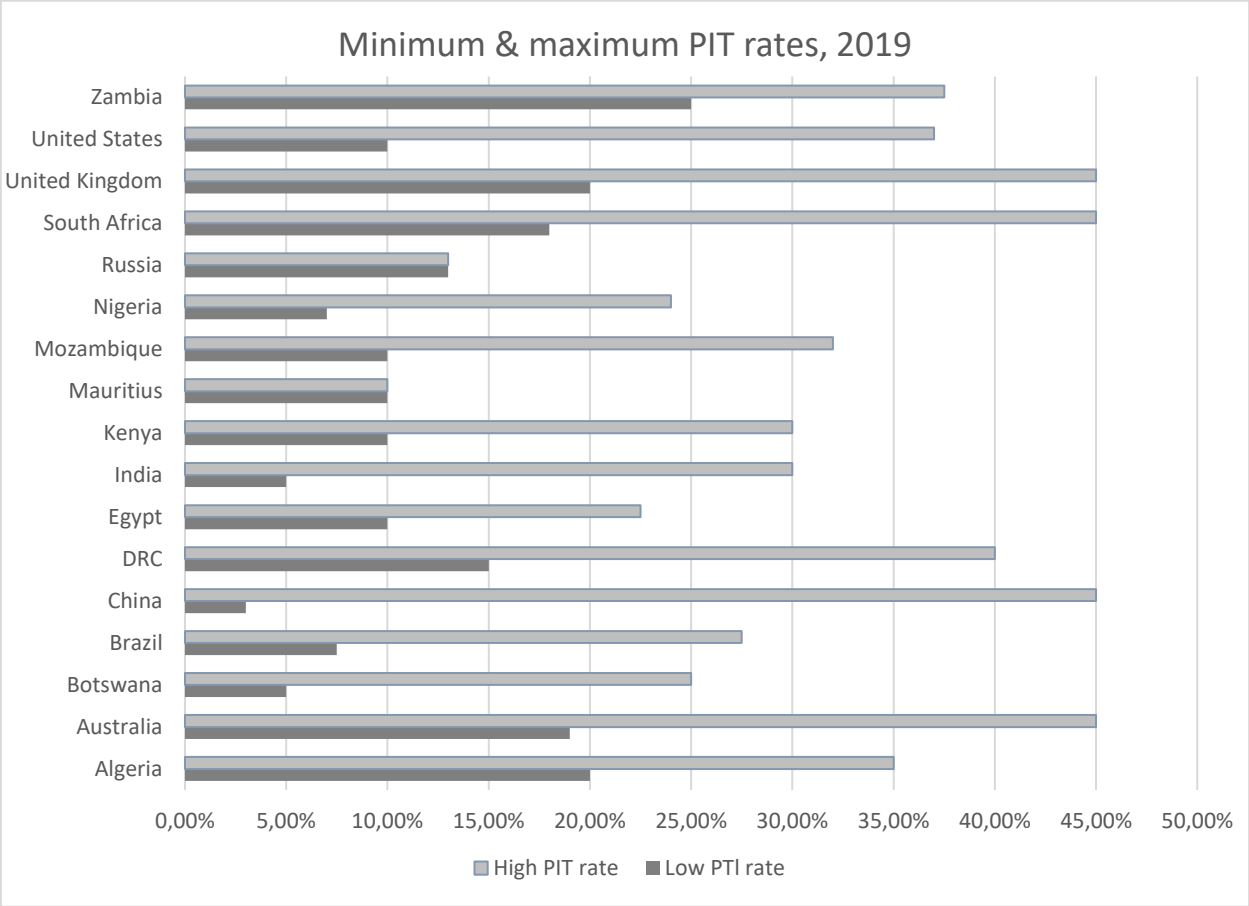

Figure 10: Minimum and maximum marginal income tax rates in 2019, cross country (PwC, 2020)

The majority of the countries looked into meet the requirement that the ideal top PIT rates should be levied at 30% to 50%, but most fail to attain the low PIT rates of between 10% and 20% as suggested above. From the 17 countries analysed above, 4 countries (China, South Africa, Australia and the UK) have the highest PIT tax rates of 45%. Again, South Africa finds itself amidst countries that have the highest rankings in terms of their nominal GDP and enjoy abundant economic growth when factors like investment in workforce, production output, natural resources and entrepreneurship are taken into account (United Nations, 2019). South Africa displays a more similar pattern to developed countries and strays away from the design of fellow SADC countries. Steenekamp (2012a) found that the average top marginal PIT rate in SADC (30%) was much lower than in the OECD (41%) and in South Africa it was at the same level as the average OECD PIT rate. The scope for higher PIT rates seems to be constrained by already-high

