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Abstract

Developing countries are often advised to broaden their tax base. The South African fiscal authorities have at various times claimed to do so, inter alia in order to reduce tax rates. The paper explores whether they have been serious about base broadening. Various conceptual issues are raised in defining base broadening and base erosion. Drawing on budget documentation, tax measures of base broadening and erosion from 1994 to 2018 were tabulated. A selection of the most salient nonquantified measures and all quantified measures are presented. Net budgeted base broadening (2018 prices) of R1.7 billion is reported, in the process of which various tax increases and decreases were also implemented. The need for a much more systematic quantification of all base-broadening and base-erosion tax measures in South Africa is indicated. This should not only occur at the time of announcement but especially to track and report the actual outcome of all such measures in subsequent years.

1. INTRODUCTION

Salient pieces of considered fiscal advice to developing countries are to broaden the tax base and improve tax compliance. There are various reasons for this. Gordon & Li (2009: 857) notes that "… the poorest countries collect two-thirds or less of the revenue collected in the richer countries, as a fraction of GDP, an observation that could reflect differences in preferences for public vs. private goods, but that could also be a symptom of problems in tax collection." All countries experience external base erosion (OECD, 2013) as well as internal base erosion associated with tax evasion, tax avoidance and poor tax administration. All of this constitute a tax gap because of noncompliance, that is, a difference between the potential tax yield, given the tax base and rates, and the actual tax collected. In this regard the IMF distinguishes between a policy gap (resulting from how tax laws are designed and applied), and a compliance gap resulting from the behaviour of tax payers (see Toro et al., 2013: 11). In addition, many developing countries have not been able to develop their tax base to the same extent as industrial countries or even some emerging market economies.

The purpose of this paper is to explore the seriousness of the South African fiscal authorities with tax base broadening, as claimed at various times. In National Treasury (2001: 74) it is stated: "Capital gains tax … could raise about R1 to R2 billion a year directly. This provides scope to advance Government's overall tax reform strategy of broadening tax bases and reducing statutory tax rates." Another example is in National Treasury (2010: 78): "Government has achieved lower rates over the past decade by broadening the tax base". And very recently (National Treasury, 2017: 39): "The corporate tax base was broadened and the rate reduced". The importance of base broadening was also implied in the terms of reference of the Davis Committee (2014) that was requested inter alia to evaluate the South African tax system against the international tax trends, principles and practices, as well as recent international initiatives to improve tax compliance and deal with tax base erosion. The focus is solely on tax measures, thus excluding the impact of economic growth and demographic factors on the tax base.

Firstly the meaning of tax base broadening (and base erosion as its opposite) is discussed in relation to some related concepts. This is followed by a brief literature review on tax base broadening, after which the research method is explained. Then tax base broadening and base erosion measures in South African since 1994 are documented. From the latter and the literature review, inferences are offered on the nature of base-changing measures with reference to properties of a good tax and some other considerations. An estimate is also made of the total extent and impact of tax base broadening/erosion in South Africa from 1994-2018.

No evidence in the economics literature was found of a systematic and comprehensive outline of base-broadening and base-eroding tax measures introduced by an emerging market economy following a major political and constitutional transformation. This paper is an attempt to fill this gap and serves as a suggested formal method of systematic record-keeping and quantification of tax base developments to be considered by South Africa and further afield, and to indicate some avenues for further research.

2. BASE-BROADENING AND CONCEPTUAL ISSUES

A definition

What is tax base broadening and what is it not? Applying South Africa's National Treasury's (2017: 190) definition of the tax base, one may describe base broadening as an increase in "(t)he aggregate value of income, sales or transactions on which particular taxes are levied." In this paper the following definition is offered: For any given tax type (e.g. corporate or personal income tax or value-added tax) any movement towards capturing the entire potential number of taxable entities, activities or values is viewed as entailing a broadening of the tax base. In this regard one is reminded of the Haig-Simons definition of comprehensive income that defines taxable resources as the change in an individual's power to consume during the year. The latter amount is the money value of the net increase in an individual's power to consume during a particular year, in other words, the amount actually consumed plus net additions to wealth (Rosen, Gayer & Civan, 2014: 376). This implies that all beneficiaries of public services contribute to the financing of public services according to their ability to pay as embodied in whatever constitutes a socially acceptable tax system. Our definition goes much wider than merely attempting to think in terms of all the legislated taxes of a particular country at any point in time. It also allows for new taxes if and to the extent that the Haig-Simons definition is not achieved by the existing tax structure, or the existing structure does not meet with socially defendable equity considerations. Base erosion, on the other hand, is nothing but inverse base broadening, or base narrowing.

