The South African Tax System: Fit for Purpose?

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Abstract

Is the South African tax system 'fit for purpose'? This article addresses this and related questions by considering the fiscal outlook in South Africa in comparison to OECD, BRIICS and other developing countries. Trends are analysed from the perspectives of tax revenue, tax mix and tax administration. The approach adopted in this paper is neither purely doctrinal nor empirical. Rather, it is analytical, practical and applied, effectively a 'conspectus' located within the broader comparative tax literature. The article suggests that South Africa has not recovered from the global financial crisis as readily as most developed countries, and that it also does not have much capacity to increase existing tax rates. Its current tax system is stretched to the point where further demands on existing tax bases could cause economic distortions and other systemic failures. Some sensible tax administrative reforms have already taken place, but more can be done to increase capacity in the current bout of tax reform. Such measures could include broadening and safeguarding the existing tax bases, improving tax compliance and tackling corruption. An efficient and effective tax system can provide sustainable sources of revenue, assist economic growth and increase employment and alleviate income inequality through its redistributive function. Although the system is not entirely 'fit for purpose' in its present form, the opportunities are there for South Africa to address its fiscal challenges.

INTRODUCTION

In 2014 South Africa celebrated 20 years since the end of apartheid, and reinforced its democratic credentials as a result of the fifth general election conducted under universal suffrage. But the nation stands at something of a crossroads so far as its fiscal outlook is concerned. On some macroeconomic fronts the country is doing very well. It continues to match, and sometimes outperform, comparable countries in many respects. And yet on other indicators there may be considerable scope for improvement (OECD, 2013c).

The purpose of this article is to evaluate South Africa's current fiscal performance, benchmarking it against those countries with whom it is often most readily compared – the five other so-called BRIICS countries[2] – as well as against the 34 apparently 'developed' countries of the Organisation for Economic Cooperation and Development (OECD), and also, on occasion, against other, non-BRIICS, developing nations.

The subtext of the article is to address a simple, but ambitious, question: to what extent is the South African tax system 'fit for purpose'? Of course that, in turn, begs a series of further questions. What is the purpose of the South African tax system? What criteria should be adopted for any such assessment of 'fitness'? How such criteria are objectively evaluated? Which countries have appropriately comparative tax regimes? What are the broader trends in tax system development?

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In the light of the analysis and global trends, how might South Africa seek to reform its tax system?

Some of these, and related, questions will be addressed in the article. The overarching motivation for the article is to identify the sorts of fiscal opportunities – particularly as they relate to policy and to administration – that will help to ensure a 'nation at the crossroads' chooses wisely in the direction it takes. The approach adopted in the article is neither purely doctrinal nor empirical. Rather it is analytical, practical and applied, effectively a 'conspectus' located within the broader comparative tax literature (Ault & Arnold, 2010; Sartori & Marian, 2011; Albi & Martinez-Vasquez, 2011; Sandford, 2000).

The analytical task is undertaken with some degree of caution. Comparative analysis can easily make the mistake of seeking to claim too much. Generalising about tax systems is always a hazardous and unreliable business (Sandford, 2000). A second word of caution relates to the lack of reliable and up to date statistics in some cases in the preparation of the article. Whilst detailed information is readily available (albeit with some time lag) in respect of the OECD countries, the sometimes lack of reliable and up to date information relating to BRIICS and to developing countries acts as a constraint in the development of the article.

So what is the purpose of the South African tax system? It is, obviously, no different from the purpose of most tax systems, whether in developed or in developing nations. In the first place it is clearly there to raise sufficient revenue to permit the government to discharge its many spending responsibilities, whether development, social welfare, education, defence, infrastructure building or whatever else. But tax systems are much more than simply revenue raising mechanisms. They also have a role to play in tackling income inequality, fostering economic growth and well-being and in building state legitimacy.

Indeed, tax systems are a fundamental component of any attempt to build nations. As Brautigam (2008, p.1) has noted, '(t)axes underwrite the capacity of states to carry out their goals; they form one of the central arenas for the conduct of state-society relations, and they shape the balance between accumulation and redistribution that gives states their social character'. In short, taxes build capacity (to provide security, meet basic needs or foster economic development) and they build legitimacy and consent (helping to create consensual, accountable and representative government) (McKerchar & Evans, 2009).

The article is structured as follows. The next section identifies key fiscal patterns and trends in OECD, BRIICS and other developing nations. After an initial discussion of the broad challenges facing developed and developing countries, it considers these trends from three key perspectives: tax revenue, tax mix (sometimes referred to as tax structure) and tax administration. Some preliminary analysis of how South Africa fits within these broad patterns and trends is made here, but the more detailed analysis of South African performance, challenges and opportunities takes place in the following section. Concluding comments are contained in the final section.

FISCAL TRENDS: THE BIG PICTURE

Developed and developing countries

Even a superficial analysis suggests there are marked differences in the tax systems of developed countries (such as those in the OECD) and developing countries. In developed economies the tax system is more likely to be reliant upon, and to focus upon, direct taxes, and particularly the personal income tax as a major source of revenue. In contrast, in developing countries there is more likely to be a greater reliance upon indirect taxes, and especially excise duties. To a significant extent these differences emanate from the very different sets of challenges faced by developed countries compared to those of developing nations (Norregaard & Khan, 2007).

There are a number of critical tax challenges facing developed countries. In the very broadest terms, those challenges relate to safeguarding the revenue bases to preserve and enhance the well-being of the nation's citizens. The threats to the tax base are both international (for example, the challenges of globalisation, debates about territoriality and the allocation of taxing rights between countries including transfer pricing issues, supra-national harmonisation of tax regimes, disputes about exchanges of information) and national (the ageing of populations, the deepening stress between human growth-fuelled activities and their impact upon wider eco-systems including damage to the environment etc, fiscal federalism issues as national and sub-national bodies each strive to get their slice of the national tax revenue to fund their expenditures). Some challenges have both international and national dimensions, such as the challenges of changing technology (for example, how do you tax e-commerce?).

Some of the tax challenges that are currently being faced by developed countries will obviously also be of concern to developing countries. But developing countries generally face significantly different priorities in confronting the challenges of taxation. As noted by the OECD (2012, p.23)

> "Taxation is key to promoting sustainable growth and poverty reduction. It provides developing countries with a stable and predictable fiscal environment to promote growth and to finance their social and physical infrastructural needs. Combined with economic growth, it reduces long term reliance on aid and ensures good governance by promoting the accountability of governments to their citizens."

For developing countries, therefore, the key challenges are likely to be those that relate to attracting overseas aid and investment to assist in the push for development and—more importantly—the need to build state capacity and legitimacy so that appropriate revenues can be raised from their own resources without having to rely too much on foreign aid and investment. These are very different from the issues that are faced by those charged with responsibility for the structure and design of tax systems in developed countries.

There are four major areas where developing countries differ from developed countries in terms of the issues they face (Norregaard & Khan, 2007; Heady, 2009):

1. Developing countries are (by definition) at lower levels of development with weaker institutions, higher dependency on agriculture, larger informal (shadow) economies and fewer tax handles (instruments that can be used by the state to control tax behaviour);
2. Many developing countries are highly dependent upon natural resources;
3. Inequality is much more of an issue for developing countries; and
4. Developing countries face a different set of global pressures and influences compared to richer countries: more aid-dependency; higher levels of debt; less political influence.

However this neat classification into developed and developing economies becomes much more blurred when it comes to a consideration of the six BRIICS nations, a bloc which straddles the divide between developed and developing and which does not comfortably fit within either. While OECD countries still dominate the global economy, their share of world trade is decreasing in favour of the BRIICS (OECD, 2008). The BRIICS countries are emerging national economies, uniquely positioned globally by their large, fast growing economies. Due to each country's geographical location, each has a significant influence on regional, as well as global, affairs. While they share the characteristics of low labour costs and youthful populations with other developing countries, what sets the BRIICS apart are their growing middle classes and improvements in communications and transport. Indeed, on many indicators they outperform many developed countries.

Armed with this background, the following analysis considers the major fiscal trends in developed, BRIICS and developing countries in relation to three components of their overall tax systems: tax revenue; tax mix; and tax administration. These components are key elements in the composition of any tax system, covering the core elements of tax policy and tax administration. In each case sufficient detail is established in order to provide a basis for the more detailed analysis in the following section.