marginal tax rates, a small tax base and a CIT rate that is lower than the top marginal PIT rate (Steenekamp, 2012a). The CIT rate in South Africa is 28% and with the top PIT rate of 45% there is room for tax arbitrages through the gap created. Overall, reduced tax rates and parallel rates between corporates and individuals might improve both vertical and horizontal equity, as lower tax rates reduce the rewards for rent-seeking, tax evasion and tax incentive relief, thereby improving the chances of taxpayers being treated equally (Thirsk, 1991). The extract below highlights why it is advisable to lower PIT rates and, more specifically, to align the top PIT rate with the CIT rate.

> The merging of the corporate and top bracket personal rates in developing countries made it easier to tax small businesses by reducing the temptation to convert capital income into labour income and vice versa, while at the same achieving closer parity of tax treatment between firms located in the corporate and unincorporated sectors. The alignment of these two rates, moreover, enhances the effective integration of these two income taxes through the technique of the dividend exclusion. This simplification and unification of the rate structures reduces opportunities for tax avoidance while the lower personal rates may also weaken the incentive to evade personal tax. As a result, whatever loss of vertical equity may have occurred as a result of these developments, there may be offsetting gains in administrative simplicity and the attainment of greater horizontal equity (Thirsk, 1991).

The examination of the tax-to-GDP ratio (tax ratio) in different countries within the OECD has been thoroughly covered, however, what is not common is an inclusive comparison across countries with varied economic levels and structures. The tax ratio usually represents the tax burden of a particular country. The tax-to-GDP ratio is the foundational indicator for the analysis of tax levels in an economy (Modica, Laudage & Harding, 2018). The tax ratio provides an indication of how much the underlying government's economy is carried through by tax revenues, and allows comparisons across tax sources (PIT/CIT/VAT) of countries and across time. Steenekamp (2007) remarks that by comparing the tax ratios for different countries, some indication can be obtained of whether a country can raise more taxes without burdening its taxpayers excessively. Bird (2008) argued that for a country to become developed it needed to collect about 25% to 30% of total income tax to GDP. Jordaan and Schoeman (2015) indicate that the optimal level of PIT to GDP needed to escalate the growth rate of the economy is estimated at 6.7%, and this can possibly be achieved by lowering marginal income tax rates. However, they caution that this may result in revenue

losses in the short term and a trade-off between maximising revenue collection and tax efficiency should be looked into. Subsequently, an examination of the overall contribution of tax revenue and, more specifically, the level of PIT to the nominal GDP of countries with developing to developed economies will be undertaken and benchmarked against South Africa.

Figure 11 below represents the average share of taxes in the economy for different countries as a percentage of GDP. The tax statistics used for the tax ratio analysis are adapted from the IMF and OECD databases and thus the tax-to-GDP is limited to the latest available information, which is the 2017/18 tax year. For all the SADC countries, the general government tax statistics were not available so the data from the central government was relied upon. Of the countries analysed, Nigeria has the lowest tax-to-GDP at 5.7% and the highest ratio is 34.2% by OECD's combined average. When an individual cross-country analysis is done, the level of taxation in South Africa (28.5%) exceeds all the countries with the most developed economies in the world (Australia, the UK and the US). South Africa is a key partner in the SADC and BRICS organisations. The tax burden of South Africa (28.5%) far exceeds the combined SADC average of 17.2% and it is even higher than all the fastest growing economies in Africa and BRICS countries combined. When the OECD group's average tax-to-GDP ratio (34.2%) is not taken into consideration and countries are examined individually, South Africa uses taxation more intensively and has the highest ratio amongst the 13 developing and 3 most developed countries sampled in this study. The most striking observation is that South Africa's tax-to-GDP ratio (28.5%) is more in line with that of Australia (26.8%) and the UK (27.4%), which are both high-income countries and amongst the leading economies in the world. Additionally, only these three countries were able to attain the level of taxation (25%) needed for a country to be regarded as a developed country as per Bird's (2008) research. Steenekamp (2012b) also established in the 2007 tax year that the unweighted average tax burden of South Africa was higher than a selected group of 13 developed countries, and this signals that South Africa has been exhibiting high levels of taxation for some time now. This begs the question of whether South African taxpayers are overburdened and to some extent unfairly taxed,

given that the level of taxation mirrors that of developed countries yet it is a country regarded as an emerging economy.