Tax base broadening therefore is to ensure that the tax base is well defined. i.e. comply on a tax-by-tax and aggregate basis with allocative and administrative efficiency, equity and flexibility – the standard properties of a good tax (see Black, Calitz & Steenekamp, 2015: 214-215), as well as being inclusive of all people, values and activities implied as such. Take personal income tax as an example. If the tax is designed so that personal income only becomes liable for taxation above a certain threshold, this does not present a leakage from the tax system. If everyone pays according

to the tax laws, the base is what it was defined to be and, given the tax rates schedule, the total revenue collected equals the potential yield. If tax incentives or opportunities for tax avoidance are included in the tax law, the base is what it is intended to be. One can argue that the base can be broadened, of course – for example by scrapping or amending a law that enables a tax incentive. In doing so, it is recognised that the base can be and is indeed broadened. The opposite can also happen. When incentives are extended, for example, base erosion occurs.

Unintended avoidance

Whilst legislated or regulated tax avoidance co-defines the base, what about unintended avoidance activities? A case in point would be when higher income groups revert to the consumption of basic foodstuff that are zero-rated under value-added tax, or when a decentralisation tax incentive results in the establishment of a corporate head office in a decentralised region purely with a view of registering a tax address but without any substantive business activity. Tax authorities have experienced substantial tax leakage on account of such activities and it may be justified to regard such activities as *informal* base-eroding actions. Steps by revenue authorities to improve compliance in such cases may indeed be viewed as the *de factor* broadening of the tax base.

Improved tax collection methods by the tax administration that succeed in eradicating unintended tax avoidance, as well as legislation that close such loopholes, therefore entail base broadening. Conversely, measures that create such loopholes constitute base erosion. These measures therefore need to be listed as well, but of course without knowing what the revenue gain is, was or will be. Tax evasion obviously constitutes an illegal base-eroding activity. Attempts to curtail evasion therefore contribute to base broadening.

Modelling and revenue neutrality

The literature offers ample examples of modelling base broadening-cum-rate reductions in a revenue-neutral context. See for example Milner and Granqvist (2002) with regard to developed countries, and Devereux, Griffith and Klemm (2002) with regard to corporate income tax in the EU and G7 countries. Examining fiscal trends, Ganghof (1999: 2) observed that the 18 most advanced OECD "(g)overnments have pursued a policy of tax-cut-cum-base-broadening, differentiated their income tax treatment according to differences in competitive pressures, and combatted international tax avoidance and evasion with legal and administrative measures." Emran & Stiglitz (2005: 599) show that "(o)nce the incomplete coverage of VAT due to an informal economy is acknowledged … the standard revenue-neutral selective reform of trade taxes

and VAT reduces welfare under plausible conditions. Moreover, a VAT base broadening with a revenue-neutral reduction in trade taxes may also reduce welfare."

A revenue neutral approach to base broadening is not only a recognised analytical approach, but is also not surprising from a fiscal policy point of view, given the political difficulty of motivating extra revenue generation in any country. In a sense tax rate reduction without a reduction in total tax revenue may indeed be viewed as the pinnacle of base-broadening success, *ceteris paribus*. But there are obviously various other considerations in a base-broadening or even base-alignment exercise, such as the distribution effect (which includes the fairness underpinning vertical and horizontal equity), the tax harmonisation requirement of regional economic integration[1] and the allocative efficiency effect as embodied in the Ramsey rule.

Base changing and bracket creep

Although base broadening and tax rate reductions seem to go hand-in-hand, base broadening is not about tax rates and is not here considered as entailing rate changes.[2] But there is a snag here as well. Are we talking about the real or the nominal tax payable? Bracket creep is a case in point. If bracket creep is not eliminated in an inflationary episode and the result is an increase in the tax yield for government and the real tax burden on an individual, without any change in the tax brackets applicable in a progressive income tax structure, does this constitute tax base broadening? If, at the same time, the tax threshold is raised, does this amount to base erosion? These two examples do in fact reflect base broadening and erosion, respectively. In both examples a nominal change in tax revenue results on account of two base-changing decisions. In the first case the change was – even if only for the particular year – to *de facto* change the tax base by allowing the addition of a tax-bracket specific inflation component to every taxpayer's taxable income. In general terms, whenever inflation is allowed to increase the tax obligation, we regard that as base broadening as this by implication entails the introduction of inflation as a tax source. This does not amount to an agreement with the method. On the contrary, this kind of base broadening is a nontransparent and underhand method of which the obscurity cannot be condoned, even though it

[1] Regional tax harmonisation and the implications for tax bases are analysed for EU countries by Jacobs, Spengel, Stetter & Wendt (2005).

[2] National Treasury (2017: 40) by implication subscribes to this view by also excluding tax rate changes when it is stated that base broadening "can involve removing tax incentives, and introducing measures to curb tax avoidance through loopholes and schemes."

stretches the tax base.[3] In South Africa the annoying practice to announce even partial elimination of bracket creep as a tax reduction despite the fact that tax payers encounter a real increase in their income tax burdens, was visible until fairly recently (National Treasury, 2014: 47).[4] It seems to have been abandoned since.[5] To the extent that information on bracket creep was available from budget documents, an estimate is included in the calculations in Section 4. On the other hand, explicit increases in unit indirect taxes above inflation rates, are not regarded as constituting tax base changes. Such increases do not automatically imply a real increase in the tax burden. Here base broadening is deemed to occur only when new items are taxed or new taxes are introduced.

