PARLIAMENT
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Taxation Brief- 2022 Taxation and Revenue Proposals– June 2022

Budget Review 2022

Parliamentary Budget Office

The Parliamentary Budget Office (PBO) was established in accordance with the 2009 Money Bills Amendment Procedure and Related Matters Act, as amended (Act No. 9 of 2009). The main aim of the PBO is to provide independent, objective and professional analysis or advice to Parliament on matters relating to the Budget and other financial legislation. The PBO supports the implementation of the Act by undertaking research and analysis for the relevant Finance and Appropriations committees.

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1. Executive Summary

The Taxation Brief (Tax Brief) provides Members of Finance Committees with an analysis of the 2022 Taxation and Revenue proposals (2022 Tax Proposals). In the 2022 Budget Review, the Minister of Finance (MoF) proposed 2022 tax and revenue measures for consideration and approval by the Parliament. Therefore, in principle, the Finance Committees reports on the tax and revenue proposals – as per section 8.4 of the Money Bills Amendment Procedure and Related Matters Act (2009) ('Money Bills Act') – in the Budget Review should inform consideration of the 2022 Tax Bills.

The National Treasury (NT) and the South African Revenue Service (SARS) aim for tax changes to be informed by set objectives; to broaden the tax base, improve administration, lower tax rates and provide tax relief. Therefore, according to the NT and SARS, the 2022 Budget proposes significant changes to give effect to the noted objectives. The proposed 2022 amendments to Personal Income Tax (PIT), Corporate Income Tax (CIT) the Employment Tax Incentives (ETI), and Fuel Levy are meant to give effect to government objectives. Therefore, this Tax Brief provide an analysis on these main tax instruments; PIT, CIT and ETI. The tax brief further provides an analysis of the proposed measures and highlights other tax policy matters issues on the horizon and requiring Parliament oversight considerations.

- Analysis of proposed changes to PIT

The 2022 Budget proposes inflationary adjusted relief through a 4.5 per cent adjustment in personal income tax brackets and rebates. The proposals are intended to provide relief to taxpayers (or affected employees) in the context of inflationary pressures. This relief would lead to R 13.5 billion in potential tax revenue forgone in the 2022/23 fiscal year. It is therefore worth noting that the South African Reserve Bank (SARB) estimates inflation for 2022 to be 5.9 per cent[1]. Therefore, the proposed relief is likely to be inadequate to address the rising costs of living affecting households.

According to the 2022 Budget, the adjustment for inflation of the tax brackets relief is intended to support middle income taxpayers (earners). However, the PBO's analysis shows that the relief disproportionately benefits upper income households. Given the context of deep inequality, unemployment and poverty, low income households (earners) are not at the core of this tax relief objective. The PBO analysis shows that 18 per cent of those within the tax income threshold (R500 – R1500+ thousand) will receive R6.1 billion (44.9%) of the tax relief which equates to 45 per cent of the total relief. The tax relief will be distributed to 1.4 million registered individuals out of 7.5 million individuals within the taxable income threshold. The PBO concludes that the distributional impacts of the income tax measures, taking into consideration principles of progressivity, may be insufficient.

- Analysis of proposed changes to CIT

In 2021, government announced the intention to restructure the CIT rate. According to government, the proposal is intended to broaden the CIT base while reducing the headline rate from 28 per cent to 27 per cent. The proposal was effected in the 2022 Budget proposals, and the amendments came into effect on 1 April 2022.

The PBO caution that, despite having a statutory rate of 28 per cent, research and the literature shows that the South African corporate taxpayers enjoy a very low Effective Tax Rate (ETR). In particular, the PBO has shown in previous presentations that the all-sector average ETR was 18.2 per cent between 2011 and 2015. The PBO is concerned that the debate around the CIT rate in South Africa largely focuses on the statutory rate. This discourse disregards the low ETR enjoyed by corporates in South Africa, which should be the key compliance focus for tax policy.

One of the assumptions made to justify the reduction in the statutory CIT rate is that corporate taxpayers will respond by investing more into the economy. However, there is no consensus in the research evidence, on the causal relationship between lower CITs and investment. The PBO's' previous research has shown that out of ten factors considered by many corporate investors before investing, CIT tax rate was among the least factors. The Davis Tax Committee (DTC) had also cautioned against using a reduction in CIT rate as a measure to attract investment. Some of the important factors considered

[1] SARB Monetary Policy Committee statement – May 2022

by investors include; reliability and price of electricity, availability of skills, cost of labour, safety etc.

