



# TAX COMPLIANCE BURDEN FOR SMALL BUSINESSES:

## a survey of tax practitioners in South Africa

*'Tax compliance is becoming so complex that only wealthy people can afford it.'*  
*'I battle with the monthly paperwork. It takes too much time to pay all the taxes.'*  
*'Have one tax for small business to reduce the compliance and administrative burden. This will encourage more people to open businesses and create employment within SA.'*

- Comments from two tax practitioners surveyed

### Why worry about taxes on small business?

In South Africa the importance of small business as a creator of jobs, particularly for those with low skills level, is widely recognised. Small, medium and micro-enterprises contribute between 30% to 40% of the country's gross domestic product and employs 68.2% of the workforce in the private sector. In the agriculture, construction and retail sectors, these businesses employ more than 80% of the total workforce. Over the past few years, the growth in employment among small businesses has exceeded the growth in their contribution to GDP – in other words, helping small businesses contributes to job growth.

Red tape or unnecessary regulation can be a headache for any firm, but small firms have an especially hard time coping in this arena. Taxation and regulation costs for small businesses have been high up on the South African policy agenda in recent years. In the 2005 Budget Speech, Finance Minister Trevor Manuel stated the following:

*"...we have directed attention this year at the costs and complexity for small businesses of the tax code, because there is compelling evidence that simplified arrangements can assist significantly in creating an environment conducive to enterprise development."*

According to tax practitioners surveyed, about 60% of businesses with an annual turnover of R300 000 and less decide to stay informal rather than formalise their business operations. Government policy is meant to encourage formalisation of small businesses and tax compliance among businesses of all

sizes. The latest 'tax amnesty' led to about 250 000 new applications for registration to SARS, which (assuming they all stay active and file regularly) would represent nearly a 25% increase in the number of 'active' firms.

Small, medium and micro-enterprises are a huge part of South Africa's tax base. For every 10 000 active company taxpayers in the SARS database as of January 2007, only 3 are 'large' firms. To understand better the burdens faced by small firms as they pay taxes, the National Treasury and South African Revenue Service (SARS) requested a survey to:

- document estimated tax compliance costs for small businesses in South Africa;
- identify the most onerous compliance burdens based on these costs as targets for reform; and
- establish a baseline against which future progress can be measured.

### How much does tax compliance cost the average firm?

Overall the compliance costs are regressive – the smaller the business, the heavier the burden. The registration process is complicated and cumbersome. The following sets out the key survey findings:

- It would cost the average small business R1 478 to register (for four key taxes -- income tax, provisional tax, value added tax and employees' tax).
- R7 030 per annum is the average fee that tax practitioners charge their small business clients to ensure that tax returns for the four key taxes are prepared, completed and submitted as required by SARS.

- R12 185 is the average fee charged by tax practitioners to help small businesses with completing/maintaining their accounting/bookkeeping records. From 1/4 to 1/3 of the average tax practitioner's clients will purchase these services.
- Registering and preparing, completing and submitting VAT returns takes the longest, and costs the most of the four key taxes. The provisional tax is the most burdensome tax for small businesses.
- Firms are required to register for VAT if their turnover is R300 000 or greater.
- Case study: For a firm with an annual turnover of just over R300 000, that makes a 20% profit rate (about R60 000), the cost of registration alone (about R1 400) would be the equivalent of an extra 2.33% in profit tax. The annual costs for basic compliance – the cost of hiring an accountant to prepare tax returns for the four major taxes alone – amount to the equivalent of an additional 12% in profit tax (on top of the statutory profit tax of 29%).

### What reforms are needed?

Tax practitioners identified the most burdensome aspect of each of the four key taxes. They also decided which reform would help the most: see table opposite.

- SARS' service standards in respect of the following were also considered in the survey: receiving a registration number; processing tax returns; responding to objections; paying out of refunds; responding to written correspondence; answering telephone calls; and providing personal assistance and addressing enquiries sufficiently.

TAX	MOST BURDENSOME ASPECT OF TAX	REFORM TO REDUCE TAX COMPLIANCE BURDEN
Income Tax	Capturing and processing errors made by SARS and the time taken to correct these errors.	A special simplified income tax regime for small businesses.
Provisional Tax	Penalties and interest incorrectly raised by SARS.	A special simplified income tax regime for small businesses.
VAT	Period taken to register as a VAT vendor and the time taken to be notified of such registration.	Higher mandatory VAT registration threshold.
Employees' Tax	Capturing and processing errors by SARS and the time taken to correct these errors in respect of employees' tax.	A special simplified tax regime for small businesses.

- At this stage, SARS does not meet any of the intended standards set out in its Service Charter, with the exception of the time it takes to process tax returns and the time (as laid down in the tax law) it takes to respond to an objection. A follow-up report, in preparation, will provide provincial comparisons.

Other main areas of concern that were raised by the tax practitioners are as follows:

- SARS call centre is not operating as optimally as it could due to the following reasons:
  - personnel not trained and do not have the required knowledge; and
  - no direct access to assessors/person dealing with the specific query or who has the authority to make decisions.
- Taxpayers have no knowledge of whom to talk to regarding a particular issue/document as the person's name is not provided – this results in the call centre putting the taxpayer through to a person who is unable to respond to his/her query.
- Some SARS personnel not competent/capable of answering technical questions.
- Loss of some documentation by SARS, even if there is proof of receipt, is a problem.
- Penalties are sometimes too high, incorrectly raised and not consistently applied.

#### Critical areas for SARS' attention:

- The registration process needs to be simplified and streamlined with prompt and reliable notification to the taxpayer when SARS has completed their registration.

- The technical knowledge of SARS personnel needs to be improved.
- The call centre functionality needs to be improved.
- Payment of refunds to taxpayers need to be done in a timely manner to help businesses avoid unnecessary cash flow difficulties.
- Responses to written correspondence, answering of telephone calls, personal assistance and efficient handling of enquiries need to be done more quickly and with more accuracy.

#### Response from SARS

- Reforms and improvements addressing most of the concerns raised in the report are already in process, including designing a more streamlined VAT registration process, automated submissions, and tracking of objections and appeals.
- In order to address the issue of capturing errors, SARS notes that it is making electronic filing more accessible this year.
- SARS described the report as a "valuable yardstick against which to measure our strategic programme," with the possibility for repeat surveys to track progress over time.

#### About the survey

- The survey was prepared and carried out by FIAS, part of the World Bank Group, with the assistance of Sharon Smulders, a senior lecturer at the University of Pretoria, and a local survey company Bluetub Design and Production. The survey benefited from the co-operation of the South Africa Institute of Chartered Accountants (SAICA), the South African Institute of Professional Accountants (SAIPA), and the South African Institute of Certified Bookkeepers (SAICB). The Government of Switzerland co-financed the survey.
- It was designed to document the compliance experience of professional accountants and bookkeepers (referred to as "tax practitioners") from SAICA, SAIPA and the SAICB in respect of their small business clients in South Africa. The survey received responses from 3 429 tax practitioners from all provinces of South Africa, regarding their work for clients with a turnover of up to R14 million.
- The survey report is available on the FIAS website: [www.fias.net](http://www.fias.net).

#### For more information, please contact:

Ms Sharon Smulders  
Senior Lecturer - Department of Taxation  
University of Pretoria  
Tel: 012 420 4665  
Fax: 086 635 8570  
Email: [sharon.smulders@up.ac.za](mailto:sharon.smulders@up.ac.za)

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