A COMPARATIVE STUDY OF SOUTH AFRICAN SMALL BUSINESS CORPORATION TAX AND TURNOVER TAX

by

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Declaration

I declare that '*A Comparative Study of South African Small Business Corporation Tax and Turnover Tax*' is my own work and that all the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

I further declare that I have not previously submitted this work, or part of it, for examination at UNISA for another qualification or at any other higher education institution.

______________________ ______________________

Signature: A. Rahim Date

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Abstract

This study compared the turnover tax and small business corporation tax systems in South Africa as applicable to micro and small businesses. Misinformed perceptions of the turnover tax system were the motivation for this study. A three phase approach was adopted to conduct this study, the phases being literature review, in-depth face-to-face interviews and quantitative analysis of financial statements which are referred to as case studies. The tax liability was calculated for each of the thirty cases and thereafter a comparative analysis was performed to establish the most beneficial tax system for each case study. The findings for year one revealed that the small business corporation tax system was the most beneficial tax system for fifteen of the thirty cases and turnover tax for the other fifteen cases. Over an average of five years, fourteen cases benefited from the small business corporation tax system and sixteen from turnover tax. There were a number of significant reasons why the above mentioned tax systems were appropriate for each of the thirty cases, one of which being, the type of business or industry where the case is located. The information obtained from this study could inform small and micro businesses about the most appropriate and beneficial tax system for their businesses. In addition the information emanating from this study could be used by tax practitioners to advise their clients on the most appropriate tax system for their businesses. Lastly, the results of this study could contribute to the debate around legislation for small and micro businesses.

Keywords

Micro businesses, small businesses, turnover tax, small business corporation tax, simplified tax, compliance cost.

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LIST OF ACRONYMS

AAT - Association of Accounting Technicians South Africa
CC - Close Corporation
CFA - Chartered Financial Analyst
CGT - Capital Gains Tax
CPA - Certified Public Accountants
DTI – Department of Trade and Industry
FIAB - Fellow International Association of Book-keepers
FIAS - Foreign Investment Advisory Service
GAAP - Generally Accepted Accounting
GDP - Gross Domestic Product
GST – Goods and Services Tax
HMRC - HM Revenue & Customs
ICD - Investment Climate Department
IMF - International Monetary Fund
IFC - International Finance Corporation
OECD - Organisation for Economic Co-operation and Development
OTS - Office of Tax Simplification
PAYE - Pay As You Earn
PwC - PricewaterhouseCoopers
SAICA - South African Institute of Chartered Accountants
SAIM - South African Institute of Management
SAIPA - South African Institute of Professional Accountants
SARS - South African Revenue Services
SEDA - Small Enterprise Development Agency
SDL - Skills Development Levy
SME - Small Medium Enterprise
SMME - Small, Medium and Micro Enterprises
STC - Secondary Tax on Companies
UIF - Unemployment Insurance Fund
UK - United Kingdom
UNISA - University of South Africa
US - United States
USAID - United States Agency International Development

VAT - Value Added Tax

WBG - World Bank Group

ZIMRA - Zimbabwe Revenue Authority

ZRA - Zambia Revenue Authority

Chapter 1 : AN INTRODUCTION TO THE STUDY

1.1 INTRODUCTION

Small businesses are instrumental in ensuring economic growth that may lead to job creation, hence relieving unemployment and contributing to a decrease in poverty (Willemse, 2010), this was also mentioned by Government already in 1995 in the following statement: "With millions of South Africans unemployed and underemployed, the government has no option but to give its full attention to the fundamental task of job creation, and generating sustainable and equitable growth" (South Africa 1995). Despite Small, Medium and Micro-Enterprises (SMME) being an important vehicle to address the South African challenges of job creation, economic growth and equity in our country is not used effectively (SBP 2009). In the first quarter of 2014, South Africa's unemployment rate increased to 25.2% (Statistics South Africa 2014). By liberating small businesses, Government can play an active role in encouraging the establishment of small businesses (Gluckman 2012) which in turn will lead to a reduction of the high unemployment rate (Radebe 2008).

During the past couple of decades, Government has introduced various initiatives to promote the development of small businesses, for example the establishment of the Small Enterprise Development Agency (SEDA) and various tax legislation reforms to assist small businesses. Initially the Ntsika Enterprise Promotion Agency was incorporated as a public entity in terms of section 9 of the National Small Business Act 102 of 1996, and is mandated to provide non-financial support services to SMME's. The Act was amended in 2004 to merge Ntsika and the National Manufacturing Advisory Centre Trust to form SEDA. SEDA was established in December 2004 as an agency of the Department of Trade and Industry (DTI) mandated to assist all levels of Government to implement its small business development strategies (SEDA [s.a.]). In 2006 small business amnesty was introduced to encourage small businesses with a turnover of up to R10 000 000 a year to enter the tax system (Mkhize 2011). At this stage small businesses that were not up to date with their affairs were given the opportunity to

regulate their tax affairs after the establishment of tax amnesty (South African Revenue Service (SARS) 2006). Small businesses had to meet certain requirements and pay an amnesty levy ranging from 2% to 5% of their taxable income. Businesses whose tax affairs are up to date qualify for certain incentives and may apply for government tenders. Tax is therefore an important consideration for most small businesses.

According to Radebe (2008) and De Clercq, Tustin and Venter (2006), the Small Medium Enterprise (SME) sector represents more than 95% of formal businesses in South Africa, but contributes a negligible amount to Gross Domestic Product (GDP). Radebe argues that the cost of tax compliance is a hindrance to the development and growth of small businesses. In addition, Sajem (2008) has indicated that the annual cost of tax compliance for small businesses with an annual turnover of R1million or less, is almost 3% of their turnover. Various other studies were also conducted to identify and measure the tax compliance costs for small businesses in South Africa (Smulders 2006, Foreign Investment Advisory Service (FIAS) 2007, United States Agency International Development (USAID) 2008, Smulders & Stiglingh 2008, Rametse 2010, Willemse 2010, Ramusetheli 2011, Franzsen 2012, Coolidge 2012, Smulders, Stiglingh, Franzsen & Fletcher 2012), these will be discussed later on.

The majority of these studies found that tax compliance costs for small businesses were effectively a regressive tax. To alleviate this problem micro businesses (as defined) have the option to be taxed on their turnover therefore they will not have to go through the complex process of assessing the deductibility of expenses in accordance with the Income Tax Act, and will not need to appoint tax consultants to handle tax issues. Tax compliance risks in small businesses differ from that of larger businesses. Large businesses have access to tax consultants for tax advice to develop strategies for the reduction of their tax liabilities, while small businesses are more likely to engage in tax evasion practices (International Finance Corporation (IFC) 2008). Crawford and Freedman (2011) point out that due to the costs of complying with tax and other regulatory burdens that fall disproportionately on small

businesses, in the United Kingdom (UK) the highest levels of non-compliance being the sole traders and partnerships. FIAS reported that it costs the average small business R36 343 (2009 value) for a range of tax related services, including accounting services (Mkhize 2011).

Although taxation is an important factor to be considered when an entrepreneur establishes a business it is only one of the several factors such as start-up costs, legal liability, finance costs and government incentives. In South Africa there are various ways in which a business may be formed, firstly, as a sole proprietor, a partnership is another possibility, or a separate legal entity with the choice of a close corporation, company or a trust (Badenhorst-Weiss, Brevis-Landsberg, Cant, du Toit, Erasmus, Kruger, Machado, Marx, Mpofu, Rudansky-Kloppers, Steenkamp, Strydom & Vrba 2010). The decision to choose one of the above types of businesses is left to the individual who is establishing the business. The legal format of a business is important in the decision making process as this affects other factors like the tax position as well as the personal liability of the owner.

For example, a sole proprietorship is not a separate legal person; the owners receive all the profits and are taxed in their personal capacity, consequently, a sole proprietor is subject to income tax levied at the rates ranging from 0% to 40% on taxable income (SARS 2014b). Sole proprietors are also subject to Capital Gains Tax (CGT), but no tax is levied when they use the profit for personal expenses.

A partnership is not liable for income tax because each partner is taxed individually on their share of profits (which is included in the partners taxable income) at a tax rate ranging from 0% to 40%. The partners are effectively taxed in the same way as sole proprietors. Normal income tax is paid by individual partners and they are also subject to CGT (SARS 2014b).

For income tax purposes a Close Corporation (CC) is regarded as a company, with the taxable income being taxed on a fixed rate of 28% (SARS 2014b). If the CC

qualifies as a small business corporation or micro business they will be taxed on a sliding scale (refer to Annexure A for tax rates). CGT is also applicable to CC's and companies. Dividends tax is the individual shareholder's liability, at a rate of 15% and is levied on the distribution to shareholders (National Treasury 2012b). As can be seen from the discussion above the legal status of a business as well as their selection of which method to use to calculate their tax liability could have a significant impact on its tax liability.

This study compared the small business corporation tax and the turnover tax laws in South Africa as applicable to small or micro businesses. Pertinent tax legislation was consulted, specifically legislation affecting small or micro businesses as well as the tax systems available to small or micro businesses. The focus of this study was on the requirements, advantages, disadvantages and benefits of the small business corporation tax and turnover tax systems. Since small businesses should be promoted in South Africa, it is anticipated that the results of this study will shed light on the benefits of the various tax systems available to small or micro businesses using case study information.

1.1.1 Background to the Study

This study focuses on small business corporations and micro businesses and the two tax systems available provided all the criteria are met, namely the small business corporation tax and turnover tax. If they do not meet the criteria they will be taxed under the normal income tax system. South African legislation allows small or micro businesses to choose a tax system that is beneficial to them based on their own business activities. When choosing a tax system it must be remembered that the tax systems are subject to annual changes by National Treasury.

Although this study focuses on small businesses, it is important to note that there are various definitions for small businesses. SMME is not the same as a small business corporation for income tax purposes. For example, the latter is restricted to a close corporation or a private company while the former could be any person (Pancha 2004). FIAS (2007) found that "SMME" is sometimes used as a synonym for "small

businesses”. Small business corporation is regulated by the Income Tax Act No. 58 of 1962 (South Africa) while SMMEs are governed by the National Small Business Act, 1996 (South Africa).

The International Monetary Fund (IMF) (2007) developed a model for small business tax systems which was used to develop the turnover tax system, as the business grows it progresses to the small business corporations tax system and finally to the normal income tax system (discussed in Chapter 2).

There was a need in South Africa, prior to 2009, to simplify the tax system for small businesses (Gluckman 2012). This led to the turnover tax system being implemented with effect from 1 March 2009 and applicable in respect of years of assessment commencing on or after that date (South Africa 1962). Turnover tax is regulated by the Sixth Schedule and section 48 of the Income Tax Act No. 58 of 1962.

In order for a natural person or a company to qualify as a micro business (which allows it to be taxed under the turnover tax system), the qualifying turnover for the year of assessment should not exceed R1-million (South Africa 1962:263). A micro business will be liable for income tax into which CGT is incorporated; Value Added Tax (VAT), provisional tax and previously Secondary Tax on Companies (STC) and now dividends tax are substituted by one single tax (SARS 2010, SARS 2011). Since 2012 micro businesses were no longer barred from registering for VAT (National Treasury 2011).

A micro business is taxed on a sliding scale based on the qualifying turnover of the business (see Annexure A for tax rates). The turnover tax rates are lower than the current tax rates for individuals and companies, but it should be noted that the basis of calculation is different. The turnover tax system is not compulsory since micro businesses have to voluntarily register to use this system. Turnover tax was introduced to reduce costs and improve tax compliance, however, turnover tax may not always be as beneficial as it is thought to be. Careful deliberation and

calculations should be performed to assess the advantages of turnover tax for the business concerned (Hassan 2009). If a micro business does not qualify for turnover tax, tax relief is available if the business qualifies as a small business corporation.

To qualify as a small business corporation certain criteria discussed in Chapter 2 have to be satisfied. As with micro businesses, small business corporations are taxed on a sliding scale but based on the taxable income of the business (see Annexure A). The taxable income is based on the normal income tax principles as per the Income Tax Act but taxed according to the small business corporation tax table (South Africa 1962). In comparison with other companies small business corporations are entitled to section 12E deductions in terms of the Income Tax Act. Section 12E allows accelerated depreciation allowances for new assets that are used in the process of manufacture.

1.2 RATIONALE FOR THE STUDY

This study was undertaken in an attempt to fill the gap in existing literature on the practical application of the turnover tax system and small business corporation tax system. This is done by providing a detailed analysis of all the relevant sections of the Income Tax Act (South Africa 1962) relating to small business corporations or micro businesses and focused on the requirements, advantages, disadvantages, benefits and knowledge of the small business corporation tax and turnover tax legislation, as it applies in practice.

The turnover tax system only came into effect on 1 March 2009, and consequently there are many uncertainties regarding the practical benefits of this tax system. This study will provide insights into small business corporations and micro businesses investigating the tax systems available to them, as well as educating small business corporations and micro business owners.

Manuel (as referred to by SBP business environment specialists 2009) and Willemse (2010) agree that small businesses are an important segment of the economy. Pancha (2004) identified finance as the greatest stumbling block for the development for SMME's. There is extensive tax literature on small business corporations internationally, to name a few: Arendse, Karlinsky, Killian and Payne (2007), Crawford and Freedman (2011), IFC (2007, 2008), IMF (2007), Investment Climate Department (ICD) (2009), Organisation for Economic Co-operation and Development (OECD) (2004, 2007, 2008, 2011), Office of Tax Simplification (OTS) (2012); however, local literature is limited. In addition, only limited studies have been conducted and articles written in South Africa on the turnover tax system. Studies have been conducted and articles have been written by BDO Spencer Stewart (2009), Coolidge (2012), Du Toit (2012), Gluckman (2012), Hassan (2009), Mkhize (2011), Pancha (2004), Radebe (2008), Ramusetheli (2011), Timm (2013), Willemse (2010) and Smulders *et al* (2012). Limited comparative studies could be identified on the turnover tax and the small business corporation tax system, therefore literature on previous research on this topic is limited. Because the turnover tax system only came into effect on 1 March 2009, there are many uncertainties regarding this tax system. A need arises for this study as no comparative study has been conducted on the turnover tax system and small business corporation tax system thus far.

1.3 STATEMENT OF PURPOSE

The purpose of this study is to identify which of the two tax systems, namely small business corporation tax or turnover tax applicable to small and micro businesses is more beneficial in specific practical situations.

1.3.1 Objectives of the Study

The following objectives assisted in achieving the purpose of the study:

Doctrinal research was performed on past research and relevant legislation.

Case studies were analysed and the tax expenses calculated for each of the 30 case studies selected for this study.

In-depth face-to-face interviews were conducted, to obtain data on knowledge and experience of tax practitioners.

1.4 RESEARCH QUESTIONS

The study was guided primarily by the following question:

Which of the two tax systems, namely small business corporation tax or turnover tax, provide the most beneficial tax dispensation to small or micro businesses?

The following questions contributed to answering the main question:

- What are the tax legislation requirements and benefits applicable to micro and small business corporations?
- What are the tax practitioners and tax representative views of the benefits and limitations of the small business corporation tax and turnover tax systems?
- What is the tax payable using the different tax systems in the selected case studies?

Having identified the questions that will guide this study it is necessary to present the research design of this study.

1.5 THE RESEARCH DESIGN

This study followed a three phase approach, the first being that of a literature review, the second phase was in-depth face-to-face interviews and the third phase was the quantitative analysis of financial statements which are referred to as case studies. The quantitative calculations (case study) and the qualitative method were chosen as it was applicable to the aims of the study, which were to identify which of the two tax systems referred to above is more beneficial to the selected small business corporations and micro businesses. Phase one of the study involved the reviewing of various sources such as legislation, previous research on the topic, journal articles, Internet sources and books published internationally and in South Africa. The

qualitative method, phase two was used to gain insight into the beliefs and understanding of tax practitioners and a tax representative regarding the two tax systems. Lastly, phase three used the quantitative method to calculate the tax expense incurred by each case study. The data collection methods are discussed in the next section.

1.5.1 Methods of Data Collection

The doctrinal research method was used in phase one to examine the Income Tax Act and other legislation pertaining to small or micro businesses. For phase two a convenience sample was drawn in order to perform in-depth face-to-face interviews with research participants (tax practitioners and a tax representative) who agreed to participate in this study. Interviews were used to establish the limitations of the tax systems, identification of the difficulties such as administration and tax difficulties encountered by small and micro businesses. The interview took the form of a semi-structured open ended interview. Quantitative data collection for phase three took the form of documents obtained using a convenience sample. The primary method of data collection was the case studies (using depersonalised financial statements). The financial statements of the case studies were used to calculate the tax expense of thirty small businesses applying the different tax systems.

1.5.2 Data Analysis

During phase one legislation pertaining to small business corporations and micro businesses was analysed to identify issues related to clarifying the requirements for taxation of small or micro businesses. Data from interviews in electronic format were transcribed and analysed using thematic content analysis (Patton 2002). The data collected for phase three were analysed using quantitative analysis. The financial statements of each case study were analysed to identify the type of business, recalculate the tax expense for all three tax systems, namely the turnover tax, small business corporations tax and the normal income tax system and lastly to identify which of the three tax systems is most beneficial to the business once all the criteria as per the Income Tax Act are satisfied. Lastly, the findings of this study have to be authenticated in order to improve the reliability and validity of the study. Reliability

and validity of the study is necessary in order to make the work pertinent (Kalof, Dan & Dietz 2008). A detailed description of the research design is found in Chapter 3.

1.6 STRUCTURE OF THE RESEARCH REPORT

The dissertation is structured into six chapters. Below is a description of the structure of this dissertation.

1.6.1 Chapter One: Introduction

This chapter introduces the study, by stating the purpose and objectives of the study with a brief discussion of the background, rationale, research questions and research design.

1.6.2 Chapter Two: Taxation of Small Businesses in South Africa

An overview of the relevant literature consulted for this study is presented in this chapter, in addition legislation underpinning tax laws were reviewed for this study. The literature reviewed provides a background to turnover tax and small business corporation tax. The advantages, benefits and disadvantages are discussed including a brief history of the small business corporation tax system. The literature reviewed included compliance costs, e-filing and the Constitution which formed part of this chapter, concluding with the evaluation of South African tax policies for SME's against international best practice. The Davis Tax Committee proposal was released after the completion of the literature chapter and therefore was not taken into consideration when completing the literature review.

1.6.3 Chapter Three: Research Design and Methodology

The research design and methodology is discussed in this chapter and deals specifically with the methodologies used for the data collection of this study. Data collection and data analysis is also discussed. The sample size, participants and their credentials are presented, followed by reliability and validity and ethical

considerations. Since the Davis Tax Committee proposal was released after the completion of the research design and methodology, its proposed changes were not used when analysing the case studies, however, a paragraph containing the analysis using the Davis Tax Committee proposal may be found in Chapter 5.

1.6.4 Chapter Four: Findings and Analysis of Interviews

The results and findings of the qualitative component of this study are presented. A description of how the raw data was handled is clarified. Included are the themes that emerged from the analysis of the raw data.

1.6.5 Chapter Five: Analysis and Findings of Case Studies (Financial Statements)

Chapter Five presents the results and research findings of the thirty case studies. Included in this chapter are analysis of the financial statements, the tax calculations and the tax system that is most beneficial to the case study once all the requirements of the Income Tax Act are satisfied. A discussion of the Davis Tax Committee proposal is presented in this chapter.

1.6.6 Chapter Six: Conclusions and Recommendations

The conclusions emanating from the findings are presented. Recommendations for tax practitioners and the National Treasury are made in this chapter as well as recommendations for future study.

The next chapter will discuss the literature and legislation that was consulted for this study.

Chapter 2 : TAXATION OF SMALL BUSINESSES IN SOUTH AFRICA

2.1 INTRODUCTION

This chapter will discuss the legislative requirements and benefits applicable to micro and small business corporations in terms of the Act. The purpose of this chapter is to describe the two tax systems, namely small business corporation tax and turnover tax that may be used by small or micro businesses in South Africa.

In addition to placing the study in context, the literature consulted provides clarity and underpins certain claims made regarding tax in relation to small business corporations and micro businesses. This chapter will show how existing studies refine or add to literature (Merriam 1998). The basis of this discussion derives from studies conducted globally as well as locally (South Africa).

A discussion of the theoretical framework follows in section 2.2 to identify which businesses qualify to be taxed according to the turnover tax system (dealt with in section 2.3), or the small business corporation tax system (dealt with in section 2.4). Small and micro businesses face many challenges, compliance costs being one (section 2.5). SARS has introduced e-filing, discussed in section 2.6, in an attempt to reduce compliance costs by assisting taxpayers with the submission, payment and queries related to tax returns. The theoretical framework which forms the basis of this study is discussed in the next section.

2.2 THEORETICAL FRAMEWORK

This chapter presents the theoretical framework utilised for this study. In developing the theoretical framework for this study, international best practice was used. Taxation in the global arena is necessary to examine taxation of small and micro businesses internationally. There are several sources of literature that evaluate and compare the small business corporation and turnover tax systems individually,

however, there are limited sources of literature that compare the tax implications and benefits of the two tax systems and therefore it is important to fill this gap. This study aims to fill the gap.

It is necessary to benchmark the appropriateness of the tax on micro and small businesses against international best practice. There is no single approach applicable to all situations when countries design a tax system for small businesses, due to the small business sectors' "heterogeneity" (IMF 2007:2). Nonetheless, international research suggests that there are key features that should be considered when designing a tax system for micro and small businesses. The tax system for micro and small businesses needs to be simple, administrable and equitable (ICD 2009).

The key features for designing a tax system are (international best practice):

- Tax systems should assist the formation and progression of small enterprises (IFC 2007).
- A good tax system must be fair (Hansford & McKerchar 2010).
- Tax systems should be easy for small businesses to ensure that tax compliance costs are minimal (IFC 2007).
- Tax systems should be designed to encourage micro and small businesses to formalise, which is to register for taxes, keep accounting records and comply with laws and legislation (IFC 2007).
- Tax systems should facilitate their integration into the formal sector from a micro business upwards to a big business (OECD 2004).
- Tax systems should promote growth and encourage the re-investment of profits in the business (IFC 2007).
- The taxpayer's capacity and skills in accounting and record keeping should be considered (ICD 2009).
- The costs of dealing with small taxpayers must be kept to a bare minimum for the tax authorities (ICD 2009).
- Transparent and equitable application of tax legislation (OECD 2004).

- Separate taxpayers into different groups for distinct special tax treatment (IMF 2007). The eligibility criteria must not be complex (Arendse *et al* 2007). VAT threshold should be used for separating taxpayers into groups (IMF 2007). Turnover is the simplest way to separate taxpayers (ICD 2009, IMF 2007).

- Determine the tax treatment to be applied to each group (IMF 2007).

- The compliance burden as well as the administrative burden for the tax authorities should be kept as low as possible (IFC 2007).

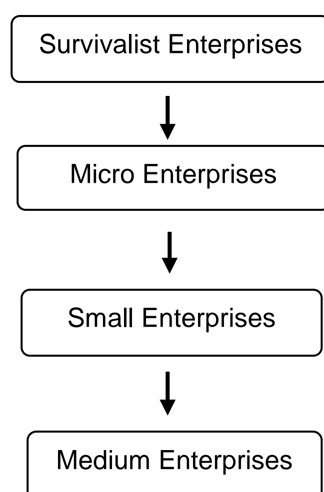
- A patent system (lump sum amount regardless of businesses profit) which should replace regular income tax for survivalist enterprises (IMF 2007, IFC 2009).

- A lump sum deduction based on a percentage of the turnover should be allowed for inventory purchases (OECD 2007).

- A presumptive tax system for micro businesses (IMF 2007, IFC 2007, ICD 2009).

Businesses differing in size require different tax treatment (ICD 2009). South Africa has three tax systems namely turnover tax, small business corporation tax and the normal income tax system. The IMF (2007) and ICD (2009) identified the tax hierarchy as follows, micro enterprises, small enterprises and medium enterprises. Using the IMF (2007) study the South African tax hierarchy may be summarised as:

Figure 1: South African tax hierarchy



Survivalist enterprises are not taxed, the turnover tax system is for micro enterprises, the small business corporation tax system for small enterprises followed by the standard (normal income) tax system for medium enterprises. The structure of this study uses this hierarchy to discuss the turnover tax system followed by the small business corporation tax system, and finally the normal income tax system.

Further insight into the turnover tax system and the small business corporation tax system will be gained by reviewing past research and legislation pertaining to small business corporations and micro businesses. International studies as well as local studies are discussed below. Many studies were conducted internationally on small businesses, in the United States (US) (Roach 2010, Crawford & Freedman 2008), UK (OTS 2012, Freedman 2003), Canada (Du Toit 2012, Evans, Hansford, Hasseldine, Lignier, Smulders & Vaillancourt 2014) and Russia (Preobragenskaya & McGree 2004, PwC & IFC 2013).

There appears to be a dearth of literature pertaining to turnover tax internationally, however, there is considerable literature available on small business tax. Turnover tax in the international context equates to presumptive tax, sales tax or VAT which is tax on the sale of goods or services (GST) (Annacondia & van der Corput 2011). A need for a presumptive tax system was identified internationally, in this regard South Africa introduced the turnover tax system (IMF 2007, IFC 2007 and ICD 2009). The aim of this tax system is to ensure businesses participate in a tax system, perform basic record keeping procedures and reduce the compliance burden (OECD 2007, IFC 2007). This presumptive tax system should replace VAT and other turnover based taxes (IFC 2007, IMF 2007). Businesses should be given the option to elect the presumptive tax system and professionals should not be included in this tax system (IFC 2007). The international framework motivates the need for the turnover tax system. A discussion of South African legislation pertaining to turnover tax follows.

2.3 THE TURNOVER TAX SYSTEM

2.3.1 Introduction

A presumptive turnover tax system for micro businesses with a turnover of R1 million or less (National Treasury 2008) was introduced by Trevor Manuel, the Minister of Finance during 2008. Turnover tax is an alternative to the normal income tax and VAT based system (National Treasury 2008). The aim of turnover tax in relation to micro businesses is to reduce corporate tax, as well as to reduce compliance costs (SARS 2008, Tustin, Abrie, Basson, De Clercq, De Hart, Doussy, Graham, Hamel, Howell, Olivier, Posthumus, Steyn, Swanepoel, Ungerer, Venter, & Wentzel 2005). Before turnover tax had been introduced a number of tax returns were required to be completed. The introduction of turnover tax obviates the time spent on completing the number of different tax returns (SARS 2008). Additionally, the turnover tax system was introduced to encourage growth and formalisation of micro businesses (SARS 2008). In order to qualify as a micro business there are requirements that a business has to meet to comply with the Income Tax Act. These requirements are discussed below.

2.3.2 Tax Legislation for Micro Businesses

Turnover tax is regulated by the Sixth Schedule and section 48 of the Income Tax Act No. 58 of 1962. For a natural person or a company to be eligible as a micro business, the qualifying turnover for the year of assessment should not exceed R1-million (South Africa 1962:263). Qualifying turnover may be defined as the total receipts from conducting business activities, excluding any amount of a capital nature; and amounts exempt from normal tax in terms of section 10(1)(*y*) (any government grant or government “scrapping payment" as per the Income Tax Act received or accrued) and 10(1)(*z*A) (rebate or assistance received or accrued for the promotion or financing of exports), 10(1)(*z*G) (any amount received or accrued to promote the production of films) and 10(1)(*z*H) (any amount received or accrued from the State) (that is total gross income excluding amounts of a capital nature) (South Africa 1962:263).

If business is conducted during the relevant year of assessment for a period of less than 12 months, the R1 million is reduced proportionally, taking into account the number of months that it did not conduct business during that year, where a fraction of a month counts as a full month (South Africa 1962:263). A micro business is taxed on a sliding scale based on the taxable turnover (refer to section 2.3.2.2) of the business (see Annexure A for tax rates). The turnover tax system is less burdensome than the income tax system (SARS 2012).