Government is committed to fiscal neutrality, which means tax policy should neither create nor lose revenue for the government. The PBO is concerned that the goal of fiscal neutrality is punitive on the fiscus given the current macroeconomic (fiscal policy) context. The reduction in CIT disregards the fact that South Africa like other developing countries relies more on income tax revenue than other forms of taxes and measures should focus on increasing ETR. In addition, the PBO raises some concern on the increases of offshoring thresholds which are counter the narrative on incentivising domestic investments.

- Analysis of proposed changes to ETI

Out of R5.2 billion in tax relief announced in the 2020 Budget, R2.2 billion is for the expansion of the ETI. The ETI Act was introduced in 2014 to allow expense deductions for every young unemployed being absorbed. This was to encourage employers to hire young and less experienced workers given chronically high unemployment rates for the youth. The ETI has subsequently been renewed multiple times since its introduction. And as of 1 March 2022, the ETI allowable expense rate has been increased by 50 per cent from R1000 to R1500.

The PBO is concerned that despite the continued implementation of the ETI incentive over the years, the real impact and benefits remain debatable. Various research evidence shows that generally, the ETI has had little to no effect on creating employment for youth. However, the evidence shows that the ETI positively impacts business profitability, particularly SMMEs. But it remains unclear whether the incentive saves jobs. The PBO proposes that there should be measures used by Parliament, including requesting government to provide evidence of effectiveness of the incentives given their impact on tax revenue.

- Analysis of Fuel Levy relief

According to the literature, the fuel levy is considered to be a regressive tax instrument. The levy disproportionally impacts low income households. Similarly, Informal business and Small Micro and Medium Enterprises (SMMEs) are disproportionately impacted by the fuel levy. For the first time in many years, the 2022 Budget did not propose increase in the fuel levy. The choice not to increase the fuel levy will provide significant relief for many households. This relief is important given that the fuel price has since increased significantly in response to deteriorating global and domestic macroeconomic conditions.

In addition, it is proposed that there be no increases to the RAF levy. These measures will provide much-needed relief to low income households that will not benefit from the relief provided through the PIT relief. In the face of rising inflation, these are welcomed measures.

- Other tax developments for MPs' consideration

Carbon Taxation (Green Taxonomy): In 2019, Parliament passed a bill that introduced a carbon tax. The 2022 Budget proposed an increase to the carbon tax rate in line with COP 26 commitments. The budget announcement further provided clarity that the first phase of the carbon tax will be extended by three years for the period 01 January 2023 to 31 December 2025. The PBO has noted and cautioned that given the status of South African socioeconomic challenges, climate fighting measures introduced by government should never disproportionally affect the low income households. For example, the increase in electricity to accommodate carbon tax.

Multilateral institution tax amendments: The Cabinet has in March 2022 approved the submission of the OECD Multilateral Instrument (MLI) Convention to Implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting (BEPS- MLI) to Parliament for ratification. A number of developing countries have raised issues around the dispute resolution requirements in the MLI. In considering instruments, it is therefore important that South Africa remains abreast of the issues that are being raised and to consider how they impact and protect the state' taxing rights (ability) to raise tax revenue. The PBO will provide detailed analysis for consideration during the Parliament ratification process.

Wealth Tax: SARS has established a dedicated new unit focusing on high-wealth individuals. This process is in line with DTC recommendations and may be seen as an important step in informing the debate about wealth tax given the context of South Africa where wealth inequality remains significantly high.

Gender dimensions of taxation policy: The National Treasury is working with other stakeholders to implement gender-responsive budgeting across government. This is expected to roll out in the 2023 Medium Term Expenditure Framework (MTEF) process. While this is welcomed, the PBO is concerned that the gender responsiveness budgeting is only limited to the expenditure side of the budget.

Tax administration: According to government, SARS has made significant strides to improve its tax revenue collection over the last two years. However, the governance and operational issues raised by the Tax Ombudsman are important to be considered and measures implemented to improve SARS administration. The PBO supports the Finance Committees decision to refocus on ensuring the legal status of the Tax Ombudsman.

Value Added Tax: the VAT was increased from 14 to 15 per cent in 2018 with the expectation that the amendment would be reviewed in 2021 (after three years). Parliament should require government to provide a status update on this policy proposal done in 2018.

2.Introduction

Over the last two years, the approach undertaken by National Treasury and the South African Revenue Service has been to make changes to the tax system the follow with the following objectives: broaden the tax base, improve administration, lower tax rates and provide tax relief. The 2022 Budget proposed significant tax policy changes to give effect to the objectives put forward. The 2022 tax proposals are summarised in the table 1.