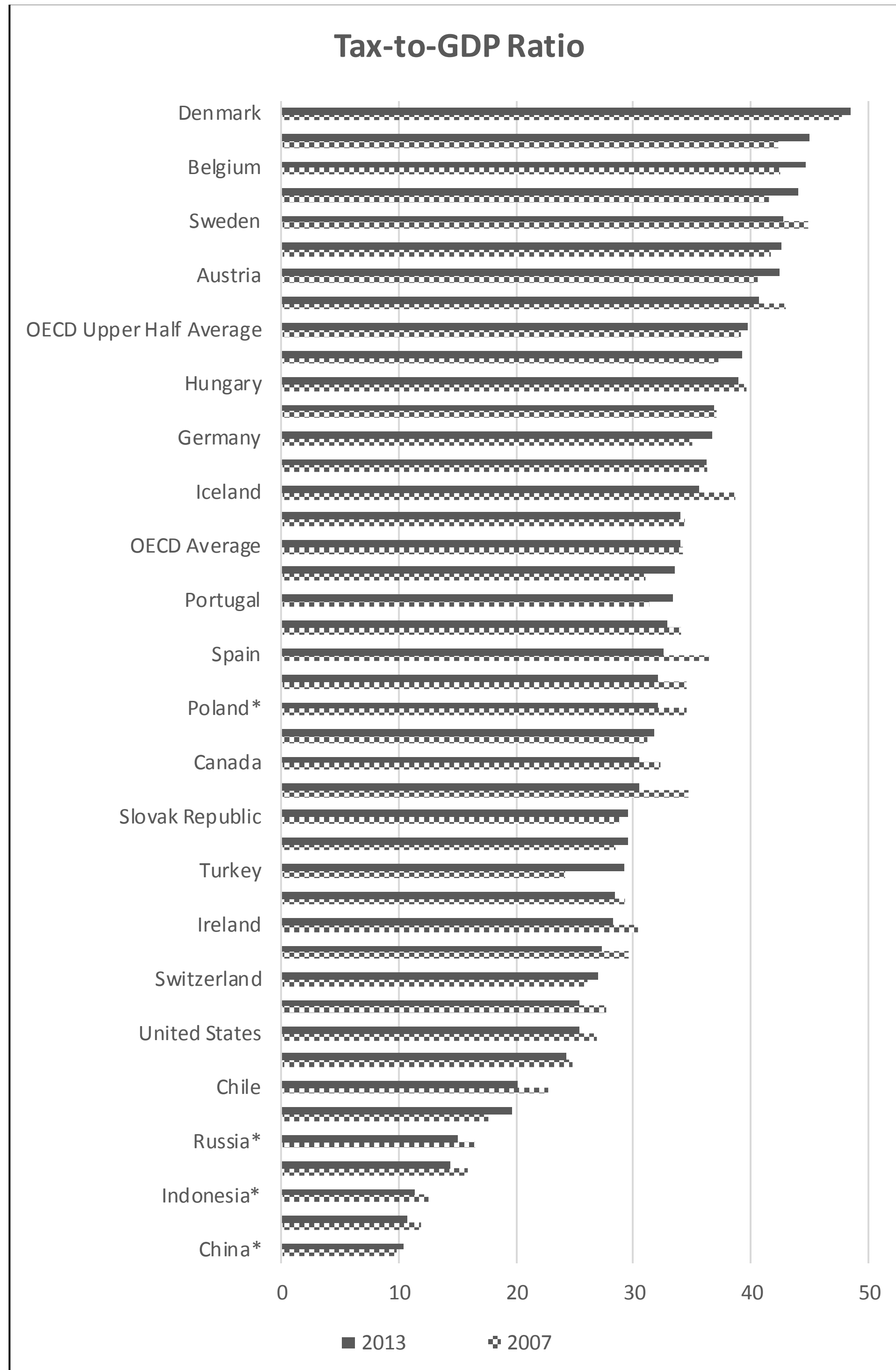
Tax revenue

The tax-to-GDP ratio is a measure of a country's tax burden. However, this 'burden' is also the source of funding for government services; the lower the ratio the more likely significant fiscal deficits will exist. The tax ratio, or tax revenue as a share or percentage of GDP, is a simple average. This assigns the same weighting to all countries, irrespective of their size or level of development. Tax ratios vary by income levels, on average rising as per capita income rises (Bird & Zolt, 2008; Bird & Zolt, 2003).

Tax ratios allow for country and regional comparisons to be made, and the tax ratios for OECD and BRIICS countries for selected recent years are summarised in Figure 1. In OECD countries, tax revenues, as a percentage of GDP, are recovering from the financial and economic crisis of 2008 and 2009. The average

ratio in OECD countries was 34.1 per cent in2013, nearly back to the average of 35 per cent in 2007 after falling in the intervening period (OECD, 2014). However, the tax burdens between OECD countries are disparate, ranging in 2013 from 19.7 per cent in Mexico to 48.6 per cent in Denmark.

Figure 1: Tax ratio of OECD and BRIICS countries 2007 and 2013



* Data for 2012
Source: OECD Revenue Statistics 1965-2013 for OECD countries; The World Bank Database for BRIICS countries

South Africa's tax ratio in 2012 was 25.5 per cent, down from 27.6 per cent in 2007 (World Bank, n.d.). Marginally below the OECD lower half average of 29.3 per cent in 2007, South Africa's tax ratio was nevertheless higher than seven OECD countries. By 2012 it was considerably lower than the OECD lower half average (28.4 per cent) and only exceeded four OECD countries. This indicates that it has not recovered from the financial and economic crisis as readily as most developed countries. The impact of the global financial crisis is also more evident and pronounced in the BRIICS countries, with only China having a higher tax ratio in 2012 than in 2007.

However, using the share of taxes in GDP as a measure of comparing the tax burdens of different countries is only meaningful when those countries have similar economic structures and levels of income. Factors such as macroeconomic, demographic and institutional constraints also affect how efficiently taxes can be collected. It is these factors that determine a country's predicted value of tax collection, or tax capacity (Moreno-Dodson & Bayraktar, 2012; Kesner-Skreb, 2014).

Thus, another method of measuring the taxation performance of countries is to consider 'tax effort'. Tax effort is an index measure of how well a country is doing in terms of tax collection, relative to what could be reasonably expected given its economic potential. The concept, which has been developed by economists at institutions such as the International Monetary Fund and the World Bank, relates the actual tax revenues of a country (as measured by the share of taxes in GDP) to its tax capacity (Chelliah, Baas & Kelly, 1975; Le, Moreno-Dodson & Bayraktar, 2012). It undertakes a sophisticated empirical estimation process using a regression methodology based upon the impact of such variables as macroeconomic factors (the income level of a country, its GDP, trade openness, agricultural contribution) demographic factors (the growth rates of the population and its age dependency) and institutional governance quality (based upon bureaucracy and corruption indices). When the tax effort index exceeds one, that country is considered to have a 'high tax effort'. This means that the country fully utilises its tax base to increase tax revenues, indicating there is little scope or potential to raise further tax revenues (Le et al, 2012).

Tax effort studies and methodologies have not been immune to criticism, and caution must be exercised in interpreting tax effort indices (Hope, 1996). For example, in an insightful analysis, Bird (1976) has identified a number of criticisms of tax effort studies, including a lack of justification for the variables used in the regression analyses and the use of poor data. Despite these criticisms, however, the general tendency has been to use these studies as the background for policy decisions" (Hope, 1996, p.35). The use of tax effort and actual tax collection benchmarks allows the classification of countries into four different groups and can provide insights as to how reform in such countries might take place by reference to tax capacity and tax revenues collected. The four possible rankings or classes, based upon the work of Le et al (2012, p.7), are:

Low tax collection and low tax effort

In this group of countries, the collection of taxes is currently low and lies below their taxable capacity. The group principally comprises low income (developing) countries (and particularly Asian countries), and also three of the six BRIICS countries (China, India and Indonesia). It also includes (somewhat surprisingly) Canada, Japan, Korea and the United States (US). The direction of reform in countries in this group, it is suggested, should be in 'deepening comprehensive tax policy and administration reforms focusing on revenue enhancement' (Le et al, 2012, p.24).

