



**Submission on Draft Rates and
Monetary Amounts and
Amendment of Revenue Laws Bill
2018**

20 April 2018

Qualitative observations and recommendations

- OUTA is a proudly non-profit civil action organisation which aims for efficient, rational, innovative and ethical collection, distribution and expenditure of fiscal revenue in government. OUTA strongly recommends that National Treasury and the South African Revenue Service prepares for zero tax increases for the next fiscal year – this should force government to reduce superfluous expenditure.
- There are conflicting perspectives regarding the virtue of the proposed tax policy amendments as contained in the Bill noted above: priorities of poverty alleviation, job creation and macroeconomic growth are mistakenly dichotomized in the public eye. OUTA recognizes the difficulty faced by government in balancing these developmental imperatives and finding trade-offs that satisfies the multiplicity of interested and affected parties.
- Fiscal measures aimed at containing sovereign debt and the persistent deficit are perceived to be implemented at the expense of fundamental transformation goals – how can we address this?
- Econometric research being orchestrated by National Treasury on the impacts of increased VAT during 2018 should have been conducted before the proposed budget was put forward. Now, NT indicates that it will facilitate public hearings on the outcome of such a study after the increase has been implemented.
- Initiatives aimed at increased involvement of civil society and the public in financial decision making of the South African economy must be reinforced with real commitment from National treasury – as opposed to superficial dedication to increased transparency. OUTA urges the Standing Committee on Finance to support, reinforce and facilitate the deepening of public participation in the Ministry of Finance and National Treasury itself.
- A predicted deficit of 3.6% remains despite a predicted increase in tax revenue. An increase in expenditure of 7.5% is proposed. Generally, public administration has not improved despite additional allocations in the past. This perpetuates a flawed precedent. R16bn increase in expenditure on executive and legislative organs is similarly problematic given government's commitment to addressing the excess of executive ministries and associated human resources. OUTA urges SCOFs and National Treasury to demonstrate to the public how exactly each department

- In general, lack of capacity is NOT necessarily a result of underfunding, but can often be ascribed to human error and structural inadequacy. Government mustn't preserve its relevance at the expense of citizens.
- It is fundamentally important to recognize that bureaucratic efficiency and administrative capacity is a prerequisite to improved utilization of tax revenue. Taxation should not increase *ad infinitum* – and if the requisite enhancement of public sector performance and public-private partnerships is realised, consistent increases in rates and monetary amounts will not be necessary.

National Treasury urged the public to view the proposed amendments to tax revenue holistically, rather than deconstructing single elements of it in a fragmented manner. This submission observes individual amendments contained in the Bill – and proceeds to scrutinize and make recommendations that speak to these collectively.

1. Proposed amendment of First Schedule to Act 45 of 1955, as substituted: Estate Duty Tax

OUTA understands the need to consider Estate duty rate increases from 20% to 25% on dutiable amount of estates of more than R30 million, since this is not regressive. This fiscal consolidation mechanism can reduce the deficit without exacerbating poverty, but can incentivize capital flight from South Africa if not carefully considered and researched. Therefore, extensive feasibility studies need to be conducted before moving forward.

The feasibility of this also is dependent on bureaucratic efficiency and administrative capacity of the Master's office, the Tax Ombud and SARS – which is lacking. The lack of an effective government response to serious, far reaching allegations of corruption, maladministration and poor governance has undermined the social contract between taxpayers, independent financial service providers and these institutions.

Considering this, concrete measures must be put in place to monitor compliance and ensure that Estate Duty Tax is not avoided as it has been in the past. This can significantly contribute to reducing the deficit and eliminate future need for increased indirect taxation that increases the cost of living – as well as the need for direct taxation which may negatively impact employment rates and production efficiency/economic growth.

In alignment with the suggestion taken up by the Davis Tax Committee, OUTA believes that a serious consideration of a robust wealth tax would be more effective in contributing to the fiscus whilst addressing injustices of the past. Due to the existing administrative underperformance of institutions mentioned above – a simpler mechanism that directly taxes super wealthy individuals might be more effective than expanded Estate Duty Tax. See section 4 for an additional motivation for consideration of a wealth tax in terms of how this can eliminate the need for regular increases in direct taxation – which reduces buying power, employment creation, business development and economic productivity.

2. Proposed amendment of Schedule 2 to Act 89 of 1991, as amended: Value Added Tax

OUTA does not support an increase in Value Added Tax as it stands because the deficit has been caused by maladministration, irregular, fruitless and wasteful expenditure, corruption and state capture. Moreover, VAT exacerbates the plight of the poor in its current form. Nonetheless, a discussion around this tax mechanism may be fruitful. According to the Organisation for Economic Cooperation and Development (“OECD”):

“Overall the performance of VAT systems depends on three main factors:

- *the degree of compliance by taxpayers;*
- *the structural features of the tax: rates, exemptions, thresholds, and*
- *the capacity of the tax administration to manage the system in an efficient way.”*

National Treasury contends that the additional revenue sourced from the fiscus through the increase in Value Added Tax will largely be contributed by higher earning individuals and intensive consumers. Many stakeholders have countered this view indicating that increased VAT is a fundamentally regressive tax mechanism – and that the range of zero rated basic food stuffs should be expanded to cushion the poor from the impacts of this amendment. OUTA recommends that the public be better informed of how exactly the additional tax revenue incurred by increased VAT will benefit poor and underprivileged communities, households and individuals; c.f. Imali Yethu.