Table 1: Impact of tax proposals on 2022/23 revenues

R million		Effect on tax proposals
Gross tax revenue (before tax proposals)		**1 603 647**
Budget 2022/23 proposals		**-5 200**
Direct taxes		**-2 200**
Personal income tax		
Increasing brackets by inflation –		
Revenue if no adjustment is made	13 500	
Increase in brackets and rebates by inflation	-13 500	
Expansion of the employment tax incentive	-2 200	
Corporate income tax		-
Reduction in corporate income tax rate to 27 per cent	-2 600	
Restriction of assessed losses	1 100	
Additional interest limitation	1 500	
Indirect taxes		**-3 000**
Fuel levy		
Not adjusting the general fuel levy	-3 500	
Specific excise duties		
Increase in excise duties on alcohol	400	
Increase in excise duties on tobacco	100	
Gross tax revenue (after tax proposals)		**1 598 447**

Source: 2022 BR

The 2022 Budget estimates the gross tax revenue collection for 2022/23 to be R1.6 trillion. Global macroeconomic conditions have deteriorated significantly since 2022 Budget announcements in February 2022. In particular, the ongoing disruptions caused by Covid-19 and the Russian invasion and continued war in Ukraine which have exacerbated supply chain disruptions and increases in fuel and food prices. Given these developments, the government is likely to miss its tax revenue targets set-out in February 2022. The PBO' Quarterly Economic Briefs analysis shows how global macroeconomic developments are likely to impact South African economy.

The 2022 tax proposals have already been implemented. However, according to Money Bills Amendment Procedure and Related Matters Ac of 2009, Parliament is required approves the fiscal framework and revenue proposals. Thus this tax brief provides analysis to inform Members on the impacts of the proposed tax changes.

The brief particularly covers proposed changes to Personal Income Tax, the Employment Tax Incentive, and Corporate Income Tax, which are considered to be significant given current macroeconomic developments. The proposed changes to the PIT and ETI compose R2.2 billion of the tax relief. The change in the statutory rate for CIT is a major change in the tax system. The brief also briefly touches on indirect taxes at the end of the document.

3. Proposed changes to Personal Income Tax (PIT)

The inflationary adjustment(relief) by 4.5 per cent for personal income tax brackets is the main 2022 tax proposal for the PIT. This proposal reduces the estimated tax revenue by R13.5 billion in 2022/23. The 202 budget projected inflation, given the current macroeconomic developments since the announcements, is lower than recent projections. Therefore, the 2020 inflationary brackets adjustments will be inadequate. The South African Reserve Bank, estimates inflation for 2022 to be 5.9 per cent.[2] Higher inflation rates, without adequate wage and tax relief adjustments, will lead to real declines in wages and disposable income for households, respectively.

The 2022 Budget proposed PIT tax relief was intended to support middle income earners. However, the PBO analysis revealed that the relief disproportionately benefits upper income earners. The analysis further revealed that 18 per cent of those within the tax income threshold (R500 – R1500+ thousand) will receive R6.1 billion (44.9%) of the tax relief proposed which equates to 45 per cent of the relief. This tax relief is distributed to 1.4 million registered individuals out of 7.5 million individuals within the taxable income threshold.

Table 2: Estimates of individuals and taxable income, 2022/23[3]

Taxable bracket	Registered individuals	Value of tax relief	% of the R13,5 billion relief	Average per capita (relief/registered individuals)
R Thousand	Number	R billion	%	Rand
R0-R91	7 700 135	-	-	-
R91-R150	1 973 185	-1,2	8,9	608,2
R150- R250	1 717 760	-1,6	11,9	931,5
R250-R350	1 231 672	-1,9	14,1	1542,6
R350-R500	1 158 117	-2,8	20,7	2417,7
R500-R750	756 629	-2,8	20,7	3700,6
R750-R1 000	274 963	-1,3	9,6	4727,9
R1000-R1500	199 837	-1	7,4	5004,1
R1500+	133 230	-1	7,4	7505,8
Total	**15 145 528**	**-13,6**	**100**	**898,0**

Source: SARS and PBO calculations

The 2022 Budget proposes to increase the medical tax credits from R332 to R347 per month for the first two members, and from R224 to R234 per month for additional members. These tax credits will proportionately benefit the minority of the population (16.4% of all individuals in South Africa were members of medical aid schemes[4]) that have medical aid, which tends to be higher income earners. Thus the inflationary