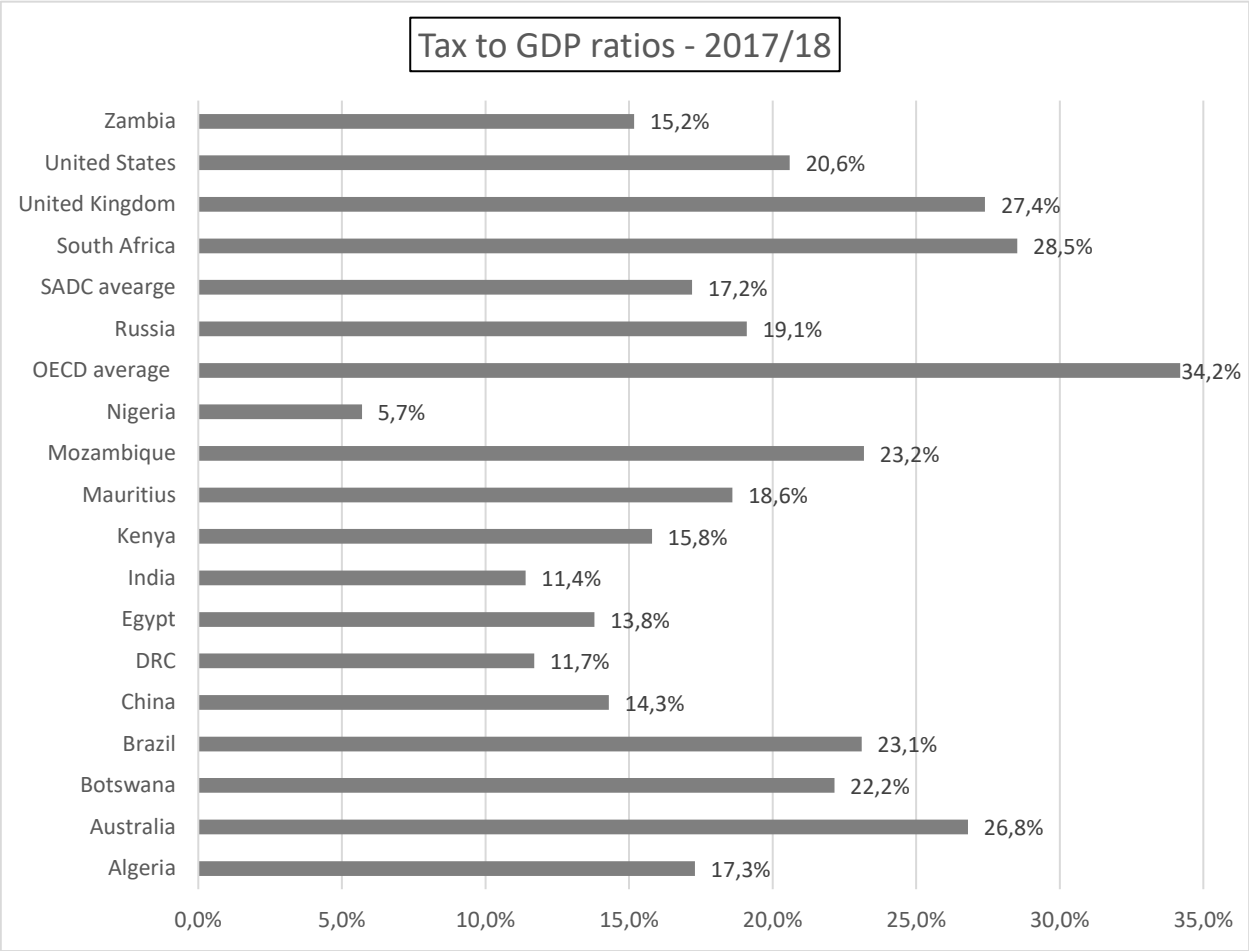

Figure 11: Tax-to-GDP ratios in 2018 – cross country (OECD, 2019) (IMF, 2020)

Modica *et al*. (2018) reiterated below why they believe that the ratio of the total income tax to the country's GDP remains fundamental as an economic indicator:

> The level of taxes in an economy gives an indication of the resources available to governments to fund public services, invest in infrastructure and to redistribute income. It also provides a rough estimate of the burden placed on the economy by the tax system. The level of the tax-to-GDP ratio is influenced by a number of different factors. These include economic factors, such as the level of income in a country, as countries with higher income per capita tend to have higher levels of tax revenues. Other economic factors including the level of consumption, the openness to trade, the size of the informal sector, or the composition of the economy by sectors also impact the level of the tax-to-GDP ratio.