In comparison to the other tax systems in South Africa, turnover tax is less complicated to calculate, micro businesses do not have to hire a tax consultant to deal with tax issues (Radebe 2008). Micro businesses may however, be liable for tax even if losses are incurred, as this tax is levied on taxable turnover and not on taxable income. The use of the turnover tax system is not compulsory since micro businesses have to voluntarily register to use this system. Previously a micro business would have to deregister from VAT, if the business is registered as a VAT vendor, however, since 1 March 2012, qualifying micro businesses are allowed to be registered for both VAT and turnover tax (National Treasury 2011). The VAT system requires a business to keep supporting documentation thus increasing administration (Kearney 2003) and reducing the cost saving benefit of this system.

Zimbabwe introduced a presumptive tax system in 2005 which was further enforced in 2011 to widen the revenue base, it was identified that the system was not implemented effectively and there is room for improvement on implementation and administering by Zimbabwe Revenue Authority (ZIMRA) (Mashiri & Mazhindu 2013). As with South Africa, the presumptive tax in Zimbabwe and Zambia was introduced to encourage informal sectors and businesses to register on a tax system (ZIMRA 2014, Zambia Revenue Authority (ZRA) 2013). Each sector is levied a different tax on a quarterly basis, for example: taxi cabs $100 per vehicle, goods vehicles more than 20 tonnes is $2 500 per vehicle, hairdressing salon is $1 500, cottage industry is $300 (ZIMRA 2014). Mashiri and Mazhindu (2013) recommended that informal traders in Zimbabwe should be educated on why they should pay taxes due to their negative attitude and the fact that presumptive taxes should encourage the informal

sector businesses to move to the formal sector. Thresholds need to be revised in order to be in line with the current economic environment (Mashiri & Mazhindu 2013).

As mentioned above Zambia also introduced a presumptive tax system. Zambia's presumptive tax system is based on the vehicle's sitting capacity and is levied annually, for example a 64 seater and above is levied K7 200 per vehicle and below 12 seater K600 per vehicle (ZRA 2013). In Zambia, businesses with turnover below K200 million pay 3% tax, the presumptive tax system is said to be simple, and the effective tax rate encourages small businesses (Stern & Barbour 2005). A discussion of VAT follows.

2.3.2.1 Value Added Tax (VAT)

Micro businesses are liable for VAT if registered as VAT vendors. VAT is complex to calculate, costly and time consuming (The World Bank 2011, Chamberlain & Smith 2007, Barbone, Bird & Vázquez Caro 2012). When deregistering for VAT, output VAT (exit VAT) is required to be paid on the value of the assets held before deregistering; this can be paid over a six month period (South Africa 1991). SARS allowed a relief of up to R100 000 of the value of the assets held by that business prior to deregistration as the business has to deregister to comply with the turnover tax requirements (SARS 2011). This was the VAT relief granted to micro businesses that applied to deregister in order to register for turnover tax. As with every tax system there are special inclusions and exclusions, turnover tax is levied on taxable turnover. Therefore it is important to discuss the special inclusions and exclusions to taxable turnover.

2.3.2.2 Special Inclusions and Exclusions in Taxable Turnover in terms of the Income Tax Act

The Sixth Schedule of the Income Tax Act (South Africa 1962:264), specifically includes in taxable turnover:

(*a*) 50 percent of all receipts of a capital nature from the disposal of-

(i) Immovable property mainly used for business purposes; other than trading stock; and

(ii) any other asset used mainly for business purposes, other than any financial instrument; and;

(*b*) in the case of a company, investment income (other than dividends and foreign dividends).

Upon the disposal of immovable property, only 50 percent of the portion used for business purposes is included in taxable turnover (par. 6(*a*)). If an asset or immovable property is used mainly for business purposes, only 50 percent of the receipt will be included in taxable turnover.

If the total dividend paid by a micro business does not exceed R200 000 for a specific year of assessment, a shareholder in a registered micro business is exempt from the new dividends tax (South Africa 1962). If the total dividend exceeds R200 000, an exemption of up to R200 000 for the shareholder will apply (South Africa 1962).

As mentioned above, as per the Sixth Schedule of the Income Tax Act (South Africa 1962:264) the following is excluded from taxable turnover:

(*a*) in the case of a natural person, investment income;

(*b*) any amounts exempt from normal tax in terms of section 12P;

(*c*) any amounts received by that registered micro business where that amount accrued to it prior to its registration as a micro business and that amount accrued was subject to tax in terms of this Act; and

(*d*) any amount received by that registered micro business from any person by way of a refund in respect of goods or services supplied by that person to that registered micro business.

"A natural person is any biologic entity of the species Homo sapiens" (Pitt & Bale 1995) while Skinner (1999) defined a natural person as someone capable of representing themselves. Generally a natural person for tax purposes can be defined as a living human being.

Amounts that do not constitute taxable turnover, for example, remuneration and investment income (received by natural persons), are taxed in the individual's hands according to normal tax provisions and are excluded from taxable turnover

(Gluckman 2012). The inclusions and exclusions will increase or decrease the amount of tax payable which could be perceived as an advantage or disadvantage depending on the nature of the business. A discussion of the disadvantages of turnover tax is provided next.

2.3.3 The Disadvantages of Turnover Tax

One of the disadvantages of turnover tax is that a business will be disqualified from registering for turnover tax if the receipts from the disposal of capital assets exceed R1 500 000 over a three year period, which covers the year of assessment during which the capital proceeds were received and the preceding two years (South Africa 1962). The business will have to deregister immediately and will have to use the small business corporation or the normal income tax system. This means the business would not have kept records of the transactions for the period it was on the turnover tax system, as it is not a prerequisite to retain transaction history with the turnover tax system (SARS 2012, Tustin, De Clercq & Venter 2006) which could disqualify it for certain deductions for example wear and tear allowance.

If a micro business deregisters due to its turnover exceeding the R1 000 000 limit, that business will have to register as a VAT vendor (if not already registered) from the date that deregistration for turnover tax takes effect (South Africa 1991). Again, it is unlikely that records of the transaction history would have been maintained. Most large businesses prefer to deal with VAT vendors (Mkhize 2011). A taxpayer must notify SARS within 21 days if its qualifying turnover exceeds or is expected to exceed R1 million for the year of assessment or if the taxpayer no longer meets the criteria as described in section 2.3.2 above, SARS will then register the taxpayer on the normal tax system (SARS 2012, De Clercq *et al* 2006). If a micro business registers as a VAT vendor, VAT will have to be accounted for on taxable supplies after becoming a vendor and input tax credits can be claimed from SARS on certain expenses (Mkhize 2011).

Another disadvantage with the turnover tax system is that certain people and businesses do not qualify as a micro business as defined in paragraph 3 of the Sixth Schedule of the Act (1962:263):

(*a*) that person at any time during that year of assessment holds any shares or has any interest in the equity of a company other than a share or interest described in paragraph 4;
(*b*) more than 20 per cent of that person's total receipts during that year of assessment consist of
(i) where that person is a natural person (or the deceased or insolvent estate of a natural person that was a registered micro business at the time of death or insolvency), income from the rendering of professional service; and
(ii) where that person is a company, investment income and income from the rendering of a professional services.
(*c*) at any time during the year of assessment that person is a "personal service provider" or a "labour broker", as defined in the Fourth Schedule, other than a labour broker in respect of which a certificate of exemption has been issued in terms of paragraph 2 (5) of that Schedule;
(e) the total amounts received by that person from the disposal of-
(i) immovable property used mainly for business purposes; and
(ii) any other asset of a capital nature used mainly for business purposes, other than any financial instrument,
exceeds R1.5 million over a period of 3 years comprising the current year of assessment and the immediate preceding two years of assessment, or such shorter period during which that person was a registered micro business;
(*f*) in the case of a company-
(i) its year of assessment ends on a date other than the last day of February;
(ii) at any time during its year of assessment, ay holder of shares in that micro business is a person other than a natural person (or the deceased or insolvent estate of a natural person);
(iii) at any time during its year of assessment, any holder of shares in that micro business holds any shares or has any interest in the equity of any other company other than s share or interest described in paragraph 4: Provided that the provisions of this item do not apply to the holding of any shares in or interest in the equity of a accompany, if the company –
(*aa*) has not during the year of assessment-
(A) carried on any trade; and
(B) owned assets, the total market value of which exceeds R5 000; or
(*bb*) has taken the steps contemplated in section 41 (4) to liquidate, wind up or deregister: Provided further that this paragraph ceases to apply if the company has at any stage withdrawn any step so taken or does anything to invalidate any step so taken, with the result that the company will not be liquidated, wound up or deregistered;
(iv) is a public benefit organisation approved by the Commissioner in terms of section 30; or
(v) it is a recreational club approved by the Commissioner in terms of section 30A;
(*g*) in the case of a person in a partnership during that year of assessment-
(i) any of the partners in that partnership is not a natural person:
(ii) that person is a partner in more than one partnership at any time during that year of assessment: or
(iii) the qualifying turnover of that partnership for that year of assessment exceeds the amount described in paragraph 2.

A partner in a partnership may elect to register for turnover tax, that partner will be liable for the turnover tax on their share of the taxable turnover of the partnership, while the other partners will be liable for normal tax, therefore the partnership will

have to comply with all the tax compliance requirements. Each partner may elect the tax system that they want their share of taxable income to be taxed on, the partnership as a whole will have to abide by the rules and regulations of each of the tax systems elected.

In essence, any company, close corporation or co-operative that has a February year-end, whose turnover for the year of assessment is less than R1 million and does not provide personal services or professional services may be a micro business (e.g. sells goods) and opt to use the turnover tax system.

> *Disqualified professional services, including any services in the field of accounting, actuarial science, architecture, auctioneering, auditing, broadcasting, broking, commercial arts, consulting, draftsmanship, education, engineering, entertainment, health, information technology, journalism, law, management, performing arts, real estate, research, secretarial services, sport, surveying, translation, valuation or veterinary science*
>
> (BDO Spencer Stewart 2009)

From the a foregoing quotation, it is difficult to conceive which service activities would qualify as a micro business therefore it is anticipated that these exclusions may discourage micro businesses from using the turnover tax system, due to the uncertainty of meeting the criteria of a qualifying micro business (BDO Spencer Stewart 2009, Gluckman 2012, Willemse 2010). A taxi business would qualify as a micro business, however, a taxi business would have substantial costs such as leasing charges, wear and tear, insurance, repairs, maintenance, wages, if not on an owner driver basis, and fuel, which would considerably dilute any benefit of tax savings (BDO Spencer Stewart 2009). Willemse (2010, 2012) concluded that a professional service is any service rendered ignoring qualifications and accreditations.

A specific anti-avoidance rule, the turnover of connected persons' business activities will be added together for the purposes of applying the turnover limit of R1 million, even though those businesses may be in separate incorporated businesses (SARS 2011). The Act defines a connected person as a relative (family member), trust, beneficiary, a partner of a partnership, a member of a close corporation or a company. In the case of a company it would only be regarded as a connected person if the company forms part of the same group of companies, if an individual or

company who individually or jointly owned, holds at least 20% of voting rights (South Africa 1962).

A major disadvantage of the turnover tax system to micro businesses is that the micro business is not entitled to the benefit of an assessed loss (Mkhize 2011). In terms of section 20(2) of the Act "an assessed loss is any amount by which the deductions admissible under section 11 exceeds the income in respect of which they are so admissible". As the taxpayer is not able to utilise the assessed loss in the turnover tax system, the taxpayer would benefit from using the normal income tax or small business corporation tax system as opposed to the turnover tax system (Mkhize 2011).

However, in Gluckman's (2012) opinion the turnover tax system is not a fair system. He discusses the "unfairness" of the turnover tax system, the main point he identifies is that if an individual belongs to a certain profession as discussed above, automatic prohibition from turnover tax is unfair. However, if an individual belongs to one of the above mentioned professions, it does not mean that he is able to afford to pay taxes and comply with the Income Tax Act (Gluckman 2012). Gluckman (2012) raised another point that all sectors are taxed at the same rate, yet different expenses are incurred by the different sectors. The turnover tax system allows no deductions to compensate for the expenses incurred.

With regard to partnerships, the collective income of all partners must not exceed R1 million. The turnover tax system does not consider the wealth of the individual partners and consequently the partnership is taxed as a whole, however, the partnership may not have the ability to shoulder the responsibility of the tax payments (Gluckman 2012). Despite the fact that one or more of the partners may be affluent, it is not a premise for a tax liability. By using the four maxims as advanced by Smith (1776), Gluckman's (2012) research provided evidence that turnover tax is not entirely fair. The four maxims that Gluckman (2012:7) used are:

> *The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is in proportion to the revenue which they respectively enjoy under the protection of the state*

The tax which the individual is bound to pay ought to be certain and not arbitrary and the fact that the time of payment, the manner of payment and the quantity to be paid, ought all to be clear and plain to the contributor and to every other person

Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it

Every tax ought to be so contrived as to take out of the pockets as little as possible, over and above that which it brings into the public treasury of the state.

Gluckman (2012:14) used four words to describe these maxims "equity, certainty, convenience and simplicity/efficiency". Using the maxims above, Gluckman (2012) discussed the first maxim that tax is paid on a proportional basis and not a progressive one, the taxpayer should be able to afford the tax due and tax should be charged based on revenue. Both turnover tax and small business corporation tax are not proportional but are progressive tax systems. The turnover tax system does not factor in the taxpayers ability to afford the tax due, as turnover tax is based on the business' taxable turnover and not taxable income. In addition, a business in an assessed loss position could still be liable for taxes on the turnover tax system.

A micro business has the option to voluntarily deregister for turnover tax. The micro business may however, only voluntarily deregister before the beginning of the year of assessment (March) or at a later date prescribed by the Commissioner, by notice in the Gazette (SARS 2012). Taxpayers that exit the turnover tax system on a voluntary or compulsory basis will not be allowed to re-enter the turnover tax system. Only 7 700 businesses have registered for the turnover tax system since 2009 (SARS 2011), this is a possible result of the disadvantages associated with the turnover tax system. Despite these disadvantages there are however, certain benefits to using the turnover tax system that are discussed in the following section.

2.3.4 Benefits of Turnover Tax

The benefits of the turnover tax system are: record-keeping is reduced; simpler compliance requirements; decrease in costs of accountancy services; possibly a lower tax burden as the system has its own tax scales; in addition, turnover tax effectively replaces CGT and VAT (Willemse 2010). However, as from 1 March 2012 micro businesses that register for VAT will not be barred from registering for turnover

tax, as the legislation has been amended by Parliament (National Treasury 2011). The VAT exclusion removes a huge administrative burden from micro businesses, because the VAT system requires detailed record keeping, which micro businesses do not have to do (if not registered as VAT vendors). If a micro business registers for VAT, the costs of the business record keeping and accountancy services will not reduce to the extent of the cost of a business that is not registered for VAT (Hassan 2009).

Micro businesses are required to keep minimal records, such as: all the amounts received by the business for each year of assessment; all dividends declared for the year of assessment; records of all assets with a cost price of more than R10 000 each; and records of all liabilities that exceed R10 000 for the financial year (SARS 2012). Thus as tax is based on turnover, proof of expenses does not have to be kept. "These measures will significantly reduce paperwork for small businesses,"(Manuel as referred to by Radebe 2008:1). Although micro businesses are required to keep minimal paperwork, if a micro business turnover approximates R1 million turnover, the business could incur a higher tax burden and should maintain accounting records in order to transfer to the normal income tax system (Mkhize 2011).

Interim tax payments may be perceived as a benefit for micro businesses. Interim tax payments are payable in terms of the turnover tax system, that are similar to provisional tax payments for normal tax purposes. The first interim tax payment is 50% of the estimated turnover tax payable for the year of assessment by the last business day of August and the second interim tax payment is the turnover tax payable less the first interim tax payment. The final payment will be made at the end of the financial year, which is February. Interest will be levied if the payment is made later than the end of the year of assessment. A penalty will be levied if the second interim tax payment is less than 80% of the actual taxable turnover (SARS 2012). Although employee's tax is not an interim tax payment, the benefit to the micro business is that employee's tax may be paid twice a year as from 1 October 2012 (Stiglingh, Koekemoer, Van Schalkwyk, Wilcocks & De Swardt 2012).

2.3.5 Conclusion

From the above explanation it is evident that, turnover tax is optional and is available to micro businesses and will replace income tax and CGT. A business with a turnover not exceeding R1 million, does not have to register for VAT. It must be noted no turnover tax is payable on the first R150 000 of taxable turnover (see Annexure A for tax rates). The bookkeeping burden for tax purposes has been reduced for micro businesses. In comparison, small business corporations pay no tax on the first R67 111 of taxable income (see Annexure A for tax rates). This discussion on the taxation of small and micro businesses highlights the introduction of the various taxation systems available to small and micro businesses in South Africa. From the above discussion, it is evident that three tax alternatives are available to small businesses, namely turnover tax, small business corporation tax or the normal income tax provisions. As previously mentioned, Government is encouraging the development of small businesses in South Africa by introducing benefits such as incentive schemes, tax incentives, reducing tax thresholds and tax amnesty (National Treasury 2012a). The next tax system that is dealt with in detail is small business corporation tax.

2.4 SMALL BUSINESS CORPORATION TAX

2.4.1 Introduction

The terms “SMME” and “small businesses” are used interchangeably in various contexts. This chapter distinguishes between these two terms and will provide the definitions as given by DTI (section 2.4.2.1 and 2.4.2.2) and the National Treasury/ SARS (section 2.4.2.3). The small business corporation for income tax purposes is regulated by the Income Tax Act No. 58 of 1962 (South Africa) while SMMEs are governed by the National Small Business Act, 1996 (South Africa). This chapter focuses on the Income Tax Act, as the Act gives beneficial tax treatment and accelerated allowances to small businesses. In addition, this chapter discusses small business corporations in detail along with the relevant legislation.

2.4.2 Definitions Related to SMME and Small Business

The development of a small business definition in South Africa went through various processes as discussed below.

2.4.2.1 White paper 1995

The White Paper on the National Strategy for the Development and Promotion of Small Business in South Africa (South Africa 1995:8) identified four distinct sectors, namely "survivalist enterprise, micro-enterprises, small enterprises and medium enterprises". During the normal business development cycle, a business will initially begin as a survivalist enterprise, the characteristics of the survivalist enterprise are discussed below:

> "**Survivalist enterprises** are activities by people unable to find a paid job or get into an economic sector of their choice. Income generated from these activities usually falls far short of even a minimum income standard, with little capital invested, virtually no skills training in the particular field and only limited opportunities for growth into a viable business. Poverty and the attempt to survive are the main characteristics of this category of enterprises. Support strategies should primarily help these people, a large percentage of whom are women, to get out of this sector. Given the large number of people involved in survivalist activities, this constitutes a vast challenge, which has to be tackled within the broader context of the Reconstruction and Development Programme"
>
> (South Africa 1995:8)

This category mainly comprises women, who are unskilled and whose sole purpose is survival (South Africa 1995). The main characteristics of this category of enterprises identified above are poverty and survival, support is a necessary factor which should be addressed. From the survivalist enterprise category there is a move to micro enterprises which is described as:

> "**Micro-enterprises** are very small businesses, often involving only the owner, some family member(s) and at the most one or two paid employees. They usually lack 'formality' in terms of business licenses, value-added tax (VAT) registration, formal business premises, operating permits and accounting procedures. Most of them have a limited capital base and only rudimentary technical or business skills among their operators. However, many micro-enterprises advance into viable small businesses.

> Earning levels of micro-enterprises differ widely, depending on the particular sector, the growth phase of the business and access to relevant support"
>
> (South Africa 1995:8)

This category comprises very small businesses with only the owner running the business and not adhering to regulations, as a result these enterprises are usually informal. Working capital is scarce and the business owner's lack the technical and business knowledge, however, many of these enterprises develop into sustainable small businesses. Revenue of these micro-enterprises is dependent upon the sector in which they are located as well as the support that they receive. The next category to which the micro-enterprise may move is the small enterprise which is described below.

> "**Small enterprises** constitute the bulk of the established businesses, with employment ranging between five and about 50. The enterprises will usually be owner-managed or directly controlled by the community-owner. They are likely to operate from business or industrial premises, be tax-registered and meet other formal registration requirements. Classification in terms of assets and turnover is difficult, given the wide differences in various business sectors like retailing, manufacturing, professional services and construction"
>
> (South Africa 1995:8)

This category has more employees than just the owner, usually comprises 5-50 employees. These businesses operate from premises and are usually registered for taxes and meet regulatory requirements. The last category to which small enterprises may move into is the medium enterprise which is described below.

> "**Medium enterprises** constitute a category difficult to demarcate vis-a-vis the "small" and "big" business categories. It is still viewed as basically owner/manager-controlled, though the shareholding or community control base could be more complex. The employment of 200 people and capital assets (excluding property) of about R5 million are often seen as the upper limit. In terms of this White Paper we are concerned with medium-sized enterprises which face obstacles and constraints which cannot be solved through normal market forces and private-sector action"
>
> (South Africa 1995:8)

This category comprises medium businesses with approximately 200 employees and capital assets, these businesses are faced with obstacles and constraints which are a

concern of the White Paper since these constraints are not able to be resolved within the market.

The above mentioned White Paper was tabled in Parliament on 20 March 2005 and the result was the enactment of the National Small Business Act (South Africa 1996).

2.4.2.2 National Small Business Act

A small business was initially defined according to National Small Business Act (South Africa 1996:2) as:

> *"a separate and distinct business entity, including co-operative enterprises and non-governmental organisations, managed by one owner or more which, including its branches or subsidiaries, if any, is predominantly carried on in any sector or subsector of the economy mentioned in column 1 of the Schedule and which can be classified as a micro-, a very small, a small or a medium enterprise by satisfying the criteria mentioned in columns 3, 4 and 5 of the Schedule opposite the smallest relevant size or class as mentioned in column 2 of the Schedule."*

Studies by Venter and De Clercq (2007a), Berry (2011), FIAS (2007), Pancha (2004), Smulders (2006) and Venter and De Clercq (2007b) define a SMME using the National Small Business Act 102 of 1996 (South Africa 1996).

This definition was amended in the National Small Business Amendment Act (South Africa 2004:3-4), which defined the term "small enterprises" rather than "small business" and it was defined as follows:

> *"a separate and distinct business entity, together with its branches or subsidiaries, if any, including co-operative enterprises, managed by one owner or more predominantly carried on in any sector or subsector of the economy mentioned in column 1 of the Schedule and classified as a micro-, a very small, a small or a medium enterprise by satisfying the criteria mentioned in columns 3, 4 and 5 of the Schedule".*

Small businesses may be classified as micro-, very small, small or medium enterprises, following a complex set of thresholds. Table 1 provides an extract of the classification in terms of the National Small Business Amendment Act (South Africa 2003:8) defined per industry. Eleven industries were identified.

Table 1: The Schedule - Classification of micro-, very small, small or medium enterprises

Column 1	Column 2	Column 3	Column 4	Column 5
Sector or sub-sector in accordance with the Standard Industrial Classification	Size of class	The total full-time equivalent of paid employees	Total turnover	Total gross asset value (fixed property excluded)
Agriculture	Medium	100	R5m	R5m
	Small	50	R3m	R3m
	Very Small	20	R0.5m	R0.5m
	Micro	5	R0.20m	R0.20m
Mining and Quarrying	Medium	200	R39m	R23m
	Small	50	R4m	R6m
	Very Small	20	R0.2m	R2m
	Micro	5	R0.20m	R0.10m
Manufacturing	Medium	200	R51m	R19m
	Small	50	R13m	R5m
	Very Small	20	R5m	R2m
	Micro	5	R0.20m	R0.10m
Electricity, Gas and Water	Medium	200	R51m	R19m
	Small	50	R13m	R5m
	Very Small	20	R5.1m	R1.9m
	Micro	5	R0.20m	R0.10m
Construction	Medium	200	R26m	R5m
	Small	50	R6m	R1m
	Very Small	20	R3m	R0.50m
	Micro	5	R0.20m	R0.10m
Retail and Motor Trade and Repair Services	Medium	200	R39m	R6m
	Small	50	R19m	R3m
	Very Small	20	R4m	R0.60m
	Micro	5	R0.20m	R0.10m
Wholesale Trade, Commercial Agents and Allied Services	Medium	200	R64m	R10
	Small	50	R32m	R5m
	Very Small	20	R6m	R0.60m
	Micro	5	R0.20m	R0.10m

Column 1	Column 2	Column 3	Column 4	Column 5
Catering, Accommodation and other Trade	Medium Small Very Small Micro	200 50 20 5	R13m R6m R5.1m R0.20m	R3m R1m R1.90m R0.10m
Transport, Storage and Communications	Medium Small Very Small Micro	200 50 20 5	R26m R13 R3m R0.20m	R6m R3m R0.60m R0.10m
Finance and Business Services	Medium Small Very Small Micro	200 50 20 5	R26m R13m R3m R0.20m	R5m R3m R0.50m R0.10m
Community, Social and Personal Services	Medium Small Very Small Micro	200 50 20 5	R13m R6m R1m R0.20m	R6m R3m R0.60m R0.10m

Source: National Small Business Amendment Act 26 of 2003:8

Three criteria are provided in this Act to categorise businesses as micro, small, very small or medium – number of employees, total turnover, and gross asset value (fixed property excluded). For example, a business that is located in the manufacturing sector which has 4 full-time employees, R0.15 million turnover and R0.10 million worth of gross assets (fixed property excluded), would be classified as a micro enterprise and meets the requirements as mentioned in columns 3, 4 and 5 of the schedule.

The above definition differs from the tax definition (under 2.4.2.3) and is driven by turnover while the National Small Business Amendment Act is driven by employees, turnover and gross asset value. A SMME differs from a small business corporation in that the small business corporation is limited to a close corporation or a private company whereas a SMME could be any person (Pancha, 2004). On the other hand FIAS (2007) points out that a SMME to a large extent is used as a synonym for small businesses which is acceptable, however, not from a taxation perspective, since companies in South Africa are governed by the Companies Act 71 of 2008 and Income Tax is governed by the Income Tax Act 71 of 1962.