[2] SARB Monetary Policy Committee statement – May 2022

[3] SARS and own calculations

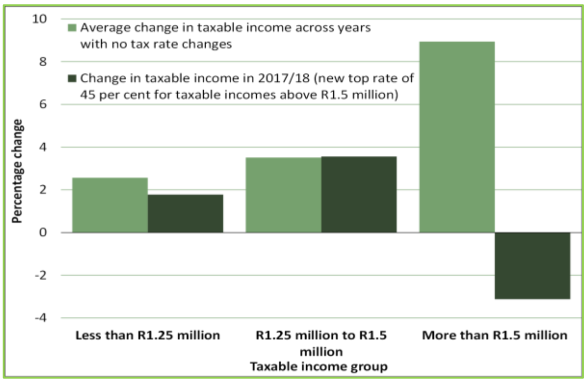
[4] Stats SA – General Household Survey 2018

adjustment of tax brackets (tax relief) plus the medical tax rebates disproportionately do not benefit low income earners.

The PBO is concerned that given the context of deep inequality, unemployment and poverty, low income earners are not at the core of the 2022 tax relief objective. Low income groups fall outside the income tax net, so the relief provided through the tax system excludes the poorest groups. In this regard, the PBO' analysis shows that the distributional impacts of the income tax measures, taking into consideration principles of progressivity, may require reassessment. This brief will further discuss indirect taxes (the fuel levy and RAF) which provide relief to low income earners.

The 2022 Budget shows that increasing the top brackets tax rate from 41 to 45 per cent for taxable incomes above R1.5 million in 2017/18 generated less than the projected R4.4 billion revenues per year. Figure 1 shows the changes in real taxable income by income group.

Figure 1: Change in real taxable income



Source: 2022 BR

A briefing by Finance of Minister, on 16 May 2022, revealed that 440 individual taxpayers owed SARS just under R22 billion. Of the money owed to SARS, 72 individual taxpayers owe 68 per cent of the total due. The PBO argues that tax avoidance by higher earning individuals who aggressively plan their tax responsibilities to lower rates can be attributable in part to the lower tax revenue generated. The PBO, therefore, argues that more efforts are required to address tax avoidance and evasion by high network taxpayers.

The PBO notes that raising tax rates for high income earners affects a small group of taxpayers and therefore does not generate a large amount of revenue. This does not mean that the taxes are not effective and should not be used to justify lowered tax rates for high net income individuals in the future.

4.Proposed changes to the Corporate Income Tax (CIT)

The 2021 Budget announced a restructuring of the CIT to broaden the base while reducing the headline rate to 27 per cent in 2022. Budget 2022 gave effect to this proposal. The proposed amendments came into effect on 1 April 2022, meaning that the tax will be effective for tax years ending on or after 31 March 2023.

The projected CIT revenue for 2022/23 will be R269.9 billion, which is lower than the projected collection of R318.4 billion in 2021/22. Part of the lower revenue projection is due to government's expectation that revenue gains from elevated commodity prices will dissipate. Given that the 2022 Budget was tabled prior to significant changes in the global macroeconomic outlook (outlined earlier), it is likely that projections for CIT may need to be revised downward.

4.1. Competitiveness of the CIT rate

The 2022 Budget highlights that South Africa's CIT rate exceeds the Organisation for Economic Co-operation and Development (OECD) average of 23 per cent. Despite this comparison, the PBO notes that South Africa, like many other developing countries, relies more on income tax (including CIT) as a source of government revenue than advanced countries. This is in contrast with to developed countries, which rely on income tax revenue is almost similar to their reliance to consumption tax. Therefore, South Africa compares fairly well with alike developing counties in relying on income tax revenue than with developed countries in the OECD. In essence, South Africa's CIT tax rate at 28 per cent, compared well with many developing countries.

According to the Tax Foundation,[5] the worldwide average statutory CIT rate, measured across 180 jurisdictions, is 23.54 per cent. Asia has the lowest regional average rate, at 19.62 percent, while Africa has the highest regional average rate, at 28 per cent.[6] Notably, the G7, which is comprised of the seven wealthiest nations in the world, has an average statutory corporate income tax rate of 26.69 per cent.