Low tax collection and high tax effort

Countries in this group tend to be low and middle income countries (for example Ghana, Kenya, Pakistan and Zambia), typified by low levels of taxation despite high tax rates on a few over-exploited revenue sources. Rampant evasion, skewed and narrow bases (as a result of widespread preferential treatment to various economic sectors) and inefficient tax administration prevent the revenues collected being commensurate with the tax effort involved. It is suggested that short term tax reform measures should include the streamlining of tax policy and tax administration procedures to reduce compliance costs, encourage formality and lower tax barriers to firms' entry and operations, while medium to long term reforms may expand the scope for raising revenue by broadening the effective tax base and enhancing the functioning of the tax system.

High tax collection and low tax effort

Countries in this group tend to be middle (for example Bulgaria, Estonia, Latvia, Turkey, Ukraine) and high (for example, Denmark, Germany, Ireland, Spain, Sweden and Switzerland) income countries, almost exclusively European and with a predominance of transitional countries from the former soviet bloc. Whilst these countries collect high taxes relative to the world average, their macroeconomic and demographic features lead to a low tax effort. Reform focus in these countries, it is suggested, should be upon implementing changes to reduce distortions and reach a higher level of efficiency in tax collection. This may involve restructuring the tax mix and improving the quality of governance.

High tax collection and high tax effort

Being in this category means that the country fully utilises its tax base to increase tax revenues, indicating there is little scope or potential to raise further tax revenues. This group comprises, primarily, middle and high income countries, including Australia, the United Kingdom (UK), New Zealand and South Africa. Le at al. (2012, p.26) note that, given the already high revenue collections which are above taxable capacity, further increases in tax revenue collection may lead to unintended economic distortions. Their suggestion is therefore that tax reform should not focus on revenue, but should rather aim at raising the efficiency of tax collection, including reducing tax-induced distortions and improving the business climate through further rationalizing the tax regimes, rebalancing the tax mix and simplifying administration procedures. Any further improvements in the quality of

governance (lower corruption or higher bureaucratic quality) can increase the efficiency of the tax system of this group of countries.

Figure 2 shows the classification of OECD, BRIICS and various developing countries into these four categories on the basis of revenue collections and tax effort for the period 1994 to 2009. Three BRIICS countries (China, India and Indonesia) are considered to be low tax collection, low tax effort while Russia is classified as high tax collection, low tax effort. South Africa, Brazil and many OECD countries are in the high tax collection and high tax effort category.

Figure 2: Classification of selected countries based on tax collection and tax effort, 1994-2009

Classified 1994-2009		Tax Effort	
		Low	High
Tax Collection	Low	37 countries including China, Ethiopia, India, Indonesia, Japan, Mexico, Thailand and the United States.	12 countries including Cote 'd'Ivoire, Ghana, Kenya, Mali, Pakistan, Sri Lanka, Togo and Zambia
	High	20 countries including Bulgaria, Estonia, Germany, Latvia, Russia, Spain, Switzerland, and Turkey	34 countries including Australia, Botswana, Brazil, France, Netherlands, New Zealand, South Africa and the United Kingdom

Source: Adapted from Le et al, 'Tax Capacity and Tax Effort: Extended Cross-Country Analysis from 1994 to 2009' p. 25.

The implications for South Africa's inclusion in the high tax collection and high tax effort category are considered in more detail in the section below.

Tax mix

As noted by Heady (2009), one of the major choices facing governments in the design of the tax system is what reliance to place on the different potential sources of tax revenue Some countries rely primarily on consumption taxes; others on income and capital taxes; in some countries social security contributions are the main source of revenues. Nevertheless, as can be seen from Table 1 below, in OECD countries the vast bulk of tax revenue comes from just three main sources: income tax, taxes on goods and services and social security contributions.

Table 1 suggests that the tax mix has been remarkably stable in the OECD over the period. South Africa's tax mix, on the other hand, has tended to fluctuate more. On average, OECD countries collect about 33 per cent of their tax revenues from personal and corporate taxes on income and profits. However, the averages conceal very significant differences. For example, in 2012 the share of the personal income tax ranged from a low of 9 per cent in the Slovak Republic and 11 per cent in the Czech Republic, through to highs of 39 per cent in Australia and 51 per cent in Denmark. For the corporate income tax the range in 2012 is from 3 per cent in Hungary, Greece and Slovenia, through to 19 per cent in Australia and 25 per cent in Norway (OECD, 2014, pp28-30).

Table 1: Tax Mix in South Africa and the OECD (percentages)

	2005		2010		2012	
	South Africa	OECD Average	South Africa	OECD Average	South Africa	OECD Average
Personal income tax	32	24	35	24	34	25
Corporate income tax	22	10	25	9	24	9
Social security contributions	0	25	0	26	0	26
Payroll taxes	0	1	0	1	0	1
Property taxes	6	6	4	5	4	5
General consumption taxes	28	20	25	20	26	20
Specific consumption taxes	9	11	8	11	9	11
Other taxes	3	3	3	3	3	3

Source: OECD 'Revenue Statistics 1965-2013', p.29; South African Revenue Services Annual Report, various years.

The share of consumption taxes in the OECD is also consistent over the period at about 31 per cent, with the larger part of that revenue accounted for by general consumption taxes such as the (nearly) ubiquitous value added tax (VAT). Nonetheless, countries such as Mexico (around 35 per cent) and Turkey (around 22 per cent) still collect a relatively large part of their tax revenues by way of taxes on specific goods and services rather than through a general consumption tax (OECD, 2014, pp28-30).

For South Africa, a far larger proportion of tax revenue than is the case on average in the OECD, comes from income taxes: roughly 58 per cent in 2012 in South Africa compared to the 34 per cent OECD average. South Africa also relies more heavily on its VAT as a significant part of its tax mix 26 per cent in 2012 compared to the OECD average of 20 per cent). This South African tax mix, with over 80 per cent of total tax revenue coming from taxes on income and VAT, matches that of countries like Australia, Denmark and New Zealand and contrasts sharply with those OECD countries where there is far heavier reliance on social security taxes. Again this has implications for the sorts of fiscal opportunities that can be appropriate in the South African context, discussed in more detail in the following section.

Tax administration

While there have been significant changes in relation to broader tax policy (including in relation to tax revenues and tax mix and typified by the mantra of lower rates and broader bases) in most countries over the period since the 1980s, dramatic changes have also taken place in the way that taxes are administered. Most notably there have been significant changes in the way that revenue authorities have been organised and the manner in which they have approached the tasks of administering the law and collecting the tax revenue that is properly due – 'extracting the maximum amount of feathers [from taxpayers] with the minimum amount of hissing.' Major trends in this sphere have included (D'Ascenzo, 2015; OECD, 2015):

1. The modernisation and professionalization of tax administrations in OECD (and other) countries, promoting increased flexibility in human resource organisation and pay scales with greater emphasis on externally validated merit based performance targets;
2. The introduction of autonomous and semi-autonomous structures whereby tax administrations operate independently, or more independently, of their political masters;
3. The growth of the internal organisation of revenue authorities by reference to market segments (eg, Large Taxpayer Units) rather than solely by reference to the type of tax being collected or the function being performed by revenue officers;
4. An increased reliance on self-assessment as opposed to official assessment;
5. Far greater use of technology in all aspects of revenue administration work; and
6. Above all, a shift away from a command and control regulatory frameworks reliant on penalties and enforcement to ensure compliance to a risk management approach designed to foster voluntary compliance – making it easy for those who wish to comply and providing plausible and effective deterrence to those who do not.

Many of these trends apply specifically to South Africa, largely as a result of the introduction of the *Tax Administration Act* 2011. This legislation modernised, integrated and made other enhancements to the common administrative elements of tax law. South Africa has also been engaging on a regional level with the ratification of the African Tax Administration Forum Agreement in 2012 and has entered into a number of Memorandums of Co-operation which enable the close co-operation and sharing of expertise between administrations.

In addition there has been a trend, in evaluating the effectiveness of revenue bodies, towards measuring outcomes (the total tax yield secured) rather than measuring output (such as the frequency of audit interventions and the resulting yield) (OECD, 2013a; OECD, 2015). Nonetheless, the latter are still useful measures of efficiency and therefore still have a role to play in assessing the overall effectiveness of tax administration.

Three specific aspects of tax administration are considered in more detail here. Firstly, a key role for tax administration is to minimise the tax gap. The tax gap is the difference between what a revenue authority theoretically should collect and what it actually does collect (McKerchar & Evans, 2009). While often associated with tax evasion and avoidance, the concept is broader than that and may embrace both intentional and non-intentional non-compliance with tax rules. A full discussion of the tax gap is beyond the scope of this article. Thus the only aspect of the tax gap discussed below relates to one particularly important aspect, very relevant in the South African context: the shadow economy.