2.4.2.3 Tax Legislation

The aim of this study is to identify which tax system is more beneficial to the selected small and micro businesses. A small business was defined earlier using the definition from the White paper (South Africa 1995) and the National Small Business Act, however, there does not appear to be one consistent small business definition in previous research. References to the term small business generally include micro and medium-sized businesses and SMME is conflated with the term small business (Smulders 2006). These are merely definitions of small businesses, however, they do not relate to the Income Tax Act. Because this study is related to taxation of small and micro businesses it is imperative that there is a common understanding of what constitutes a small business in terms of the Income Tax Act. For the purpose of this study a small business corporation is defined by the Income Tax Act in section 12E(4) (South Africa 1962:95-96) as:

(*a*) **"small business corporation"** means any close corporation or co-operative or any private company as defined in section 1 of the Companies Act, 2008 (Act No. 71 of 2008), all the shareholders of which are at all times during the year of assessment natural persons, where—

(i) the gross income for the year of assessment does not exceed an amount equal to R20 million: Provided that where the close corporation, co-operative or company during the relevant year of assessment carries on any trade, for purposes of which any asset contemplated in this section is used, for a period which is less than 12 months, that amount shall be reduced to an amount which bears to that amount, the same ratio as the number of months (in the determination of which a part of a month shall be reckoned as a full month), during which that company, co-operative or close corporation carried on that trade bears to 12 months: (gross income must not exceed R20 million)

(ii) none of the shareholders or members at any time during the year of assessment of the company, close corporation or co-operative holds any shares or has any interest in the equity of any other company as defined in section 1, other than-

(*aa*) a company contemplated in paragraph (a) of the definition of 'listed company'; or

(*bb*) any portfolio in a collective investment scheme contemplated in paragraph (e) of the definition of 'company';

(*cc*) a company contemplated in section 10(1)(e)(i)(aa), (bb) or (cc);

(*dd*) less than 5 per cent of the interest in a social or consumer co-operative or a co-operative burial society as defined in section 1 of the Co-operatives Act, 2005 (Act No. 14 of 2005), or any other similar co-operative if all of the income derived from the trade of

that co-operative during any year of assessment is solely derived from its members;

(*ee*) any friendly society as defined in section 1 of the Friendly Societies Act, 1956 (Act No. 25 of 1956);

(*ff*) less than 5 per cent of the interest in a primary savings co-operative bank or a primary savings and loans co-operative bank as defined in the Co-operative Banks Act, 2007, that may provide, participate in or undertake only the following—

(A) in the case of a primary savings co-operative bank, banking services contemplated in section 14(1)(a) to (d) of that Act; and

(B) in the case of a primary savings and loans co-operative bank, banking services contemplated in section 14(2)(a) or (b) of that Act;

(*gg*) a venture capital company as defined in section 12J;

(*hh*) any company, close corporation or co-operative if the company, close corporation or co-operative—

(A) has not during any year of assessment carried on any trade; and

(B) has not during any year of assessment owned assets, the total market value of which exceeds R5 000; or

(*ii*) any company, co-operative or close corporation if the company, co-operative or close corporation has taken the steps contemplated in section 41(4) to liquidate, wind up or deregister: Provided that this item ceases to apply if the company, co-operative or close corporation has at any stage withdrawn any step so taken or does anything to invalidate any step so taken, with the result that the company or close corporation will not be liquidated, wound up or deregistered;

(iii) not more than 20 percent of the total of all receipts and accruals (other than those of a capital nature) and all the capital gains of the company, close corporation or co-operative consists collectively of investment income and income from the rendering of a personal service; and

(iv) such company is not a personal service provider as defined in the Fourth Schedule;

(*b*) [deleted by the Revenue Laws Amendment Act No. 60 of 2008];

(*c*) **"investment income"** means—

(i) any income in the form of dividends, foreign dividends, royalties, rental derived in respect of immovable property, annuities or income of a similar nature;

(ii) any interest as contemplated in section 24J. (other than any interest received by or accrued to any co-operative bank as contemplated in paragraph (a)(ii)(ff)), any amount contemplated in section 24K and any other income which, by the laws of the Republic administered by the Commissioner, is subject to the same treatment

as income from money lent; and

(iii) any proceeds derived from investment or trading in financial instruments (including futures, options and other derivatives), marketable securities or immovable property;

(*d*) **"personal service"**, in relation to a company, co-operative or close corporation, means any service in the field of accounting, actuarial science, architecture, auctioneering, auditing, broadcasting, consulting, draftsmanship, education, engineering, financial service broking, health, information technology, journalism, law, management, real estate broking, research, sport, surveying, translation, valuation or veterinary science, if-

(i) that service is performed personally by any person who holds an interest in that company, co-operative or close corporation; and

(ii) that company, co-operative or close corporation does not throughout the year of assessment employ three or more full-time employees (other than any employee who is a shareholder of the company or member of the co-operative or close corporation, as the case may be, or who is a connected person in relation to a shareholder or member), who are on a full-time basis engaged in the business of that company, co-operative or close corporation of rendering that service.

All the requirements above have to be satisfied in order to be classified as a small business corporation. This definition is limited in the sense that it does not cover natural persons, sole proprietorships and partnerships operating as small businesses and therefore they cannot be small business corporations (South Africa 1962).

From the definition that the Income Tax Act provides, it is evident that service-related companies may only benefit if they effectively deal with the following two obstacles: a small business does not render a personal service from which it derives more than 20% of its total receipts and accruals (including capital gains) and if it is an "employment company" it cannot be defined as a small business corporation (Arendse, as referred to by Smulders 2006:36-37). The above mentioned benefit is mainly targeted at manufacturing companies.

Literature presents evidence of small businesses that SARS rejected as small businesses; below follows a discussion of two court cases where the court found that the defendants claim to be small businesses was correct.

In *XYZ CC v the Commissioner for SARS* 2013 JDR 0352, the defendant disputed its income tax assessment as it believed that the business was a small business corporation however, SARS was of the view that the business provides personal services and also derives more than 20% from investment income and therefore does not meet the requirements of a small business corporation as defined in section 12E of the Act. The business provides promotional activities including ancillary activities (such as advising clients; placement of client products, promotions of client products, assisting with consumer complaints and providing feedback on consumer demands and requests, attending bi-monthly sales meetings with sales staff of clients), the court held that this is not a personal service and the ancillary activities which include providing advice to its clients are incidental to the service provided.

In *TML Consultancy CC v the Commissioner for SARS* 2012 JDR 1061, the defendant disputed its income tax assessment as it believed that the business was a small business corporation however, SARS assessment stated that the business provides personal services. The court held that marketing is not ‘broking’ and ‘management’ and is not a personal service and that the defendant is a small business corporation.

Small business corporation tax was introduced due to the growth of SMME’s and therefore employment. History shows how the small business corporation tax system was changed to improve its working and therefore it is important to look at the history of the small business corporation tax.

Small business corporation tax was introduced in the year 2000 and in order to be classified as a small business corporation, the criteria are the same as those mentioned above except for the gross income criteria. The gross income for the year of assessment could not exceed R1 million however, in 2006 it increased to R14 million and has currently been increased to R20 million (National Treasury 2013a). The fact that Government has decreased the gross income criteria over the past fourteen years is indicative that Government is making an effort to promote small businesses in South Africa (National Treasury 2012a).

With respect to the history behind the tax rate for years of assessment commencing on or after 1 April 2000, the rate of normal tax payable was 15% on the first R100 000 of taxable income and 30% on the taxable income exceeding R100 000 (Karro 2000). For financial years ending on any date between 1 April 2013 and 31 March 2014, the rate of normal income tax payable is 0% on the first R67 111 of taxable income, 7% on the taxable income R67 112 to R365 000, 21% on the taxable income R365 001 to R550 000 and 28% on the taxable income exceeding R550 000 (refer to Annexure A). On perusal of the tax rates from the year 2000 to 2013, it is apparent that the tax threshold has decreased each year. Government introduces tax reliefs annually to encourage the development of small businesses and to encourage household savings as well as to compensate small businesses for the compliance costs incurred (National Treasury 2012a).

Currently, a small business corporation's gross income for the year of assessment does not exceed R20 million; none of the shareholders or members of the business hold any shares or have any interest in the equity of any other company as defined in section 1, other than those listed above from section 12 (4)(*a*)(ii) of the Income Tax Act (South Africa 1962); not more than 20 percent of the total receipts and accruals (other than those of a capital nature) and all the capital gains of the business operations consists collectively of investment income and income from the rendering of a personal service and such company is not a personal service provider as defined in the Fourth Schedule of the Income Tax Act. Apart from small business corporation tax, there are other taxes applicable to small businesses which are discussed below.

2.4.3 Other Taxes Applicable to Small Business Corporations

Small businesses need to consider the other taxes when choosing a tax system, other taxes that are particularly relevant to small businesses are STC, CGT and VAT. However, STC was terminated on 31 March 2012 and a dividend tax of 15% was implemented on 1 April 2012, this was put into effect in order to align South Africa to other countries (National Treasury 2012b). Prior to March 2012, the small business was liable for STC at a rate of 10% while currently the shareholder is liable for

dividends tax, except if it is a dividend in specie, then the company declaring it is liable for the dividend tax; the small business will withhold and pay the tax on behalf of the shareholder (South Africa 1962).

CGT was introduced in 2001 and is governed by the Eighth Schedule to the Income Tax Act (South Africa 1962). CGT applies to individuals, trusts and companies. It is imposed when an asset is disposed of. The proceeds realised or deemed to be realised on disposal exceed the assets' base cost this is the capital gain or loss of that asset (SARS a [s.a.]). The base cost includes those costs incurred to acquire, enhance or dispose of the asset and excludes current cost such as interest, repairs, insurance premiums and rates and taxes (SARS 2000).

Taxable capital gains is taxed at a maximum effective rate of normal tax of 18.6% (28% x 66.6%), calculated on an inclusion rate of 66.6% on the maximum normal tax rate (National Treasury 2012b). In addition, the exclusion threshold for the disposal of a small business when a person is 55 years or older, has been increased from R900 000 to R1.8 million, and the maximum market value of assets prescribed for a small business disposal for business owners 55 years or older has been raised from R5 million to R10 million (National Treasury 2012a).

VAT is an indirect tax, which is levied at 14% on the supply of most goods and services and on the importation of goods (SARS b [s.a.]). Small businesses with taxable supplies not exceeding R1 million over a twelve-month period are not required to register for VAT and are therefore relieved from having to submit VAT returns (National Treasury 2011). These businesses may register voluntarily and benefit from input tax credit on certain expenses, but they are then obliged to lodge VAT returns and levy output VAT (Smulders 2006). There are a number of advantages and disadvantages of small business corporation tax which are discussed below.

2.4.4 Advantages and Disadvantages of Small Business Corporation Tax

A significant advantage to small business corporations is the fact that it is entitled to an accelerated wear and tear allowance in terms of section 12E of the Income Tax Act. If the asset is brought into use for the first time and is used in the process of manufacture, a deduction equal to the cost of such asset shall be allowed in the year that such asset is brought into use. If the asset is not used in the process of manufacture, a deduction equal to an amount of 50% of the cost of the asset in the first year, 30% in the second year and 20% in the third year is allowed. Any expenditure incurred in moving the asset will be allowed as a deduction, subject to the provisions of the Income Tax Act (South Africa 1962).

Small business corporations may benefit from a lower tax expense due to the reduced tax thresholds, deductions on start-up costs and accelerated write-off allowances listed above. Other benefits such as deductions of professional and legal expenses; dedicated services for the business such as advertising, telephone, internet, insurance, qualifying donations; cost of continuing education and training, and also bad debts are deductible if the income has been declared.

The four maxims advanced by Smith (1776) could also be used to discuss the fairness of the small business corporation tax. The small business corporation tax does factor the ability to afford the tax, as taxes are based on taxable income, which is income after deductions and allowances. Businesses in an assessed loss position may carry over the assessed loss to the next year and enjoy the tax benefit. Maxim one indicates that tax should be levied based on revenue, turnover tax is based on taxable turnover while small business corporation tax is based on taxable income. The two systems clearly do not apply the same principles in calculating the ‘revenue’ on which the tax are levied and therefore departing from the principle of fairness in the system.

The ability to bear principle is not considered in the turnover tax system and the small business corporations tax system, in layman’s terms, the ability to bear principle means the ability to afford the tax due (Gluckman 2012). The small business

corporation tax system factors the cost of living, as deductions are allowed for wear and tear, repairs, electricity, water, advertising, and training. Although businesses with high profit margins are not taxed at the same rate as those with low profit margins, this is a progressive tax system and not a proportional tax system and consequently it does not promote maxim one.

For maxim two Gluckman (2012) recommends that the tax payable should be logical and understandable to the taxpayer and the government. Small business corporation tax is complex to understand as there are many inclusions and exclusions to taxable income and does not incorporate any of the other taxes, it merely provides small businesses with lower tax rates and further deductions compared to other businesses, thus also not promoting maxim two. Uncertainty lies in the interpretation of 'personal service' and thus poses a disadvantage to small businesses, and consequently not promoting maxim two.

Maxim three according to Gluckman (2012) is that the method and timing must be convenient for the taxpayer and is entity dependent, the convenience of the method and timing of payments will depend on the nature of the business. Small business corporation tax is paid on a provisional basis, making it easier for taxpayers.

The tax administration should be simple and easy to comply with according to maxim four (Gluckman 2012). The small business corporation tax system is complex and difficult to comply with and does not satisfy the requirements of maxim four. There needs to be qualifying rules and principles within a tax system, which prevent taxpayers from evading taxation (Gluckman 2012). Within the turnover tax and small business corporation tax system there are principles that are fair, however, both systems are not perceived to be fair, based on Smith's maxims. In conclusion, based on Smith's four maxims, the small business corporation compliance burden is high, although the tax rates are lower, the compliance costs put the business on par with normal taxes and thus the system is not completely fair to small business corporations. Many studies were conducted internationally on small businesses, a discussion follows.

The US operates on a progressive income tax system with a federal and state tax system (Roach 2010), the tax rate increases with the increasing income. Federal tax rates vary from 15% to 30% and state taxes and rules vary by jurisdiction. The different type of businesses are: corporation and S corporations which are taxed as corporate businesses and sole proprietors, limited liability companies, cooperative, and partnership profits form part of the individual's personal income tax (Small Business Administration [s.a]). Businesses in the US have a choice of tax treatment regardless of its business's legal form (Crawford & Freedman 2008). Small businesses in the US include their business profit or loss on their personal tax returns (Murray 2014). Small businesses that are not corporations can be sole proprietors, limited liability companies and partnerships, they may deduct expenses that are ordinary and necessary for the business, for example, start-up costs, cost of goods, interest, insurance, rent, expenses for business use of a vehicle (using the actual costs or mileage) (IRS 2014).

Small businesses have the largest non-compliance in the US and are likely to be owner managed, farming was at 71% and non-farm sole proprietor income at 57% (Logue & Vettori 2010). People pay taxes to avoid penalties therefore it can be assumed the tax saving is compared to the estimated penalty when being non-compliant. Logue and Vettori (2010) suggest larger tax penalties for tax evasion and also a presumptive tax system to replace the existing income tax system for small businesses in US, possibly a tax on a percentage of gross receipts or asset value.

The UK has various legal forms of small businesses being incorporated and unincorporated (sole proprietors and partnerships) (Freedman 2003). As with South Africa, small businesses form an integral part of all economies everywhere in the world, they create jobs and contribute to the economy of a country (Du Toit 2012; Crawford & Freedman 2011). Small businesses that make an annual profit up to £300 000 are taxed at 20% at the small profit rate and profits from £300 000 up to £1.5 million or more at 21% (ByteStart 2014). Small businesses are entitled to deduct business expenses and capital allowances on plant and machinery used for business

purposes (Business tax 2014). A small business is defined by Freedman (2003) as fewer than 50 employees. In the UK, small businesses account for 99% of UK businesses (Freedman 2003, Crawford & Freedman 2008). Crawford and Freedman (2008) define small businesses as owner managed businesses, managed in their owners personalised way.

Crawford and Freedman (2011) discuss how small, owner managed businesses are taxed and what the disadvantages are that small businesses face in the UK. They concluded that smaller firms are largely affected by market inefficiencies due to their size; they are also at a disadvantage as they generally have fewer staff members who lack expertise regarding taxation as well as the time to understand and apply the tax regulations. The above is consistent with Smulders (2006), Smulders and Stiglingh (2008) and Smulders *et al* (2012) point of view. Regarding compliance costs, Crawford and Freedman (2011) raised a valid point; there is a relationship between compliance cost increases and the opportunity for tax evasion.

Crawford and Freedman (2011) examined the status of organisations, whether the small business was incorporated or unincorporated. They investigated the nature of the economic activity involved and the consequent tax implications. They stated that the legal form of a business should not influence the tax treatment. In comparison to the UK, businesses in South Africa are taxed according to their legal form. Tax incentives are an important aspect when deciding which tax system to elect.

Du Toit (2012) concluded that tax incentives for small businesses in South Africa are similar to those tax incentives of developed countries and that the South African tax system could draw on the tax incentives legislated in Australia and Canada. As Du Toit's (2012) study was a comparison of tax legislation in South Africa, Australia and Canada, her research is relevant to this study because she investigated South African tax legislation and compared it with Australia and Canada. She selected Australia and Canada based on the fact that small businesses account for 96% and 98% of all businesses respectively and research also indicated that these countries have developed their tax systems to accommodate small businesses by providing tax

relief and concessions. Australia pays income taxes at a flat rate of 30% on profits, reduced by any pay as you go instalments made during the year (Du Toit 2012).

Compared to South Africa, Australia does not have any tax free thresholds for companies whereas South Africa taxes small business corporations with taxable income of less than R67 111 at 0%. Canada on the other hand, pays a basic tax rate of 38% which is reduced by federal tax abatement to 26.5% (Du Toit 2012). South Africa may enhance their tax incentives by increasing the gross income limit of R14 million to R16 million (Du Toit 2012), subsequently, this limit has been increased to R20 million (National Treasury 2013b). A recommendation by Du Toit (2012) is that South Africa should implement a limit of R40 000 on the movement in stock levels from the opening to closing balance for small businesses and implement a manufacturing and processing profit deduction for small manufacturing companies. This could encourage the growth of small businesses in South Africa and South Africa could employ similar methods to Russia. Russia in their effort to install a system of taxation and public finance experienced challenges, however, they modified their system of taxation to cope with these challenges and South Africa could perhaps take a lesson from Russia.

Russia had to increase the turnover tax to pay off the shortfall in enterprise taxes due to the decline of the state enterprise profit taxes, this approach had failed and a new structure had to be designed to develop an efficient tax collecting machine in Russia (Preobragenskaya & McGree 2004). The Russian tax system is similar to South Africa because tax in both Russia and South Africa is based on substance rather than form (South Africa 1962) and the tax rates continue to decline for small businesses (Preobragenskaya & McGree 2004). Despite the similarities between South Africa and Russia, there is no direct relevance to this study, however, it provides insight into the Russian tax system and South Africa could possibly learn from the Russian experience. Russia has adopted a flat rate tax system which eliminates the complication of the various tax systems and encourages growth (Preobragenskaya & McGree 2004). Russia was one of the countries included in the Paying Taxes 2013 report.

An international study known as 'Paying Taxes 2013' is a joint publication produced by PricewaterhouseCoopers (PwC) and the IFC. This report discusses the tax payments and the total tax rate of 185 countries. The tax payment reflects the frequency of payments, method of payment, the frequency of filling and the total number of taxes and contributions paid by each country. The findings for South Africa show a total of 9 tax payments, 2 payments for profit taxes, 3 payments for labour taxes and 4 payments for other taxes (PwC & IFC 2013). In 2011, 121 economies had between 6 and 35 payments compared to 199 economies in 2010, most economies have the option to file multiple tax returns and pay online (PwC & IFC 2013). The average number of payments in Africa is 37 while the global average payments is 27.2, South Africa falls below both of these averages (PwC & IFC 2013). Having established South Africa's position regarding the payment of taxes it is now necessary to discuss the tax rate.

PwC and IFC computed the total tax rate which measures the amount of taxes and contributions expressed as a share of commercial profit, where commercial profit is computed as sales less cost of goods sold, gross salaries, administrative expenses, other expenses, provisions, add capital gains less interest expense, add interest income and less commercial depreciation (PwC & IFC 2013). The total tax rate is the actual tax payable divided by the commercial profit and not the statutory tax rate (PwC & IFC 2013). South Africa's total tax rate is 33.3%, this comprises 24.3% profit tax, 4.1% labour tax and 4.9% other taxes (PwC & IFC 2013). In 2011, 116 economies had a tax rate of between 26% and 50%, this is higher than the previous year, and when compared to 2004 results, the total tax rates have decreased (PwC & IFC 2013). Tax rates are highest in Africa with an average of 57.4%, while the global average is 44.7%, South Africa's total tax rate of 33.3% is below the average of 44.7%, however, Africa's average of 57.4% is above the global average of 44.7% (PwC & IFC 2013). South Africa needs to work towards being on a par with the global average tax rates.

South Africa's overall payment of taxes is ranked number 32 from 185 economies, the first five economies being: United Arab Emirates, Qatar, Saudi Arabia, Hong Kong and Singapore (PwC & IFC 2013). The report showed the total tax rate, time to comply and number of payments had fallen over the eight years of the study, reflecting that governments have implemented reforms to make paying taxes less burdensome (PwC & IFC 2012).

The findings of another study conducted worldwide, across 185 economies known as 'Doing Business', were that Poland had improved their small business tax system compared to the previous year. Globally reform efforts have focused on making it easier to begin a new business; also to increase the efficiency of tax administration and facilitating trade across international borders; while the European economies in fiscal distress are making efforts to improve the business climate (World Bank & IFC 2013).

It was found that South Africa was ranked 39th in the Doing Business research study. The findings from the first Doing Business research study were that low-income economies had very 'cumbersome' regulatory systems, ten years later business regulatory practices in these economies have slowly converged toward the more efficient practices in higher-income economies (World Bank & IFC 2013). Singapore; Hong Kong; New Zealand; the US; Denmark; Norway; UK; the Republic of Korea; Georgia; and Australia are the ten economies with business friendly regulations while South Africa ranks 39th (World Bank & IFC 2013). Although Doing Business's research relates to small and medium businesses in the private sector, this study provides information on small and medium businesses around the world. It was found that economies that ranked highest are due to governments having created policies that facilitate interactions in the marketplace without hindering the growth of the private sector (World Bank & IFC 2013). The Doing Business Team examines the company law, the civil law, the labour code, gathers data regarding the inputs and indicators on the complexity and cost of regulatory processes and the strength of the legal institutions (World Bank & IFC 2013).

There were also guidelines released by the OECD (2008 and 2011) for multinational enterprises, these are recommendations addressed by forty four governments that adhere to these guidelines namely, Argentina, Australia, Austria, Belgium, Brazil, Canada, Chile, Columbia, Czech Republic, Denmark, Egypt, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, South Korea, Latvia, Lithuania, Luxembourg, Mexico, Morocco, Netherlands, New Zealand, Norway, Peru, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, Switzerland, Turkey, Tunisia, UK and US (OECD b [s.a.] to ensure that the operations are in agreement with government policies, to boost the contribution to sustainable development and advance foreign investment climate. The guidelines also provide 'non-binding' principles and standards in a global context uniform with applicable laws and internationally recognised standards (OECD 2011). The OECD guidelines discuss due diligence, disclosure, human rights, employment, environment, bribery, consumer interest, science and technology, competition and taxation (OECD a [s.a.]). Although these guidelines discuss taxation, the focal point is transfer pricing, the guidelines discuss the efficiency and effectiveness of co-operation with authorities.

Extensive research has been conducted on small businesses; however, the studies focused on survival and compliance costs rather than taxation therefore the above mentioned studies are not applicable to this study. Limited research has been conducted on tax implications and benefits of the tax systems for small or micro businesses. This study focuses on a comparison of taxation on small business corporations and micro businesses, consequently the literature available is limited. However, as previously indicated compliance cost and tax rates affect small business compliance, therefore the effect of compliance cost in deciding which system to use will be reviewed in the next section. Many smaller private businesses seem to be emerging because of South Africa's high unemployment figures; however, they will not survive due to the lack of financial planning and control systems (Berry 2011).

The aim of Mkhize's (2011) research was to analyse the impact of small business tax legislation on both the small business taxpayer and SARS, both turnover tax and small business corporation tax was discussed in his study, however, these tax

systems were not compared. The small business corporation legislation has enhanced the compliance "culture" therefore meeting the goals of SARS and National Treasury (Mkhize 2011). Small business corporation taxpayers decreased from 103 656 in 2009, 106 628 in 2010, 103 928 in 2011 to 86 333 in 2012 (National Treasury & SARS 2013). This decrease was driven by the tertiary sector being wholesale and retail, catering, accommodation, transport, storage, communication, financial intermediation, insurance, real estate and business services (National Treasury & SARS 2013).

The findings of the 'Enterprise Surveys' conducted by the World Bank and IFC were used by Fjeldstad, Schulz-Herzenberg and Sjursen (2012) in their research. "These are firm-level surveys that are a tax representative sample of a country's private sector" (Fjeldstad *et al* 2012:12). Their research only focused on African countries, thus only the findings of the Enterprise Surveys applicable to the African countries were used. It is necessary to point out that this discussion deals with all the African countries involved in the survey and the reason for the inclusion here is to indicate that these countries have numerous obstacles compared with South Africa, however, despite these issues being identified as lesser obstacles, the greatest obstacle for South Africa is crime. Firms were given a range of issues (listed below) and were asked whether they found these issues to be obstacles to the current operations of their firms. The largest tax related obstacles identified were practices of the informal sector, tax rates, corruption, customs and trade regulations, tax administration and business licensing and permits. On average tax rates were found to be the most burdensome, followed by practices of the informal sector, corruption, customs and trade regulations, business licensing and permits and tax administration (Fjeldstad *et al* 2012). South Africa did not identify any of these issues to be large obstacles, however, Kenya identified tax rates and Mozambique identified practices of the informal sector to be the largest obstacles. The largest non-tax related obstacles identified by the African counties were electricity; access to finance; political instability; crime, theft and disorder; access to land and transportation.

On average electricity was found to be the most important constraint followed by access to finance; transportation; crime, theft and disorder; access to land and lastly

political instability. Tanzania, Uganda and Senegal's response to electricity were high, while South Africa's response to crime, theft and disorder was high (Fjeldstad *et al* 2012). There were no significant differences between firms of different sizes (small, medium and large) except in Kenya, Sierra Leone and Zambia that found the difference in the size of the business of consequence (Fjeldstad *et al* 2012). Although there are many similarities between the African countries and South Africa, South African firms' rate crime, theft and disorder as a major challenge, however, the rest of Africa found electricity to be a major challenge and crime was only rated as the seventh challenge (Fjeldstad *et al* 2012). Apart from these obstacles compliance cost is yet another challenge that small businesses face.

2.5 COMPLIANCE COSTS FOR SMALL AND MICRO BUSINESSES

The cost of compliance with regulations is noted as a key inhibitor to small business development (Chamberlin & Smith 2006) and combined with tax rates have a major impact on selecting which system to use. Compliance costs are on-going costs that a business would need to deal with in order to comply with regulations.

There are various interpretations of what is referred to as compliance cost, Pancha (2004) identifies the following as compliance cost burdens: the time required for filing, completing returns and dealing with SARS related queries, gaining the knowledge required to comply in a complex environment. In Maseko (2013) opinion tax rates, tax audits, perceptions of government spending, role of tax authority and tax administration, simplicity of tax return and personal financial constraints determine tax compliance. SMMEs choose to outsource this function but the cost in terms of professional fees and technology required is expensive and the potential alignment of GAAP (Generally Accepted Accounting Principles) with tax policy and legislation should be explored. Although the actual tax payable by small business corporations is less than normal income tax, studies have identified that the proportionate cost of compliance is higher (Smulders 2006, USAID 2008, Smulders & Stiglingh 2008, Rametse 2010, Willemse 2010, Ramusetheli 2011, Franzsen 2012, Coolidge 2012 and Smulders *et al* 2012).

Small businesses bear a higher compliance burden due to tedious compliance procedures required by tax authorities (Eichfelder & Schorn 2008). Maseko (2013) observed the most important reason for small businesses to be tax compliant is to obtain the tax clearance certificate followed by avoidance of tax penalties. The use of experts improve the tax compliance however, increases the cost of compliance (Maseko 2013). Nyamwanza, Mavhiki, Mapetere and Nyamwanza (2014) identified that small businesses evade compliance by indulging in illegal activities such as paying bribes, keeping two sets of records, relocating to new premises without notifying authorities, and temporarily closing businesses.

In an attempt to compensate for compliance cost, a reduction of paperwork was introduced in turnover tax thus contributing to a saving (Radebe 2008). An estimate by Upstart Business Strategies of VAT compliance costs suggest it amounts to around R8 441 (Pancha 2004). A small business will have to employ a tax practitioner/accountant and a filing clerk. In comparison, Smulders and Stiglingh (2008) revealed that the annual tax compliance cost is R7 030 for small businesses. In addition, according to independent research commissioned by SARS and the National Treasury, in 2009, it costs small businesses an average of R7 000 a year to ensure that tax returns for income tax, provisional tax, VAT and employees' tax are prepared, completed and submitted (SA info reporter 2009). Subsequent studies have not elicited any current information on the figure for compliance cost. Therefore the average cost of compliance appears to be in the range of R7 000 for small businesses. Consequently, turnover tax is aimed at reducing this cost for micro businesses by reducing the compliance requirements, as stated above by simplifying the tax calculations and reducing the paperwork (SARS 2008). Blazic (as referred to by Barbone *et al* 2012:36) identified compliance cost of small businesses as 0.8 percent of GDP in Croatia while Plamondon (as referred to by Barbone *et al* 2012:37) identified compliance costs in Canada to be 20 to 40 percent lower than those countries operating manually, and Tran -Nam and Glover (as referred to by Barbone *et al* 2012:38) identified small businesses incurred compliance costs of AUD$4,853 (mean) in Australia.