Table 3: Average Corporate Tax Rate by Region or Group, 2021

Region	Average Rate
South Africa	28.0%
Africa	27.97%
Asia	19.62%
Europe	19.84%
North America	26.37%
Oceania	23.75%
South America	26.63%
G7	26.69%
OECD	23.04%
BRICS	27.40%
EU27	21.30%
G20	26.75%
World	**23.54%**

Source: Tax Foundation

Government is further arguing that many countries with strong investment and trading ties to South Africa have significantly lower rates, which provides a strong incentive for tax avoidance. Tax avoidance is a global phenomenon, and is largely a result of an outdated global tax system and lack of global political consensus to agree on suitable solutions for both developing and developed jurisdictions. PBO is concerned that the use

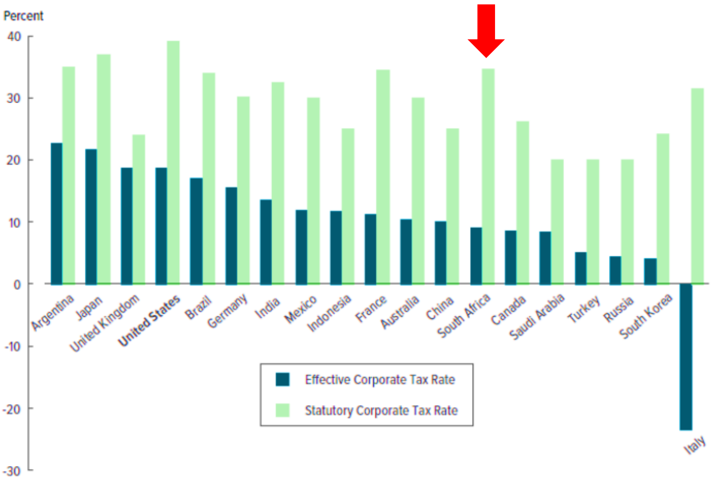
[5] The Tax foundation is an independent tax policy non profit

[6] Tax foundation, Corporate Tax Rates around the World, 2021

of lowering CIT rate will fail to resolve tax avoidance yet government will lose much need tax revenue.

The research evidence suggests that the focus should rather be on Effective Tax Rates, meaning the actual tax paid made by corporate tax payers. Despite the CIT rate of 28 per cent, the all-sector average Effective Tax Rate was 18.2 per cent, which was lower than many countries including advanced countries at the OECD. Some sector ETR are far lower, for e.g., the mining sector reported rates of lower than 13.7 per cent between 2005 and 2011.[7] The ETR in South Africa has remained significantly lower than the statutory rate as demonstrated by the Figure 2.

Figure 2: CIT G20 countries – Statutory Tax vs ETR- 2017 Stats



Source: CBO 2017

The Figure 2 data shows contrary to the 2022 Budget proposals; corporate taxpayers may not be overburdened by taxes. The data trends on CIT EFT is more concerning when taking into account tax burden and size of firm. Firm analysis by Carreras, Dachapalli, and Mascagni, published by UNU-WIDER shows that the relationship between burden and size is U-shaped.[8] In that SMMEs(by revenue) taxpayers bears highest ETR than larger (by revenue) taxpayers. The tax burden decreases to a minimum for medium-sized companies, while it increases slightly for the largest ones. The largest companies however, still face a lower tax burden than small corporations.

The question of whether corporate taxpayers pay their fair share of taxes will remain unanswered until the inequality in ETR are resolved. Tax avoidance is largely driven by the ability to aggressively plan for a reduced tax burden using legal loopholes. The PBO emphasises that it is important to focus on closing the loopholes.

4.2. Investment

The 2022 Budget outlines that the changes to CIT tax have significant impact on investor behaviour – influencing jobs, wages and prices – and can support economic growth. The recent PBO research and analysis has demonstrated that out of ten factors considered before investing, corporate tax rate was ranked only at number five as important factor to invest. The DTC noted that while South Africa's statutory corporate tax rate may be somewhat higher than that in other countries, the CIT tax system overall is not a major deterrent to investment. The DTC report further noted that countries that attract foreign direct investment by offering lower tax rates are not necessarily more competitive than countries with high tax rates.

The PBO is concerned that proposed reduction of CIT rate assume that the rate is a key consideration for investment, whereas other factors may be important – e.g. reliability and price of electricity, availability of skills, cost of labour, safety etc.

The PBO is further concerned that while the lowering of the statutory CIT rate has been proposed to encourages more domestic investment, the amendments to offshore investments policy limits seemingly contradict the goal of increased domestic investment.[9] The new proposals increase the foreign direct investment limit for companies investing funds offshore increase from R1 billion to R5 billion. In addition, authorised dealers may process transfers from the parent company to the domestic treasury management companies up to a maximum of R5 billion (an increase from R3 billion) per calendar year for listed entities. Lastly, the offshore limit for all insurance, retirement and savings funds is harmonised at 45 per cent inclusive of the 10 per cent African allowance. The previous maximum limits were set at 30 per cent or 40 per cent for different investors. The PBO is concerned that these offshore related policy proposals are likely to contradict the policy objective of CIT rate reduction. In particular, this might have negative effect on the net investment. In essence these measures may encourage further diverting investments from local entities.