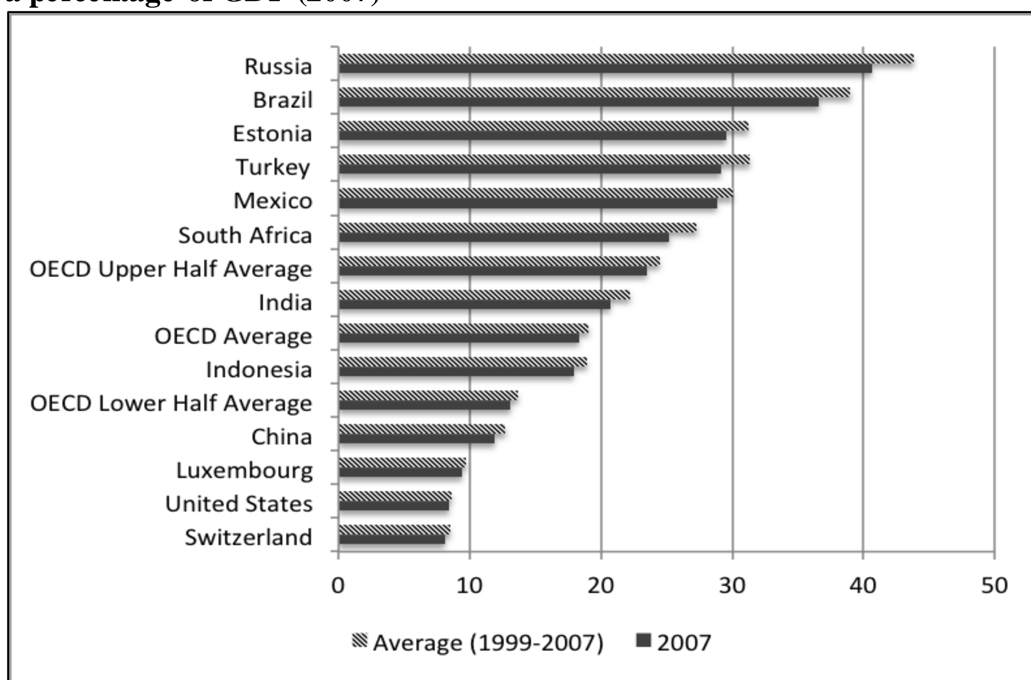
The second aspect discussed in this section is the tax operating costs of the tax system, from both the administrative (revenue authority) and compliance (taxpayer) perspectives. Given the critical role played by small and medium enterprises (SMEs), in the South African context, special mention is made of these (Smulders, Stiglingh, Franzsen & Fletcher, 2012). Finally, the concept of corruption is also canvassed, together with perceptions and measures, although this discussion is not restricted to corruption solely in tax administration. It will be appreciated that there are many other aspects of tax administration that potentially could have been covered. These three areas, however, provide an appropriately representative coverage of tax administration in its broadest sense, and are therefore relevant for the purposes of this article.

The shadow economy

There is compelling evidence that the level of tax is a main driver of shadow economic activity (Schneider & Williams, 2013; Schneider, Buehn & Montenegro, 2010). This is followed, in order, by tax morale, the quality of state institutions and labour market regulation (Schneider & Williams, 2013).

Data suggests that over the last decade the size of the shadow economies (expressed as a percentage of GDP) in all OECD and BRIICS countries appears to be falling (Schneider et al, 2010). This is shown in Figure 3 for selected OECD countries and for the six BRIICS countries. Whilst in OECD countries the average has decreased by less than one per cent of GDP in the period concerned, the BRIICS have decreased by between one per cent (Indonesia) and 3.2 per cent (Russia).

Figure 3: The shadow economy for selected OECD and BRIICS countries as a percentage of GDP (2007)



Source: Schneider et al, (2010) 'New Estimates for the Shadow Economies of the World', Table 2.

The size of South Africa's shadow economy has apparently decreased by 2.1 per cent over the last decade, slightly above the average of the BRIICS countries. Nonetheless, at 25.2 per cent, the shadow economy is currently around one quarter of the total economy. This puts it well above the 2007 OECD average of 18.3 per cent and slightly above the OECD upper half average of 23.5 per cent. According to these figures, South Africa's shadow economy is also larger than China's (11.9 per cent), Indonesia's (17.9 per cent) and India's (20.7 per cent). It is nevertheless smaller than both Brazil (36.6 per cent) and Russia (40.6 per cent).

The figures are not entirely reliable for a number of reasons. In the first place, there is little or no agreement as to what should, or should not, be included in calculations of the size of the shadow economy, or indeed, what the shadow economy actually is. This uncertainty is reflected in the large variety of terms that refer to the existence of the shadow economy, often referred to alternatively as the non-observed, cash, hidden, underground, invisible, unrecorded, or black economy. By its very nature, and given such difficulties of definition, it is difficult to establish the size of the problem with any ease.

This initial uncertainty is compounded by fundamental differences in the methods used to calculate the shadow economy. For example, Ahmed and Rider suggest there are at least five identifiably different 'top-down' methods for measuring the shadow economy (the national accounts method, the labour force method, the monetary transactions approach, the currency demand method and the electricity consumption method), as well as a number of 'bottom-up' methods (Ahmed & Rider, 2008). Unfortunately the different methods produce widely converging results, with the result that researchers and policy makers can have little faith in the integrity of the measurements (Feige & Urban, 2008).

Notwithstanding such concerns, the estimates that are available do at least suggest that the size of the shadow economy in South Africa, particularly relative to other comparable countries, represents a real challenge for policy makers in that country.

Tax operating costs

Another means by which the efficiency of the tax system can be assessed is by looking at the tax operating costs of the system. There are two components to tax operating costs: the administrative costs incurred by revenue authorities in collecting tax revenue and administering the tax system; and the compliance costs incurred by taxpayers in order to meet their tax obligations.

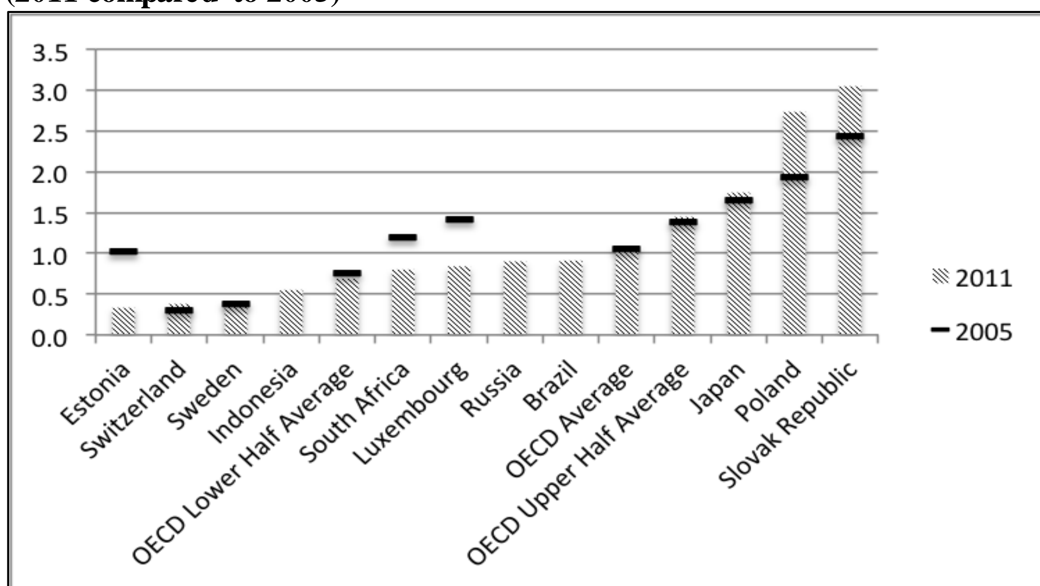
Various measures have been used to identify such costs, although it is slightly surprising how few truly international comparative studies have taken place in recent years (Chittenden, Kauser & Poutziouris, 2003; Evans, Hansford, Hasseldine, Lignier, Smulders & Vaillancourt, 2014). The dangers of international comparisons are well known to most researchers. Sandford (1994, pp.291-309) identified a number of reasons why such comparisons are more likely to mislead than enlighten, and offered the advice that 'comparisons of … operating costs should be used sparingly, with the greatest care and with a comprehensive statement of their limitations'. Such caution is duly noted in the following analysis.