Research was conducted in four countries (Australia, Canada, South Africa and the UK) and it was found that tax compliance costs for small businesses remain high and regressive in all four countries (Evans *et al* 2014). Evans *et al* (2014) defined compliance costs as the cost incurred by taxpayers or third parties in meeting the requirements to comply with the tax law. Compliance cost is higher relative to the size of the business and does not diminish over time (Evans *et al* 2014). Internal compliance costs were further analysed as those incurred within the limitations of the firm and external as those outsourced. VAT/GST (internal costs) takes the most time: 58.2% in Australia; 38% in South Africa; and 41.3% in the UK following with Income Tax, PAYE, CGT and lastly other (Evans *et al* 2014). External costs are tax related, payroll and non-tax related. Internal costs are higher than external, comprising 61% (South Africa), 81% (Canada), 68% (Australia) and 64% (UK) of the total tax compliance costs (Evans *et al* 2014).

Another widely used definition for tax compliance cost is: “Costs incurred by taxpayers in meeting the requirements laid on them by the tax law and the revenue authorities … over and above the actual payment of tax; costs which would disappear if the tax was abolished” (Sandford, as referred to by Coolidge 2012:251). However, Smulders (2006) summarised tax compliance cost as the time spent by management on understanding and applying the rules, costs for record keeping, the payments made to professional advisors and the tax authority. On the other hand USAID (2008) defined tax compliance cost as all those costs incurred in the course of ensuring proper compliance with the relevant tax regulations. The OECD (2011) shares a different view; it defined compliance costs as providing information that is relevant or required by law in a timely manner to authorities. The difference being the costs incurred in preparing and submitting tax returns.

These definitions have common aspects such as understanding and complying with legislation, meeting the requirements and submitting the returns. Smulders (2006) concluded that complying with the tax laws is a constraint on small businesses’ growth. On the other hand, the USAID (2008) study surveyed the opinions of small business corporations with respect to the measures to achieve greater degrees of tax compliance in their sector, it was found that businesses that were fully compliant

stated there is nothing SARS could do to improve compliance while other small businesses suggested that there should be more SARS offices closer to business locations, SARS should improve their overall level of service, SARS should be quicker with VAT refunds, SARS should employ more staff and ensure direct access to their assessors via the telephone. All these suggestions are measures that may be taken into consideration by SARS. Smulders and Stiglingh (2008) state that the smaller the business, the heavier the burden, while Willemse (2010) found that the current income tax system has more compliance requirements than the turnover tax system, translating into higher compliance cost than turnover tax. The OECD (2007) concluded that the tax system is non-neutral and discourages small business creation, however, by reducing tax compliance costs and lowering the overall tax burden on small businesses, thus achieving neutrality across firms of varying sizes.

Compliance costs also include tax planning, psychological, social, and computational as well as accounting costs (Smulders & Stiglingh 2008). The study conducted by Smulders and Stiglingh (2008) found that the costs to prepare, complete and submit the tax returns increases steadily as the turnover increases, the findings of this study is summarised in Table 2 below (Smulders & Stiglingh 2008). Coolidge (2012), Rametse (2010) and Smulders and Stiglingh (2008) agree that the higher the turnover, the higher the compliance costs. The World Bank Group (WBG) has carried out a number of tax compliance cost surveys for businesses in developing countries, and concluded that small businesses incur tax compliance costs of up to 15% or more of turnover (Coolidge 2012).

Table 2: Average time taken (hours) per annum to prepare, complete and submit tax returns

		AVERAGE TIME TAKEN (HOURS)			
TAX		**TURNOVER**			
	Total	**R1 - R300 000**	**R300 001 - R1m**	**R1m - R6m**	**R6m - R14m**
Income Tax	3.07	2.87	2.99	2.97	2.91
Provisional Tax	2.27	2.22	2.25	2.29	2.22
VAT	18.77	18.41	19.02	19.40	18.76
Employees' tax	13.93	13.25	13.47	13.79	13.44
Total time taken (p/a)	**38.04**	**36.75**	**37.73**	**38.44**	**37.34**

Source: Smulders & Stiglingh 2008:14

What may be concluded from this information is that as the turnover increases, the time taken (hours) per annum to prepare, complete and submit tax returns increases. Preparation, completion and submission of VAT returns (per VAT period – ranging to 12 returns), this takes on average 1.5 hours per return. While income tax takes 3 hours on average.

The Paying Taxes 2013 report, determined that compliance costs have reduced steadily over the years with the introduction of online filing and payment. However, in economies where the tax rules are complicated, compliance time for businesses increased by an average of 39%. Smulders *et al* (2012) shares the same point of view regarding the time taken to understand and comply with the tax rules. The Paying Taxes 2013 report incorporates the common compliance cost, being the preparation and filing of tax returns by recording the time taken to prepare the tax returns, file the returns and pay the three major taxes namely, income tax, VAT and labour taxes, including payroll taxes and social contributions (PwC & IFC 2013).

This global Paying Taxes 2013 reports that it takes 200 hours to perform the above mentioned functions in South Africa (PwC & IFC 2013) and has not changed when compared to the previous year (PwC & IFC 2012) or 2011 (PwC & IFC 2011). However, over the last eight years the average time to comply in Africa has fallen by 25 hours and globally by 54 hours, in addition the average time to comply in the African region for 2013 is 313 hours (PwC & IFC 2013). The decrease in the average time is attributable to implementation of major reforms, increased use of accounting software for the preparation of tax filing information and various taxes being abolished (PwC & IFC 2013). The global average is 267 hours to comply, although South Africa has been stable over the past two years, it is below the normal range and the global average time (PwC & IFC 2013).

Smulders *et al* (2012) identified the following as internal tax compliance costs: the cost of collecting, paying and accounting for tax on products or profits of the business, and on the wages and salaries of employees, together with the costs of acquiring the knowledge to enable this work to be done, as well as external costs, mainly in the form of advisors' costs. The use of professional tax service providers is one of the main costs contributing to the cost of complying with taxation legislation. An average of 255 hours per year for small businesses and 155 hours for micro businesses is spent complying with tax legislation (Smulders *et al* 2012). In comparison to Smulders *et al* (2012) study the 'Paying Taxes 2013' reported 200 hours per year for businesses. The variance is due to different costs being classified as compliance costs. Therefore compliance cost may be defined as the time taken to understand and apply the regulations, the costs incurred for a professional advisor, the tax authority and submission of the returns.

Coolidge (2012) performed surveys on tax compliance costs in developing countries, she found that the time and cost related to preparing, filing, payment and interacting with the tax authorities on tax returns can be more than the actual tax payments. It was identified that in South Africa there were mixed approaches by businesses, some preferred to perform all their tax compliance in-house, while others outsourced and some both (Coolidge 2012). This decision is based on the availability of the required skills, if the business has the required expertise in-house or not (Coolidge

2012). Only 25% of small businesses do not outsource this function because the cost is high (Coolidge 2012). Compared to other countries, the former Soviet countries prefer in-house and Latin American outsourcing (Coolidge 2012). It was identified that the combination of in-house and outsourced tax compliance in South Africa was substantially more expensive than doing all the work in-house or outsourcing all (Coolidge 2012).

SARS is working on simplifying the various compliance systems and reducing the number of hours taken to comply with tax legislation. SARS has introduced e-filing to reduce the number of hours taken to file, submit and make payment and is in the process of streamlining registration and filing for both businesses and individuals and introducing a new company income tax form that require less fields to be completed by smaller businesses (National Treasury 2013a). This confirms that SARS is attempting to reduce the compliance cost burden for small businesses. Turnover tax was implemented with the aim of improving tax compliance and simplifying tax rules and regulations for micro businesses (Gluckman 2012). However, this simplified tax system may possibly be more burdensome to the taxpayer than the normal income tax system (Hassan 2009). If this is the case then micro businesses may not be in a financially improved situation and ultimately may not benefit from the turnover tax system. A need was identified by National Treasury to make changes to small business corporation taxes as it was identified that the lower tax rates do not address tax compliance costs (National Treasury 2014). Compliance cost was reviewed by the Davis Tax Committee and proposals were released, as mentioned previously, the literature was completed when the review was released, consequently the tax proposals are discussed in Chapter 5. As evidenced in the literature above, small businesses spend a considerable amount of time and money on tax compliance.

Research was conducted by Coolidge and Yilmaz (2014) on whether e-filing reduces tax compliance costs in developing countries (South Africa, Ukraine and Nepal), 74 economies implemented e-filing by 2011 and 29 in the previous 8 years. It was identified that e-filers spend more time and money in tax compliance, this is because they are usually larger firms with multiple taxes and a larger volume (Coolidge & Yilmaz 2014). South Africa enjoys a higher reduction of 22.4% in tax compliance

costs partly because e-filing fully replaced paper filing, while Nepal increased by 33% as their e-filing system was in addition to paper submission and Ukraine increased by about 20% to 25% for the same reason as Nepal (Coolidge & Yilmaz 2014).

2.6 SARS E-FILING

Previously all related tax returns were completed, submitted and paid to SARS manually, subsequently SARS e-filing was introduced and has been in operation since 2009. SARS e-filing is an online process for the submission of related tax returns, declarations, payments and other related services (SARS 2014a). A variety of tax returns including VAT, Pay as You Earn (PAYE), Skills Development Levy (SDL), Unemployment Insurance Fund (UIF), income tax, dividend tax and provisional tax may be submitted through the e-filing website. Once registered for e-filing taxpayers may engage with SARS online for the submission of tax returns, declarations and payments (SARS 2014a). For the financial year 2012/13 64.8% of the value of all payments was made through the e-filing system (National Treasury & SARS 2013). This service is similar to services offered in the US, Australia, Singapore, Ireland, Chile and France (SARS 2014a).

Research was conducted by the OTS (2012) to provide recommendations on improving administration of the tax system for small businesses in the UK. The OTS (2012) identified that businesses are not always aware of the amount of support on tax issues available to them by the HM Revenue & Customs (HMRC), there are tips, guidance and tools available to small businesses. Communicating with tax authorities (SARS) in South Africa is costly, and travelling to and fro to SARS is time consuming and costly, this is also experienced in the UK. OTS (2012) suggests a two way email communication with a set time frame for responses. Businesses requested a dedicated small business telephone helpline; this could also be implemented for small businesses in South Africa. Additionally this was also suggested by small businesses in South Africa (USAID 2008). OTS (2012) concluded that small businesses want to be in control of their tax affairs and look to HMRC for help, however, they have to involve external tax advisors to comply with tax regulations.

The above research was conducted in the UK and focused mainly on the HMRC's role with small businesses and how it could improve its role. OTS (2012) recommended that guidance, tips and tools should be provided from the early stages of the small business registration process, two way email communication, updates and impact of tax changes, an option to choose an accounting period, allow all forms to be submitted online, and lastly to choose language on forms, statements and all correspondence that would be easier to understand and to complete for taxpayers. The results of the surveys conducted in the UK highlight the need for HMRC to strengthen its support of small businesses from the registration process until the submission of the first return. This may shed some light to SARS.

Comparing e-filing to other countries, only 2% of Armenia use e-filing, in Ukraine even those who used e-filing still visited the tax office to submit the required hard-copy documentation, in Uzbekistan about 1% of businesses used it and in Nepal about 16% of businesses are registered for e-filing (Coolidge 2012). In South Africa businesses with higher turnover reported greater usage of e-filing (Coolidge & Yilmaz 2014). Coolidge and Yilmaz's (2014) study identified six recommendations for tax authorities in implementing e-filing, namely: simple, user friendly and voluntary for small businesses; reliable fast internet connection; awareness, options and benefits of e-filing; phase in e-filing; offer training and consider monetary incentives for e-filing. South Africa meets most of the recommendations mentioned above, the e-filing system is voluntary, user-friendly, internet connection is dependent on the service provider the business chooses, the benefits and options are published and the public is made aware of the e-filing system, there are SARS offices and a helpline available to the public. The South African tax policies for SME's are evaluated against international best practice next.

2.7 EVALUATION OF SOUTH AFRICAN TAX POLICIES FOR SME'S AGAINST INTERNATIONAL BEST PRACTICE

The South African tax policies for SME's will be evaluated against the international best practice discussed in the theoretical framework (2.2). As previously mentioned, there is no single approach applicable to all situations and countries in respect of the taxation of small businesses (IMF 2007), therefore all South African tax policies may not be in line with international best practice, however, the challenges faced by South Africa should be considered.

In Hansford and McKerchar's (2010) opinion a good tax system is dependent on its inherent fairness. Smith (as referred to by Hansford & McKerchar's 2010) defined fairness as the ability to pay, Asprey (as referred to by Hansford & McKerchar's 2010) on the other hand defined fairness as being treated equally when in the same situation, however, this is not the case with small businesses in South Africa. Small businesses are taxed at different rates and this can result in one business paying lower taxes than another business which is 90% identical, maybe because one of the shareholders owns shares in another company. Hansford and McKerchar's (2010) concluded that fairness is an important principle in a good tax system and fairness has many dimensions being vertical and horizontal equity. Stith (1976) defines vertical equity as the tax treatment of persons with different amounts of income. A more recent interpretation by Hansford and McKerchar's (2010:179), "Vertical equity requires that a person in unequal circumstances be treated with an appropriate degree of inequality". Horizontal equity requires that persons in the same situation should be liable for the same amount of tax that is a person who is earning the same amount and has similar obligations (Hansford & McKerchar's 2010).

The IMF (2007) and the IFC (2009) recommended the use of a "patent system" which is a fixed tax irrespective of the size or turnover of the individual business, this is the recommended design for survivalist enterprises. In South Africa no tax is generally paid by these businesses. With the turnover tax system, tax is levied at 0% on taxable turnover of up to R150 000, which is likely to be the survivalist enterprise

level. This is not in accordance with international best practice, but considering the high unemployment levels in South Africa this provision is appropriate.

National Treasury introduced a presumptive tax system, which is the turnover tax system. This system is based on turnover as per international best practice. The eligibility criteria are quite extensive for micro businesses which is not in line with international best practice (Arendse *et al* 2007) since the South African turnover tax system excludes professionals. Taxpayers have to elect the turnover tax system and the VAT threshold is linked to the turnover tax system while there is a choice to operate as a VAT vendor. These are all in line with international best practice. International best practice suggests different tax rates for trade and services, however, South Africa only has one set of tax rates for micro businesses. This may be the reason why only 7 700 businesses have registered on the turnover tax system since 2009 (SARS 2011).

International best practice suggests that medium enterprise level should be subject to the standard income tax system, accordingly, in South Africa small business corporations are subject to the standard income tax system. However, small business corporations are taxed at reduced tax rates and are allowed accelerated wear and tear allowances. Similar to the turnover tax criteria, the eligibility criteria is quite extensive (Arendse *et al* 2007). Section 11D of the Act was introduced to align South African tax to international best practice which suggests that a research and development incentive should allow a larger amount as a deduction than the actual expenditure incurred in the research and development activity.

The overall tax design of the South African tax policies that are in place for SME's are generally in line with international best practice. The introduction of the turnover tax system is a positive move towards aligning the South African tax systems with international best practice. The turnover tax system was introduced to encourage the growth of micro and small businesses and to reduce the compliance burden. This system is simple to use and requires minimal record keeping. The overall design of the turnover tax and small business corporations tax systems are in accordance with

international best practice while deviations have a rationale behind them. Emanating from the number of micro businesses registered on the turnover tax system there seems to be little incentive for micro businesses to elect to use this tax system, a situation that National Treasury should address. Since the Constitution of the Republic of South Africa plays an important role in the lives of its citizens, it is therefore necessary to discuss its relevance for taxation, consequently the constitution will be presented next.

2.8 THE CONSTITUTION OF THE REPUBLIC OF SOUTH AFRICA

Although this study will not provide a detailed discussion on the provision of the Constitution and taxation, some important considerations will be mentioned. Because there are different tax systems in South Africa this may be perceived as discrimination. The South African legal system is based on the idea of constitutional supremacy, consequently any law or conduct which is inconsistent with the Constitution would be considered unconstitutional. The Constitution was enacted to control the powers and obligations of the three arms of government, which is the executive, the law-making body and the courts of law.

The preamble to the South African Constitution seeks to achieve freedom, equality and dignity of every citizen of South Africa. Furthermore, section 9 of the Constitution states that "everyone is equal before the law and has the right to equal protection and benefit of the law." What this entails is that no law may unfairly discriminate against anyone. Legislation must therefore assist in bringing this equality through tax legislation and promote the values of the Constitution (Maroun 2007). Studies suggest that the South African tax system is not seen to promote equality, consequently this inequality will lead to an increase in tax evasion by taxpayers (Gluckman 2012). Equality is thus an important aspect of fairness (Maroun 2007) and fairness is essential to ensure that society does not evade tax (Gluckman 2012). However, in the case of small business corporations and micro businesses lower tax rates are imposed, it is evident that there is equality as these small business

corporations and micro businesses are taxed according to their size and their turnover or taxable income.

Small and micro businesses are taxed at different rates and this could result in one business paying lower taxes than another business which is 90% identical, maybe perhaps because one of the shareholders owns shares in another company. This discriminates against one of the businesses, is it constitutional to discriminate between businesses or is it a technicality? No research was found that indicated whether turnover tax or small business corporations tax is constitutional, however, research studies (Van Schalkwyk 2004a, Van Schalkwyk 2004b, Goldswain 2009, Goldswain 2012, Swanepoel 2014) found that certain sections of the Income Tax Act (1962) is constitutional. These studies will be discussed below.

The Act provides different benefits to different type and sizes of businesses in order for them to survive and contribute to employment. Section 36 of the Constitution tolerates discrimination in different situations, the limitation is allowed on reasonable and justifiable grounds, taking into account all relevant factors and therefore equating to fair discrimination. Factors include importance of the purpose, nature, extent and relationship between the limitation and purpose, nature of the right and less restrictive means to achieve the purpose. Economically these exclusion provisions in the Act with respect to turnover tax and small business corporations are unconstitutional in terms of section 9. However, in *Minister of Finance and Other v Van Heerden* 2004 (12) BLLR 1181 (CC) the court held that when determining contextual fairness, societal factors should be considered. The Government has the right to discriminate in terms of section 36 for governmental purposes in order to reduce poverty, encourage economic development and reduce political inequality.

Although these technicalities may be interpreted as an infringement upon an individual’s right to equality in terms of section 36 it is not unfair discrimination and therefore not unconstitutional.

The Katz Commission questioned the Constitutionality of the Income Tax Act in 1994, subsequent to the Constitution being implemented, in 2004 Van Schalkwyk (2004a) identified that some progress was made to amend the Income Tax Act, however, indicated that SARS should amend section 104(2) of the Act. This section is the reverse onus of proof provision and was later amended.

Goldswain (2009) concluded section 82 of the Act is ‘reasonable’ and ‘justifiable’ and therefore constitutional. This section of the Act deals particularly with general tax anti-avoidance rules. Following his study in 2012 Goldswain conducted an analysis and appraisal of selected constitutional issues affecting the rights of taxpayers. The conclusion reached was that “the judiciary have been forced to reappraise their approach to the interpretation of statutes from a strict and literal to a purposive approach that is in accordance with the values underpinning the new constitutional order...” (Goldswain 2012:2). Constitutionally unsound provisions “reverse onus of proof” were subsequently amended (Goldswain 2012:2). What may be inferred from this study is that the Act has been amended to adhere to the Constitution and should create fairness and consistency for taxpayers. Goldswain (2012) suggests that further research be conducted on small business corporations constitutionality.

The constitutionality (in terms of section 33 of the Constitution) of the discretionary powers of SARS was assessed by Van Schalkwyk (2004b). The Act gives SARS various discretionary powers, Van Schalkwyk (2004b) stated that 96 sections in the Act were identified, although many have been deleted over the years, the Act still contains discretionary powers. Taxpayers have a right to just administrative action in terms of section 33 of the Constitution.

Swanepoel (2014) conducted research on unintended gender discrimination in taxation and concluded that there was no direct gender discrimination, however, with respect to household consumption and household disposable income, it does not have the same effect for men and women. As a result it may be concluded that turnover tax and small business corporations tax in terms of the Constitution, is equal without discrimination.

2.9 SUMMARY

This chapter discussed the pertinent literature consulted for this study. A comprehensive review of both international and national literature pertaining to small and micro businesses was conducted. Since turnover tax was only introduced in 2009, there is limited literature available in South Africa and turnover tax is equivalent to a presumptive tax, GST/VAT globally. The gap in all the previous literature consulted is that there was no comparison performed between the two tax systems, which this study aimed to address.

Definitions and tax legislation relating to turnover tax and small business corporations tax have been covered in-depth in this chapter. The advantages and disadvantages of these tax systems were presented as well. Compliance costs and SARS e-filing came under scrutiny where the relevance was identified for this study. The chapter concluded with a discussion of the Constitution. The results may be summarised as follows:

	Turnover Tax	**Small Business Corporation Tax**
Turnover Limit	R1m	R20m
Persons qualifying	All natural and legal persons, sole proprietors (individuals), partnerships, close corporations, companies and co-operatives	Only legal persons, close corporations or a company (sole proprietorships and partnerships excluded)
Basis of taxation	Taxable turnover	Taxable Income
Taxes replaced	VAT (in the instance that you have not decided to elect back into the VAT system), provisional tax, income tax, CGT and STC. Dividends tax	None

	Turnover Tax	**Small Business Corporation Tax**
	(subject to certain exceptions)	
Allowances	Reduced tax rates, based on sliding scale, Annexure A.	Reduced tax rates, based on sliding scale, Annexure A. Section 12E, accelerated wear and tear allowance
Exclusions	Brokers	Personal services and labour broker

The next chapter will lay out the methodology used in this study.

Chapter 3 : RESEARCH DESIGN AND METHODOLOGY

3.1 INTRODUCTION

In this research the main research question is ‘which of the two tax systems, namely small business corporation tax or turnover tax, provide the most beneficial tax dispensation to small or micro businesses’, this chapter will describe the method followed to answer the question. A review of the research method and design, appropriateness (section 3.2), as well as a discussion of the population and sample size (section 3.3) are presented below. Methods of data collection (section 3.4) and data analysis (section 3.5) will be discussed followed by reliability and validity (section 3.6) and ethical considerations (section 3.7). The justification and rationale for the choice of the research methods for this study is discussed below.

3.2 METHODOLOGICAL APPROACH

In order to achieve the aim of this study a qualitative method of data collection was firstly used, this was subsequently supported by certain quantitative analysis of financial information of businesses. Qualitative research involves the recording of actual events such as interviews, discussions, observing behaviour and also analysing existing records (Neuman 2000). The analysis of existing records in this study pertains specifically to the financial statements of small businesses. In addition it was necessary to consult current legislation that underpins taxation in South Africa. Qualitative data is said to be unstructured compared to quantitative data (Flowerdew & Martin 2005). On the other hand the quantitative research method examines the mathematical importance of data (Neuman 2000). Quantitative data-gathering instruments establish relationships between measured variables. Measurement, numerical data and statistics are the main substance of quantitative instruments (Neuman 1997). However, this study did not involve the measurement of variables but merely involved an analysis of financial statements of small businesses which for the purpose of this study are referred to as case studies. The information of each

case study was captured on an excel spread sheet and analysed. A detailed discussion of the process is presented under section 3.5.

“By combining quantitative and qualitative research methods, researchers may simultaneously conform to and transcend dominant research conventions, making use of the most valuable features of each” (Schulze 2003:19). A combination of the two methods builds on the strengths and weaknesses of each other (Creswell & Clark 2011, McKerchar 2010). In addition, it allows for “cross validation” in order to gain a broader understanding (Gluckman 2012:35).

The methodology used in this study consists of a three phase approach, the first being that of the literature review, the second phase was in-depth face-to-face interviews and the third and final phase was the quantitative analysis of financial statements which to reiterate are referred to as case studies. The quantitative calculations (case study) and the qualitative method were chosen because it is appropriate to the aims of the study, which are to identify which of the two tax systems referred to above is more beneficial to the selected small or micro businesses. Phase one involved the reviewing of various sources such as legislation, prior research, journal articles, internet sources as well as books published internationally and in South Africa. The qualitative method, phase two, was used to gain insight into the beliefs and understanding of participants regarding the two tax systems as well as to expand on and complement the quantitative results. Finally phase three used the quantitative method to calculate the tax expense incurred by each case study. Each phase of the data collection method will be discussed below.

3.2.1 Phase One Literature Review

A doctrinal research method was used to examine the Income Tax Act and other legislation pertaining to small business corporations or micro businesses. Doctrinal research is defined as a research methodology that postulates a systematic explanation of the rules pertaining to a specific legal group, analysing the connection between rules, clarifies sections of difficulty and possibly envisages future improvements (McKerchar 2010). On the other hand, Dobinson and Johns (2007:19)

define doctrinal research as “research which asks what the law is in a particular area”. Primary sources which are case law and any relevant information, and secondary sources such as journal articles, other commentary on the legislation are collected and analysed, with the aim of describing and explaining how to apply the law, which is a qualitative method as it is not arithmetical (Dobinson & Johns 2007). This doctrinal research method was mainly used for phase one, which consists of a review of the relevant provisions of the Income Tax Act 58 of 1962. Various textbooks relating to small business corporations and micro businesses were consulted as well and are discussed in Chapter 2. A comprehensive literature search was conducted and the appropriate literature relating to this study was selected and presented in Chapter 2. A discussion of phase two, which is the qualitative research method ensues.

3.2.2 Phase Two the Qualitative Research Design

The qualitative research method was appropriate for this study in order to gain information from tax practitioners and tax representatives. Qualitative research emphasises the “human factor” and the intimate first-hand knowledge of the research setting (Neuman 2000:21). It was necessary to incorporate the qualitative research approach in order to understand a phenomenon in a specific context, this case, taxation of small business corporations and micro businesses. Qualitative methods in research are used to gain insight into the perceptions of participants (Creswell 2009, Kitchen & Tate 2000, Flowerdew & Martin 2005).

The qualitative research method was used with a small sample of participants. The aim of using the qualitative method was to provide a detailed analysis of the processes and views of the participants involved in the study (Flick 2011). In addition, the purpose of qualitative research is to understand phenomena in a specific context, where a phenomenon of interest cannot be manipulated (Patton 2002). Qualitative research is thought to be appropriate to elicit data pertaining to participants’ perceptions and beliefs (Neuman 2011). In depth face-to-face interviews were conducted with the participants, comprising tax practitioners and a tax representative who agreed to participate in the study. Plamondon (as referred to by Barbone *et al*

2012), Rametse (2010) and Venter and De Clercq (2007a, 2007b) conducted interviews as part of their qualitative research component. Phase three, the quantitative research method is discussed next.

3.2.3 Phase Three the Quantitative Research Method

In exploring the best taxation options for the selected case studies a quantitative analysis approach was used. In this study the two tax systems namely small business corporation tax and turnover tax were examined to establish which of the two tax systems would be beneficial to the selected small business corporations and micro businesses, in addition, normal tax was examined. As previously mentioned each financial statement provided by the participants was referred to as a case study. Depth, flexibility, versatility and manageability are strengths of the case study analysis (Rule & John 2011). The advantages of the case study analysis are that actual data is used; this eliminates the possibility of manipulation and the figures being non-realistic. Users will be able to see the line by line item in the financial statements and possibly relate it to their own business.

An explanatory sequential design was used for this study, which involved collecting and analysing quantitative and qualitative data (Creswell & Clark 2011). Financial statements were used to calculate the tax expense of thirty small businesses, constituting the quantitative component. Calculations were based on the turnover tax, the small business corporation tax and the normal income tax systems. Once the tax expense was calculated by applying the three tax systems referred to above, based on the relevant information contained in the financial statements, a comparative analysis was performed. In the researcher’s opinion, it is anticipated, that the use of actual figures and explanations will enhance the understanding of the tax legislation and its practical application.

The tax practitioners provided the necessary data of thirty (30) most recent depersonalised (names of the businesses, directors, members and registration numbers were removed) financial statements of small businesses with a turnover of less than one million rand, as this is the criteria for a micro business (South Africa

1962). Due to the confidentiality of this data, it was not possible to obtain thirty small businesses that belonged to the same industry. This study used financial statements from a variety of industries and geographical locations. The participants in this study are discussed below.