Phasing out a particular tax

There is even another snag. How are we to view the case where a particular item is removed from the tax base, at which time the applicable tax rate is effectively reduced to zero? Because the particular item leaves the base, the tax loss (and by implication the rate reduction) at the point of removal entails a permanent reduction of tax revenue and therefore should be counted as a reduction in the tax base. A case in point is the decision to abolish the 5% import surcharge on capital and intermediate goods with effect from 23 June 1994, estimated at the time to amount to a revenue loss of R1.2bn for a full year (2014 prices) (Department of Finance, 1994: 5.7). To apply this approach consistently becomes problematic when a tax is phased out over a number of years by means of systematic rate reductions but without an announcement to that effect at the outset. In all likelihood only the final rate reduction or removal of the tax will be picked up as base reduction.

The tax gap

Another strand of research is about the tax gap. How does this relate to base broadening issues? The tax gap is defined as the "difference between the amount of tax that should, in theory, be collected … against what is actually collected." (HM Revenue & Customs, 2014a: 4). Ahmed &

[3] One is reminded of the fiscal illusion theory developed by the Italian economist Amilcare Puviani in his 1903 book *Teoria della illusione finanziaria*: if it is less costly, it makes sense to collect taxes in a way that is not completely transparent nor perceived by taxpayers!

[4] This reads as follows (italics added): "To compensate for the effects of inflation, which pushes some individuals into higher tax brackets and reduces their purchasing power, the personal income tax brackets and rebates will be adjusted, *providing individuals with R9.3 billion in personal income tax relief.*"

[5] By own admittance (National Treasury, 2017: 40): "In recent years, government has not been in a position to provide full inflationary relief and has raised the effective personal income tax rate." Since 2016 one actually finds a figure in the *Budget Review* of the amount of bracket creep that was not eliminated in a particular year – a commendable development that assisted in the calculation of base changes in Table 4.

Rider (2013: 335) refer to the tax gap as those taxes not collected when taxpayers are not complying with the tax system. They indicate that a distinction should be made between tax avoidance (which include activities within the law to reduce or minimise the tax liability) and noncompliance (when taxpayers do not comply with their tax liabilities). It is the latter that causes the tax gap. Toder (2007: 1) refers to the gross tax gap as the "difference between tax liability in any year and the amount of tax that is paid voluntary and on time". There are three components to this gap: underreporting, nonfiling and underpayment (i.e. not paying the tax by the due date) (Toder, 2007: 1). Analysing corporate income tax in South Africa, it was calculated that the marginal effective tax rate in respect of the different economic sectors differed substantially, reflecting very unequal tax treatment at the margin of investment (World Bank, 2015: 23). This suggests great disparities in the effective (as opposed to the statutory) corporate tax base.

The IMF refers to two factors influencing tax gap definitions, i.e. compliance (the compliance gap), and the impact of policy on revenues (the policy gap) (Toro et al., 2013: 11). The former relates to the gap emanating from noncompliance, whereas the latter arises as a result of policy provisions allowing deductions or exemptions. When determining tax gaps, it is recommended that both the compliance and policy gaps are measured, as the latter provides significant information on foregone tax revenues to policymakers when they are considering changes to the tax regime. Both gaps entail an erosion of the tax base and measures of both of them are included in this discussion. One has to allow for the possibility, however, that tax exemptions (i.e. base erosion) may actually incentivise compliance over time, with a net revenue gain as result (see Das-Gupta, Lahiri & Mookherjee (1995)). This is typically the argument when tax allowances are viewed in a dynamic context, whereby they are supposed to generate downstream income with tax payments in excess of the allowance.

Summary

The above dimensions of base broadening are summarised in Table 1.

Table 1: Dimensions of tax base broadening

Basic definition of base broadening	Any movement towards capturing the entire potential number of taxable entities, activities or values
Extension of existing tax bases	Legislating the extension of the coverage of an existing tax with reference to entities, activities or values

New taxes	Legislation and implementation of new taxes
Combating tax avoidance	Any legislative, regulative or administrative measure that reduces avoidance
Combating tax evasion	Any legislative, regulative or administrative measure that reduces avoidance
Bracket creep	Allowing inflationary increases in the tax base

3. METHODOLOGY

The question about whether the SA fiscal authorities are serious with base broadening is investigated by studying the South African Budget Reviews from 1994 to 2018. The identified base-broadening and base-erosion tax measures were tabulated. Where provided in Budget Reviews, the estimated revenue effect in the particular year, as well as the calculated value in 2018 prices, are indicated. The total list of measures, with comments and calculations, is too long for inclusion in this paper but is available from the author. A condensed version appears in three tables in Section 4.