5.3 Fiscal neutrality

The 2021 Taxation Laws Amendment Bill (TLAB) shows how the reducing CIT rate forms part of a reform package to broaden the tax base in an overall revenue neutral manner. The proposals made to "make-up" for the R2.6 billion that will be revenue forgone as a result of reduction in the rate the following will be implemented:

- Restrictions on the offsetting of accumulated assessed losses against taxable income; and
- There will be additional interest limitations.

In the proposed restrictions on the offsetting of accumulated assessed losses corporate taxpayers can only carry forward 80 per cent of such losses. In this way the 20 per cent will be subject to CIT. In the current form

[7] Davis Tax Committee(DTC): Macro Analysis First Report: December 2014

[8] WIDER Working Paper 2017/162. Effective corporate tax burden and firm size in South Africa.

[9] Budget Review 2022

the provision works like this; if a company made a profit equivalent to the company's previous years assessed losses, the profit would not be taxable. And the amendments would make sure that the 20 per cent of the profit will be liable to taxation. The current framework allows for the balance of assessed losses can currently be carried forward indefinitely. The Small, Medium and Micro Enterprises (SMMEs) taxpayers with a taxable income below R1million, are exempt from the amendments. The PBO believe the provision to protect SMMEs is necessary as it also maintains progressivity in the tax system.

The additional interest limitations entail broadening the definition of interest to include;

- payments made under interest rate swap agreements,
- the finance cost element of finance leases, and
- foreign exchange differences;

to curb the circumvention of the rules by using back-to-back loans and ensuring that the rules apply even if the interest is subject to interest withholding tax in South Africa. Unlike in the restriction of the assessed loss, it is unclear if SMMEs will be exempt from these changes.

The amendments proposed are in line with the Base Erosion and Profit Shifting (BEPS) project of the organisation for Economic Co-operation and development (OECD), recommendation that jurisdictions implement a mechanical rule to limit interest deductions. The PBO see these amendment as a positive approach which demonstrates South Africa's commitment to the BEPS project.

Effectively, the restrictions on the offsetting of accumulated assessed losses against taxable income and additional interest limitation measures limit the tax relief for corporate taxpayers have enjoyed in the past. While the amendments to assessed losses and interest limitations are a good measure, the PBO remains concerned about a use of such progressive measures to justify the lowering of the CIT rate. This therefore lead to a question is to whether fiscal neutrality[10] should be focus of tax policy given the current massive expenditure pressures as opposed to tax policy that attempts to increase revenue in a progressive manner? The PBO is remain concerned that lowering the CIT rate will negatively impact the government's ability to raise revenue through tax policy in the future?

The analysis shows that R5.2 billion more in revenue could have been the projected additional revenue for 2022/23 without the reduction in the statutory CIT rate. The PBO is concerned that the goal of fiscal neutrality is punitive on the fiscus given the current macroeconomic (fiscal policy) context. Maybe the proposal should be motivating for extra revenue generation that distributes income and wealth in a fair and equitable manner (both horizontally and vertically).

5. Proposed changes to Employment Tax Incentive (ETI)

Out of R5.2 billion tax relief announced in the 2020 Budget, R2.2 billion of is for the expansion of the ETI. The ETI Act was introduced in 2014 to allow expense deduction for every young unemployed being absorbed. This was to encourage employers to hire young and less experienced workers given chronically high unemployment rates for the youth. The ETI was subsequently renewed multiple times since its introduction. And as of 1 March 2022, the ETI allowable expense has been increased by 50 per cent from R1000 to R1500.

The 50 per cent increase means that the maximum of R1 000 will increase to a maximum of R1 500 per month in the first 12 months, and from R500 to a maximum of R750 in the second 12 months of eligibility. The table 4 summarises the proposed amendments to the ETI.

Table 4: New ETI Values effective from 1 March 2022

Monthly Remuneration	**Formula Up to 28 February 2022**	**Formula As of 1 March 2022**	**Formula Up to 28 February 2022**	**Formula As of March 2022**
	First 12 Months	**First 12 Months**	**Second 12 Months**	**Second 12 Months**
R0 to R1 999,99	50% of Monthly Remuneration	75% of Monthly Remuneration	25,0% of Monthly Remuneration	37,5% of Monthly Remuneration
R2 000 to R4 499,99	R1 000,00	R1 500,00	R500	R750
R4 500 to R6 499,99	R1 000 – (50% x (monthly remuneration – R4500))	R1 500 – (75% x (monthly remuneration – R4500))	R500 – (25% x (monthly remuneration – R4 500))	R750 – (37.5% x (monthly remuneration – R4 500))

Source: SARS

As anticipated, the ETI has supported jobs by subsidising wages. The support, which is seen as a positive impact, is documented in the research submitted to Nedlac. For example, the ETI has not led to a displacement of older workers in the workplace. Even though the program has not seen a full take up, businesses report that the support impacts positively on their profitability while they hire younger employees, particularly for SMMEs. However, despite the unanimous recommendations in the Nedlac, in 2016 and 2018, that the program should be extended, the real impacts of the ETI remain contested.