3.3 PARTICIPANTS OF THIS STUDY

The participants in this study were four tax practitioners who own consulting and auditing companies and a tax representative who works for a consulting and auditing company. These participants are mainly involved with small and micro businesses. The sampling method and sample size employed is discussed next.

3.3.1 The Sampling Method and Sample Size Used

A convenience sampling technique was employed to identify participants who were accessible and willing to participate in this study. Convenience sampling is also known as haphazard sampling which is when convenient samples are selected for research (Neuman 1997). Tax practitioners were approached and selected to participate in this study based on their willingness to participate. The reason for selecting the convenience sampling technique was that tax practitioners respected the confidentiality regarding the sensitive content of the financial statements, in addition tax practitioners have confidential agreements with their clients which they were not willing to breach. Additionally time was a constraint as tax practitioners were not available to participate in the study.

Neuman (2000:196) states that qualitative researchers select samples (a small collection of cases) or an activity that “illuminates social life” and that the primary purpose of sampling is “to collect specific cases, events or actions that can clarify and deepen understanding”. Small sample sizes enhance the quality of the research findings, by ensuring that only participants who are knowledgeable of the Income Tax Act are engaged and are selected based on the fact that they are easily and conveniently available (Maree & Pietersen 2012, Neuman 1997, Salkind 2012). Small

sample sizes contribute towards reliability and validity of a study (Patton 2002). This study is interpretive in nature, the use of large sample sizes to justify extrapolation of findings is not required (Creswell 2003). Gluckman (2012) applied a similar approach, where a small sample was selected in order to study the fairness of turnover tax in South Africa.

There were five participants in total of whom, four were tax practitioners and one was a tax representative of auditing and consulting firms. The five participants who were approached were willing to participate in this study and provided the qualitative data for this study. Consequently, the participants limited the number of financial statements to a maximum of thirty for the quantitative data analysis. Although it cannot be claimed that this is representative of the small business corporations and micro business and tax practitioner population, based on the nature of the study this sample will provide a good indication of the experiences and opinions of participants towards the turnover tax and small business corporation tax systems. The quantitative analysis will contribute to identifying which tax system is most beneficial to the selected businesses. The specific participants will now be identified and elaborated upon.

3.3.2 Research Participants in this Study

Since this study required the assistance of tax practitioners in providing financial statements as previously mentioned, it was necessary to identify tax practitioners who were willing to participate in this study. The criteria for the selection of the participants for phase three was based on their qualifications, whether they are members of the South African Institute of Chartered Accountants (SAICA), South African Institute of Professional Accountants (SAIPA) or other professional bodies. Other criteria for selection of the participants were their experience in the taxation field, and their involvement in the taxation of small business corporations and micro businesses. These criteria were identified by the researcher in order to verify whether the participants were knowledgeable about the tax systems and were able to understand the interview questions and answer them appropriately. Pseudonyms

were assigned to each participant and financial statements for ethical reasons (Neuman 1997).

Face-to-face interviews were conducted for phase two with five participants. The credentials of these participants are found below:

“Mr Conroy” qualified as a chartered accountant in 1987; other qualifications to his credit are a Masters in Taxation and a Higher Diploma in Taxation. He is currently a tax partner at a small/medium sized firm.

“Mr Moosa” has been practicing for nineteen years, he qualified as a chartered accountant in 1979; another qualification to his credit is a Higher Diploma in Taxation. He is currently the director of Respondent A.

“Mr Adam” has been managing his own practice for thirty years. His qualifications are a Bachelor of Accounting Science (BCompt) honours, Chartered Financial Analyst (CFA), a Higher Diploma in Taxation and a Master of Business Administration. He is a member of the Certified Public Accountants (CPA) and the Association of Accounting Technicians South Africa (AAT) and currently the director of Respondent B.

“Mr Khan” has been an accountant since 1981 and has had his own practice for thirty two years. This participant is a member of Fellow International Association of Book-keepers (FIAB), an MIACC Accounting Tax Practitioner and South African Institute of Management (SAIM). He is currently the director of Respondent D.

“Miss Essop” has six years tax compliance and bookkeeping experience. She is currently studying towards a Bachelor of Commerce and works in a consulting and auditing firm.

The following respondents agreed to participate in this study and provided their financial statements for the 30 case studies:

Respondent A located in Fordsburg provided 10 cases studies,

Respondent B located in Benoni provided 11 cases studies,

Respondent C located in Mayfair provided 4 cases studies and

Respondent D located in Lenasia provided 5 cases studies.

Each of the thirty financial statements were assigned a pseudonym case study one to case study thirty. Five of the financial statements provided were from small businesses located in Lenasia, four in Mayfair, ten in Fordsburg, six in Benoni, one in Sandton, one in Kempton Park, one in Springs and two in Ormonde therefore covering different geographical locations. The businesses were from different industries, nine were from the service industry, and thirteen were real estate, seven retailers and one farmer.

The case studies' turnover levels are presented below:

Number of case studies	**Turnover**
5	Below R200 000
15	R200 000 - R500 000
1	R600 000 - R700 000
3	R700 000 – R800 000
1	R800 000 – R900 000
5	R900 000 – R1 000 000

Twenty six businesses made an accounting profit before tax while four made an accounting loss before tax. The process of data collection will be discussed next.

3.4 DATA COLLECTION

Phase two of the study took the form of face-to-face interviews to obtain the perceptions and opinions of the participants regarding the two tax systems, namely the turnover tax and small business corporation tax systems. An interview is defined as a systematic form of asking questions in an open form or in a standardised form (Flick 2011). According to Neuman (2011) interviews have the highest response rate and permit the lengthiest questions. Another advantage of the interview, identified by Oppenheim (2009) is that the research participants may give a prepared explanation

more convincingly. Questions may be formulated to gain further understanding of the research topic as well as of the actual business practice.

The interview took the form of semi-structured open-ended questions. In this type of interview the conversation is controlled by the interviewer through semi-structured and standardised questions (Kitchen & Tate 2000). This type of interview allowed the participants to elaborate and reflect upon their own thinking rather than restrict their responses through close ended questions (Creswell 2009, Kitchen & Tate 2000). Face-to-face interviews also allowed the opportunity to probe experiences, opinions and concerns regarding the small business corporation tax and turnover tax systems. Furthermore, the interview enabled the researcher to obtain clarity on answers that were unclear or incomplete. In this case the researcher was able to ask additional, more probing questions, where responses lacked detail there were follow up questions asked as well (Vos, Strydom, Fouche & Delport 2002).

Interviews were conducted with participants in their choice of location, as a researcher it was necessary to accommodate the participant. Three (Mr Moosa, Mr Adam and Mr Khan) of the participants were interviewed at their place of business, two were conducted in boardrooms away from the noise and business activities, while one was conducted at the participants desk which was not ideal given the distractions. It was convenient for the researcher as well to conduct the interviews at the place of business as these participants were able to provide the financial statements on the same day. The other two participants were interviewed at their home and a coffee shop respectively. The atmosphere of the home contributed to collecting rich, thick data which was more informative. Although the coffee shop was not an ideal venue for data collection, as it was midday the coffee shop was not busy and the interview could be conducted without any disturbance. Mr Conroy was scheduled for a business meeting thereafter and had made time to accommodate the researcher for the interview. Mr Moosa’s and Khan’s interviews were conducted in October 2013, Mr Adam in November 2013, Miss Essop in December 2013 and Mr Conroy in June 2014. Interview questions were pertinent to answering the main research question, which tax system is more beneficial to the selected small and micro businesses.

Semi-structured open-ended questions were used in the interviews.

Question 1 and 2 was to determine the knowledge of the tax practitioners and tax representative in relation to small and micro businesses. This provided the context for the study as to whether the tax practitioners and tax representatives were knowledgeable about the legislation and changes to the legislation regarding small business corporations and micro businesses to advise their clients.

1. *Describe the tax regimes in terms of which micro businesses will be taxed?*
2. *Describe the tax regimes in terms of which small businesses will be taxed?*

In order to elicit information pertaining to the tax practitioners' and tax representative's opinion of the turnover tax and small business corporation tax systems the following questions guided the investigation:

3. *How do tax practitioners view the benefits and limitations of the turnover tax systems?*
4. *How do tax practitioners view the benefits and limitations of the small business corporation tax system?*

In order to identify which of the two tax systems is more beneficial, it is important to gain the opinions and experiences of the participants about the tax systems. Question 5, 6 and 7 obtained these.

5. *What are your general views of the turnover tax system?*
6. *What are tax practitioners experiences of the small business corporation tax?*
7. *What are tax practitioners' experiences of the turnover tax systems?*

Questions 8 and 9 dealt with how e-filing contributed to the completion, submission and payment of returns and the implications for small and micro businesses.

8. *Does SARS e-filing enable micro businesses to comply with the completion, submission and payment of returns?*
9. *Does SARS e-filing enable micro businesses to deal with disputes?*

Compliance cost appears to be an important aspect when a micro or small business chooses a tax system, question 10 addresses the compliance cost with regard to small and micro businesses. Question 11 enquires whether National Treasury's aim has been achieved and the administrative burden has been reduced for micro businesses.

10. *How does compliance cost affect small and micro businesses?*
11. *Has the administrative burden been reduced for micro businesses?*

Questions 12 and 13 contributed to this study by identifying the types of challenges faced to identify the most applicable tax system for small and micro businesses.

12. *Explain the challenges faced by small businesses?*
13. *Explain the challenges faced by micro businesses?*

As with any tax system, there are changes that need to be made. The research questions below addressed the tax practitioners' and tax representative's suggestions to identify which of the two, namely turnover tax or small business corporations tax is more beneficial to small business corporations and micro businesses and what changes could be made to make these tax systems beneficial to small business corporations and micro businesses. In order to stimulate discussion on the above mentioned suggestion the following research questions were posed:

14. *Do you have any suggestions on how the turnover tax system can be improved to benefit micro businesses?*
15. *Do you have any suggestions on how the small business corporation tax system can be improved to benefit small businesses?*

Once ethical clearance was obtained in accordance with University of South Africa's (UNISA's) ethical policy, the study was undertaken. All interviews were digitally recorded, after having obtained written consent from those tax practitioners and the tax representative who volunteered to participate in this study. Quantitative data

collection took the form of financial statements. As previously mentioned, due to confidentiality, hard copies of depersonalised financial statements of small business corporations and micro businesses with a turnover of less than R1 million were obtained from tax practitioners. The actual financial statements were used in the data analysis and the method of analysing the raw data collected from the interviews is explained below.

3.5 ANALYSIS OF RAW DATA

Raw data collected from face-to-face interviews for this study were transcribed and prepared for analysis using a qualitative data analysis method. “Data analysis means a search for patterns in data – recurrent behaviours, objects, or a body of knowledge” (Neuman 2000:426). The transcribed interviews were coded and analysed for themes using thematic content analysis (Patton 2002). In Oats’ (2012) opinion content analysis involves methodical classification of text in order to “elicit” meaning from it.

Three stages of data analysis were used for phase two, namely, open coding, axial coding and selective coding (Neuman 2011). As stated by Patton (2002) without classification there is chaos. Open coding is performed during the first pass through the raw data. In order to reduce the raw transcribed data, the researcher reads through and assigns codes and labels (Neuman 2011). The comments made by participants were highlighted and assigned a label, for example “knowledge of tax system”. A list of labels was extracted from the labels assigned and put into a word document. The next step in the process of coding was axial coding which is the second pass through initially coded data. The researcher began with the list of labels identified during the open coding process and looked for labels or concepts that could be categorised (Neuman 2011). Additional codes or new ideas may emerge during this process. “During axial coding, the researcher asks about causes and consequences, conditions and interactions, strategies and processes, and will look for categories and concepts that cluster together” (Neuman 1997:423). Common labels are clustered and assigned as themes during the axial coding phase. The final

step is selective coding, which is the final pass through the already coded data. Selective coding is when the strongest themes that emerged are selected (Neuman 2011). This process entails scanning the data and previous codes, looking for themes that emerged in response to the research questions, as well as making comparisons and contrasts (Neuman 2011).

Since the comments made by the participants in this section were not quantified it is necessary to illuminate some of the major themes that emerged after analysis, some of the labels identified during open coding were: knowledge of tax system, good system, negative view, positive view, positive experience, benefits, limitations, recommendation, opinion, compliance costs, threshold, audit trail and lower tax bracket. After axial coding which is the second pass through the data, the following themes emerged: knowledge of the tax systems for small and micro businesses, benefits and limitations of the turnover tax and small business corporation tax systems, compliance costs for small and micro businesses, and tax practitioners and tax representative's suggestions for turnover tax and small business corporation tax. Phase three which employed quantitative analysis of financial statements is discussed below.

The data collected for phase three were analysed using quantitative analysis methods. The financial statements of each case study were analysed to identify the type of business and to recalculate the tax expense for all three tax systems, namely the turnover tax, small business corporation tax and the normal income tax system and lastly to identify which of the three tax systems is most beneficial to each business once all the criteria as per the Income Tax Act are satisfied. The tax expenses were then presented based on the hierarchy identified by the IMF (2007), which is turnover tax then small business corporation tax and finally normal income tax.

The tax expense was calculated using the financial statements, each line item on the financial statement was analysed and the tax consequences were considered. The tax expense on the turnover tax system was calculated using the turnover of the case

study multiplied by the applicable tax rate in Annexure A for micro businesses. The taxable income was calculated for each case study after assessing the income inclusion in taxable income or exclusion, as well as allowable deductions, in accordance with the Income Tax Act (South Africa 1962). Small business corporation tax expense was calculated using the taxable income of the case study multiplied by the applicable tax rate in Annexure A for small businesses. The taxable income was multiplied by 28% for the normal income tax system.

The 2013/2014 tax rates were used to recalculate the tax expense as they were the applicable tax rates when the data (financial statements) were collected, tax rates change annually and are announced by the Minister of Finance during the budget speech. After calculating the tax expense under the three tax systems, each case was assessed against the requirements of the Income Tax Act (South Africa 1962). This was followed by establishing which of the three tax systems is most beneficial to each individual business. Yin (as referred to by Creswell 2013) suggests a table be created to identify similarities and differences among each case as part of the case study analysis. Consequently a spread sheet was used to collate the analysis of the thirty case studies by entering turnover, tax expense, taxable income, accounting fees, expenditure, type of business, the identified tax system based on the analysis referred to in Chapter 5 and lastly the tax system applied by the tax practitioner for each of the case studies. This spread sheet was used to group the businesses into the most beneficial tax system for each case study before the criteria of the Income Tax Act were met (see Annexure B). The reliability and validity of this study will now be discussed.

3.6 RELIABILITY AND VALIDITY

Quantitative research is measured by reliability and validity (Neuman 2011). In order to ensure reliability and validity in this study, financial statements were obtained from tax practitioners and interviews were conducted with tax practitioners and the tax representative to enhance the credibility of this study (Patton 2002). Case studies from different sectors and geographical locations were obtained which aided in

discarding bias and improving validity from different perspectives. Reliability and validity of the study is necessary in order to make the work trustworthy (Kalof, Dan & Dietz 2008). Reliability was achieved as actual figures were used in the case study analysis. The tax rates in Annexure A were used to calculate the tax expense thus ensuring the validity and reliability.

Both quantitative and qualitative methods were used which helped to validate the results and ensured reliability (Golafshani 2003). The reason for choosing tax practitioners was because they would understand tax related statements and questions pertaining to taxation, thus answering these questions appropriately and ensuring overall validity. In addition, participants from different backgrounds were interviewed. “Independent readers may authenticate the findings of the study by following the audit trail of the researcher” (Merriam 2002:27). The audit trail, including the recording of interviews and the thirty financial statements, enhanced the study’s reliability and validity by demonstrating that data had been collected in an authentic manner (Merriam 2002).

In the case of phase one, validity and reliability was attained by performing an extensive literature survey, using credible sources such as the books, legislation, prior research, journal articles, and lastly an analysis and interpretation of the data was performed. The ethical considerations pertaining to this study are presented below.

3.7 ETHICAL CONSIDERATIONS

In order to ensure validity and reliability of a study it is necessary to conduct the investigation in an ethical manner (Merriam 2002). For phase two, upon identifying participants who were willing to be interviewed they were presented with a consent agreement form also known as “informed consent”. This consent agreement was explained to participants in detail, each participant in this study was given a brief overview of the aims and purpose of this study. Participants were informed that their

participation in this study was voluntary and that they could withdraw at any time without any consequences. Written consent to record interviews was obtained from participants. Transcriptions of interviews were kept in a locked cupboard to which no one but the researcher had access to.

The case studies are the financial statements of the clients of the participants in phase two of the study. These financial statements were depersonalised by the tax practitioners prior to the researcher having access to them. Once again, the consent agreement was presented and explained to tax practitioners. Confidentiality was maintained at all times and pseudonyms were assigned to each participant to protect the identity of each individual participating in this study. The depersonalised financial statements collected for this study were not made available to any party, only the researcher and her supervisor had access to these. Participants were provided with the opportunity to peruse the results of this study on completion.

3.8 SUMMARY

This chapter presented and justified the choice of the research methods used in this study. The qualitative and quantitative methodology and analysis were used in this study. A description and explanation of the research participants and case studies used in this study were presented. The next chapter presents the findings and analysis for phase two, which comprised the interviews.

Chapter 4 : FINDINGS AND ANALYSIS OF INTERVIEWS

4.1 INTRODUCTION

This chapter discusses the views of the tax practitioners and a tax representative on the benefits and limitations of the small business corporation tax and turnover tax systems. Chapter two identified and discussed the various forms of taxation applicable to small business corporations and micro businesses and the administrative and taxation implications for small business corporations and micro businesses.

This chapter sets out the findings with regard to the analysis of the data collected from interviews with tax practitioners and a tax representative, for this study. This study included five participants; four tax practitioners who own consulting and auditing companies and a tax representative who works for a consulting and auditing company mainly involved with small business corporations and micro businesses (refer to section 3.3.2). Semi-structured open-ended questions were used in the interview. The data collected from the interviews were analysed using content analysis as described in chapter 3.

Each theme that emerged from the research questions will be discussed and presented under each sub section in response to the questions that elicited the themes. Section 4.2 describes the knowledge of the participants regarding the tax regimes in terms of which small business corporations and micro businesses will be taxed. The benefits and limitations of the turnover tax and small business corporation tax systems are discussed under section 4.3. Section 4.4 deals specifically with compliance costs with respect to small business corporations and micro businesses and participants suggestions for the turnover tax and small business corporation tax system is discussed in section 4.5. Responses are presented for micro and small businesses individually under each theme that emerged. The participants' knowledge of the tax systems for small business corporations and micro businesses is presented below.

4.2 KNOWLEDGE OF THE TAX SYSTEMS FOR SMALL AND MICRO BUSINESSES

4.2.1 Introduction

Research questions 1 and 2 aimed to ascertain the knowledge of the participants in relation to small and micro businesses.

1.	*Describe the tax regimes in terms of which micro businesses will be taxed?*
2.	*Describe the tax regimes in terms of which small businesses will be taxed?*

4.2.2 Tax regimes in terms of which micro businesses will be taxed

The following were responses from the participants. Mr Moosa pointed out that "*turnover tax is available to businesses that have turnover under R1 million*", all but one respondent concurred with him regarding the tax system available to micro businesses. This is in accordance with the Income Tax Act (South Africa 1962). In addition, participants indicated that micro businesses do not have to register for VAT. This is indeed correct although at the time of the interviews the National Treasury had already announced that small businesses will have the option to register for VAT in order to facilitate the access to government tenders. The benefit of this was pointed out by Mr Moosa who stated that "*the VAT system is complex; VAT is levied at 14% on standard products noting few exceptions*". Mr Khan's response was *"micro businesses do not have to register for VAT"*. From this response it may be inferred that turnover tax is beneficial to micro businesses since the VAT administrative burden is removed, thereby making the administrative load lighter as no VAT records are necessary nor do VAT returns have to be filed.

What emerged quite strongly in response to question one was that participants continually referred to the type of businesses such as a sole proprietor and partnership as tax systems. What may be inferred from this incorrect use of terminology is that there may be confusion on the part of the participants regarding

the correct tax terminology and which business would qualify as a micro business as there are specific tax systems available to small businesses.

4.2.3 Tax regimes in terms of which small businesses will be taxed

The participants identified the small business corporation tax system that is available to small businesses, however, they quoted the old gross income requirement of R14 million and below. The statement highlights the fact that the participants have not kept abreast with changes to the tax legislation. Gross Income was amended to R20 million in 2013 (before the interviews were conducted) (National Treasury 2013a).

Apart from their knowledge of the tax regimes in terms of which small businesses will be taxed, the participants indicated that they are aware of the restrictions regarding an individual's interest in other businesses in accordance with the Income Tax Act which states that "*none of the shareholders or members at any time during the year of assessment of the company, close corporation or co-operative holds any shares or has any interest in the equity of any other company as defined in section 1*" (South Africa 1962). Another aspect discussed by the participants was the tax rates, Mr Moosa pointed out that "*a close corporation or company would pay tax at 28%* f*rom the first line of profit*" that is taxable income however, "*a small business corporation is taxed on a sliding scale instead of a fixed 28%".* Mr Moosa stated that "*the tax rates for a small business corporation in 2014, as every year it changes, any profit under R67 111 is 0%, thereafter 7% on anything above R67 112 to R365 000, anything thing above R365 001 to R550 000 is 21%, anything above R550 001 is 28%*". The fact that Mr Moosa did not mention the base tax per bracket to be paid, and merely mentioned the tax rates to be applied to each tax bracket, indicates that he may be providing the marginal tax rate instead of the average tax rate to his clients.

4.2.4 Summary

This section dealt specifically with the participants' knowledge of the tax systems for micro and small businesses. Additionally, it was evident from the responses to the

questions that they lacked tax knowledge as they had not kept abreast with the current legislation and therefore could not speak with authority. The next theme that emerged was benefits and limitations of the turnover tax and small business corporation tax systems.

4.3 BENEFITS AND LIMITATIONS OF THE TURNOVER TAX AND SMALL BUSINESS CORPORATIONS TAX SYSTEMS

4.3.1 Introduction

The benefits and limitations identified by participants of the turnover tax and small business corporation tax system are discussed below. In addition, the benefits of SARS e-filing to small and micro businesses as well as the challenges and administrative burden on small business corporations and micro businesses will follow. The research questions addressed the benefits and limitations to identify which of the two, namely the turnover tax or small business corporation tax system is more beneficial to micro businesses and small business corporations. The benefits and limitations according to the participants are presented next.

4.3.2 Benefits and limitations of the turnover tax system

3.	*How do tax practitioners view the benefits and limitations of the turnover tax system?*
5.	*What are your general views of the turnover tax system?*
7.	*What are tax practitioner's experiences of the turnover tax system?*

The general consensus among the participants was that turnover tax is not a complicated system. Mr Moosa claims that "*it is a simple system, every month you get the businesses turnover and by August you estimate the turnover for the year, make the payment in August and February. Very easy, nothing cumbersome about it, you do not have to keep any records, no purchases, and no expenses".* Mr Adam concurs with Mr Moosa as he says *"do not have to keep records, do not have to do monthly recording. At year end just have to extract balance sheet".* Mr Khan agrees

that turnover tax *is "easier, based on information supplied, easy to do, less paperwork".* These comments are in accordance with the External guide - Turnover tax (SARS, 2012) which clarifies the tax requirements for turnover tax.

A major limitation of the turnover tax system identified by Mr Moosa is that *"you have to apply at the end of February every year, as the year of assessment for turnover tax is February. People come to accountants during the year, even though they qualify for the turnover tax system, they have to wait for the next year. Therefore they register into a system that is not suitable for their business or set up. Cumbersome, you send a document in February and receive a response six to eight months later. What do you do in the interim?"* What may be inferred from the above response is that micro businesses may only register for the turnover tax system at the end of February. If a micro business does not meet the February deadline for registration for turnover tax, they will have to remain on their current tax system or in the case of a new business they will have to register on the normal income tax system or the small business corporation tax system if all the requirements are satisfied.

Therefore as pointed out by Mr Moosa micro businesses have to register on a tax system that is "*not suitable*" for their business. The turnover tax system was repeatedly described as "*cumbersome*" by Mr Moosa, "*cumbersome, should be available throughout the year. And also if someone applies in February, only receive an answer six to eight months later. What does a micro business do for 14 months of the year? How do you advise him? Therefore timing is a limitation. Should be able to go into the system and 24 hours later have it*". From the above response it is evident that despite Mr Moosa's earlier comment that turnover tax is easy, it is evident that he has had negative experiences with the turnover tax system.

Mr Adam does not have any businesses on the turnover tax system, he says "*discourage businesses as it is a* waste of time". *"Tedious and not a good system because personal services are excluded from the definition of a micro business"* is Mr Conroy's opinion of the turnover tax system. What may be inferred from these

comments is that they may be discouraging micro businesses from registering on the turnover tax system.

In Ms Essop's opinion "*being fully taxed on turnover and not on net income, therefore after expenses. Even if turnover less than R1 million they will be taxed on turnover and not on net, if they register as a SME, they will pay lower tax in that sense. They have to weigh up their options, whether SME or turnover tax will benefit them*". Micro businesses are taxed on turnover before expenses are taken into consideration, Ms Essop perceives this as a disadvantage because had they registered for taxes as SME's they would pay lower tax. All the other participants concurred with Ms Essop. The benefits and limitations of the small business corporation tax system according to the participants are presented next.

4.3.3 Benefits and limitations of the small business corporation tax system

4.	*How do tax practitioners view the benefits and limitations of the small business corporation tax system?*
6.	*What are tax practitioners experiences of the small business corporation tax?*

Ms Essop is of the opinion that "*the only benefit is the tax rate, the first bracket up to R300 000, thereafter it is the same as the normal tax system for any big business or company. SARS does not care if you are a sole trader, close corporation or what company you are, they require the same information and documents. Regardless of the type of company, the same rules apply*". With reference to the tax rates for small business corporations in Annexure A, taxable income up to R300 000 is beneficial to small business corporations as no base tax that is no fixed amount in addition to the percentage is payable, only 7% of taxable income above R67 111 is payable. On the other hand Mr Khan claims that "*tax itself across the line is the same. With small businesses you do not require a chartered accountant, a bookkeeper can compile the financial statements*". According to Mr Adam small business corporation tax is "*very much easier, a lot is based on information supplied, easy to do because you will take it from information and less paperwork, easy to do*". Mr Conroy is of the opinion that the small business corporation tax system is a good system because "*it is better than*

paying 28 percent." The above mentioned participants found various benefits to the small business corporation tax system, however, three limitations to the system were also highlighted by Ms Essop "*personal service providers are not allowed to register, companies are practically only allowed, trusts cannot register. Turnover requirements are low. They have to be a close corporation, companies, cannot be trust".* Although Ms Essop highlighted the turnover requirement as low, the government has increased this from R14 million in 2012 to R20 million in 2013 (National Treasury, 2013a).

"*On a bookkeeping side you still have to keep records the fees will be high for a small business. Have to do a cash book, trial balance, financial statements*" is what Mr Adam views as a limitation. In other words he believes that the workload would be the same as that of a larger business. It is necessary to mention that there are also benefits and limitations of e-filing as perceived by the participants.

4.3.4 Benefits and limitations of e-filing

8.	*Does SARS e-filing enable micro businesses to comply with the completion, submission and payment of returns?*
9.	*Does SARS e-filing enable micro businesses to deal with disputes?*

Research question 8 and 9 assisted in identifying the benefits and limitations of e-filing. SARS e-filing has proved to be quite beneficial to the participants. Although e-filing is a general benefit, due to the size of small business corporations and micro businesses, it saves time as opposed to manually submitting and delivering the return and also reduces the compliance costs. According to Ms Essop "*it's brilliant. Most productive and progressive thing the country has done with regards to its tax system. No manual submission, does not require you to go into SARS office, can collect data, submit, file and pay online. And get assessed online. It makes it easier for micro businesses can file income tax, VAT and PAYE online. They have taken away the debit pull system away but that is to reduce fraud*".