4. POLICY MEASURES PERTAINING TO TAX BASE BROADENING AND COMPLIANCE

Base broadening, base protection and base erosion

In practical terms the tax base is broadened by incorporating untaxed or hard-to-tax subjects or groups or activities into the tax system, as defined, and by stemming, stopping or reversing intended and unintended leakages from the tax base, be they in the form of tax avoidance or evasion. These attempts are of course counter-balanced by measures that constitute a narrowing or erosion of the tax base. As indicated at the outset, this paper therefore does not deal with the impact of economic growth or population growth on the tax base, factors which of course play a substantial role in their own right.

This section gives an overview of both sets of measures (i.e. base broadening and base eroding) since 1994. We distinguish between nonquantified and quantified measures. Only a selection of

the most prominent nonquantified ones are provided (Tables 2 and 3). Comments are added about the link of each of the latter to either properties of a good tax as well as some other considerations.

In the case of quantified measures (Table 4), the money values are provided for the relevant fiscal year and then, by using the consumer price index, expressed in 2018 prices. The last line of Table 4 shows the total for base broadening (column 4) and base erosion (column 6), as well as the net base effect (column 7). It shows an estimated net base increase (broadening) of about R 1.7 billion (2018 prices) over the period 1994-2018.[6] These tables are followed by explanations of the nature of and trends regarding changes in the tax base.

Table 2: A selection of nonquantified base-broadening measures

Year	Measure	Considerations
1997	Establishment of SARS.	Administrative efficiency; enhanced compliance.
1997-	Various administrative and regulatory measures (2003, 2004, 2005, 2006, 2008, 2010, 2011, 2015, 2018). Example 1: Investigative unit established for high net worth individuals to identify undisclosed income (2005). Example 2: Enhancing rules on foreign companies controlled by a South African resident, so that a portion of profits earned by a South African-owned subsidiary operating in another country is taxed in SA	Administrative efficiency; enhanced compliance.

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

Year	Measure	Considerations
	if no meaningful economic activity took place in the other country (2016).	
2001	Loopholes closed through various measures (including procedural reforms).	Reforms (laws and procedures) to reduce avoidance.
2001	Introduction of capital gains tax.	A new tax on income to combat corporate income tax avoidance. National Treasury's (2001:74)'s potential revenue gain of R1bn to R2bn is too vague to include in the quantified list in Table 4.
2001	Education of taxpayers (service centers; special attention to previously neglected communities and key players in the cash economy).	Education as a means to convey and inculcate the symbiosis of citizens' rights under the Constitution and their responsibilities as tax payers.
2003	Measures to ring-fence tax base (losses from secondary trade – "weekend" business).	Formal rules; protect tax base; promoting horizontal equity and allocative efficiency.
2003	SA tax law to be amended to specifically address bribes, penalties and other forms of illegal activity.	Combating tax evasion.
2007	Closure of dividend schemes.	Withdrawal of tax rules that enabled avoidance.

Year	Measure	Considerations
2009	Income derived from the disposal of primary certified emission reductions (CERs) tax-exempt or subject to capital gains tax instead of normal income tax; secondary CERs to be classified as trading stock & taxed accordingly.	Market-based solution to negative externality.
2011	Voluntary disclosure for taxpayers in default.	Compliance.
2012	Income tax deductions for medical scheme contributions for taxpayers below 65 years to be converted into tax credits.	Enhance equity by replacing a progressive allowance with a regressive lump-sum tax credit (base erosion). Capping results in a reduced fiscal cost and protection of the tax base.
2013	Measures to avoid erosion i.r.o. corporate debt, long-term insurers, unlisted real estate investment trusts; hedge funds.	Protection of tax base.
2014	Employee tax incentive (cost not capped).	Stimulation of youth employment.
2014	Tax-preferred savings accounts.	Encourage household savings.
2014	Changes to the taxation of contributions to retirement funds in line with the Taxation Laws Amendment Act (2013): additional	Encourage individuals to provide for retirement.

Year	Measure	Considerations
	relief to most retirement fund members and encouragement to save for retirement.	
Source: Department of Finance (various years); National Treasury (various years).		

Table 3: A selection of nonquantified base-eroding measures[7]

Year	Measure	Considerations
1995, 1996, 2000	▪ Tariff reductions and rationalisation in ad valorem excise duty rates. ▪ Abolition of import surcharge on imported capital and intermediary goods.	Reform customs duties in accordance with WTO agreement (94/95-99/00), including a more uniform tariff structure, scrapping of approximately 3000 eight digit tariff lines and investigating 2500 more.
2006	Bursaries and scholarship for further education: bursaries and scholarships for current and future employees tax-exempt as long as employer's funds go directly to tuition and tuition-related expenses.	Education as positive externality; legitimised nontax liability.
2008	Biodiversity conservation and management incentive: landowners to receive income tax	Internalising positive externality (Pigouvian tax subsidy).

[7] This of course does not mean or suggest that the revenue effect of these or some of these measures cannot be estimated. It would however require a deliberate effort by the fiscal authorities at the time of announcement or at a subsequent point in time.