Shockingly, when one looks at South Africa as a developing country, the level of taxation is parallel to developed countries and does not match the level of the economic growth nor support the objective to redistribute income and wealth more evenly, as evidenced by the trends in the tax buoyancy (see Table 5 above). The growth of the economy has been slower than the demand for the government to raise the levels of tax. The imperative to reduce income inequalities and poverty levels in South Africa requires not less, but more (and more effective) public expenditure and probably higher tax levels if economic growth does not accelerate over the medium to longer terms (Steenekamp, 2012b).

Table 10 below compares the contribution made from PIT to GDP collected by the central governments of the selected countries in 2017 (based on the latest available data). As indicated earlier, the most favourable PIT as a percentage of GDP ratio should be at 6.7% in order to accelerate the level of economic growth and tax efficiency, and still raise the much-needed revenue in a country. Only 5 out of 15 countries analysed below meet the optimal ratio required to strengthen the economy. Only two SADC countries, being Botswana (7.7%) and South Africa (9.9%), and all the OECD countries attained the benchmark, however, South Africa's PIT to GDP ratio surpassed that of the UK (9.2%) and is more aligned with that of the US (10.4%) and Australia (11%). This is not far from the observation made by Bird and Zolt that PIT plays a much smaller role in developing countries than in developed countries, as the PIT to GDP ratio usually averages 8% - 10% in developed countries and only 1% - 2% in developing countries (Bird & Zolt, 2005). Once again, South Africa's tax levels mirror that of developed countries instead of its counterparts.

Country	PIT to GDP ratio
Algeria	Not available
Australia	**11.0%**
Botswana	**7.7%**
Brazil	2.7%
China	2.5%
DRC	0.6%
Egypt	1.5%
India	2.6%
Kenya	4.1%
Mauritius	1.9%
Mozambique	3.7%
Nigeria	Not available
Russia	3.4%
South Africa	**9.9%**
United Kingdom	**9.2%**
United States	**10.4%**
Zambia	3.6%

Table 10: PIT-to-GDP ratio – cross country (IMF, 2020)

Table 11 below is adapted from an OECD study analysing the tax levels and structures of over 80 countries globally and it ranks countries according to their share of PIT revenue. What was closely examined in the study were the tax-to-GDP ratios and the share of each tax category in comparison to the total tax revenue for the 2015 tax year. The study encompasses selected countries with

similar economic levels from Asia, Latin America and the Caribbean (LAC), Africa and the OECD. In the study it was indicated that OECD countries generally have higher tax levels than any group of countries. The study unveiled that in 2015, PIT as a total of tax collected constituted a larger share for most OECD countries than for African and LAC countries, with the exception of South Africa at 33.4% followed by Swaziland at 28.7%, where the PIT shares were relatively high (Modica, et al., 2018). Although both Swaziland and South Africa are two African regions amongst the countries with a high share of PIT contribution, the difference is that the overall tax burden in Swaziland (15.3%) is considerably less than that of the majority of the countries listed in Table 11 below. Once more, South Africa is featured among countries with high levels of taxation against individuals and, repeatedly, the country manifests itself as an advanced economy.

	PIT	CIT	SSC	VAT	Other G&S	Other taxes	tax-to-GDP ratio
Denmark	55.2	5.6	0.1	20.0	11.6	7.5	45.9
Australia	41.5	15.3	0.0	13.0	14.5	15.8	28.2
United States	40.5	8.5	23.7	0.0	17.0	10.3	26.2
New Zealand	38.1	13.8	0.0	29.7	8.7	9.8	33.0
Canada	36.9	9.9	15.1	13.2	9.9	15.1	32.0
Iceland	36.7	6.5	9.8	22.6	9.7	14.6	36.7
South Africa	33.4	16.4	1.4	23.8	16.5	8.5	29.0
Ireland	31.6	11.3	16.8	19.7	12.9	7.6	23.1
Switzerland	31.1	10.8	24.6	12.4	9.3	11.7	27.7
Finland	30.2	4.9	28.9	20.6	11.8	3.5	43.9
Sweden	29.1	6.9	22.4	20.9	7.2	13.6	43.3
Swaziland	28.7	19.7	10.7	27.5	10.2	3.2	15.3
Belgium	28.3	7.4	31.9	15.0	8.8	8.6	44.8
Norway	27.9	11.5	27.3	21.4	9.0	2.9	38.3
United Kingdom	27.7	7.5	18.7	21.2	11.7	13.1	32.5
Italy	26.0	4.7	30.1	14.2	13.1	11.8	43.3
Luxembourg	24.5	11.9	29.0	17.6	7.9	9.2	36.8
Mexico	20.6	20.1	13.9	23.9	14.7	6.8	16.2
Korea	17.2	13.1	26.6	15.3	12.7	15.1	25.2
Trinidad and Tobago	16.9	44.0	9.3	15.7	10.2	3.9	30.6
Singapore	16.6	25.6	0.0	18.6	13.1	26.1	13.6
Malaysia	14.8	42.5	1.6	15.2	16.5	9.3	15.3
Philippines	13.7	25.2	14.0	13.1	26.0	8.1	17.0