Other participants concur with Ms Essop, that SARS has made it easier for taxpayers. Small and micro businesses can comply with the completion, submission and payment of returns through the e-filing system. In addition, they are able to deal with disputes online. However, Mr Moosa stated that "*you still have to take the documents and hand it to SARS. Time consuming, takes four hours of a person's day and there is no return on that money, will not be paid by client for that time. They do not have the time or knowledge or expertise to deal with disputes. Micro businesses cannot leave their business, they do not have time to go to SARS. When you go to SARS, you get a ticket, wait three hours, SARS accepts the document and they say they will contact you. Do not achieve anything*". Overall, all the participants agreed that despite the advantages related to e-filing it was still necessary to present the tax documents at the SARS offices. There are various challenges faced by small and micro businesses which are discussed next.

4.3.5 Challenges faced by small and micro businesses

12.	*Explain the challenges faced by small businesses?*
13.	*Explain the challenges faced by micro businesses?*

Non-compliance by businesses that compete with small businesses is a challenge for small and micro businesses. "*Very difficult to get finance, continuously shrinking market, every big company, conglomerate, departmental store now sells everything, example, Game now sells food, what does a small business do. Kills all the small grocers, stationery, cosmetic shops. Conglomerates have everything and at better rates, they can sell at better rates because they buy in bulk and get better rates to sell to customers*" said Mr Moosa, when asked about challenges that small and micro businesses face.

The overall response from the participants was that the main challenge faced by small and micro businesses is competition from larger businesses. In this regard Mr Adam claims, "*now small businesses are taking the back seat due to the corporates, the new malls. Small businesses are suffering, turnover has decreased on clients.*

Also the economy and the rand/dollar affects everything across the line". Small businesses are unable to survive in the current economic climate as is evident from Ms Essop's comment "*competition, big chain stores, they have better rates. Small businesses cannot grow. Cannot blame consumers for supporting bigger chain stores. In South Africa we do not support small businesses and they are being killed by vendors and foreigners and Chinese markets, they do not register for VAT. In small areas alone there are China Malls and their prices are lower. Foreign vendors do not register, they trade below the thresholds and do not contribute to our economy, they put prices lower, they have no living costs so can keep prices low and kill our local businessmen*". This is the opinion of Ms Essop however, there is no empirical evidence to support this claim.

4.3.6 Summary

This section presented the benefits and limitations of the turnover tax and small business corporation tax system. Based on the information gathered the benefits outweigh the limitations for the turnover tax and small business corporation tax system. The benefits of e-filing were also presented above. In addition the challenges faced by small and micro businesses were highlighted. At this point it is necessary to discuss compliance costs for small and micro businesses.

4.4 COMPLIANCE COSTS FOR SMALL AND MICRO BUSINESSES

4.4.1 Introduction

Compliance costs are the costs to comply with legislation or regulations and compliance costs with respect to the turnover tax and small business corporation tax system is presented below.

10.	*How does compliance costs affect small and micro businesses?*
11.	*Has the administrative burden been reduced for micro businesses?*

4.4.2 Compliance Costs

All of the participants were of the opinion that small businesses face the same as or higher compliance cost than larger businesses. The participants indicated that the administration burden has been reduced for micro businesses, therefore turnover tax might be cheaper. In Mr Khan's opinion micro businesses face lower compliance costs due to the size of their business. Ms Essop found compliance costs,

> "*… huge for small businesses. On a broad scope, not only looking at tax the requirements to the labour department. Look at workman's compensation. They have massive payrolls. Like construction sites there is so many employees, although they pay them minimal the compliance costs is huge. Like metal workers, there are industry requirement per your industry, so have to register under certain regulations per industry. Compliance payments kills small businesses, it restricts growth and have to protect employees. Also tax compliance, look at SME their tax compliance is costly, they are required to pay PAYE and VAT, they are required to keep bookkeeping systems. They need accounting software and payroll software and so on also depending on the size. Maybe streamline system into a smarter way of controlling the accounting system. Our country cannot streamline compliance however, they need to. They work because their functions are separate. Looking at SARS and labour departments, they work because they are separate.*"

What may be inferred from Ms Essop's statement is that smaller businesses bear a high compliance burden despite its size. As stated by Mr Moosa "*the owner does everything, he's the marketing person, selling person, purchasing person, packer, administrator, accountant, distributor, difficult to fulfil all the roles of the business. Cannot afford to employ other people*". The above statements bear evidence to the fact that it is difficult for small and micro businesses to comply with the taxation rules and regulations thus forcing them to outsource the taxation function.

4.4.3 Summary

From the discussion of compliance costs and the participants opinions of compliance costs that are presented above it is evident that small business corporations and micro businesses experience similar compliance costs to large businesses. Additionally, because of their size they are forced to outsource the accounting and taxation functions which are a financial burden to the small businesses. The

participants' suggestions for turnover tax and small business corporation tax are discussed below.

4.5 TAX PRACTITIONERS AND TAX REPRESENTATIVE SUGGESTIONS FOR TURNOVER TAX AND SMALL BUSINESS CORPORATION TAX

4.5.1 Introduction

From the interviews conducted with the participants a number of suggestions were made regarding turnover tax and small business corporation tax, how the systems may be improved to benefit small and micro businesses.

14.	*Do you have any suggestions on how the turnover tax system can be improved to benefit micro businesses?*
15.	*Do you have any suggestions on how the small business corporation tax system can be improved to benefit small businesses?*

4.5.2 Tax practitioners' and tax representative's suggestions for turnover tax and small business corporation tax

Mr Moosa suggests that SARS should "*increase the turnover threshold. R1 million is too low, should be at least R3 million*". Ms Essop and Mr Adam support this suggestion, and Mr Khan suggested that an audit trail be maintained in order for micro businesses to be compliant. The tax expense for each taxable income bracket for small business corporation tax should be lowered.

Participants believed the tax threshold should be increased for small and micro businesses. Compared to the fixed expenses of a micro business, currently the tax thresholds are too low. Mr Khan suggested that the government should assist small businesses with finance.

4.5.3 Summary

The general consensus of the participants was that the tax thresholds should be increased thereby reducing the tax payable by small business corporations and micro

businesses. Micro businesses should maintain a paper trail of all records in order to be more compliant.

4.6 SUMMARY OF CHAPTER FOUR

This chapter presented the results of the analysed data. Each theme that emerged from the analysis of the data was discussed in depth presenting the actual words of the participants. The knowledge of the participants regarding the tax systems for small business corporations and micro businesses was discussed as well as the benefits and limitations of the turnover tax and small business corporation tax systems. Compliance costs also came under scrutiny with respect to small business corporations and micro businesses and finally participants' suggestions for turnover tax and small business corporation tax were discussed. The next chapter presents a quantitative analysis of the financial statements of the thirty cases selected for this study.

Chapter 5 : ANALYSIS AND FINDINGS OF CASE STUDIES (FINANCIAL STATEMENTS)

5.1 INTRODUCTION

The tax payable using the different tax systems in the thirty selected case studies are presented below. This chapter sets out the analysis and findings of the most recent financial statements of businesses which will be referred to as case studies. The study consisted of thirty financial statements of small business corporations and micro businesses with a turnover of less than R1 million. The data collected from the financial statements were analysed using quantitative analysis as described in Chapter Three.

A quantitative analysis was carried out on each case study by analysing the financial statements to identify the type of business, to recalculate the tax expense for all three tax systems, namely turnover tax, small business corporation tax and the normal income tax system and lastly to identify which of the three tax systems is most beneficial to the business once all the criteria as per the Income Tax Act are satisfied. The tax expense was presented based on the hierarchy identified by IMF (2007), which is turnover tax then the small business corporation tax and finally the normal income tax. The demographics of the thirty financial statements are presented next in 5.2 followed by the analysis of the thirty financial statements in 5.3 and the Davis Tax Committee proposal in 5.4.

5.2 DEMOGRAPHICS OF FINANCIAL STATEMENTS

As previously mentioned, five businesses are located in Lenasia, four in Mayfair, ten in Fordsburg, six in Benoni, one in Sandton, one in Kempton Park, one in Springs and two in Ormonde consequently covering different geographical regions. The businesses are located in different industries, nine are from the service industry, thirteen are in the real estate industry, one is a farmer and seven are retailers.

Twenty six businesses made an accounting profit before tax while four made an accounting loss before tax. Of the thirty case studies, only sixteen had capital assets and fourteen did not.

The cases were grouped according to their demographics and analysed, to avoid repetition. The cases were presented according to the different industries, seven cases that belong to the retail industry and one to farming, nine that belong to the service industry and thirteen that belong to real estate. A presentation of the analysis of the financial statements is discussed below.

5.3 ANALYSIS OF FINANCIAL STATEMENTS

5.3.1 Introduction

Case studies were categorised based on their demographics as mentioned above. For each of the categories a summary of the information available will be provided, this will take the form of a description of the business activities as well as the basic financial information for the business and is followed by a discussion of the tax liability of the case study under each of the different tax systems investigated in this chapter.

In order to compare the tax liability under the different tax systems, it was assumed that each case study had qualified to be taxed under each of the tax systems and were either companies or CC's. The tax liability of each case was calculated despite the fact that the description of the business could indicate that it might, for example, not qualify as a small business corporation due to the fact that the owner owns shares in more than one company. Following a discussion of the case study results, a recommendation of the best tax system for each case study will be made, based on the description of the business and the information contained in the financial statements.

In order to calculate the tax liability under the different tax systems the cost of assets were calculated on the assumption that the accounting depreciation was calculated over a five year period. Similarly the wear-and-tear allowance that could be claimed under section 11(*e*) read with Binding General Ruling No 7, was calculated over a five year period. Based on the assumption that the assets qualified for a section 11(*e*) allowance, the corresponding section 12E(1A) allowance was used for a small business corporation.

In order to ensure comparability of the tax liability under the different systems it is assumed that all profit (after normal tax) will be distributed to the owners of the business. It was assumed that no prior year reserves exist for dividend distribution. It is further assumed that this distribution will constitute a dividend or deemed dividend subject to the provisions of Part VIII of the Income Tax Act. The thirty case studies are presented below.

5.3.2 Farming and Retailers

Description of the businesses

In terms of informed consent procedures, the tax practitioner elected to remove the type of business, making it difficult to determine the type of business. An analysis of the financial statements suggests that case studies one to seven sell goods to the public and case study eight sells livestock.

Financial information

Table 3 below presents the financial information available for case studies one to eight.

Table 3: Financial information for case studies one to eight

	One (R)	Two (R)	Three (R)	Four (R)	Five (R)	Six (R)	Seven (R)	Eight (R)
Turnover (Gross income in terms of gross income definition in *s1* of the Income Tax Act)	357 916	352 100	202 464	925 580	271 236	768 645	425 869	983 891
Less: Cost of goods sold	(214 963)	(53 350)	(133 910)	(476 128)	(186 002)	(505 625)	(181 174)	(625 102)
Opening Stock (deductible in terms of s22*(2)* of the Income Tax Act)	0	18 500	0	0	31 269	38 220	115 247	153 207
Purchases (deductible in terms of s11*(a)* of the Income Tax Act)	245 875	54 000	133 910	901 387	184 850	507 381	187 163	638 012
Closing Stock (included in terms of s22*(1)* of the Income Tax Act)	(30 912)	(19 150)	0	(425 259)	(30 117)	(39 976)	(121 236)	(166 117)
Less: Allowable deductions (deductible in terms of s11*(a)* of the Income Tax Act)	(139 314)	(272 028)	(74 371)	(323 235)	(50 155)	(243 625)	(167 736)	(314 444)
Accounting Fees	6 000	3 600	1 450	20 000	1 250	5 500	2 850	4 000

	One (R)	Two (R)	Three (R)	Four (R)	Five (R)	Six (R)	Seven (R)	Eight (R)
Advertising	0	14 500	2 250	0	0	0	0	0
Bank Charges	0	0	3 110	7 416	436	1 523	1 599	3 886
Computer costs	0	0	0	0	0	0	0	369
Feed	0	0	0	0	0	0	0	35 127
Finance Charges	0	0	16 509	0	0	0	0	0
First aid	0	0	0	0	0	0	0	501
Insurance	0	0	9 000	0	0	6 627	0	0
Members salaries	0	0	0	209 439	0	60 000	0	72 000
Motor, travelling and deliveries	0	0	0	21 133	13 671	17 269	28 455	41 225
Owners salary	55 000	57 600	0	0	0	0	0	0
Packaging and wrapping	0	0	0	0	449	0	0	0
Printing and stationery	0	0	0	0	236	375	0	1 767
Rent, water and electricity	48 417	90 500	37 285	54 520	12 000	61 081	74 611	25 339
Salaries and wages	20 800	80 213	0	0	15 000	91 250	45 700	126 000
Security	0	0	0	0	0	0	5 965	3 115
Telephone and postages	5 877	12 250	4 767	10 727	6 978	0	8 556	369
Teas and cleaning	3 220	13 365	0	0	135	0	0	746

	One (R)	Two (R)	Three (R)	Four (R)	Five (R)	Six (R)	Seven (R)	Eight (R)
Less: Maintenance and Repairs (deductible in terms of s11(*d*) of the Income Tax Act)	0	(10 900)	0	(9 839)	0	0	0	(1 345)
Taxable income sub-total (before capital allowances)	3 639	15 822	(5 817)	116 378	35 079	19 395	76 959	43 000
Depreciation on capital assets	3 727	3 543	26 106	9 841	2 059	9 034	359	6 430
Calculated value of capital assets (depreciation x 5 years)	18 635	17 715	130 530	49 205	10 295	45 170	1 795	32 150

5.3.2.1 Case Study One

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R357 916. Based on the sliding scale the tax liability would be R2 658 (R1 500 + 2% x (R357 916 - R300 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study ones total tax liability under this option would therefore be R2 658.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be entitled to claim the following capital allowances in each of the first three years that the asset is used. It is assumed that the loss from one year would be carried over to the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	3 639	3 639	3 639	3 639	3 639
Less: Section 12E(1A) allowance	(9 318)	(5 590)	(3 727)	0	0
Less: Assessed loss (section 20)	0	(5 679)	(7 630)	(7 718)	(4 079)
Taxable income/ (loss)	(5 679)	(7 630)	(7 718)	(4 079)	(440)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(5 109)				

Since the business had made a loss there will not be any liability for normal tax and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above)	3 639	3 639	3 639	3 639	3 639
Less: Section 11(*e*) allowance	(3 727)	(3 727)	(3 727)	(3 727)	(3 727)
Less: Assessed loss (section 20)	0	(88)	(176)	(264)	(352)
Taxable income/ (loss)	(88)	(176)	(264)	(352)	(440)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(264)				

As the business made a loss there will not be any liability for normal tax and no dividends tax liability as there is no income to be distributed.

Figure 2: Summary of case study ones total tax payable

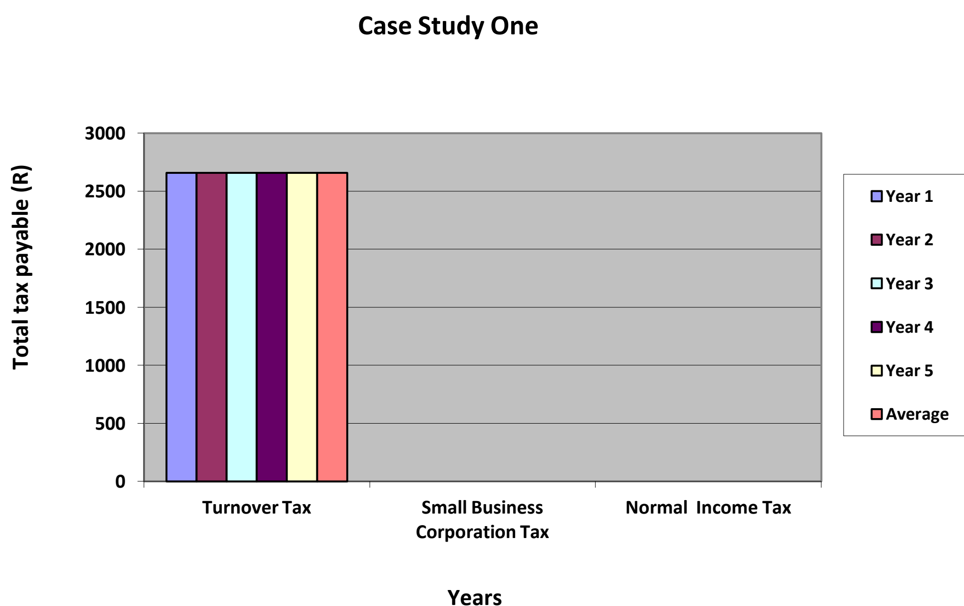


Figure 2 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For small business corporation and normal income tax, if all requirements are met, case study one can offset the tax loss against future taxable income.

5.3.2.2 Case Study Two

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R352 100. Based on the sliding scale the tax liability would have been R2 542 (R1 500 + 2% x (R352 100 - R300 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twos total tax liability under this option would therefore have been R2 542.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year will be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	15 822	15 822	15 822	15 822	15 822
Less: Section 12E(1A) allowance	(8 858)	(5 314)	(3 543)	0	0
Taxable income	6 964	10 508	12 279	15 822	15 822
Normal tax payable	0	0	0	0	0
Dividend tax	1 045	1 576	1 842	2 373	2 373
Total tax payable	1 045	1 576	1 842	2 373	2 373
Average total tax for 5 years	1 842				

Had the business chosen the small business corporation tax system, their tax liability for year one would have been calculated based on its taxable income of R6 964 calculated above. Based on the sliding scale the tax liability would be R0 (R6 964 x 0%). The dividends tax liability would be R1 045 (R6 964 x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	15 822 (3 543)	15 822 (3 543)	15 822 (3 543)	15 822 (3 543)	15 822 (3 543)
Taxable income	12 279	12 279	12 279	12 279	12 279
Normal tax payable	3 438	3 438	3 438	3 438	3 438
Dividend tax	1 326	1 326	1 326	1 326	1 326
Total tax payable	4 764	4 764	4 764	4 764	4 764
Average total tax for 5 years	4 764				

The tax liability for year one would have been calculated on its taxable income of R12 279, with a tax liability of R3 438 (R12 279 x 28%). The dividends tax liability would have been R1 326 ((R12 279 - R3 438) x 15%).

Figure 3: Summary of case study twos total tax payable

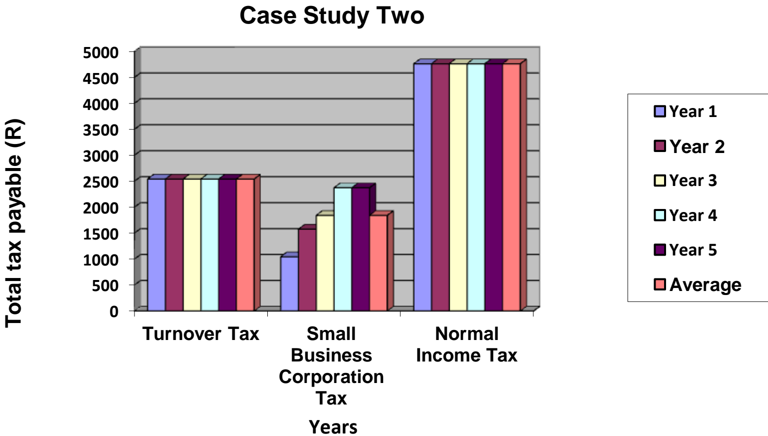


Figure 3 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.2.3 Case Study Three

Turnover tax liability

Had the business chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R202 464. Based on the sliding scale the tax liability would have been R525 (1% x (R202 464 – R150 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study threes total tax liability under this option would therefore have been R525.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year will be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	(5 817)	(5 817)	(5 817)	(5 817)	(5 817)
Less: Section 12E(1A) allowance	(65 265)	(39 159)	(26 106)	0	0
Less: Assessed loss (section 20)	0	(71 082)	(116 058)	(147 981)	(153 798)
Taxable income/ (loss)	(71 082)	(116 058)	(147 981)	(153 798)	(159 615)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(129 707)				

As the business is making a loss there will be no liability for normal tax and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance Less: Assessed loss (section 20)	(5 817) (26 106) 0	(5 817) (26 106) (31 923)	(5 817) (26 106) (63 846)	(5 817) (26 106) (95 769)	(5 817) (26 106) (127 692)
Taxable income/ (loss)	(31 923)	(63 846)	(95 769)	(127 692)	(159 615)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(95 769)				

As the business made a loss there will be no liability for normal tax and no dividends tax liability as there is no income to be distributed.

Figure 4: Summary of case study threes total tax payable

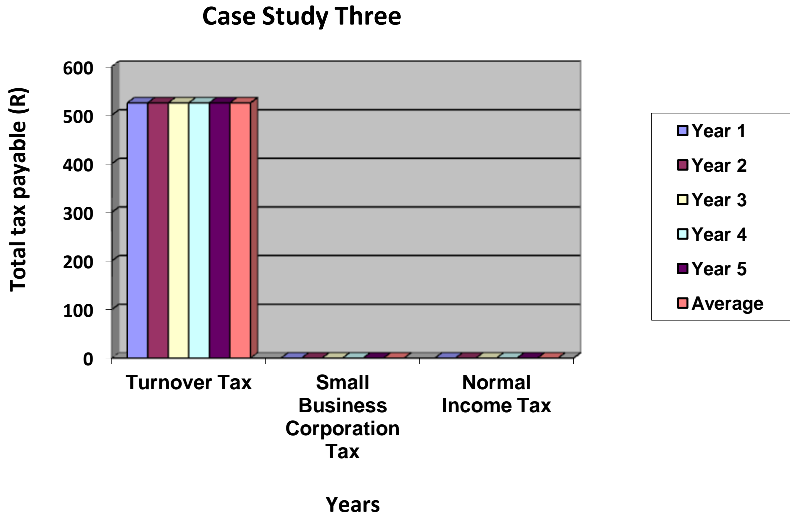


Figure 4 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the small business corporation and normal income tax if all requirements are met, case study three can offset the tax loss against future taxable income.

5.3.2.4 Case Study Four

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R925 580. Based on the sliding scale the tax liability would have been R26 035 (R15 500 + 6% x (R925 580 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study fours total tax liability under this option would therefore have been R26 035.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year will be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	116 378 (24 603)	116 378 (14 761)	116 378 (9 841)	116 378 0	116 378 0
Taxable income	91 775	101 617	106 537	116 378	116 378
Normal tax payable	1 726	2 415	2 760	3 449	3 449
Dividend tax	13 507	14 880	15 566	16 939	16 939
Total tax payable	15 233	17 295	18 326	20 388	20 388
Average total tax for 5 years	18 326				

The tax liability for year one would have been calculated on its taxable income of R91 775, with a tax liability of R1 726 (7% x (R91 775 – R67 111)). The dividends tax liability would have been R13 507 ((R91 775 – R1 726) x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	116 378 (9 841)	116 378 (9 841)	116 378 (9 841)	116 378 (9 841)	116 378 (9 841)
Taxable income	106 537	106 537	106 537	106 537	106 537
Normal tax payable	29 830	29 830	29 830	29 830	29 830
Dividend tax	11 506	11 506	11 506	11 506	11 506
Total tax payable	41 336	41 336	41 336	41 336	41 336
Average total tax for 5 years	41 336				

Under the normal income tax system, in year one the business would have had a tax liability of R29 830 (R106 537 x 28%). The dividends tax liability would have been R11 506 ((R106 537 – R29 830) x 15%).

Figure 5 Summary of case study fours total tax payable

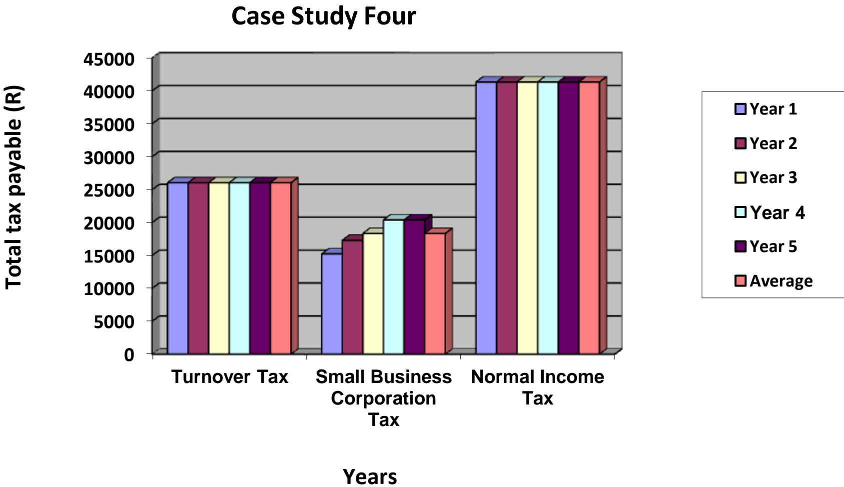


Figure 5 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.2.5 Case Study Five

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R271 236. Based on the sliding scale the tax liability would have been R1 212 (1% x (R271 236 – R150 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study fives total tax liability under this option would therefore have been R1 212.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	35 079 (5 148)	35 079 (3 088)	35 079 (2 059)	35 079 0	35 079 0
Taxable income	29 931	31 991	33 020	35 079	35 079
Normal tax payable	0	0	0	0	0
Dividend tax	4 490	4 799	4 953	5 262	5 262
Total tax payable	4 490	4 799	4 953	5 262	5 262
Average total tax for 5 years	4 953				

Had the business chosen the small business corporation tax system, their tax liability for year one would have been calculated based on its taxable income of R29 931

calculated above. Based on the sliding scale the tax liability would be R0 (R29 931 x 0%). The dividends tax liability would be R4 490 (R29 931 x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	35 079 (2 059)	35 079 (2 059)	35 079 (2 059)	35 079 (2 059)	35 079 (2 059)
Taxable income	33 020	33 020	33 020	33 020	33 020
Normal tax payable	9 246	9 246	9 246	9 246	9 246
Dividend tax	3 566	3 566	3 566	3 566	3 566
Total tax payable	12 812	12 812	12 812	12 812	12 812
Average total tax for 5 years	12 812				

The tax liability would have been calculated on its taxable income of R33 020, with a tax liability of R9 246 (R33 020 x 28%). The dividends tax liability would be R3 566 ((R33 020 - R9 246) x 15%).

Figure 6: Summary of case study fives total tax payable

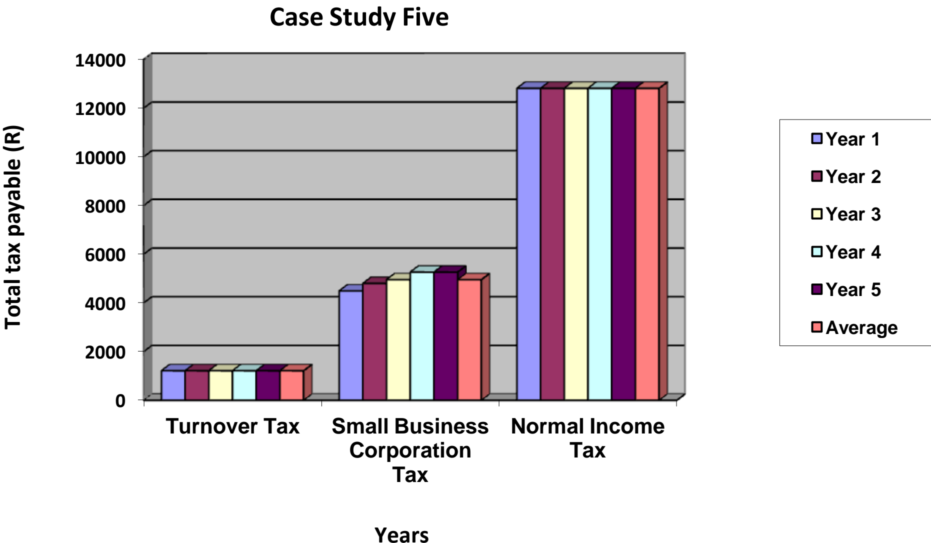


Figure 6 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.2.6 Case Study Six

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R768 645. Based on the sliding scale the tax liability would have been R16 619 (R15 500 + 6% x (R768 645 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study sixs total tax liability under this option would therefore be R16 619.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be eligible to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be used in the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance Less: Assessed loss (section 20)	19 395 (22 585) 0	19 395 (13 551) (3 190)	19 395 (9 034) 0	19 395 0 0	19 395 0 0
Taxable income/(loss)	(3 190)	2 654	10 361	19 395	19 395
Normal tax payable	0	0	0	0	0
Dividend tax	0	398	1 554	2 909	2 909
Total tax payable	0	398	1 554	2 909	2 909
Average total tax for 5 years	1 554				

As the business made a loss in year one there would not be any liability for normal tax and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	19 395 (9 034)	19 395 (9 034)	19 395 (9 034)	19 395 (9 034)	19 395 (9 034)
Taxable income	10 361	10 361	10 361	10 361	10 361
Normal tax payable	2 901	2 901	2 901	2 901	2 901
Dividend tax	1 119	1 119	1 119	1 119	1 119
Total tax payable	4 020	4 020	4 020	4 020	4 020
Average total tax for 5 years	4 020				

Under the normal income tax system, the business would have had a tax liability of R2 901 (R10 361 x 28%). The dividends tax liability would have been R1 119 ((R10 361 – R2 901) x 15%).