Year	Measure	Considerations
	deduction for preserving habitats and biodiversity on their land.	
2009	Incentives for investments in energy-efficient technologies.	Internalise positive externality (Pigouvian tax subsidy).
2004	Broad-based tax-free share transfers to employees.	Legitimised tax burden alleviation.
2011	A third income tax rebate is announced for taxpayers 75 years and older.	Equity considerations.
2011	Introduction of industrial development zones (IDZs).	Tax rules legitimising nontax liability, reflective of developmental state thinking.
2013	Tax incentives in special economic zones: corporate income tax of 15%; tax reduction as an employment incentive; accelerated depreciation allowances.	Tax rules enabling tax reduction, perhaps the regional decentralisation argument of positive externality.
2014	Introduction of tax-preferred savings accounts.	Incentive to encourage household savings.
Source: Department of Finance (various years); National Treasury (various years).		

Table 4: Quantified tax base changing amounts by tax type, 1994-2018

TAX	YEAR	BASE INCREASE		BASE DECREASE		NET BASE ∆
		(FY prices) Rm	(2018 prices) Rm	(FY prices) Rm	(2018 prices) Rm	(2018 prices) Rm
(1)	(2)	(3)	(4)	(5)	(6)	(7)
PERSONAL INCOME TAX						
Various base-broadening measures	1998	2 000	5 748			5 748
Introduction of gender neutrality in tax	1995			2 000	7 166	-7 166
Limitation placed on various employee deductions	2002	85	191			191
Fringe benefit tax: occasional free service	2002	5	11			11
Capping of medical scheme contributions	2007	180	325			325
Measures to limit tax avoidance through salary structuring	2010	1 800	2 623			2 623
Reforms of dividends tax	2012			1 900	2 497	-2 497
Non-elimination of bracket creep	2016	7 600	8 003			8 003
Non-elimination of bracket creep	2017	12 100	12 100			12 100
Non-elimination of bracket creep	2018	6 018	6 018			6 018
CORPORATE INCOME TAX						
Ring-fencing tax base	2003	50	106			106

TAX		YEAR	BASE INCREASE		BASE DECREASE		NET BASE Δ
			(FY prices) Rm	(2018 prices) Rm	(FY prices) Rm	(2018 prices) Rm	(2018 prices) Rm
(1)		(2)	(3)	(4)	(5)	(6)	(7)
Small And Medium-Sized Enterprises							
Graduated rate structure for SMEs & micro businesses	15% on first R100 000 taxable income and 30% thereafter	2000			100	259	-259
	Extended 2002	2002			40	90	-90
Accelerated depreciation (full cost in year of purchase)		2001			40	98	-98
Additional deduction for start-up expenses of up to R20 000 & increase to R5m in turnover limit for small businesses		2003			10	21	-21
Three-year accelerated tax depreciation write-off period for all nonmanufacturing assets for small business		2005			485	982	-982
Small businesses exempt from tax on first R35 000 of income (subsequently increased)		2005			900	1 822	-1 822
Presumptive tax structure for very small businesses		2008			200	326	-326
RETIREMENT FUND TAX							
Initial tax of 17% on gross interest and net rental income		1996	2 725	9 092			9 092

TAX	YEAR	BASE INCREASE		BASE DECREASE		NET BASE Δ
		(FY prices) Rm	(2018 prices) Rm	(FY prices) Rm	(2018 prices) Rm	(2018 prices) Rm
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Tax reduced from 18% to 9% (1st step in abolition)	2006			2 400	4 645	-4 645
Abolition of the Retirement Fund Tax	2007			3 000	5 421	-5 421
TAX ON TRUSTS						
Tax rate of 40% set for trusts	2002	90	202			202
TRANSFER DUTIES						
Rules amended to prevent avoidance through 'nominee transactions'	2003	300	637			637
LEVIES AND USER CHARGES						
Environmental levy introduced	2009	2 780	4 225			4 225
Environmental fiscal reform: Vehicle CO2 emissions tax	2010	450	656			656
Health promotion levy (sugary beverages)	2018	1 930	1 930			1 930
TAX AMNESTY						
Tax on repatriated capital	2006	400	774			774
TAX INCENTIVES						
Diesel fuel concession for primary production sector	2001			417	1 022	-1 022
Learnership incentives	2002			80	180	-180
Energy-efficiency savings tax incentive	2015			50	56	-56
Accelerated depreciation for strategic investments	2002			295	663	-663

TAX	YEAR	BASE INCREASE		BASE DECREASE		NET BASE Δ
		(FY prices) Rm	(2018 prices) Rm	(FY prices) Rm	(2018 prices) Rm	(2018 prices) Rm
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Accelerated depreciation allowances for urban development zones	2003-2006			1 300	2 759	-2 759
R5 billion in tax subsidies over the next three years to support the emerging industrial policy	2008-2012			5 000	8 139	-8 139
Youth employment subsidy	2011-2013			5 000	6 940	-6 940
TAX RELATED TO FINANCIAL TRANSACTIONS						
Removal of securities taxes on certain warrant transactions	2002			80	180	-180
Financial transaction tax relief for the new issue of company shares	2005			350	708	-708
Stamp duties on insurance policies and fixed deposits abolished	2003			200	424	-424
Stamp duties on banking debit entries are abolished	2005			350	708	-708
Stamp duties on short-term leases (< 5 years) abolished	2007			90	163	-163
TAX PERTAINING TO PUBLIC BENEFIT ORGANISATIONS						
List extended	2003			60	127	-127
VALUE-ADDED TAX						
Zero-rating of paraffin	2001			400	982	-982
Zero rating of municipal property rates	2006			1 000	1 935	-1 935