Table 11: Countries with high share of PIT in 2015 (Modica, et al., 2018)

Without fail and with all measures used in this study being considered, South African tax levels surpass those of its international counterparts within the SADC and BRICS countries when the tax-to-GDP, PIT to GDP and share of PIT to total revenue levels are scrutinised. OECD countries generally have high tax levels and Australia, the UK and the US collect most of their tax revenue from individuals and South Africa follows in their footsteps. The tax regime adopted in South Africa is more in line with that of the UK when marginal tax rates, share of PIT as the main source of total tax revenue and PIT to GDP are taken into account. Governments around the world must seek to reform their tax structure or system to meet their specific fiscal needs, taking into consideration how this will affect the country on a micro and macro level. The possible tax reforms that may be viable in the case of South Africa are considered in chapter 5 below.

CHAPTER 5: ALTERNATIVE PIT REFORMS

There are numerous structural tax changes that have been brought about by the National Treasury in conjunction with SARS and occasionally at the instruction of various tax commissions over the years. Like everything else in this world, tax systems evolve. PIT reforms should align with the government's tax policy, which is aimed at improving tax collection efficiency, reducing the economic distortions associated with the tax structure and lowering the costs of investment and job creation, and releasing household spending power and savings (Steenekamp, 2012a). Again, the lesson for developing countries is not that nothing can be done through the fiscal system to deal with inequality, but rather that effective marginal tax rates should be kept as low as possible by increasing the tax base – this is why the usual broad-base, low-rate recipe for tax reform makes sense from both an efficiency and a distributional perspective (Bird & Zolt, 2005). The government has, over the years, strived to enhance the progressive character of the tax system, to improve tax efficiency and to realise a structural improvement in revenue (PwC, 2014). It is common that in developing countries, PIT reforms have focused on remedying the unequal income and wealth distribution as well as meeting the revenue targets of the government.

Bird (2008), like many other tax experts, believes that in developing countries, tax reforms should primarily focus on these three fundamental issues: (1) broadening the tax bases especially by shifting the burden from income to consumption taxes; (2) reducing income tax rates of individuals and corporates; (3) improving the tax administration including revenue collection. The very same approach was taken by the Margo Commission during the time when South Africa's economy was heavily sanctioned and was met with fiscal challenges such as high inflation and low foreign investments and, as a consequence, was tasked to remodel the tax structure into a revenue-maximising and tax base-broadening regime. The commission was to achieve this by enforcing reforms aimed at creating job opportunities, reducing human capital flight, enhancing tax compliance and morality, encouraging foreign investment and promoting entrepreneurship (Black, et al., 2015). In the same manner, the Katz Commission

(1994), which was appointed at a critical time (the post-apartheid era, when an inclusive and radical economic transformation was needed in South Africa), recommended that a comprehensive tax reform approach be introduced, and the objectives of the tax reforms are summarised as:

- broadening the tax base by removing or limiting deductions, exemptions and other preferences available to taxpayers;
- reducing the gradation of the marginal tax schedule;
- reducing the number of marginal tax brackets, thereby leading to simplified tax administration;
- reducing the maximum marginal income tax rate;
- raising the tax threshold, thereby removing lower-income taxpayers from the tax registry and enhancing horizontal equity; and
- adjusting brackets, credits, standard deductions and other nominal amounts for inflation for enhanced progressivity of the PIT regime.

The Association of International Certified Professional Accountants (AICPA) has developed twelve guiding principles for good tax policy which consists of a framework for evaluating tax proposals or laws to be enacted by governments (AICPA, 2017). Tax authorities must strive to evaluate that an all-encompassing and objective approach is being followed to ensure a good tax system and rules are achieved. The guiding principles are: equity and fairness, certainty, convenience of payment, effective tax administration, information security, simplicity, neutrality, economic growth and efficiency, transparency and visibility, minimum tax gap, accountability to taxpayers and, finally, appropriate government revenues (AICPA, 2017).