Various research evidence shows that generally the ETI has had little to no effect on creating employment for youth. However, the evidence shows that the ETI positively impacts business profitability, particularly SMMEs. But it remains unclear on whether the incentive saves jobs. The counterfactual, meaning what would have happened without the incentive, it has not been adequately substantiated to indicate that significance of the program. Despite the evidence, or lack of, the ETI

[10] Fiscal neutral; taxes that neither create nor lose revenue for the government

has been expanded and there remain continued calls to extend the program. The proposal within the Nedlac has been to extend the ETI by a further 5-10 years, the NT has proposed 5 years.

The ETI has been extended to 28 February 2029. The ETI has also been subject to abuse which has led to amendments to the ETI Act to impose understatement penalties on reimbursements that are improperly claimed. The PBO is further concerned about lack of evidence that ETI creates "decent jobs".

Youth unemployment continues to be a critical concern in South Africa. The Quarterly Labour Force Survey reports that the Youth aged 15-24 years and 25-34 years recorded the highest unemployment rates of 63.9 per cent and 42.1 per cent respectively. There were 3.8 million young people aged 15–24 years which were not in employment, education or training (NEET), which equates to 37 per cent of this demographic group.

In the context of rising youth unemployment, the PBO is concerned there lack of sufficient evidence to support the ETI. The PBO is concerned that the ETI could be seen to contribute to further inefficiencies of current corporate tax incentives. This is also given that the DTC had noted a need for government to review variety of corporate tax incentives. Aggregated actual ETI credits refunds were R7.2 billion in 2020/21 and R6.6 billion in 2021/22. With the ETI increasing by 50 per cent as of 1 March 2022, the value of revenue forgone value is expected to increase. The PBO proposes consideration that this revenue forgone be collected and the funds utilised to support real youth employment initiatives.

The PBO if further concerned that the distributional impacts of the ETI have been left unaddressed. For example, Black African and Coloured and Women are considered to be the most vulnerable in the labour market. Therefore, the PBO proposes that the evaluations and monitoring of the ETI should include an assessment on the distributional effects of the ETI along gender, geography, and disabilities to ensure that those who are most vulnerable in the market benefit from the incentive.

6.Other tax discussions/developments on the horizon

In the previous sections of this brief, the PBO mainly provided analysis of PIT, CIT and the ETI. In this section of the brief, the Office highlights other important tax matters on the horizon requiring Parliament oversight considerations.

6.1. Indirect taxes

Fuel Levy

According to the literature, fuel levy is considered to be a regressive tax instruments. The levy disproportionally impacts low income households. Low income households spend more of their income in transport than the rich. Similarly, informal business and Small Micro and Medium Enterprise (SMMEs) are disproportionately impacted by the fuel levy. For the first time in many years the 2022 Budget did not propose increase in fuel levy. The lack of increase in fuel levy provide significant relief for many households. This relief is important given that the fuel price has since increased significantly in response to deteriorating global and domestic macroeconomic conditions.

In addition, government proposed that there be no increases to the RAF levy. These measures will provide much needed relief to low income households that will not benefit from the relief provided through the PIT relief. In the face of rising inflation, these are welcomed measures.

VAT

The VAT was increased in 2018 with the expectation that the amendment would be reviewed in 2021. Given the COVID-19 disruptions, it is understandable that the review has not taken place however a review is needed. The reconsideration of zero rated items, for example, could provide further relief to households.

6.2. Green taxonomy

The first phase of the carbon tax will be extended by three years for the period 1 January 2023 to 31 December 2025. Parliament may request government to provide clarity on the impact of the low increase (1 cent per litre for petrol and diesel) on future increases to meet COP26 obligations.

The PBO has previously raised that climate fighting measures introduced by governments around the world must never disproportionally affect the low income households. When the South African government introduced the carbon tax in 2019, the intention was to avoid passing on the added cost of the carbon tax to consumers through higher electricity prices and more expensive goods. The 2022 Budget speech announcements have ensured that electricity prices will be buffered against the carbon tax until 31 December 2025. Therefore, PBO is concerned that distributional impacts, may have not been considered.