National Treasury has responded to public consultation – indicating that thorough consideration of the potential impacts of this proposal will be undertaken during 2018. One can argue that this is too little, too late. The Davis Tax Committee states that, at best, it may be appropriate to consider only retaining those items that more clearly benefit the poor households, such as maize meal, brown bread, rice and vegetables, while withdrawing those items more clearly consumed by the more affluent households, such as fruit and milk. This is because additional taxation of food items that are predominantly consumed by affluent households might be a progressive avenue for increased tax revenue. OUTA contends that multiple rates for certain goods and services further increases the administrative complexity of taxation; which exacerbates existing administrative problems.

Consider the relative commercial impact of VAT generally. To provide ideological context, South Africa's economy has evolved into a neoliberal form in which commercial entities consistently shift the burden of taxation onto final consumers. Considering this, the Davis Tax Committee found that VAT does not decrease "production efficiency" and employment – where direct taxation such as Corporate Income Tax (CIT) and increased Personal Income Tax (PIT) might negatively impact these parameters. Nevertheless, it is important to note that this is simply because commercial entities deflect such additional expenses through downscaling, capital flight and retrenchments etc. – preserving marginal profitability. Businesses also offload the burden of VAT onto final consumers. What would radical economic transformation look like – and how would it depart from these traditional principles without crippling the economy's international competitiveness? Prospects of profitability are essential to incentivize sustainable foreign direct investment and successful entrepreneurial initiatives in the global economic system.

OUTA recommends that the legislature, and particularly the Standing Committee on Finance – in collaboration with National Treasury – provides a platform in which tax policy can be fundamentally reconsidered and discussed over several months or years. This aligns with the intention of impending Parliamentary proceedings on the Report of the High-Level Panel on the Assessment of Key Legislation and the Acceleration of Fundamental Change. National Treasury has consistently responded to criticism of the increase in VAT with demands for proposed alternatives – but the scope of these public hearings does not really allow for radically unorthodox recommendations.

With regards to VAT, OUTA understands that this is a relatively neutral and fair tax mechanism in theory, but as it stands, it does have a negative impact on poor and working classes and is not justified in the context of persistent corruption, maladministration and financial mismanagement. This is asserted in good faith considering the recent media statement by National Treasury indicating that the Minister of Finance has requested the chair of the Davis Tax Committee, Judge Dennis Davis, to appoint a panel of independent experts to review the current list of zero-rated items, and consider the most effective way to mitigate the impact of the increase in the VAT rate on poor and low-income households. OUTA supports this and intends to participate extensively in the process, as well as subsequent Parliamentary hearings to represent the public interest and civil society.

Poverty and inequality should be eradicated by aggressively facilitating employment, industrialization and sustainable economic growth through circumspect, effective and

progressive use & collection of tax revenue – as opposed to poverty and inequality being accommodated through fiscal policy as if these problems were permanent, inevitable features of South African society. Unemployment is the root cause of persistent poverty and inequality – symptomatic relief and political jousting will not cure this disease. Indirect taxation that does not worsen the plight of the poor can be an effective means of incurring needed tax revenue without undermining productivity, job creation and economic growth – but this is not yet the case.

Finally, the dichotomization between increased indirect taxation and progressivity must be deconstructed. Again, OUTA strongly recommends that the Standing Committee on Finance and National Treasury commit to the revision of tax policy in our country in a manner that is objective, apolitical and purely intent on benefitting current and future generations of ordinary South Africans.

3. **Proposed amendment of Schedule 1 to Act 91 of 1964, as amended: Customs and Excise Duties**

OUTA holds that the increase in customs and excise duties is an overly simplistic amendment that does not adequately address the budget deficit or alleviate socioeconomic problems. Better avenues exist, as discussed above. Nonetheless, it is essentially a luxury tax and can be avoided by preferential consumer behaviour – which may contribute to public health. The classification of customs and excise duties must however be discussed, because items such as books and computers that contribute to education may become unaffordable with excessive tax increases, therefore excluding parts of the South African population from affordable quality education.

4. Proposed amendment of section 6 of Act 58 of 1962, as amended: Personal Income Tax

The South African fiscus is highly dependent on Personal Income Tax revenue – especially from individuals in the highest income brackets. Previously, during the Budget 2018 public hearings, OUTA asserted that this reliance is not sustainable.

The Standing Committee on Finance responded by indicating that proportional taxation of higher income individuals is necessary to address the legacy of apartheid. OUTA agrees with this in principle, but contends that better alternatives exist which can achieve this goal without reducing the amount of disposable income circulating in the economy. The primary contributor to a reduced deficit should be increased efficiency of public sector expenditure. Direct taxation of middle and upper-class individuals can no longer be understood to apply exclusively to a certain demographic profile of taxpayers. In our view, the goal of inclusive economic growth is ultimately to increase the number of taxpayers in all income brackets by means of sustainable and equitable job creation – which will further empower government to alleviate poverty and increase the average standard of living in South Africa by means of targeted public expenditure.

This, we argue, would be better than consistently forcing already overburdened taxpayers to pay more Personal Income Tax to finance the state while unemployment and corruption reigns. It is essential to recognize the imperative of allowing our economy to gradually become somewhat independent of governmental intervention. Excessive political control of economic dynamics can catalyse corruption, maladministration, nepotism and even state capture. Poverty, inequality and unemployment are fundamental problems that must be addressed – but what is the best way to do this? South East Asian nations accomplished great successes in overcoming such societal ills 30 years ago by means of aggressive investment in industrialization and socio-technical regime change which dramatically increased employment rates. This, in turn, increased tax revenue without significant annual increases in Personal Income Tax rates *per se*.

Going forward, OUTA urges National Treasury not to consider any additional increases in Personal Income Tax rates since this has been increased consistently in the past decade despite deteriorating public service delivery and increased maladministration, corruption and wasteful-, irregular- and fruitless expenditure.