The central question in this study is: are South African individuals taxed too much? Consequently, of a particular interest to this study are the guiding principles focusing on equity and fairness, economic growth and efficiency, and appropriate government revenues. The principle of equity is often viewed as a fairness principle (AICPA, 2017). Thus, it is vital that the PIT structure is set out in a way that endeavours to push for vertical and horizontal equity and fair

distribution of the tax burden amongst taxpayers, thereby curbing income and wealth inequality that is so rife in South Africa. As it has been indicated earlier, equity and fairness goals can be partly attainable if the progressivity of the PIT system is promoted so that taxpayers who earn higher incomes are taxed at marginally higher tax rates than lower-income taxpayers and effective rules are established regarding wealth taxes which often escape the tax net. The Davis Tax Committee (2018) was therefore appointed by the Minister of Finance to evaluate the feasibility of increasing the share of wealth taxes in the overall tax mix of South Africa, in order to achieve social stability and economic inclusiveness in an economically and administratively efficient manner.

Ultimately, the primary objective of taxation is to provide funding for the government and possibly improve the overall economy of a country. Taxes can reduce economic efficiency and create distortions; therefore a good tax policy revolves around enhancing economic growth, capital formation and international competition of the country (AICPA, 2017). The objectives of the tax reforms and policies should be aligned with the economic goals of the country. The implementation of certain tax reforms can affect the economic decisions of agents affected by the tax structure. Most of the PIT reforms have tried to create a fiscal environment that encourages saving, investment and entrepreneurship and provides increased work incentives and, as a result, contributes positively to the overall economy (OECD, 2010). Likewise, certain tax policies can hamper economic growth and efficiency hence the design of it should be looked into holistically.

The principle of appropriate government revenue is vital when designing the appropriate tax structure and implementing tax policies. The tax system should evolve easily and become flexible to the changing needs of the economy and, moreover, the tax system should be predictable, stable and reliable to enable the government to determine the appropriate timing and amount of tax revenue that can be raised (AICPA, 2017). Determining the appropriate and different sources of tax to rely on provides a more stable and flexible tax base for the government, and during the economic downturns, the government is able to adjust their

revenue needs and place more reliance on the taxes that are less affected by changes in the economy. For instance, if the unemployment rate of the country is very high or mass retrenchments are imminent, there should be less dependence placed on PIT to alleviate the tax burden on individuals and perhaps the tax rates could be lowered and tax thresholds increased so that individuals are less adversely affected by this. Thus, it is necessary to review tax systems regularly to ensure they are supportive of the government's fiscus or at least not hindering their attainment, and to change revenue targets and the tax system accordingly based on technological, social and commercial developments (AICPA, 2017). Although it is advisable to consider the twelve guiding principles collectively when implementing tax reforms, it is usually difficult for taxing authorities to achieve this as there are many factors at play, as discussed below:

> A key challenge is the reality that achievement of all of the principles is not possible to the same degree for all proposed tax changes. For example, to exclude a particular type of economic benefit from taxation may satisfy the simplicity principle, but not the equity or neutrality principles. Thus, lawmakers must carefully balance the guiding principles to achieve an optimal law. (AICPA, 2017)

In developing countries, there are different schools of thought in what a successful tax system or reform for PIT entails. The different PIT reforms will not be discussed exhaustively in this study. Broadly speaking, there are four PIT systems that countries can pursue: the comprehensive PIT system, the flat tax system, presumptive taxation and the dual income tax system (Steenekamp, 2012a). Globally, income tax systems do not conform to the ideals of a comprehensive income tax system as it tends to not be fair to taxpayers; it applies the same rate for labour and capital income thereby exacerbating income inequality. It is a less efficient tax system as it can be easily manipulated to reduce the tax liability and there are administrative complexities and compliance issues resulting from the comprehensive income tax system (Black, et al., 2015). Notwithstanding this, South Africa subscribes to a tax structure that is leaning more towards a semi-comprehensive PIT system which employs a progressive rate schedule for all sources of income while providing various tax reliefs for individuals (Steenekamp, 2012a). The semi-comprehensive tax system combines a progressive rate schedule for all sources of income with certain tax reliefs offered, and it is therefore prone to tax arbitrage as individuals restructure

their tax affairs to exploit exemptions, allowances, savings and investments and after-tax rate differentials (Steenekamp, 2012a). Alternatively, most tax experts agree that the one promising approach to taxing personal income more effectively in developing countries like South Africa is to introduce a dual income tax system which separate regimes for the taxation of labour and capital income (Bird & Zolt, 2005).