Administrative costs

The cost of collection ratio is a commonly used standard measure of administrative costs, or more particularly of the efficiency with which revenue authorities collect tax (Evans, 2003). It compares the annual costs of administration with the total revenue collected for a particular fiscal year. A downward trend is associated with reduced administrative costs (or improved efficiencies) or improved tax compliance (or improved effectiveness) (OECD, 2013b).

Figure 4 compares the cost of collection ratio for OECD and most BRIICS countries for 2011 with the 2005 year. On this measure, South Africa has done exceptionally well, reducing its ratio by 0.40 points from 1.20 per cent to 0.80 per cent. Only Estonia and Luxembourg have done better, decreasing their ratios by 0.68 and 0.58 points, respectively.

Figure 4: Cost of collection ratio for selected OECD and BRIICS countries (2011 compared to 2005)



Note: No data for China or India.
Source: OECD, 'Government at a Glance 2013', Table 2.24.

However, it is important to note that many factors can influence this ratio, including differences in tax rates and structures, and prevailing economic conditions. For example, an increase in the ratio may be due to a reduction in tax revenue as a result of the financial and economic crisis rather than to any improvement in tax administrative efficiency. Conversely, a downward improvement in the ratio may be the simple result of increased taxes collected as the result of a rate rise or base broadening rather than any improvement in administrative practice.

Tax compliance burden

There are a number of ways that tax compliance costs can be assessed. For example, the compliance burden can be measured by the time taken to comply with the tax law and the number of tax payments required. The PricewaterhouseCoopers (PwC) (2015) 'Paying Taxes' annual publication does this, assessing both the tax cost and tax compliance burden of business taxes. Countries are effectively ranked according to the ease of paying taxes.

Table 2 Ease of paying taxes ranking OECD and BRIICS countries (2013)

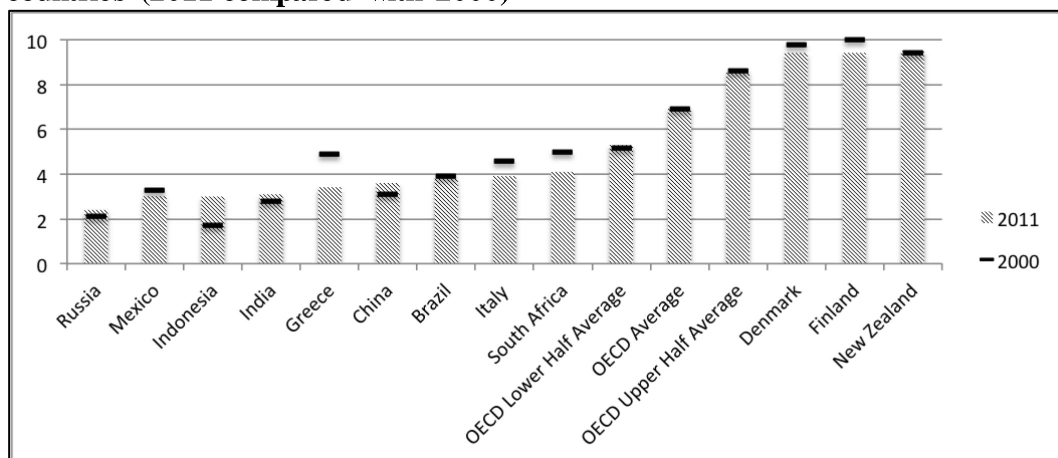
Economy	Overall ranking	Total tax payments	Time to comply (hours)	Total tax rate (%)
Ireland	6	9	80	25.9
Canada	9	8	131	21.0
Denmark	12	10	130	26.0
Norway	15	4	83	40.7
United Kingdom	16	8	110	33.7
Switzerland	18	19	63	29.0
South Africa	19	7	200	28.8
Luxembourg	20	23	55	20.2
Finland	21	8	93	40.0
New Zealand	22	8	152	34.4
Netherlands	23	9	123	39.0
Korea, Rep.	25	10	187	32.4
Estonia	28	7	81	49.3
Chile	29	7	291	27.9
Sweden	35	6	122	49.4
Australia	39	11	105	47.3
Slovenia	42	11	260	32.0
Iceland	46	26	140	29.7
United States	47	11	175	43.8
Russian Federation	49	7	168	48.9
Turkey	56	11	226	40.1
Greece	59	8	193	49.9
Portugal	64	8	275	42.4
Germany	68	9	218	48.8
Austria	72	12	166	52.0
Spain	76	8	167	58.2
Belgium	81	11	160	57.8
Poland	87	18	286	38.7
Hungary	88	11	277	48.0
France	95	8	137	66.6
Israel	97	33	235	30.1
Slovak Republic	100	20	207	48.6
Mexico	105	6	334	51.8
Czech Republic	119	8	413	48.5
China	120	7	261	64.6
Japan	122	14	330	51.3
Italy	141	15	269	65.4
India	156	33	243	61.7
Indonesia	160	65	254	31.4
Brazil	177	9	2600	69.0

There are a number of limitations of the measures used in this index, not the least of which is the very restrictive 'snapshot' that is used – effectively it is based upon data in relation to one medium sized company in each country. So, for example, the 'time to comply' ranking only takes into account the time taken to comply with corporate income, labour and consumption taxes. Nonetheless the results can be taken as indicative even if not entirely reliable. The results for the latest year available (2013) has South Africa with an overall ranking of 19, which puts it ahead of most OECD countries and all of the other BRIICS countries, as shown in Table 2. South Africa was ranked 24 in 2012 and 32 in 2011, and its decrease in compliance burden is largely attributable to the abolition of the secondary tax on companies. However, the PwC report notes that new withholding taxes, enhanced disclosure requirements and increased gathering of third party information may increase compliance obligations and impact future rankings (PwC, 2015).

Corruption

'Corruption' is defined as 'the abuse of entrusted power for private gain' (Transparency International, n.d.). The Corruption Perception Index is based on experts' opinion of government corruption. On a scale of 0 (highly corrupt) to 10 (very ethical), one third of OECD and BRIICS countries scored below 5 in 2011, roughly the same as in 2000 (Transparency International, n.d.). Figure 5 shows the corruption 'scores' for selected OECD and all BRIICS countries.

Figure 5: Corruption Perception Index for selected OECD and all BRIICS countries (2011 compared with 2000)



Source: Transparency International, Corruptions Perception Index 2011, 2000.

The OECD average has remained steady over that period at a score of 6.9. All of the six BRIICS countries are in the bottom ten for 2011, and all with a score of below 5 points. South Africa was ranked 34th in the world in 2000 but slipped to 64th position in 2011, although only dropping 0.9 points (2011: 4.1; 2000: 5.0). Indeed, South Africa was the only country in the BRIICS bloc that did not maintain or improve its rating.

Corruption, therefore, is still perceived as an issue for South Africa although this does not necessarily mean it applies to its taxation system or administration thereof. Rather the measurement of perceived corruption pertains to all government functions combined. However, the pervasiveness of the South

African Revenue Service (SARS) in South African society means that it has an important role to play in modelling best practice in the fight against corruption. Armed with this necessary background, the article now explores specific fiscal challenges and opportunities for South Africa.