TAX	YEAR	BASE INCREASE		BASE DECREASE		NET BASE ∆
		(FY prices) Rm	(2018 prices) Rm	(FY prices) Rm	(2018 prices) Rm	(2018 prices) Rm
(1)	(2)	(3)	(4)	(5)	(6)	(7)
EXCISE AND OTHER DUTIES						
Removal of ad valorem duties on computers	2003			572	1 214	-1 214
Ad valorem excise duties on printers, recorded music and some cosmetic products abolished	2004			270	565	-565
Ad valorem excise duties on sun protection products and on professional digital cameras are abolished	2005			10	20	-20
Excise duties on listed products abolished	2006			22	43	-43
Ad valorem excise duties on listed products abolished	2007			85	154	-154
Property transfer duty thresholds are increased	2011			450	625	-625
TOTAL	**1994-2018**	**-**	**52 641**	**-**	**50 935**	**1 707**
Source: Department of Finance (various years); National Treasury (various years).						

The concept of properties of a good tax conveys the idea that governments have – or should have! – a vested interest in a tax system that generates income such that allocative and administrative efficiency and fairness (equity) are served. After 1994, the focus initially was on "… improving the tax administrative capacity of the South African Revenue Services (to enhance tax compliance and thus revenue collections), in order to ensure essential base-line support for future reforms. Subsequent tax reforms, such as simplifying the tax system, broadening the tax base and reducing tax rates, have supported other policy initiatives of government ensuring a stable, neutral, efficient

and equitable tax regime" (National Treasury, 2007: 2). These tax imperatives remain in the forefront of the fiscal mind, as the following statement demonstrates (National Treasury, 2004: 93): "The low effective tax rates in specific sectors of the economy have continued to act as a catalyst for discussions between SARS and these sectors to understand the causes of the low rates and to collaborate in addressing them. As an example, the banking sector has agreed to look into its effective tax rate following discussions with SARS. Discussions with this and other sectors have yielded fruitful results but much remains to be done."

There are ambiguous trends as well. Some tax measures may amount to an increase in the real tax burden by stealth, such as when bracket creep is not fully eliminated with respect to personal income tax – as discussed earlier. Furthermore, it is necessary to distinguish between static and dynamic effects. The introduction of the graduated corporate income tax schedule to incentivise small and medium sized enterprises in 2000 (National Treasury, 2000: 86-87), for example, could in the static sense of the word be viewed as an erosion of the corporate tax base. The possibility that this could unintentionally incentivise organisational restructuring is a case in point. Dynamically speaking, this very step may be a credible way of facilitating the movement from the informal into the formal sector of the economy and thus expanding the tax base over time.

Taxation and tax expenditures (i.e. subsidies) aimed at addressing negative and positive externalities (i.e. Pigouvian measures) also entail some ambiguity. The essence of a Pigouvian tax is that it is supposed to reduce consumption of the particular good or service to a societal optimal level. In this sense such a tax may well initially generate revenue (base broadening), but with the actual longer-term aim of curbing consumption and thus reducing the associated revenue (base reduction). When the particular tax becomes a lucrative money spinner for the fiscal authorities such as is the case with so-called sin taxes or could happen with the recently introduced health levy on sugary beverages, the fiscal authorities are in danger of developing a vested interest in maximising its revenue yield. It then becomes virtually impossible to distinguish between a Pigouvian tax to internalise the negative externality and a tax measure (with an undisclosed motive) of revenue enhancement. In the latter case the measure then embodies elements of tax base broadening as well. Such alleged Pigouvian taxes and tax subsidies have therefore been listed as well so as to register that they have (or could have) a meaningful base-broadening impact on revenue yield.

Another complicating factor from a classification point of view is when a particular tax has explicit equity features, such as the tax treatment of medical scheme contributions, where the aim is to relieve the burden on the poor and simultaneously cap the allowance at a certain income level. A

case in point is the replacement of the deductibility of medical scheme contributions in terms of the progressive tax system, with a lump-sum tax credit. The former amounted to a progressive tax benefit; the latter, i.e. its substitute, amounts to a regressive tax benefit. The replacement step is on the one hand an increased benefit for lower-income groups and thus a reduction of the tax base; on the other hand, the cap is a protection of the tax base with regard to higher income groups. This ambiguity results in having to classify such a measure – and similar others – as both a base-eroding and a base-broadening step.