The dual income tax system is already used in Nordic countries, namely Denmark, Iceland, Finland, Norway and Sweden. A dual tax system levies a single proportional rate for capital income, and labour income is subject to a progressive rate structure (Black, et al., 2015). A dual tax reform offers an efficient way to deal with problems of capital flight and tax arbitrage activities, and reduces the distortions caused by different treatment when it comes to different sources of capital income (Steenekamp, 2012a). Additionally, variable labour income is well accommodated under the dual tax system through the progressive tax schedules and it provides the flexibility that developing countries need to adhere to for international competition for capital income (Black, et al., 2015). The following statement further substantiates why the dual income tax system is a superior tax reform:

> In developing countries, the two major advantages of a dual income tax system would be rationalisation of the taxation of capital income and improved enforcement and compliance, because adopting a single flat tax rate on capital income may allow for an opportunity to expand the tax base to include types of income that were previously exempt from taxation, such as interest on government and publicly traded corporate bonds (Bird & Zolt, 2005).

Both the Margo and Katz Commissions highlighted the need for South Africa to lower the overall tax burden in order to align with international tax competition and tax harmonisation, hence there have been numerous reductions in the top marginal rates. The PIT top rate was at 45% in 1996 then decreased to 40% in 2003 and moved to 41% in 2016 and, most recently, a new marginal tax rate bracket of 45% for individuals earning above R1.5 million was introduced in 2017. Contrary to the efforts made by the different tax commissions in South Africa to alleviate the PIT levels through the decrease in marginal tax rates, the tax burden of individuals is constantly increasing one way or another. One option to widen

the tax base without affecting the marginal tax rates would be to reduce tax expenditures such as fringe benefits, exempt interest and dividends, medical and retirement deductions and rebates (Steenekamp, 2012b). The significant changes or measures listed below were put in place to maintain the progressive character of the PIT system over the years, and to concurrently increase the tax base and reduce the tax burden imposed on individual South African taxpayers. The list below draws attention to changes that were significant in the PIT regime or those that affected individual taxpayers on a larger scale. The information below is from various budget reviews published by National Treasury between the 2001 and 2019 tax years.

- CGT was introduced in 2001.
- Effective CGT rates have also been increased over time to build on the progressive character of the tax system.
- The tax system of source-based income was replaced by residence-based income.
- General sales tax was phased out and replaced by VAT.
- The child rebate was removed.
- Determining the tax liability of an individual based on marital status was scrapped, thus an individual became the standard unit of taxation, which allowed for the equal treatment of both genders and enhanced tax neutrality.
- The Standard Income Tax on Employees system was discontinued by 2010.
- For motor vehicle allowances, the deemed business kilometre procedure was scrapped. A logbook had to be kept for actual business kilometre readings as from 1 March 2010.
- In addition to the primary and secondary rebates, a third rebate was introduced for taxpayers over 75 years of age from 1 March 2011.
- Effective from 1 March 2012, the medical deductions were converted to medical tax credits.
- The Tax Administration Act (TAA), 2011 which legislates all general administrative provisions was promulgated in 2012.

- The secondary tax on companies was converted to dividend withholding tax in 2012 and the withholding tax rate was increased from 15% to 20%, effective from 1 March 2017.
- Effective from 1 March 2015, the following applied: all qualifying medical expenses for all taxpayers (below the age of 65 years and 65 years or older) were converted into tax credits.
- The tax treatment of contributions to different retirement funds and vehicles was harmonised, effective from 1 March 2016.
- Donations tax and estate duty were previously levied at the rate of 20% irrespective of the level of donations or the value of the estate. With effect from 1 March 2018, a higher rate of 25% of the value of the estate or on a donation exceeding R30 million applies.
- The number of tax brackets was reduced from ten to six and recently increased to seven in the 2018 tax year.
- The employment tax incentive was extended by ten years as from 2018 to continue to boost job creation.

The National Treasury continually strives to improve on the tax levels and structure of South Africa, hence the consistent efforts to implement the recommendations made by the various tax commissions and to strengthen the tax administration and the capacity within SARS, leading to the appointment of the new SARS Commissioner in 2019 (National Treasury, 2019). As an alternative to the current comprehensive income tax system, the best tax reform for South Africa to implement given its challenges is the dual income tax system, as it provides the flexibility that developing countries need to meet the international competition for capital and to maintain or even increase the progressiveness generated by the PIT system (Steenekamp, 2012a).

CHAPTER 6: CONCLUSION

The objective of this study was to critically analyse and compare the tax burden of individual South African taxpayers from the 2003 to 2019 tax years. Different quantitative data and methods were used to measure the PIT levels for the period under review, in an attempt to answer the question “are South African individuals taxed too much?”