SOUTH AFRICA: FISCAL CHALLENGES AND TAX OPPORTUNITIES

Fiscal challenges

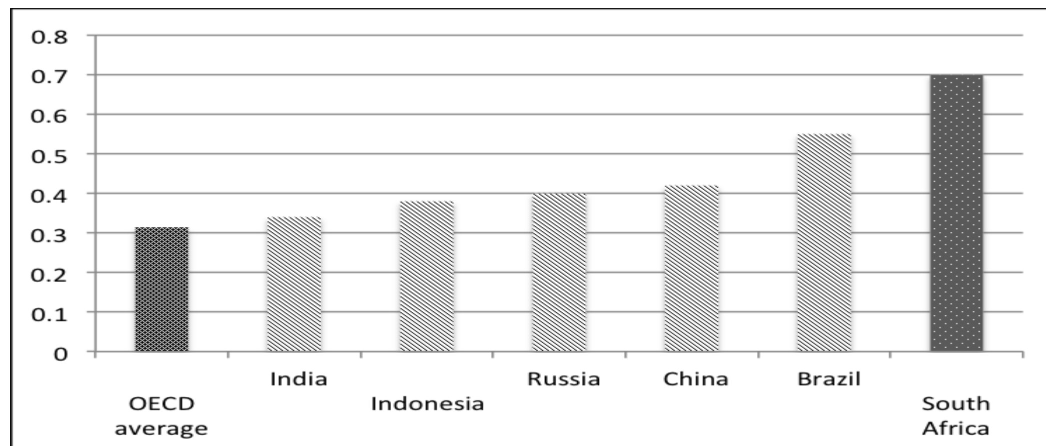
According to the 2013 Economic Survey for South Africa (OECD Report), public finances are in reasonable shape and core inflation is stable. However, the 'extremely high' income inequality, the 'extremely high' unemployment rate, the sluggish output growth and the fact that environmental challenges are threatening the sustainability of economic growth were all identified as key fiscal concerns (OECD, 2013c). The OECD Report also found that the macroeconomic policy mix had been 'insufficiently supportive of economic growth while allowing large budget deficits to persist' (OECD, 2013c, p.8).

These fiscal challenges – income inequality, high unemployment, sluggish economic growth and environmental concerns are now considered in more detail, along with an analysis of the specific constraints and opportunities that exist as a result of regional considerations. As will be shown, these regional considerations are particularly relevant in determining South Africa's capacity to respond to its fiscal challenges.

Income inequality

Income inequality, as measured by the Gini coefficient, is shown for South Africa, the other BRIICS countries and the OECD average in Figure 6. It averages around 0.70 in South Africa compared with the OECD average of 0.314 (OECD, 2013c). This makes it among the highest in the world. This can be contrasted with 0.55 in Brazil, 0.42 in China, 0.40 in Russia, 0.38 in Indonesia and 0.34 in India (World Bank, n.d.). In 2008 the world income inequality Gini, at a global level, was estimated at 0.62 (OECD, 2013c).

Figure 6: Income inequality: Gini coefficient for OECD average and BRIICS countries 2013



Source: World Bank, 'World Development Indicators: Distribution of income or consumption' Data Catalogue.

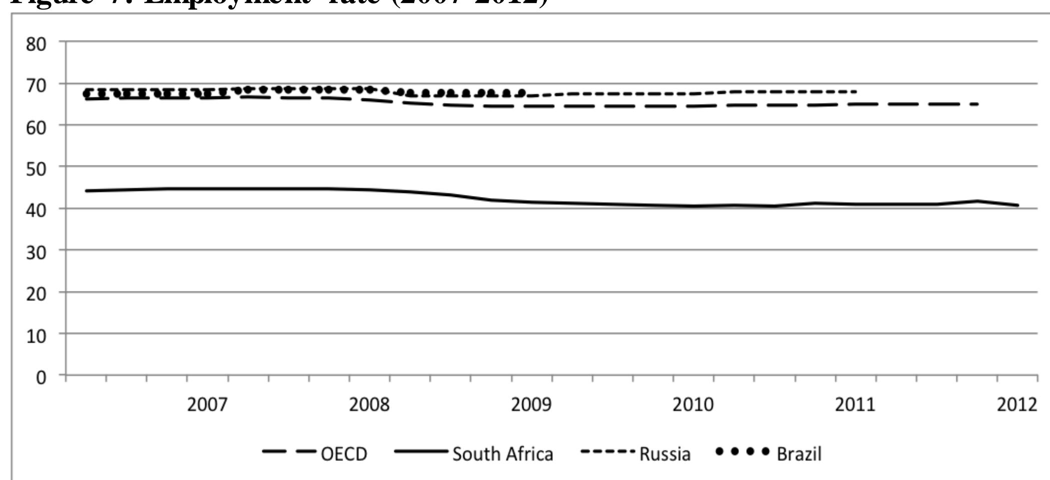
Thus, it would appear that the income differences are greater within South Africa than at the global level. This is confirmed by the large income ratio between top and bottom deciles. The OECD calculated this in 2010 to be around 20, compared with a level of 5 for the US, considered to be one of the most unequal countries in the OECD (OECD, 2013c).

There has been some impact from the government's use of the tax and benefit system to alleviate inequality. It is estimated that redistributive policies, particularly social transfers, have reversed around 40 per cent of the increase in income inequality (Leibbrandt, Woolard, Finn and Argent, 2010). However, notwithstanding an increase of progressivity in income taxes and an increase in social transfers, income inequality is arguably South Africa's number one issue.

High unemployment

Labour market outcomes are closely related to income inequality. Indeed, much of South Africa's income gap is explained by high rates of unemployment. An OECD study has found that labour market income contributes between 85 per cent and 90 per cent of income inequality each year (Leibbrandt, Woolard, Finn and Argent, 2010). This is largely due to high unemployment where less than half the working-age population (15-64) are in employment (40.8 per cent compared with OECD average of 64.9 per cent) (OECD, 2013c). From the data available, even Brazil (up to 2009) and Russia (up to 2011) have higher employment rates than the OECD average. This is illustrated in Figure 7.

Figure 7: Employment rate (2007-2012)



Source: OECD, 'OECD Economic Surveys: South Africa 2013', p. 13.

Increasing the employment rate is central to both the National Development Plan and the New Growth Path. The National Development Plan is a government-endorsed strategy whose central objectives are the eradication of poverty and to greatly reduce income inequality by 2030 (National Planning Commission, 2010). In order to meet its intermediate and end targets, the action plan involves a number of institutional and structural reforms. The New Growth Path establishes an economic framework for the period 2010 to 2020 (Economic Development Department, 2010). It is tasked with the creation of a new economic plan to

replace the Accelerated Share Growth Initiative for South Africa (AsgiSA) which had been criticised for failing to deliver on increased employment and reduced inequality (OECD, 2013c).

Sluggish economic growth

Since the end of apartheid little investment has been made in infrastructure, creating a backlog that is now deemed imperative to address. In his State of the Nation speech in February 2012, President Zuma (2012) announced a major infrastructure program, covering electricity, water and transport, to be overseen by the specially created Presidential Infrastructure Coordinating Commission. The need for investment in infrastructure is contained in both the National Development Plan and New Growth Path. The 2013 Medium Term Expenditure Framework outlines the Government's plan to divert more public expenditure to capital spending over the medium term (National Treasury, 2012).

Revenue is also required to reduce the cyclically adjusted deficit as well as to fund spending in high priority areas such as education and the national health insurance being phased in. This requires policies to encourage economic growth. Indeed, the 2014 National Budget recognises that higher levels of growth are required to address the challenges of unemployment and inequality (National Treasury, 2014). Economic growth needs to be sufficiently vigorous not only to absorb the growing labour supply but also to absorb current excess labour supply. Small businesses play a large role in most economies (Freedman, 2009). In the 2012 National Budget, the Treasury increased the tax-free threshold for firms, in order to encourage the growth of small businesses (National Treasury, 2012).

Environmental challenges

Economic growth is impacted by environmental challenges. South Africa is ranked among the top twenty countries measured by absolute carbon dioxide emissions (National Treasury, 2013a). However, the Government is committed to action and is a signatory to the United Nations Framework Convention on Climate Change. At the World Climate Business Summit President Zuma (2011) reiterated South Africa's commitment to support efforts dealing with the challenges posed by climate change, stating: 'We are forging ahead with our programme of greening the economy to improve the economic, social and environmental resilience of the country in the face of climate change'.

The KPMG Green Tax Index, shown in Table 3, analyses those economies seen as representing a major share of global corporate investment activity, that use their tax systems to achieve green policy objectives (KPMG, 2013).

Of the 21 economies analysed, South Africa has an overall ranking of 13. With respect to tax incentives only, it ranks joint twelfth and is ranked joint ninth for tax penalties only. South Africa performs strongly in energy and water efficiency, scoring joint fourth and joint third ranking, respectively. Most countries included in the analysis use either incentives or penalties. The most notable exceptions are China and the United Kingdom who use both extensively.

