Budget 2022: Longer-term solutions to curb financial difficulty

By Patricia Williams , issued by SAICA

8 Mar 2022

Tax surplus has facilitated financial relief for the everyday consumer

Finance Minister Enoch Godongwana was able to report on record tax revenues of R1.55 trillion in his 2022 Budget Speech on Wednesday, 23 February 2022; R182 billion higher than estimates from Budget 2021, and R62 billion higher than the revised estimates from the medium-term budget policy statement. This surplus, which was mainly because of the impact of higher commodity prices in the mining sector, has facilitated some financial relief following the catastrophic impact of Covid-19.

The key financial relief for the everyday consumer includes no increases in fuel levies (other than a 1 cent per litre increase in the carbon fuel levy) to mitigate fuel price increases and the knock-on effects on household consumption from increased transport costs on goods; and a 12-month extension of the R350 social relief of distress grant, at a cost to the fiscus of R44 billion.

As noted by the finance minister in his budget speech, South Africa now pays grants to more than 46 percent of the population.

SARS needs to come up with longer-term solutions that do not involve tax rate increases

The finance minister was clear that the government cannot plan permanent expenditure on the basis of short-term increases in commodity prices. In the circumstances, longer-term plans are necessary to stabilise the tax base. However, as highlighted by the finance minister in his budget speech, now is not the time to increase taxes and put the economy's recovery at risk.

This leaves the South African Revenue Service (SARS)to step in and do what needs to be done considering the consequences of the COVID-19 pandemic. But whichsteps need to be taken?

The first step is stopping tax evasion in its tracks and targeting audits based on risk areas. Tax research suggests that tax evasion increases during periods of financial difficulty. In a 2019 paper titled *"Financial constraints and firm tax evasion"*, Alm, Liu and Zhang conclude that there is strong evidence that financially constrained firms are more likely to be involved in tax evasion activities, and that this effect is stronger for firms of private ownership, of smaller size, and of a younger age. This indicates that to stop tax evasion in its tracks before it can become endemic, SARS should be focusing its audit efforts in these areas.

In light of the "bounce-back scheme to support SMEs" proposed in Budget 2022 to help businesses in distress owing to the Covid-19 pandemic, the hope is that taxpayers suffering from financial difficulty would be able to access financial relief through legal channels, rather than resorting to tax evasion.

Interestingly, Alstadsæter, Johannesen and Zucman found, in a 2019 paper titled *"Tax evasion and inequality"*, that wealthier groups evade tax substantially more than average taxpayers, which suggests that evasion is not always linked to financial difficulty. This supports SARS' focus on high net wealth individuals as another group of interest, to protect the tax base. The Budget 2022 proposal that provisional taxpayers with assets above R50 million should be required to declare specified assets and liabilities at market values in their 2023 tax returns, may help to gather data that will refine SARS' audit approach within this area.

The second step SARS should take is to Increase third-party reporting requirements. Alstadsæter, Johannesen and Zucman also found that third-party reporting strongly limits tax evasion. No legislative changes are necessary for SARS to improve the levels of third-party reporting. Section 26 of the Tax Administration Act already allows the Commissioner to require third-party returns containing the information required by SARS by means of public notice. While SARS audit teams no doubt have numerous ideas of what third-party information would improve their audit capacity, industries that immediately come to mind for third-party reporting are the legal, medical and financial exchange industries.

Advocates are generally paid by attorneys, and as such it should be possible to introduce third-party returns (on a similar basis to IT3(a) and IT3(b) certificates) for attorneys, reporting earnings paid to advocates. Many medical payments are made by medical aids, and the data is frequently consolidated by the medical aid even where the payment has been made "out of pocket". This should facilitate third-party returns, reporting earnings paid to medical professionals.Third-party reporting should be available for financial exchanges, including cryptocurrency exchanges that fall within the South African legal regime.

As far back as March 2017, at a conference on tax evasion and illicit financial flows organised by the Alternative Information Development Centre in Cape Town, Judge Dennis Davis highlighted that wealthy individuals, including advocates, appear to be escaping the tax net. In this respect, Davis stated: *"I know more people on the Johannesburg Bar earning R5 million a year than the tax tables show."*

By introducing higher levels of third-party reporting, the possibilities for tax evasion are significantly decreased, and the principle of equality (that persons earning similar amounts must pay similar amounts of taxes) is promoted.

ABOUT THE AUTHOR

Patricia Williams is a tax partner at Bowmans and member of the Tax Administration Act committee at the South African Institute of Chartered Accountants (SAICA).

- **Directors' role as the cornerstone of the governance ecosystem** 25 Apr 2024
- **2-pot system: Key considerations before you withdraw your retirement savings** 27 Mar 2024
- **Saica launches business podcast to empower small businesses** 19 Mar 2024
- **Accountancy and loss adjusting** 15 Mar 2024
- **Making the auditing profession attractive to Gen Z** 8 Mar 2024