One also gets the impression that over the years, many of the obvious methods to improve compliance, i.e. those with relatively big revenue benefits, were addressed. The following statement by National Treasury (2004: 74) resonates with this observation: “As the tax system approaches an appropriate structure, reflecting enhanced efficiency and fairness, the net incremental benefits from further improvements become more modest.” The type of changes in recent years tends to be more sectoral or micro in nature, whereby a particular tax type is refined more accurately so as to avoid unintended consequences.

Occasionally notice is given of matters under investigation, such as when issues with obvious tax compliance implications are reported (National Treasury, 2012: 59). The following topics for research were mentioned in this case: taxation of financial instruments (including derivatives); taxation of long-term insurance companies (review of the taxation, accounting and regulatory practices of the four-fund system); and taxation of income from capital (interest income, dividends, capital gains, rental) to be reviewed to ensure greater equity and minimise opportunities for tax arbitrage. This paper (and the background classification of measures) steer away from announcements of intent and only record measures as and when they were actually implemented.

In various cases the tax change was announced without an estimate of the revenue implication – hence the category of nonquantified measures (Tables 2 and 3). Nonquantification may reflect various things, such as: mere ignorance; the conviction that it is the right thing to do, e.g. switching from a source to a residence tax base; and that an estimate of the increase in the number of small businesses that register will probably at best be a wild and useless guess.

Another category of change that occurs from time to time, is the ironing out of inconsistencies, often unintended, that are discovered retrospectively and that enabled avoidance, with horizontal inequity (uneven playing fields) and compliance discrepancies as a result. A case in point is the reintroduction of an excise duty on computer monitors (National Treasury, 2011: 71), when it was

discovered that they were used as televisions, thus putting the users tax-wise in a better position than the owners of televisions (which were subject to excise duties).

Institutional arrangements

One of the biggest challenges of the post-apartheid government in South Africa was to inculcate that democratic constitutional rights imply (or go hand-in-hand with) responsibilities of tax compliance. Before the constitutional change of 1994 there were a number of factors that threatened tax compliance. Amongst these were the following: in the business community exchange controls were circumvented, implying an escape from tax liabilities; the sentiment that gave rise to the anti-apartheid slogan "no taxation without representation" eroded the personal and small business income tax bases or hampered their development; and the country's integration into international trade and financial markets opened its economic borders for tax leakage. Resurgence of compliance problems occurred in recent times when poor delivery of public services incentivised tax disobedience and, more specifically, resulted in nonpayment of rates and taxes at local government level. Lately various political leaders were suspected of dodging tax liabilities in different ways.

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

This reform gave SARS the ability to attract very competent tax experts[8] and to greatly improve communication with and education of the entire tax community. SARS was destined to operate from more than 45 service centres to educate South Africans about their tax obligations in order to improve compliance (National Treasury, 2001: 66), thereby strengthening norms and behaviour of tax responsibility in the democratic state. SARS remained aware of the importance of tax compliance education (see, for example, National Treasury, 2004: 92).[9]

The educational programme was accompanied by various organisational and process changes to reduce compliance cost, such as e-filing, the collection system known as SITE (Standard Income

[8] The establishment of a high profile tax office in Sandton to better service the corporate sector is a case in point.

[9] It is stated that SARS will build on its successful 2003 filing season by launching an intensive taxpayer education campaign in 2004.

Tax on Employees)[10] and programmes to promote tax compliance of small business and newly enfranchised citizens (see, for example, National Treasury, 2006: 82; 2008: 56, 63). The latter included simplifying the tax forms and reducing the number of returns that must be filed (National Treasury, 2002: 85). Various measures were put in place to improve compliance (Department of Finance, 2000: 71), such as: strengthening the anti-avoidance provisions of the Income Tax Act; requiring 'declarations of good standing' before taxpayers can obtain government contracts or permission to invest outside the country; publishing the names of tax offenders; launching a multi-pronged programme to reduce value-added tax and customs fraud, including reducing the number of international border posts; and introducing a fraud hotline.

The fiscal authorities faced the challenge of ensuring that the Income Tax Act conformed to the Interim and Final Constitutions (National Treasury, 2007: 10). To this effect education and tax reform measures went hand in hand with enforcement measures. Gradually, SARS's tone also became more assertive.[11] Intrinsic to all of this is taxpayer integrity, on which the Government relies for improved compliance results (National Treasury, 2006: 82) – a clear recognition of the importance of informal institutions (i.e. norms of behaviour) in the new institutional economics sense of the word (North, 1991). In this respect Ali, Fjeldstad & Sjursen (2014) show that in South Africa (as well as in Kenya, Tanzania and Uganda) tax compliance is likely to increase as citizens become more satisfied with the quality of the public goods being provided.[12]

In the summary tabulation of the base-broadening and -erosion measures and the accompanying consideration (Tables 2-4), the following factors by inference may be identified as having impacted adversely on the tax base, which was why rectifying measures of base protection or base broadening were taken:

- tax rules (laws and regulations) enabling avoidance or evasion;
- inefficient administration (including compliance procedures and practices);
- tax measures to internalise presumed positive externalities, often presented as tax incentives to support economic growth initiatives and job creation;

[10] Subsequently terminated when its usefulness was overtaken by the functionality of e-filing.