Figure 7: Summary of case study sixes total tax payable

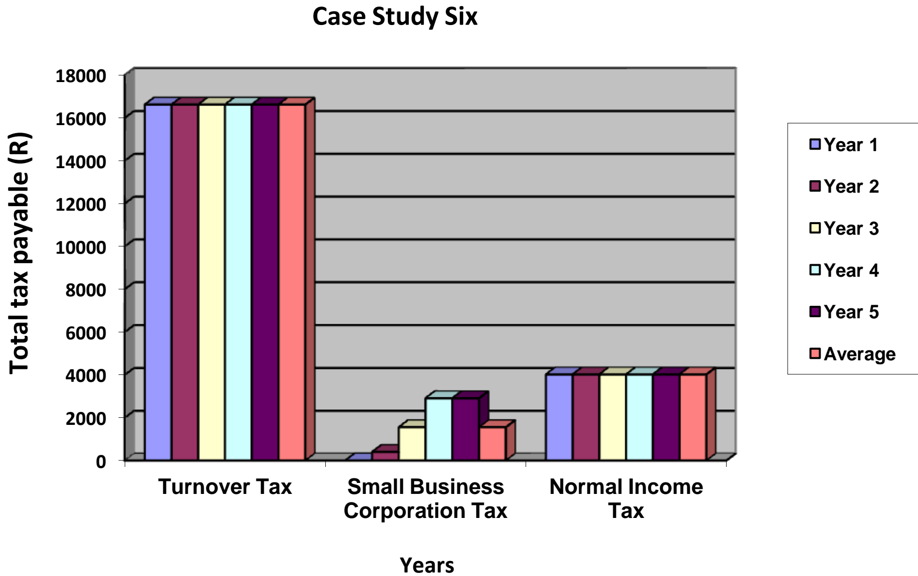


Figure 7 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.2.7 Case Study Seven

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R425 869. Based on the sliding scale the tax liability would be R4 017 (R1 500 + 2% x (R425 869 – R300 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study sevens total tax liability under this option would therefore have been R4 017.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	76 959 (898)	76 959 (538)	76 959 (359)	76 959 0	76 959 0
Taxable income	76 061	76 421	76 600	76 959	76 959
Normal tax payable	626	651	664	689	689
Dividend tax	11 315	11 365	11 390	11 440	11 440
Total tax payable	11 941	12 016	12 054	12 129	12 129
Average total tax for 5 years	12 054				

The tax liability would have been calculated on its year one taxable income of R76 061, with a tax liability of R626 (7% x (R76 061 – R67 111)). The dividends tax liability would have been R11 315 ((R76 061 – R626) x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	76 959 (359)	76 959 (359)	76 959 (359)	76 959 (359)	76 959 (359)
Taxable income	76 600	76 600	76 600	76 600	76 600
Normal tax payable	21 448	21 448	21 448	21 448	21 448
Dividend tax	8 273	8 273	8 273	8 273	8 273
Total tax payable	29 721	29 721	29 721	29 721	29 721
Average total tax for 5 years	29 721				

Under the normal income tax system, the business would have had a tax liability of R21 448 (R76 600 x 28%). The dividends tax liability would be R8 273 ((R76 600 – R21 448) x 15%).

Figure 8: Summary of case study sevens total tax payable

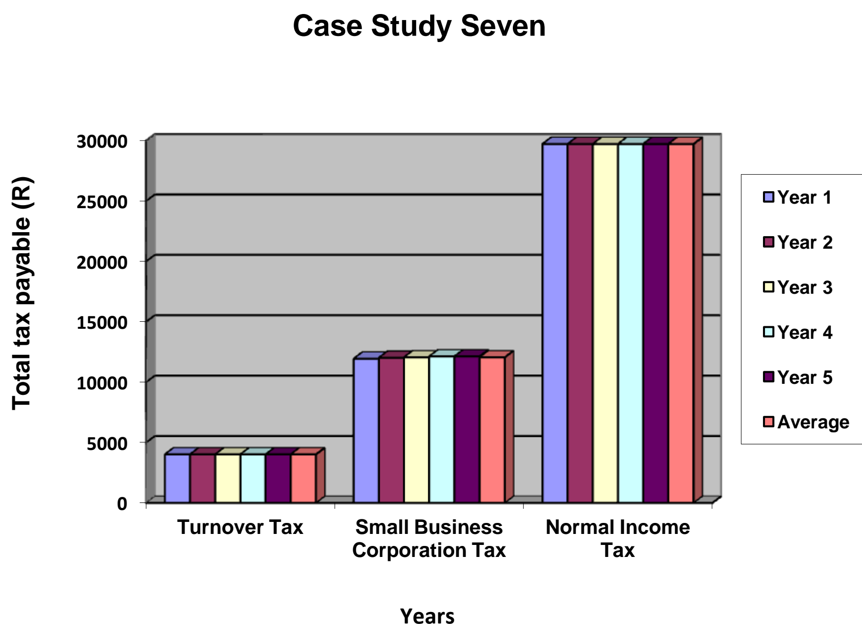


Figure 8 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.2.8 Case Study Eight

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R983 891. Based on the sliding scale the tax liability would have been R29 533 (R15 500 + 6% x (R983 891 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study eights total tax liability under this option would therefore have been R29 533.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be eligible to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over to the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	43 000 (16 075)	43 000 (9 645)	43 000 (6 430)	43 000 0	43 000 0
Taxable income	26 925	33 355	36 570	43 000	43 000
Normal tax payable	0	0	0	0	0
Dividend tax	4 039	5 003	5 485	6 450	6 450
Total tax payable	4 039	5 003	5 485	6 450	6 450
Average total tax for 5 years	5 485				

The tax liability would have been calculated on its year one taxable income of R26 925, with a tax liability of R0 (0% x R26 925). The dividends tax liability would have been R4 039 (R26 925 x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	43 000	43 000	43 000	43 000	43 000
Less: Section 11(*e*) allowance	(6 430)	(6 430)	(6 430)	(6 430)	(6 430)
Taxable income	36 570	36 570	36 570	36 570	36 570
Normal tax payable	10 239	10 239	10 239	10 239	10 239
Dividend tax	3 950	3 950	3 950	3 950	3 950
Total tax payable	14 189	14 189	14 189	14 189	14 189
Average total tax for 5 years	14 189				

Under the normal income tax system, the business would have had a tax liability of R10 239 (R36 570 x 28%). The dividends tax liability would have been R3 950 ((R36 570 – R10 239) x 15%).

Figure 9: Summary of case study eights total tax payable

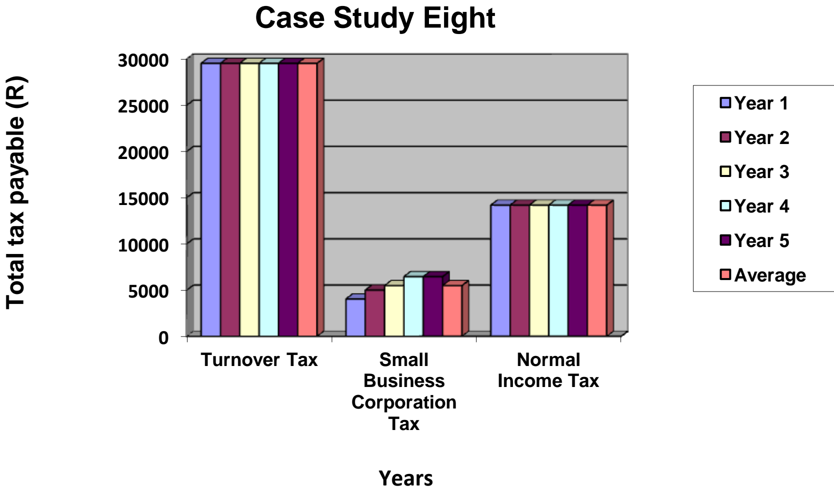


Figure 9 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.2.9 Summary and Conclusion for Case Studies One to Eight

The results for case studies one to eight can be summarised as follows:

Table 4: Total tax liability/ (taxable loss) for case studies one to eight for year one

Case Study	**Turnover Tax (R)**	**Small Business Corporation Tax/ (Taxable Loss) (R)**	**Normal Tax/ (Taxable Loss) (R)**
1	2 658	(5 679)	(88)
2	2 542	1 045	4 764
3	525	(71 082)	(31 923)
4	26 035	15 233	41 336
5	1 212	4 490	12 812
6	16 619	(3 190)	4 020
7	4 017	11 941	29 721
8	29 533	4 039	14 189

Table 4 is a summary of the total tax liability/ (taxable loss), includes dividends tax for case studies one to eight on each of the three tax systems. This data was collated from the above calculations.

The most beneficial tax system for case studies one to four, six and eight would be the small business corporation tax system as the businesses would have had the lowest or no tax liability and would have been entitled to carry over the assessed loss to the next financial year and offset against future taxable income, if all the prerequisites are met. All the requirements of section 12E(4)(*a*) of the Income Tax Act have to be satisfied to apply the small business corporation tax system, the Income Tax Act defines a small business corporation as any close corporation or co-operative or any private company as defined in section 1 of the Companies Act,

2008 (Act No. 71 of 2008) and the gross income should not exceed R20 million, none of the members hold any shares in other companies, not more than 20 percent of total receipts and accruals consist of personal service or investment income. Case studies four, six and eight meet all the requirements of a small business corporation.

It may be assumed that it would be more beneficial for cases one to three to register as companies or close corporations and apply the small business corporation tax system as the tax expense is easy to calculate. The tax liability is based on the income and expenses of the business and the business could take advantage of the lower tax rates, and accelerated wear and tear allowance on assets. However, as per the Companies Act, no new close corporations may be formed or converted to companies after 1 May 2011 (Cassim, Cassim, Cassim, Jooste, Shev & Yeats 2012).

The most beneficial tax system for case study five and seven would be the turnover tax system as the least total tax after dividend tax would be payable. The tax payable is based merely on the turnover of the business. To use the turnover tax system all the criteria of the Sixth Schedule and section 48 of the Income Tax Act have to be met. The Income Tax Act states that the qualifying turnover for the year of assessment does not exceed R1 million. None of the exclusions of paragraph 3 to the Sixth Schedule apply. Case studies five and seven meet all the requirements of the turnover tax system.

Table 5: Total average tax liability/ (taxable loss) for case studies one to eight for five year period

Case Study	Turnover Tax (R)	Small Business Corporation Tax/ (Taxable Loss) (R)	Normal Tax/ (Taxable Loss) (R)
1	2 658	(5 109)	(264)
2	2 542	1 842	4 764
3	525	(129 707)	(95 764)
4	26 035	18 326	41 336
5	1 212	4 953	12 812
6	16 619	1 554	4 020
7	4 017	12 054`	29 721
8	29 533	5 485	14 189

Table 5 is a summary of the average of the total tax liability/ (taxable loss) over five years, including dividends tax for case studies one to eight in terms of each of the three tax systems. The data was collated from the above case studies calculations. The same results as year one is evident over the five year period. The most beneficial tax system for case studies one to four, six and eight would be the small business corporation tax system and case studies five and seven would be turnover tax. This is due to the lower tax rates compared to the normal income tax system.

The analysis suggests that a business that is making a tax loss should not register for turnover tax as it will impose a liability which does not exist under any of the other options. The administrative saving of not having to keep detailed accounting records should however, be compared to the potential saving in tax for companies; however, this does not form part of this study. The next industry to be dealt with is the service industry.

5.3.3 Service Industry

Description of the businesses

As with the above mentioned cases, in terms of informed consent procedures, the tax practitioner elected to remove the type of business, making it difficult to determine the type of business. On analysis of the financial statements it was possible to identify that the businesses provide services to the public. Case studies ten, eleven, fourteen, sixteen and seventeen have cost of goods sold items in their financial statements, these are the goods used in the provision of services.

Financial information

Table 6: Financial information for case studies nine to seventeen

	Nine (R)	Ten (R)	Eleven (R)	Twelve (R)	Thirteen (R)	Fourteen (R)	Fifteen (R)	Sixteen (R)	Seventeen (R)
Turnover (Gross income in terms of gross income definition in *s1 of the Income Tax Act)*	215 650	300 600	282 134	892 710	298 332	383 195	275 569	996 367	907 127
Less: Cost of goods sold	0	(123 350)	(415 620)	0	0	(146 818)	0	(440 756)	(426 868)
Opening Stock (deductible in terms of s22(2) of the Income Tax Act)	0	6 500	0	0	0	140 117	0	57 101	53 205
Purchases (deductible in terms of s11(*a*) of the Income Tax Act)	0	125 150	415 620	0	0	148 946	0	438 891	430 764
Closing Stock (included in terms of s22(1) of the Income Tax Act)	0	(8 300)	0	0	0	(142 245)	0	(55 236)	(57 101)

	Nine (R)	Ten (R)	Eleven (R)	Twelve (R)	Thirteen (R)	Fourteen (R)	Fifteen (R)	Sixteen (R)	Seventeen (R)
Less: Allowable deductions (deductible in terms of s11(*a*) of the Income Tax Act)	(209 457)	(150 700)	(178 971)	(769 651)	(317 347)	(206 343)	(221 066)	(476 318)	(399 304)
Accounting Fees	7 200	3 600	10 000	12 000	5 000	3 500	1 000	5 500	5 500
Advertising	1 800	0	0	0	0	0	0	0	0
Bank Charges	2 200	0	0	12 739	2 492	1 614	0	15 502	11 236
Cotton and zips	0	0	0	0	0	0	61 257	0	0
Entertainment	0	0	0	0	15 205	0	0	0	0
Insurance	9 000	0	0	25 693	0	3 406	0	0	0
Office expenses	0	0	0	0	7 050	0	0	0	0
Owners salary	0	72 000	0	0	0	96 888	0	72 000	72 000
Printing and stationery	3 600	0	0	184	6 480	389	316	2 978	2 114
Protective clothing	0	0	0	0	0	0	1 262	0	0
Rent, water and electricity	39 719	68 800	168 971	18 000	79 506	59 119	49 503	152 074	136 205
Salary and wages	137 270	0	0	143 427	111 258	13 887	37 500	177 193	123 457

	Nine (R)	Ten (R)	Eleven (R)	Twelve (R)	Thirteen (R)	Fourteen (R)	Fifteen (R)	Sixteen (R)	Seventeen (R)
Security	0	0	0	0	0	5 806	0	0	0
Subcontracting costs	0	0	0	0	0	0	32 458	0	0
Telephone and postages	8 668	3 000	0	0	31 509	8 007	9 117	18 825	17 711
Teas and cleaning	0	3 300	0	0	239	57	1 734	3 377	3 380
Transport cost	0	0	0	557 608	58 608	13 269	19 802	28 868	27 701
Wrapping and packaging	0	0	0	0	0	401	7 117	0	0
Less: Maintenance and Repairs (deductible in terms of s11(*d*) of the Income Tax Act)	(4 200)	(7 150)	0	(505)	0	0	0	0	0
Taxable income sub-total (before capital allowances)	1 993	19 400	(312 457)	122 554	(19 015)	30 034	54 503	79 293	80 955
Depreciation on capital assets	2 496	9 621	8 684	38 350	7 201	229	2 715	45 465	51 192
Calculated value of capital assets (Depreciation x 5 years)	12 480	48 105	43 420	191 750	36 005	1 145	13 575	227 325	255 960

5.3.3.1 Case Study Nine

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R215 650. Based on the sliding scale the tax liability would have been R657 (1% x (R215 650 – R150 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study nines total tax liability under this option would therefore have been R657.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be entitled to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	1 993	1 993	1 993	1 993	1 993
Less: Section 12E(1A) allowance	(6 240)	(3 744)	(2 496)	0	0
Less: Assessed loss (section 20)	0	(4 247)	(5 998)	(6 501)	(4 508)
Taxable income/(loss)	(4 247)	(5 998)	(6 501)	(4 508)	(2 515)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(4 754)				

As the business made a loss there will not be any liability for normal tax and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above)	1 993	1 993	1 993	1 993	1 993
Less: Section 11(*e*) allowance	(2 496)	(2 496)	(2 496)	(2 496)	(2 496)
Less: Assessed loss (section 20)	0	(503)	(1 006)	(1 509)	(2 012)
Taxable income/(loss)	(503)	(1 006)	(1 509)	(2 012)	(2 515)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(1 509)				

As the business made a loss there will be no liability for normal tax, and no dividends tax liability as there is no income to be distributed.

Figure 10: Summary of case study nines total tax payable

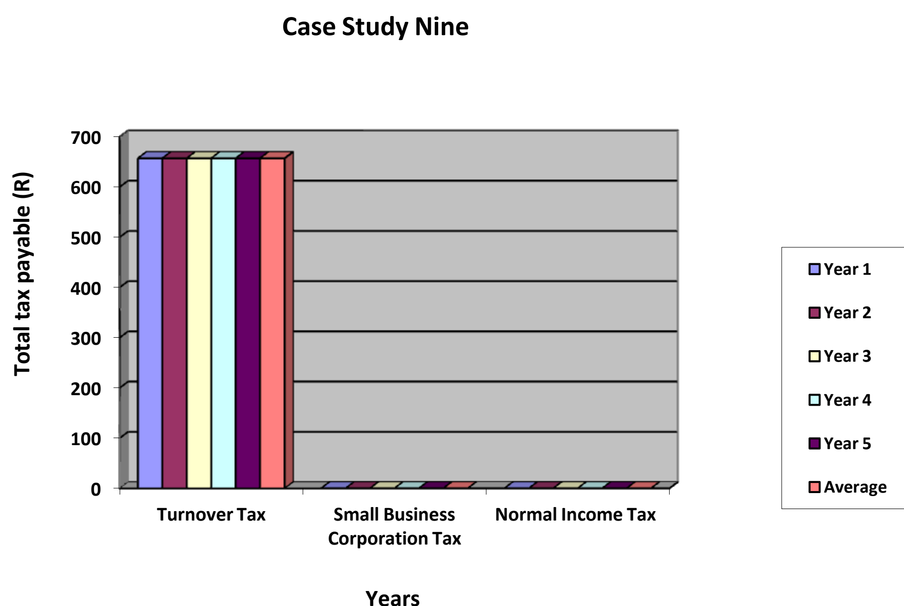


Figure 10 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the small business corporation and normal income tax if all requirements are met, case study nine can offset the tax loss against future taxable income.

5.3.3.2 Case Study Ten

Turnover tax liability

Had the business chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R300 600. Based on the sliding scale the tax liability would be R1 512 (1 500 + 2% x (R300 600 – R300 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study tens total tax liability under this option would therefore have been R1 512.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be in a position to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	19 400	19 400	19 400	19 400	19 400
Less: Section 12E(1A) allowance	(24 053)	(14 431)	(9 621)	0	0
Less: Assessed loss (section 20)	0	(4 653)	0	0	0
Taxable income/(loss)	(4 653)	316	9 779	19 400	19 400
Normal tax payable	0	0	0	0	0
Dividend tax	0	47	1 467	2 910	2 910
Total tax payable	0	47	1 467	2 910	2 910
Average total tax for 5 years	1 467				

As the business made a loss in year one there will not be any liability for normal tax and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	19 400 (9 621)	19 400 (9 621)	19 400 (9 621)	19 400 (9 621)	19 400 (9 621)
Taxable income	9 779	9 779	9 779	9 779	9 779
Normal tax payable	2 738	2 738	2 738	2 738	2 738
Dividend tax	1 056	1 056	1 056	1 056	1 056
Total tax payable	3 794	3 794	3 794	3 794	3 794
Average total tax for 5 years	3 794				

The tax liability for year one would have been calculated on its taxable income of R9 779, with a tax liability of R2 738 (R9 779 x 28%). The dividends tax liability would have been R1 056 ((R9 779-R2 738) x 15%).

Figure 11: Summary of case study tens total tax payable

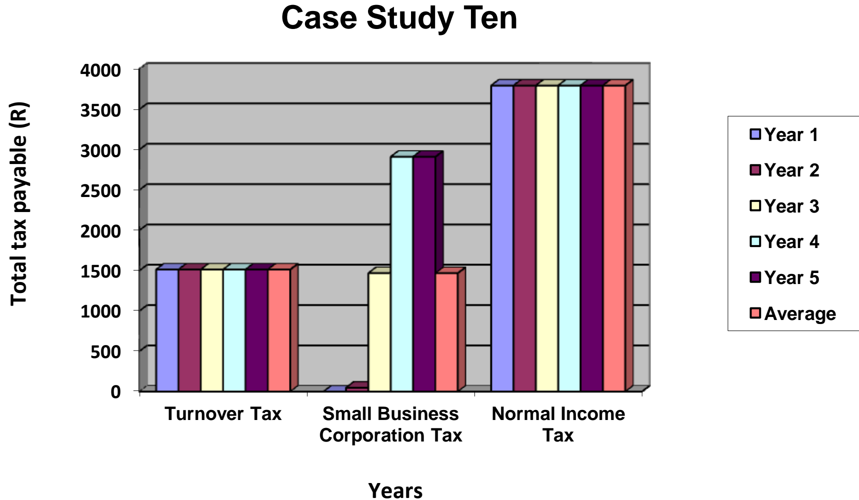


Figure 11 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the small business corporation, if all requirements are met, case study ten can offset the tax loss against future taxable income.

5.3.3.3 Case Study Eleven

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R282 134. Based on the sliding scale the tax liability would have been R1 321 (1% x (R282 134 – R150 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study elevens total tax liability under this option would therefore have been R1 321.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	(312 457)	(312 457)	(312 457)	(312 457)	(312 457)
Less: Section 12e (1A) allowance	(21 710)	(13 026)	(8 684)	0	0
Less: Assessed loss (section 20)	0	(334 167)	(659 650)	(980 791)	(1 293 248)
Taxable income/(loss)	(334 167)	(659 650)	(980 791)	(1 293 248)	(1 605 705)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(974 712)				

As the business made a loss there will be no liability for normal tax, and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	(312 457)	(312 457)	(312 457)	(312 457)	(312 457)
Less: Section 11(*e*) allowance	(8 684)	(8 684)	(8 684)	(8 684)	(8 684)
Less: Assessed loss (section 20)	0	(321 141)	(642 282)	(963 423)	(1 284 564)
Taxable income/(loss)	(321 141)	(642 282)	(963 423)	(1 284 564)	(1 605 705)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(963 423)				

As the business made a loss there will be no liability for normal tax, and no dividends tax liability as there is no income to be distributed.

Figure 12: Summary of case study elevens total tax payable

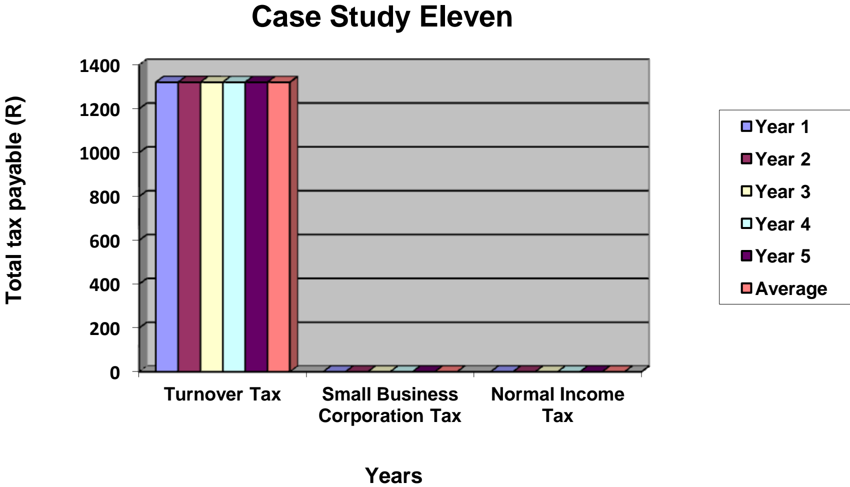


Figure 12 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the small business corporation and normal income tax if all requirements are met, case study eleven can offset the tax loss against future taxable income.

5.3.3.4 Case Study Twelve

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R892 710. Based on the sliding scale the tax liability would have been R24 063 (R15 500 + 6% x (R892 710 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twelves total tax liability under this option would therefore have been R24 063.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be entitled to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	122 554 (95 875)	122 554 (57 525)	122 554 (38 350)	122 554 0	122 554 0
Taxable income	26 679	65 029	84 204	122 554	122 554
Normal tax payable	0	0	1 197	3 881	3 881
Dividend tax	4 002	9 754	12 451	17 801	17 801
Total tax payable	4 002	9 754	13 648	21 682	21 682
Average total tax for 5 years	14 154				

The tax liability for year one would have been calculated on its taxable income of R26 679, with a tax liability of R0 (R26 679 x 0%). The dividends tax liability would be R4 002 (R26 679 x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	122 554 (38 350)	122 554 (38 350)	122 554 (38 350)	122 554 (38 350)	122 554 (38 350)
Taxable income	84 204	84 204	84 204	84 204	84 204
Normal tax payable	23 577	23 577	23 577	23 577	23 577
Dividend tax	9 094	9 094	9 094	9 094	9 094
Total tax payable	32 671	32 671	32 671	32 671	32 671
Average total tax for 5 years	32 671				

Under the normal income tax system, the business would have had a tax liability in year one of R23 577 (R84 204 x 28%). The dividends tax liability would have been R9 094 ((R84 204 – R23 577) x 15%).

Figure 13: Summary of case study twelves total tax payable

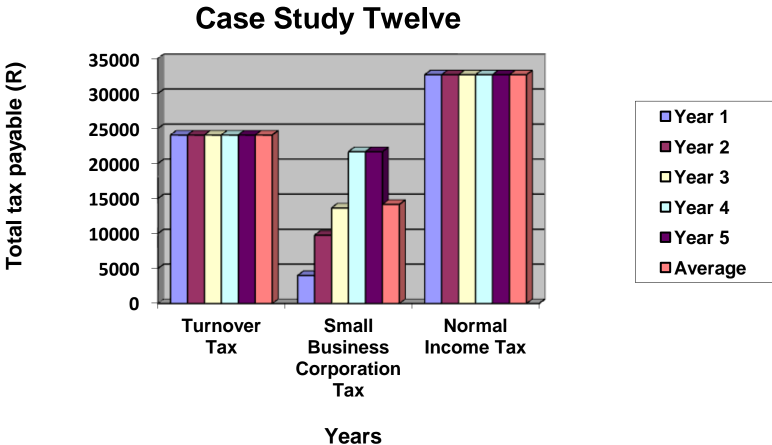


Figure 13 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.3.5 Case Study Thirteen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R298 332. Based on the sliding scale the tax liability would have been R1 483 (1% x (R298 332 – R150 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study thirteens total tax liability under this option would consequently have been R1 483.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be entitled to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income/ (loss) (before allowances) (refer above) Less: Section 12E(1A) allowance Less: Assessed loss (section 20)	(19 015) (18 002) 0	(19 015) (10 802) (37 017)	(19 015) (7 201) (66 834)	(19 015) 0 (93 050)	(19 015) 0 (112 065)
Taxable income/(loss)	(37 017)	(66 834)	(93 050)	(112 065)	(131 080)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(88 009)				

As the business made a loss there will be no liability for normal tax, and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income/ (loss) (before allowances) (refer above)	(19 015)	(19 015)	(19 015)	(19 015)	(19 015)
Less: Section 11(*e*) allowance	(7 201)	(7 201)	(7 201)	(7 201)	(7 201)
Less: Assessed loss (section 20)	0	(26 216)	(52 432)	(78 648)	(104 864)
Taxable income/(loss)	(26 216)	(52 432)	(78 648)	(104 864)	(131 080)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(78 648)				

As the business made a loss there will be no liability for normal tax, and no dividends' tax liability as there is no income to be distributed.