This study revealed that tax revenue is the number one and by far the most important source of revenue which the South African government uses to raise money to fund the ever-increasing social needs and public services of its citizens. What was evident is that PIT plays an integral part as the main contributor to the total tax revenue and there has been constant growth in the PIT collections from 2003 to 2019 in South Africa. Although the number of registered individuals has been growing considerably year-on-year, the number of individuals who are actually assessed and ultimately bear the burden of PIT has been on a decline. With the tax base shrinking, the desire to lower the marginal income tax rates (as recommended by the OECD, various tax experts and all the tax commissions ever appointed in South Africa, in pursuit of growing the economy and aligning with international standards from an efficiency and equity perspective) becomes almost impossible for the country to attain. South African individuals and not corporates are taxed more intensively to support government spending. Steenekamp (2012a) also reached a similar conclusion after assessing the tax levels of South African individuals and cautioned against any further increase in PIT rates, as they seem to be constrained by already-high marginal tax rates, a small tax base and a corporate income tax rate (28%) that is lower than the top marginal PIT rate (45%).

Moreover, this study signalled that the use of taxes and PIT in particular to reduce high income and wealth inequality in South Africa is not very effective nor sustainable. Although the collection of taxes on individuals has been improving, there has been little improvement on the redistribution of income and wealth as proven by the deteriorating Gini-coefficients (as seen in Chapter 3 of this study).

The study made mention of the fact that the majority of South Africans are considered poor and taxes have not helped much in this regard. Failure on the part of the Minister of Finance to adjust the PIT regime for inflation consistently has done more damage than good for the majority of poor South Africans, by favouring the top income earners who are already in the high tax brackets while disadvantaging low-income earners who are unjustly pushed to higher tax brackets due to the tax bracket creep. Consequently, this further increases the tax burden and unfairly redistributes the effective tax burden borne by the majority of the low-income earners. A rather effective way to enhance horizontal and vertical equity and concurrently raise revenue and broaden the tax base may be to implement alternative measures to properly tax and administer the informal sector and the self-employed (Steenekamp, 2012a). Bird (2008) cautions that an optimal way to reduce income inequality is not through imposing higher levels of taxation, but rather through spending programmes targeted at the poor and their overall personal growth.

When the PIT levels of South Africa are scrutinised at a macro level, it becomes evident that for a developing country, individuals are taxed more intensively than companies and too much reliance is placed on PIT, which is unheard of for most of the developing economies. South Africa has abnormally high minimum (18%) and maximum (45%) marginal income tax rates when compared with some SADC (average of 30% maximum PIT rate) nations and three of the fastest developing countries in Africa (Egypt, Kenya and Nigeria). South Africa is the only African country represented in the BRICS organisation and the tax burden levied on individuals far exceeds that of the counterparts by any possible measure used. Several studies have indicated that the PIT levels of South Africa are very high for a developing country and the tax burden on individuals is more aligned with the PIT levels levied on taxpayers from OECD countries, which all thrive on advanced economies and social landscapes.

The hard lesson for developing countries is that a perfect tax system does not exist; however, governments must assess their country’s unique social and economic needs in implementing tax reforms to improve the PIT regime.

However, tax authorities must keep in mind how their tax system and structure affect the country's participation in the global context. Therefore, tax policies and reforms that promote international tax competition and harmonisation while simultaneously striving to grow the tax base, lower tax rates and advance tax administration are desirable. As indicated in the previous chapter, the current comprehensive income tax system may not be the most advantageous for a developing country like South Africa because of the imbalances presented by it. Perhaps a tax reform leaning towards the dual income tax system is needed to grow the tax base and strength tax compliance whilst achieving economic efficiency and promoting income equality. Bird and Zolt (2005) concluded that everyone benefits in terms of both improved economic well-being and a more sustainable political system if the tax policies are accompanied by expenditure policies that focus on health, education, and infrastructure improvements to develop the country's human capital, which contributes to higher productivity and growth in the long term.

The study used different methods and measures to analyse the PIT levels of South African individuals over the 2003 – 2019 tax period, and the results proved the hypothesis or assumption made by several tax experts that the tax burden on individuals is indeed high when scrutinised on a micro and macro level.

Future research

Of great interest for a country with multi-faceted social and economic challenges like South Africa would be a practical and comprehensive study that focuses on the possible PIT tax reforms that can raise the much-needed tax revenue without burdening individual taxpayers further. This study should also highlight the possible sustainable and growth-orientated expenditure programmes that the South African government can introduce to supplement tax revenue raised in order to eradicate poverty, encourage entrepreneurship and improve income and wealth equity.

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