[11] This is evident from the following (National Treasury, 2002: 69: "SARS … has introduced a new assertiveness in its approach to compliance with the tax and customs laws." Various administrative steps were listed (National Treasury, 2002: 69-70).

[12] Their study showed that respondents are more likely to have an attitude of tax compliance if the government improves the provision of certain public services, such as policing.

- poor or incomplete registration of taxpayers in hard-to-tax groups (notably the informal sector, small and medium-sized businesses and the financial sector);
- tax evasion tendencies, some of which related to poor service delivery;
- equity and ability-to-pay considerations; and
- in general, a preference for government intervention that was sometimes based on contestable arguments.

Unfortunately in recent times much of the good work were undermined. In National Treasury's (2018: 2) own words, "The extent of corruption and wasteful expenditure in the public sector, together with governance and efficiency challenges in tax administration, have affected tax morality." This impacted adversely on tax revenue.

Tax reforms

The major base-broadening tax reforms constituted the introduction of a graduated tax for small business, the subjection of financial services to value-added tax (VAT), the shift from a source- to a residence-based tax dispensation, the introduction of a capital gains tax (recognised for its role to reduce corporate income tax leakages), reduction in import duties in terms of the membership of the World Trade Organisation (WTO), and using excise tax to build an element of progressiveness into the tax system. The latter of course constitutes a mix of two conflicting considerations: revenue-enhancing base-broadening and internalisation of negative externalities of which the effective and correct implementation may well entail less revenue. The introduction of a graduated corporate tax structure, as stated earlier, may in the long run turn out to be base broadening as well.

A worrisome feature has been the persistence and increased number of base-eroding tax incentives, especially without any or without convincing *ex ante* or *ex post* evidence of their cost-benefit advantages. The huge tax benefit afforded to the development of the motor industry and, more recently, selective tax incentives supportive of certain industrial sectors or subsectors (including urban and industrial development zones) are cases in point. The tendency to fall back on tax incentives goes against the view expressed by the Katz Commission (see National Treasury, 2007: 12): "In recent years, Government has focussed its efforts to minimise on the use of selective tax incentives, thereby providing scope for reducing the statutory tax rates that are applied to a broad tax base. It is advanced that this is the most appropriate means to promote economic development, rather than relying on selective incentives that erode the tax base, distort investment decisions and complicate the tax legislation and administration." In 2015/16 tax expenditure in South Africa

amounted to 14.9 percent of total tax revenue and 3.9 percent of GDP (National Treasury, 2018: 124). Earlier Calitz, Wallace & Burrows' South African analysis (2013: 21) confirmed the intuitive view that a replacement of tax incentives for private investment with a reduction of the corporate tax of equal money value, generates a substantially higher benefit-cost ratio, as measured by the ratio of tax to national output.

5. CONCLUSION

This study explored tax base changes in South Africa as reported in the annual Budget Review from 1994 to 2018 with a view to answering the question whether the South African fiscal authorities are serious about tax base broadening. This was done against the backdrop of literature on base broadening. As in all countries, South Africa took many steps since 1994 to broaden the tax base. Many measurers were also implemented that amounted to a narrowing (erosion) of the base and the latter tendency seems to have been increasing as evidenced by the rising number of tax incentives. A selection of the quantified and most salient nonquantified measures of base broadening and base erosion, respectively, were tabled. The evidence suggests that the estimated revenue yields of base-broadening tax measures, as reported in annual budget documentation and as expressed in 2018 prices, add up to about R1.7 billion (budgeted figures) more than the total revenue losses associated with the base-eroding measures. On balance this testifies to some fiscal seriousness with base broadening which appears to have been close to a revenue-neutral tax reform process. Over the period 1994-2018 the process was in fact accompanied by reductions in the top marginal personal income tax rate from 45% (in 1996[13]) to the most recent low of 40% (as was in force in 2014), before rising again to 45% in 2017; and a reduction in the corporate income tax rate from 40% to 28% (National Treasury, 2014: 46; 2018: 45). The apparent revenue-neutrality should nonetheless be interpreted with caution, given that many other tax changes occurred over the same period, such as the substantial increase in fuel and various excise levies and the introduction of a withholding dividend tax.

In order to further investigate the seriousness question raised at the beginning, there clearly are opportunities for further research. One aspect would be to establish the actual revenue outturn of quantifiable base-changing measures, not only in the budget year but also in subsequent years and to expand the estimate to (hitherto) unquantified measures. Unless the fiscal authorities keep track

[13] The 1996-rate was chosen for comparison purposes so as to move beyond the period during which the transition levy was in force.

of the actual revenue trend of each of these measures and make the data available, such research is unlikely to be possible. The other is to explore macro-econometrically the impact of economic growth and demographic factors on the tax base.

Finally, there clearly is a case for a much more systematic quantification of all base-broadening and base-erosion tax measures, not only at the time of announcement but especially to track and report the outcome of all such measures in subsequent years.

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