In 2022, the Climate Risk Forum, chaired by the National Treasury, will be publishing its green taxonomy and principles for effective climate-related disclosure. The PBO proposes that this paper should be presented to the Finance Committees for oversight purposes.

6.3. Multilateral institution tax amendments

The cabinet has approved the submission of the Multilateral Convention to Implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting (BEPS MLI) to Parliament for ratification. The multilateral treaty instrument enables its members to modify existing double tax treaties and to make provision for BEPS project outcomes that deal with aggressive tax planning which leads to treaty abuse, without having to renegotiate them individually. This is important because it can often take many years to renegotiate a single tax treaty that South Africa has with another country and, without the multilateral treaty instrument, effectively applying the outcomes of the BEPS project to the country's tax treaties would be very difficult.

South Africa is one of 95 countries that signed the BEPS agreement which seeks to reshape the global tax system in 2017 and its amendments in 2021. The agreements are set to come into effect in 2023. A number of developing countries have raised issues around the dispute resolution requirements. It is important that South Africa remains abreast of the issues that are being raised and to consider how we are effected by them. The issues raised should form part of reporting to Parliament and government providing clarity on how they will be resolved.

When South Africa signed the multilateral treaty instrument, it provided a list of double tax treaties covered by the multilateral treaty instrument. The list is made up of double tax treaties with more than 70 countries and jurisdictions, with the oldest treaty being that between South Africa and Israel which came into force in 1978, while the latest treaties came in to force in as recent as 2016 with Qatar, the UAE and other countries.

In its statement before signing the multilateral treaty instrument, South Africa declared that only double tax treaties would be affected by the provisions of the multilateral treaty instrument. As a result, it is unclear whether any multilateral treaties that South Africa is party to would immediately and directly be affected by the multilateral treaty instrument, except that the multilateral treaty instrument is, itself, the first multilateral treaty related to taxation matters.

6.4. Global Minimum Effective Tax Rate (METR)

The African Union has stated on several occasions, that the minimum effective tax rate (METR) should be at least 20 per cent to be effective in protecting African tax bases and stem Illicit Financial Flows (IFFs) by reducing profit shifting by multinational enterprises. The Tax Justice Network estimates that with the current 15 per cent minimum tax, South Africa could get $1.5 billion more in revenue, whereas at a statutory rate of 21 per cent, South Africa could get a projected revenue gain of $3.5 billion. In this regard, PBO proposes that government to reconsider and assess the current provisions against the potential to raise additional revenue.

The reconsideration of the 15 per cent METR for multinationals and how it intersects with South Africa's tax rates in the context of great revenue needs. The reconsideration should further take into account compliance and administrative costs related to implementation the tax measures. In this way, these costs should not be disproportionate to the policy objectives.

6.5. Wealth Tax

The South African Revenue Service has established a dedicated new unit focusing on high-wealth individuals. This process is in line with the DTC recommendation. In this way government is able to determine the level of wealth in control of taxpayers and give the significant inequality in South Africa. The World Bank has previously highlighted that 10 per cent of the population owns more than 80 per cent of the wealth. The additional information is expected to help in determining the levels and structure of wealth holdings as recommended by the DTC. In the interim, renewed focus should be turned on the wealth tax. The United Nations, for example, proposes wealth taxes as a response to global inequality with a particular focus on those who have disproportionately benefited from the crisis.

6.6. Gender dimensions of taxation policy

The National Treasury is working with other stakeholders to implement gender-responsive budgeting across government. This is expected to roll out in the 2023 Medium Term Expenditure Framework (MTEF) process. The PBO is concerned that the gender responsiveness is mainly limited to the expenditure side of the budget. The PBO is further concerned that while explicitly gender biased taxes were removed from the tax system, the South African literature has shown that there are discriminatory policies that are implicit within the tax system.

6.7. Tax Administration

According to government, SARS has made significant strides to improve its tax revenue collection over the last two of years. These improvements are a result of increasing human capacity (recruiting 490 additional staff) across various levels and skills areas, and investing in modernising its ICT infrastructure.

The Tax Ombudsman has raised some critical issues that warrant the attention of SARS, National Treasury and Parliament. A key issue that has been raised, is the legislative provisioning for the existence of the Tax Ombudsman. However, the governance and operational issues raised by the Tax Ombudsman are important to be considered and measures implemented to improve SARS administration. The PBO notes that the Tax Ombudsman is critical for the protection of taxpayers, which includes all those who pay direct and indirect taxes. Therefore, the PBO supports the Committees' decision to refocus on ensuring the legal status of the Tax Ombudsman.