Table 3: Green Tax Index country ranking (2013)

Overall ranking		Tax incentives only		Tax penalties only	
United States	1	United States	1	France	1
Japan	2	South Korea	2	Japan	2
United Kingdom	3	China	3	United Kingdom	3
France	4	India	4	Finland	4
South Korea	5	United Kingdom	5	China	5
China	6	Canada	6	Ireland	6
Ireland	7	Netherlands		Spain	
Netherlands	8	Japan	8	Australia	
Belgium	9	Ireland	9	Netherlands	9
India	10	Belgium	10	South Korea	
Spain	11	Singapore	11	South Africa	
Canada		Brazil	12	Belgium	
South Africa	13	South Africa		Germany	
Singapore	14	Argentina	14	United States	14
Finland	15	Spain	15	Singapore	15
Germany		France	16	Canada	16
Australia	17	Germany	17	Russia	17
Brazil	18	Mexico	18	India	
Argentina	19	Australia	19	Argentina	19
Mexico	20	Russia	20	Brazil	
Russia	21	Finland	21	Mexico	

Source: KPMG, 'The KPMG Green Tax Index 2013' p. 4.

Thus, South Africa already uses environmental taxes extensively with a carbon tax scheduled to be implemented in 2016. First proposed in 2010, it has been subsequently revised and repeatedly postponed. However, with the initial rate expected to be very low, it is unlikely to have a significant impact on behaviour until rates increase (OECD, 2013c). It is also unlikely to aid in economic growth (OECD, 2013c).

Regional considerations

There are also regional considerations. South Africa is a member state of the Southern African Development Corporation (SADC) and a signatory to the Memorandum of Understanding on Co-operation in Taxation and Related Matters. This provides for a publicly accessible tax database containing detailed tax information, building capacity and expertise among tax officials, and harmonising policies on tax incentives, tax treaties and indirect taxes. The objective of harmonising tax regimes and cooperating on tax matters is to improve regional economic performance by minimising disparities in tax systems that could cause inequities between national and regional strategies. The coordination of direct and indirect taxes is seen as especially important for achieving the policy objectives for finance and investment as well as to facilitate trade (SADC, 2003).

South Africa is also a member of the African Tax Administration Forum (ATAF). This was established as a platform for sharing best practices on taxation matters in the region (ATAF, n.d.). The Agreement on Mutual Assistance in Tax Matters covers areas such as exchange of information, cooperation in 'examinations' or

audits and providing assistance in collection of tax revenue. From a review of major issues, challenges and current needs, a number of priorities have been identified. These include the automation and promotion of integrated tax systems, strengthening audit skills in specialised industries and in specialised areas of taxation, promoting voluntary compliance, and finding suitable solutions to deal with the predominance of the informal sector (ATAF, 2012).

Compared with the other members of the SADC and ATAF, South Africa has arguably the most advanced tax regime. While there are undoubtedly advantages in its membership of these regional bodies, South Africa is also bounded and constrained by them. In a way, its progress is dependent on how rapidly the region can mature to a comparable level. Yet it can also be contended that South Africa has a responsibility to lead by example.

Tax opportunities

With budget deficits, and hence public debt, becoming increasingly unsustainable, raising taxes, whether through introducing new taxes or increasing the rate of existing taxes, is often considered a viable solution. It is generally more difficult to cut public spending than to increase taxes due to the latter generally relating to a large number of dispersed and heterogeneous economic entities (Kesner-Skreb, 2014). However, increasing the tax burden has its limits.

One way of assessing whether the tax burden can be increased is to compare the share of total tax collected in GDP with comparable countries. If South Africa's tax burden is higher than the others, this may indicate that there is little room for more tax increases. Another method is the tax effort index, discussed above. As noted, South Africa is a high tax collection, high tax effort country. This means its share of actually collected taxes in GDP exceeds its estimated tax capacity and hence South Africa does not appear to have much capacity either to introduce new taxes or to increase existing tax rates.

There are a number of factors affecting this. Firstly, the income level of a country is expected to be a significant factor determining actual tax collection. As a result, it is expected that GDP per capita will have a positive and significant impact on tax collection, as well as on fiscal revenue (Bahl, 1972; Fox & Gurley, 2005). Secondly, higher age dependency and higher population growth are expected to distort a country's tax collection capacity and decrease the proportion of production population (Bird, Martinez-Vazquez & Torgler, 2004). These factors are expected to have a negative impact on both taxes and fiscal revenue. A third factor is trade openness (Aizenman & JinJarak, 2009; Norregaard & Khan, 2007). While increased trade openness can have a negative impact on taxes and fiscal revenue by lowering taxes collected on imports and exports, the more dominant effect is that trade openness is associated with increased economic growth, thus with increasing tax collection and increasing the tax base (Hines & Summers, 2009). An increasing agricultural sector in relation to GDP is expected to narrow the tax base, thereby decreasing tax collection and fiscal revenue. This is due to the fact that it is relatively harder to tax the agricultural sector (Leuthold, 1991; Tanzi, (1992). Finally, institutional and governance quality are essential factors in

determining the efficiency and adequacy of tax collection (Gupta, 2007; Bird et al, 2004).

In summary, tax revenue is positively correlated with GDP per capita and trade openness and negatively correlated with an aging population, population growth and the size of agricultural sector. The efficiency of a country's tax administration can go either way. Thus, for South Africa, successful tax reform means addressing all of these factors.

Where the amount of taxes collected exceed tax capacity, any additional increases in taxes, whether by way of new taxes or increases in tax rates, will result in undesirable macro-economic distortions and undermine international competitiveness (Kesner-Skreb, 2014). Consequently, tax reforms should focus on improving the efficiency of collecting tax revenue. The establishment of autonomous or semi-autonomous revenue bodies such as SARS provides a platform for initiating deeper tax administration reforms that have made possible improvements in both tax operations and service delivery (Kidd & Crandall, 2006; Fjeldstad & Moore, 2009). South Africa has also undertaken major tax administration reforms including improving compliance management and small taxpayers' administration (International Tax Dialogue, 2010).

But more than just building capacity and legitimacy is required. Tax capacity needs to be increased. Revenue bases need to be broadened as well as safeguarded, further improvements in efficiency are required to reduce tax compliance costs and corruption needs to be tackled. These are the essential tax opportunities for South Africa which are now considered.

Broaden the tax base

One way to broaden the tax base is – subject to the constraints already identified – to introduce new taxes. South Africa is doing this with the proposed carbon tax. Introducing an annual wealth tax would be counter to most of the trends in developed and developing countries (Chatalova & Evans, 2013) and would also be unlikely to gain political traction. The existence of an estate duty in South Africa does at least raise the possibility of some wealth redistribution, at least once in a generation.

Removing concessions and exemptions (the so-called tax expenditures that litter so many tax systems) can also broaden the base. With a large informal sector, presumptive taxation is attractive. It is estimated that the informal sector costs up to 55 per cent of total tax revenues in some countries (Joshi & Ayee, 2008), and in South Africa it may account for one quarter of the economy as noted above. Conventional tax reforms do not address the issue, often failing to even take it into consideration. Yet spreading the tax net contributes to the state-building capacity and the legitimacy of developing economies (Joshi & Ayee, 2008; Fjeldstad & Moore, 2008). Base-broadening measures also have efficiency benefits as they usually improve compliance, reduce tax compliance costs and opportunities to engage in tax-minimising behaviour (Brys, 2011).

Improve tax compliance

While South Africa has done well in reducing its cost of collection ratio (see Figure 4), there is nevertheless still room for improvement. The tax gap exists as a result of a number of possible factors. These may be demographic (including age, gender and level of education), personal (including attitudes, experiences, morale and financial circumstances) or result from aspects of the tax system itself (such as tax rates, penalties and complexity) (Kornhauser, 2007).

As McKerchar and Evans (2009) note, 'many of these factors are not constant, [and] it is to be expected that compliance behaviour can change over time'.McKerchar and Evans (2009) have outlined a number of strategies available to developing economies, and some of these resonate in a country such as South Africa. These are (1) creating a more effective tax administration; (2) fostering voluntary compliance and taxpayer morale; (3) strengthening and enforcing compliance; and (4) tackling the shadow economy.

Tax administrative reforms

South Africa has already made considerable progress on this front. For example, it established its autonomous revenue authority (SARS) in 1997 and more recently has passed its Taxation Administration Act in October 2012. These structural reforms create a more effective tax administration and this has been shown in South Africa's case (Taliercio, 2004; OECD, 2015). One cause of South Africa's success in this area is that SARS is supported by political champions and mentors. This enables a strong and continuing management team to be entrenched. But the administrative burden is inevitably increased when a revenue authority such as SARS is required to support the implementation of the government's social security and wage subsidy interventions, and to administer a cash reimbursement system for employers (SARS, 2009; African Development Bank Group, 2010).

It is said that '[t]he taxpayer registry is the backbone of all tax administrations' (Gallagher, 2005, p.125). As a result of the Taxation Administration Act this has been established. However, it is in the area of verification that South Africa, as with all economies, both developed and developing, can do better. This involves increasing both the amount and quality of information collected. Sources include both internal (central registry, tax returns, information about other taxes) and external or third party (government agencies, financial institutions, trade associations) data points. As D'Ascenzo (2015) notes, 'The effective use of digital information and the employment of analytics - including data and text mining and visualisation tools - are at the centre of modern tax administration. Optimising the potential of data can also help spur innovative thinking and new approaches'.

Fostering voluntary compliance and taxpayer morale

As a result of the growing recognition that cooperative and positive engagements are more productive than adversarial and antagonistic approaches, tax administrations are adopting two broad and mutually supportive strategies: building positive taxpayer and tax community morale; and making compliance both simpler and cheaper for taxpayers (Hoffman, Gangl, Kirchler & Stark, 2014).

The relationship involves more than just the revenue authority and the taxpayer. It must also encompass tax practitioners, industry associations, trade unions and other key stakeholders. A network of trusted alliances will enhance the success of any strategy addressing compliance issues (OECD, 2004).

It is recognised that the small business sector has the potential to be a major employer and strategies need to continue to be developed to promote this. It is also known that tax compliance costs are regressive, falling more heavily on small businesses rather than on large businesses (Evans, 2003). As noted by Smulders et al (2012), reducing the compliance costs for its small business sector is one area where South Africa can make a substantial difference.

Strengthening and enforcing compliance

The third strategy noted by McKerchar and Evans is to strengthen and enforce compliance. This is, by definition, more resource intensive. Nevertheless, having escalating levels of sanctions increases the risk perception and demonstrates both the capacity and willingness of tax authorities to combat non-compliance (Gill, n.d.). Further, according to Ayers and Braithwaite (OECD, 2004), the threat of severe penalty is most effective when used in conjunction with a scale of lesser sanctions. Methods that can be used effectively are audits and investigations, customised letters and prosecution.

Tackling the shadow economy

Tackling the shadow economy, the last strategy noted by McKerchar and Evans (2009, p.197), is notoriously seen as 'too difficult, requiring considerable effort with few returns'. However it has to be a priority. If it is not, legitimate businesses are disadvantaged in that the playing field is not level and confidence in the tax system is undermined. Prevention, detection and deterrence strategies designed to encourage compliance are relevant here (McKerchar & Evans, 2009). The network of trusted alliances could play an important role in uncovering elements or aspects of the shadow economy.

Tackling corruption

While South Africa has apparently improved its own position in relation to its scoring on perception of corruption indices since 2000, it has deteriorated in relation to other countries (see Figure 5). This is seen as an increasingly important barrier to improved public service delivery (OECD, 2013c). Indeed, corruption is identified as one of nine primary challenges facing the economy (National Planning Commission, 2011), and the African Development Bank Group is of the view that corruption is one of three main factors that will play out in the fiscal governance of South Africa in the short to medium term (African Development Bank Group, 2010). Approaches to combating corruption in tax administration generally aim at addressing the main drivers of corruption. Many of these are the trends discussed above and, in South Africa's case, include increased use of technology as in electronic filing of tax returns and increased reliance on self-assessment (Martinin, 2014).

It is commendable that tackling corruption is entrenched in SARS's strategy (SARS, 2009). A policy of zero tolerance for corruption is incorporated into its value statement. It established an Anti-Corruption and Security Unit in 2007 that has prevention, detection and investigation activities, informed by research and analysis activities.

These efforts need to be continued, even stepped up, as corruption also contributes to the composition of the tax gap and increases both administrative and compliance costs. Corruption is not only an institutional issue; it is also a moral and political issue.

CONCLUSION

For a tax system to be deemed to be successful it must provide a sustainable source of revenue, adequate for the needs of the government, and meet the three further objectives of assisting economic growth, providing for the appropriate distribution of income and performing a stabilisation function (Bird, 1992). In doing so it must also meet the evaluative criteria of efficiency, equity and simplicity.

Tax systems need to be sustainable. As they exist primarily to raise revenue to fund government operations and services, they need to raise an adequate amount of such revenue. A lack of revenue may result in budget deficits which generally have adverse consequences such as increased inflation and decreased private investment. It will also impact on what services can be provided by the government. Alternative sources of revenue, which can include: printing money (with its inflationary implications); domestic and foreign borrowing (which create interest and repayment obligations); and relying on foreign aid (which can have many other deleterious consequences) are not attractive.

The sustainability of the tax system includes widening the tax base and improving revenue collection through tax compliance. Of a South African population of around 51 million in 2012 according to the World Bank, only 5.9 million or approximately 12 per cent are registered as taxpayers (ATAF, 2012). While policies that only affect those in employment can have only a limited effect when a significant portion of the working-age population is unemployed, there is nevertheless still a role for tax policy in addressing the fiscal challenges facing South Africa.

The tax system needs to promote economic growth so as to increase employment and productivity levels. This may also assist in identifying informal economies and bringing them into the tax net. The small business sector is vital to economic growth and further tax measures should be considered to assist. Further, it is recognised that the threat of climate change is 'an opportunity to develop our green, inclusive, sustainable and shared growth' (Juma, 2011). Indeed, the New Growth Path recognises that the opportunity may come from the global effort to address climate change (Economic Development Department, 2010).

Foreign direct investment (FDI) is also often viewed by developing countries as a means of stimulating economic growth. Such investment is encouraged through the use of tax incentives or preferential rates (Shihata, 1991; Bird, 1992). However, their effectiveness is uncertain and a sufficient link between such policies and economic growth is lacking (Shihata, 1991; OECD, 2002). Indeed, the conventional wisdom is that tax incentives are bad in theory because they distort investment decisions and bad in practice because they are often ineffective, inefficient and prone to abuse (Easson & Zolt, 2003). Yet they are used by all countries, both developed and developing, as they are politically attractive.

The redistribution role of taxes is especially important in emerging countries such as South Africa where disparities in income can prevent development and increase demand on government spending. A progressive tax system that takes ability to pay into account (where the tax rate increases as taxable income increases) is possibly the most significant tool available to counteract income inequality. Indeed, because of the concern about inequality, any tax change will need to be scrutinised on the basis of its effect on the distribution of the tax burden. The main explicitly redistributive tax in most tax systems is the personal income tax (Zee, 2005). However, where there are large disparities in income as is the case in South Africa progressivity can be an illusion.

So what role can and should the tax system play in ensuring the fiscal needs of South Africa can be met and to what extent is the current tax system 'fit for purpose'? Traditionally emerging and developing countries have focused on increasing their tax-to-GDP ratios in order to reduce budget deficits, fund the services they provide and optimise the effectiveness of their tax systems. South Africa has undertaken significant tax reform over the past two decades, and is currently undertaking a further systematic and comprehensive review of its tax system. Although its revenue performance has improved over the period, it is still comparatively low and does not meet South Africa's needs as outlined above. Yet it is also clear from its tax effort index that South Africa does not have the scope to increase taxes. Thus any tax reform must increase revenue in a way that gives due consideration to its prevailing social, environmental and economic conditions. The key focus has to be on the efficiency gains that can be derived from broadening the base, improving compliance and tackling institutional corruption.
Tax policy and tax administration are fundamentally linked. As the Minister of Finance recently commented, "…the issue of tax morality is critical to the success of implementing our tax policies…" (Nene, 2015, p.2) It was also acknowledged that "[t]ax policy is also about effective tax administration. Hence an important policy consideration is to ensure that taxes are collected where and when they were due" (Nene, 2015, p.2). To this end the Tax Review or Davis Tax Committee has an ongoing role in advising government on future refinements to the tax system.

The current South African tax system performs remarkably well on many indicators. But it is stretched to the point where further demands may cause economic distortions and other systemic failures. It is not entirely 'fit for purpose' in its present form, but it is to be hoped that the current reform process will successfully identify those areas where it can be improved in order to play the most effective possible role in ensuring a "nation at the crossroads" takes the right

path forward in addressing the underlying macro-economic problems of sluggish economic growth, massive income and wealth inequality and high unemployment.

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