Figure 14: Summary of case study thirteens total tax payable

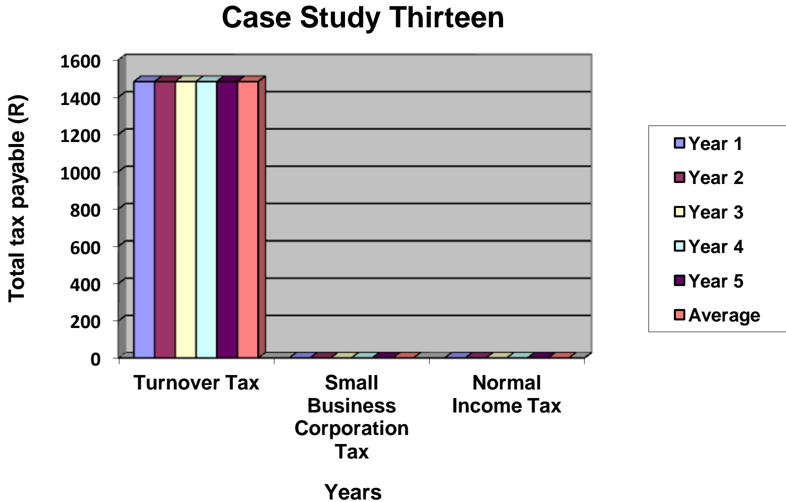


Figure 14 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the small business corporation and normal income tax if all requirements are met, case study thirteen can offset the tax loss against future taxable income.

5.3.3.6 Case Study Fourteen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R383 195. Based on the sliding scale the tax liability would have been R3 164 (R1 500 + 2% x (R383 195 – R300 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study fourteens total tax liability under this option would therefore have been R3 164.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried forward into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	30 034 (573)	30 034 (343)	30 034 (229)	30 034 0	30 034 0
Taxable income	29 461	29 691	29 805	30 034	30 034
Normal tax payable	0	0	0	0	0
Dividend tax	4 419	4 454	4 471	4 505	4 505
Total tax payable	4 419	4 454	4 471	4 505	4 505
Average total tax for 5 years	4 471				

The tax liability for year one would have been calculated on its taxable income of R29 461, with a tax liability of R0 (0% x R29 461). The dividends tax liability would have been R4 419 (R29 461 x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	30 034 (229)	30 034 (229)	30 034 (229)	30 034 (229)	30 034 (229)
Taxable income	29 805	29 805	29 805	29 805	29 805
Normal tax payable	8 345	8 345	8 345	8 345	8 345
Dividend tax	3 219	3 219	3 219	3 219	3 219
Total tax payable	11 564	11 564	11 564	11 564	11 564
Average total tax for 5 years	11 564				

The business would have had a tax liability of R8 345 (R29 805 x 28%). The dividends tax liability would have been R3 219 ((R29 805 – R8 345) x 15%).

Figure 15: Summary of case study fourteens total tax payable

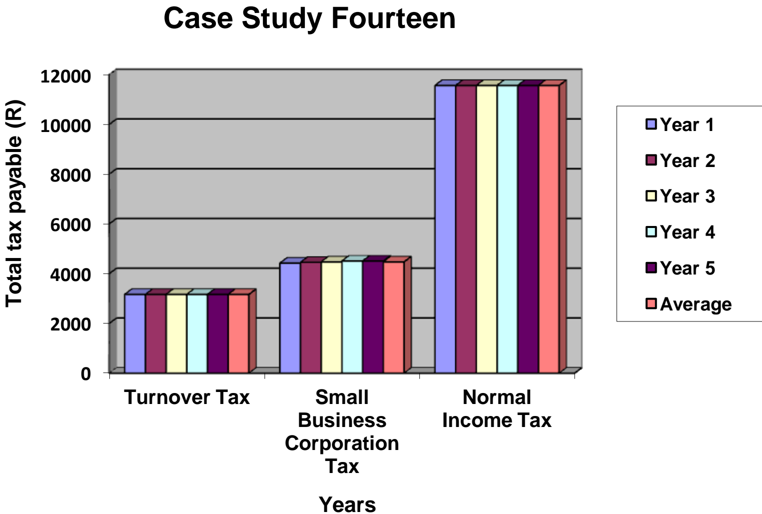


Figure 15 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.3.7 Case Study Fifteen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R275 569. Based on the sliding scale the tax liability would have been R1 256 (1% x (R275 569 – R150 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study fifteens total tax liability under this option would therefore have been R1 256.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be deferred to the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 12E(1A) allowance	54 503 (6 788)	54 503 (4 072)	54 503 (2 715)	54 503 0	54 503 0
Taxable income	47 715	50 431	51 788	54 503	54 503
Normal tax payable	0	0	0	0	0
Dividend tax	7 157	7 565	7 768	8 175	8 175
Total tax payable	7 157	7 565	7 768	8 175	8 175
Average total tax for 5 years	7 768				

The tax liability for year one would have been calculated on its taxable income of R47 715, with a tax liability of R0 (0% x R47 715). The dividends tax liability would have been R7 157 (R47 715 x 15%).

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	54 503 (2 715)	54 503 (2 715)	54 503 (2 715)	54 503 (2 715)	54 503 (2 715)
Taxable income	51 788	51 788	51 788	51 788	51 788
Normal tax payable	14 501	14 501	14 501	14 501	14 501
Dividend tax	5 593	5 593	5 593	5 593	5 593
Total tax payable	20 094	20 094	20 094	20 094	20 094
Average total tax for 5 years	20 094				

Under the normal income tax system, the business would have had a tax liability of R14 501 (R51 788 x 28%). The dividends tax liability would be R5 593 ((R51 788 – R14 501) x 15%).

Figure 16: Summary of case study fifteens total tax payable

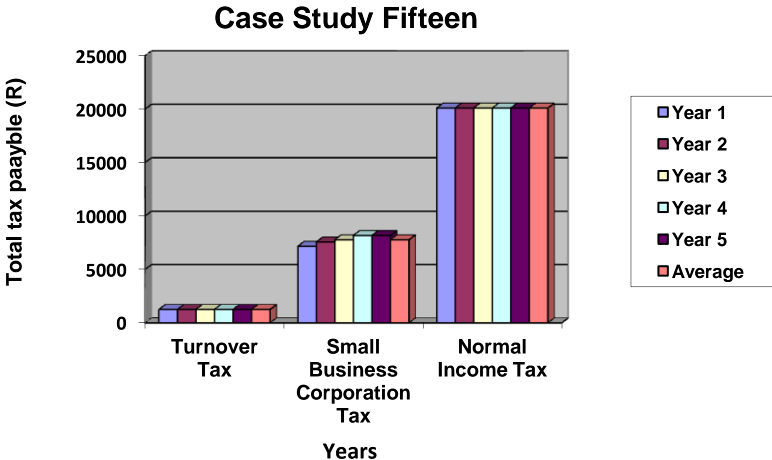


Figure 16 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.3.8 Case Study Sixteen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R996 367. Based on the sliding scale the tax liability would have been R30 282 (R15 500 + 6% x (R996 367 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study sixteens total tax liability under this option would therefore have been R30 282.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year will be carried forward into the following year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	79 293	79 293	79 293	79 293	79 293
Less: Section 12E(1A) allowance	(113 663)	(68 197)	(45 465)	0	0
Less: Assessed loss (section 20)	0	(34 370)	(23 274)	0	0
Taxable income/(loss)	(34 370)	(23 274)	10 554	79 293	79 293
Normal tax payable	0	0	0	853	853
Dividend tax	0	0	1 583	11 766	11 766
Total tax payable	0	0	1 583	12 619	12 619
Average total tax for 5 years	5 364				

As the business had made a loss in year one there will be no liability for normal tax, and no dividends tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability will therefore be:

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (before allowances) (refer above) Less: Section 11(*e*) allowance	79 293 (45 465)	79 293 (45 465)	79 293 (45 465)	79 293 (45 465)	79 293 (45 465)
Taxable income	33 828	33 828	33 828	33 828	33 828
Normal tax payable	9 472	9 472	9 472	9 472	9 472
Dividend tax	3 653	3 653	3 653	3 653	3 653
Total tax payable	13 125	13 125	13 125	13 125	13 125
Average total tax for 5 years	13 125				

Under the normal income tax system, the business would have had a tax liability in year one of R9 472 (R33 828 x 28%). The dividends tax liability would be R3 653 ((R33 828 – R9 472) x 15%).

Figure 17: Summary of case study sixteens total tax payable

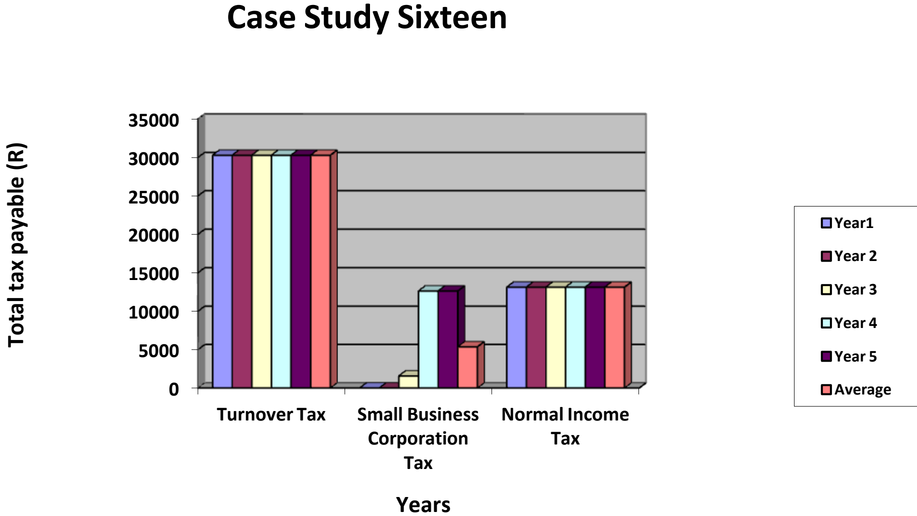


Figure 17 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the small business corporation tax if all requirements are met, case study sixteen can offset the tax loss against future taxable income.

5.3.3.9 Case Study Seventeen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R907 127. Based on the sliding scale the tax liability would have been R24 928 (R15 500 + 6% x (R907 127 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study seventeens total tax liability under this option would therefore have been R24 928.

Small business corporation normal tax liability

In terms of section 12E(1A) of the Act, the business would be able to claim the following capital allowances in each of the first three years the asset is used. It is assumed that the loss from one year would be carried over into the next year of assessment:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	80 955	80 955	80 955	80 955	80 955
Less: Section 12E(1A) allowance	(127 980)	(76 788)	(51 192)	0	0
Less: Assessed loss (section 20)	0	(47 025)	(42 858)	(13 095)	0
Taxable income/(loss)	(47 025)	(42 858)	(13 095)	67 860	80 955
Normal tax payable	0	0	0	52	969
Dividend tax	0	0	0	10 171	11 998
Total tax payable	0	0	0	10 223	12 967
Average total tax for 5 years	4 638				

As the business had made a loss in year one there will be no liability for normal tax, and no dividends' tax liability as there is no income to be distributed.

Normal taxpayer normal tax liability

If the business does not qualify for any other capital allowances on its assets it will qualify for a section 11(*e*) allowance of the Act, its tax liability would therefore have been:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (before allowances) (refer above)	80 955	80 955	80 955	80 955	80 955
Less: Section 11(*e*) allowance	(51 192)	(51 192)	(51 192)	(51 192)	(51 192)
Taxable income	29 763	29 763	29 763	29 763	29 763
Normal tax payable	8 334	8 334	8 334	8 334	8 334
Dividend tax	3 214	3 214	3 214	3 214	3 214
Total tax payable	11 548	11 548	11 548	11 548	11 548
Average total tax for 5 years	11 548				

Under the normal income tax system, the business would have had a tax liability of R8 334 (R29 763 x 28%). The dividends tax liability would have been R3 214 ((R29 763– R8 334) x 15%).

Figure 18: Summary of case study seventeens total tax payable

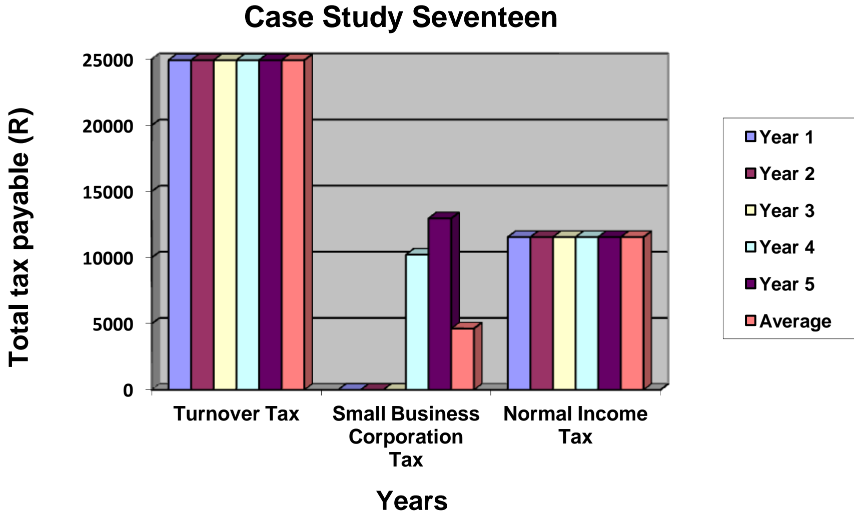


Figure 18 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money.

5.3.3.10 Summary and Conclusion of Case Studies Nine to Seventeen

The results for case studies nine to seventeen can be summarised as follows:

Table 7: Total tax liability/ (taxable loss) for case studies nine to seventeen for year one

Case Study	Turnover Tax (R)	Small Business Corporation Tax/ (Taxable Loss) (R)	Normal Tax/ (Taxable Loss) (R)
9	657	(4 247)	(503)
10	1 512	(4 653)	3 794
11	1 321	(334 167)	(321 141)
12	24 063	4 002	32 671
13	1 483	(37 017)	(26 216)
14	3 164	4 419	11 564
15	1 256	7 157	20 094
16	30 282	(34 370)	13 125
17	24 928	(47 025)	11 548

Table 7 is a summary of the total tax liability/ (taxable loss), includes dividend tax for case studies nine to seventeen on each of the three tax systems. This data was collated from the case study calculations above.

Based on the above tax calculations the most beneficial tax system for case studies nine to thirteen, sixteen and seventeen would be the small business corporation tax system as the businesses would incur no tax liability or carry over the assessed loss to the next financial year if all prerequisites are met. All the requirements of section 12E(4)(*a*) of the Income Tax Act have to be satisfied to apply the small business

corporation tax system, the Income Tax Act defines a small business corporation as any close corporation or co-operative or any private company as defined in section 1 of the Companies Act, and the gross income should not exceed R20 million, none of the members hold any shares in other companies, not more than 20 percent of total receipts and accruals consist of personal service or investment income. Case studies eleven to thirteen, sixteen and seventeen meet all the requirements of a small business corporation.

For case study fourteen and fifteen the most beneficial tax system would be the turnover tax system as the lowest total tax would be payable. The tax payable is based on the turnover of the business. All the criteria of the Sixth Schedule and section 48 of the Income Tax Act have to be met to use the turnover tax system. The Income Tax Act states that the qualifying turnover for the year of assessment does not exceed R1 million. None of the exclusions of paragraph 3 to the Sixth Schedule apply. Case studies fourteen and fifteen meet all the requirements of the turnover tax system.

Table 8: Total average tax liability/ (taxable loss) for case studies nine to seventeen for five year period

Case Study	**Turnover Tax (R)**	**Small Business Corporation Tax/ (Taxable Loss) (R)**	**Normal Tax/ (Taxable Loss) (R)**
9	657	(4 754)	(1 509)
10	1 512	1 467	3 794
11	1 321	(974 712)	(963 423)
12	24 063	14 154	32 671
13	1 483	(88 009)	(78 648)
14	3 164	4 471	11 564
15	1 256	7 768	20 094
16	30 282	5 364	13 125
17	24 928	4 638	11 548

Table 8 is a summary of the average of the total tax liability/ (taxable loss) over a period of five years, including dividends tax for case studies nine to seventeen on each of the three tax systems. This data was collated from the above case study calculations.

Once again, the same results are achieved as for year one except for case study ten, due to the dividend tax and lower tax rates the turnover tax is more beneficial when calculating the average total tax payable over the five years. The next group of businesses to be dealt with is real estate.

5.3.4 The Real Estate Businesses

Description of the businesses

In terms of informed consent procedures, the tax practitioner elected to remove the type of business, making it difficult to determine the type of business. However, an analysis of the financial statements suggests that case studies eighteen to thirty invest in real estate.

Financial information

Table 9: Financial information for case studies eighteen to twenty four

	Eighteen (R)	Nineteen (R)	Twenty (R)	Twenty One (R)	Twenty Two (R)	Twenty Three (R)	Twenty Four (R)
Turnover (Gross income in terms of gross income definition in s *1* of the Income Tax Act)	140 125	473 750	338 108	931 608	789 023	185 333	135 912
Capital gain (66.6% of the capital gain is included in taxable income in of paragraph 10 of the 8th Schedule of the Income Tax Act)	0	3 924	0	3 924	0	0	0
Less: Allowable deductions (deductible in terms of s11(*a*) of the Income Tax Act)	(59 797)	(66 202)	(71 472)	(334 164)	(71 900)	(3 192)	(3 664)
Accounting Fees	6 000	5 000	5 000	3 000	3 000	1 000	1 000
Administration and management fee	0	8 000	8 000	0	0	0	0
Annual duty	0	100	450	450	450	450	450
Assessment rates and municipal charges	0	40 812	43 715	282 543	22 125	0	0
Auditors remuneration	0	0	2 500	2 500	2 500	1 500	1 500
Bank Charges	1 359	2 500	2 027	3 336	1 430	128	600
Cleaning and casual wage	0	0	0	29 450	29 500	0	0

	Eighteen (R)	Nineteen (R)	Twenty (R)	Twenty One (R)	Twenty Two (R)	Twenty Three (R)	Twenty Four (R)
Insurance	3 189	9 690	9 680	12 785	12 795	0	0
Rent, water and electricity	39 703	0	0	0	0	0	0
Secretarial	0	100	100	100	100	114	114
Security	9 546	0	0	0	0	0	0
Less: Other allowable deductions	(30 831)	(182 071)	(79 164)	(233 929)	(587 366)	0	0
Bad debts (deductible in terms of s11(*i*) of the Income Tax Act)	0	0	0	0	119 156	0	0
Donations (deductible in terms of s18A of the Income Tax Act)	0	0	0	7 500	0	0	0
Finance costs (deductible in terms of s24*J* of the Income Tax Act)	0	182 071	69 663	150 530	240 981	0	0
Maintenance and repairs (deductible in terms of s11(*d*) of the Income Tax Act)	30 831	0	9 501	75 899	227 229	0	0
Taxable income	49 497	229 401	187 472	367 439	129 757	182 141	132 248

Table 10: Financial information for case studies twenty five to thirty

	Twenty Five (R)	Twenty Six (R)	Twenty Seven (R)	Twenty Eight (R)	Twenty Nine (R)	Thirty (R)
Turnover (Gross income in terms of gross income definition in s*1* of the Income Tax Act)	786 981	688 150	351 671	244 142	138 947	96 000
Capital gain (66.6% of the capital gain is included in taxable income in of paragraph 10 of the 8th Schedule of the Income Tax Act)	3 924	0	0	0	0	0
Interest received (Gross income in terms of gross income definition in s1 of the Income Tax Act)	8 899	0	0	0	0	0
Less: Allowable deductions (deductible in terms of s11(*a*) of the Income Tax Act)	(415 547)	(336 210)	(3 191)	(4 784)	(101 660)	(91 161)
Accounting Fees	7 000	7 000	1 710	1 710	7 870	4 500
Administration and management fee	28 000	28 000	0	0	0	0
Annual duty	100	450	100	450	0	0
Assessment rates and municipal charges	290 675	224 007	0	0	0	18 653
Auditors remuneration	7 300	7 300	1 140	1 140	0	0
Bank Charges	7 534	5 047	127	1 370	4 274	0
Cleaning and casual wage	0	0				3 123

	Twenty Five (R)	Twenty Six (R)	Twenty Seven (R)	Twenty Eight (R)	Twenty Nine (R)	Thirty (R)
Employee costs	24 480	24 458	0	0	0	0
Insurance	12 785	12 795	0	0	11 699	4 885
Members salary	0	0	0	0	0	60 000
Rates, taxes and water	0	0	0	0	77 817	0
Secretarial	100	100	114	114	0	0
Security	37 573	27 053	0	0	0	0
Less: Other allowable deductions	(503 044)	(382 896)	(90 122)	0	0	0
Bad debts (deductible in terms of s11(*i*) of the Income Tax Act)	0	25 000	0	0	0	0
Finance costs (deductible in terms of s24*J* of the Income Tax Act)	287 354	277 869	90 122	0	0	0
Maintenance and repairs (deductible in terms of s11(*d*) of the Income Tax Act)	215 690	80 027	0	0	0	0
Taxable income/(loss)	(118 787)	(30 956)	258 358	239 358	37 287	4 839

5.3.4.1 Case Study Eighteen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R140 125. Based on the sliding scale the tax liability would have been R0 (0% x R140 125).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Under this option case study eighteen would have had a R0 tax liability.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R49 497, with a tax liability of R0 (R49 497 x 0%). The dividends tax liability would be R7 424 (R49 497 x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	49 497	49 497	49 497	49 497	49 497
Normal tax payable	0	0	0	0	0
Dividend tax	7 424	7 424	7 424	7 424	7 424
Total tax payable	7 424	7 424	7 424	7 424	7 424
Average total tax for 5 years	7 424				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R13 859 (R49 497 x 28%). The dividends tax liability would be R5 346 ((R49 497 – R13 859) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	49 497	49 497	49 497	49 497	49 497
Normal tax payable	13 859	13 859	13 859	13 859	13 859
Dividend tax	5 346	5 346	5 346	5 346	5 346
Total tax payable	19 205	19 205	19 205	19 205	19 205
Average total tax for 5 years	19 205				

Figure 19: Summary of case study eighteens total tax payable

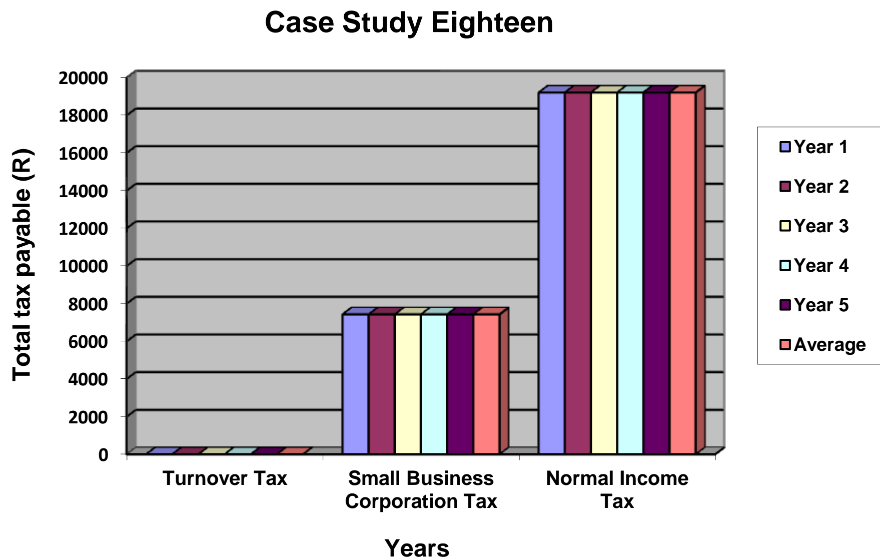


Figure 19 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Since there is no wear and tear allowance years one to five have the same tax payable.

5.3.4.2 Case Study Nineteen

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R473 750 and 50% of proceeds R2 946 (50% x R5 892). Based on the sliding scale the tax liability would have been R5 034 (R1 500 + 2% x (R473 750 + R2 946) – R300 000).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. The dividends' tax liability would have been R3 655 (((R229 401 – R5 034) –R200 000) x 15%). Case study nineteens total tax liability under this option would therefore be R8 689.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R229 401, with a tax liability of R11 360 (7% x (R229 401 – R 67 111)). The dividends tax liability would have been R32 706 ((R229 401 – R11 360) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	229 401	229 401	229 401	229 401	229 401
Normal tax payable	11 360	11 360	11 360	11 360	11 360
Dividend tax	32 706	32 706	32 706	32 706	32 706
Total tax payable	44 066	44 066	44 066	44 066	44 066
Average total tax for 5 years	44 066				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R64 232 (R229 401 x 28%). The dividends tax liability would have been R24 775 ((R229 401 – R64 232) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	229 401	229 401	229 401	229 401	229 401
Normal tax payable	64 232	64 232	64 232	64 232	64 232
Dividend tax	24 775	24 775	24 775	24 775	24 775
Total tax payable	89 007	89 007	89 007	89 007	89 007
Average total tax for 5 years	89 007				

Figure 20: Summary of case study nineteens total tax payable

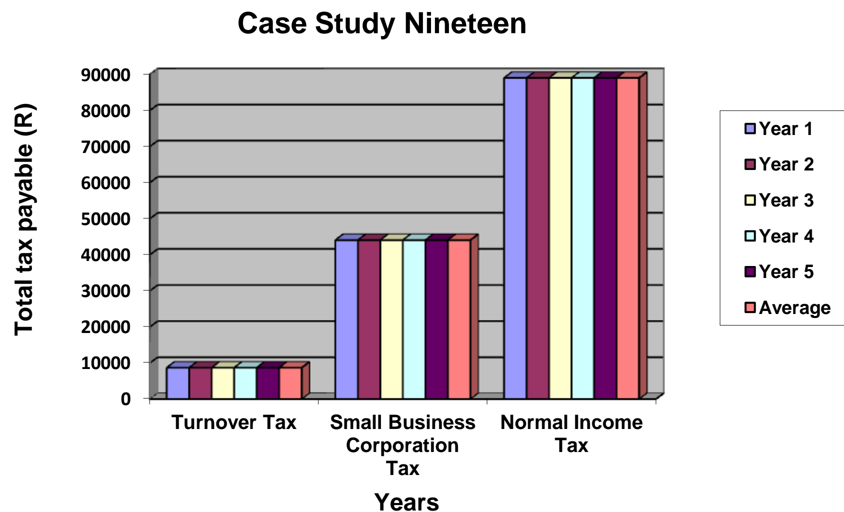


Figure 20 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Since there is no wear and tear allowance years one to five have the same tax payable.

5.3.4.3 Case Study Twenty

Turnover tax liability

Had the business chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R338 108. Based on the sliding scale the tax liability would have been R2 262 (R1 500 + 2% x (R338 108 – R300 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twentys total tax liability under this option would therefore have been R2 262.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R187 472, with a tax liability of R8 425 (7% x (R187 472 – R67 111)). The dividends tax liability would be R26 857 ((R187 472 – R8 425) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	187 472	187 472	187 472	187 472	187 472
Normal tax payable	8 425	8 425	8 425	8 425	8 425
Dividend tax	26 857	26 857	26 857	26 857	26 857
Total tax payable	35 282	35 282	35 282	35 282	35 282
Average total tax for 5 years	35 282				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R52 492 (R187 472 x 28%). The dividends tax liability would have been R20 247 ((R187 472 – R52 492) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	187 472	187 472	187 472	187 472	187 472
Normal tax payable	52 492	52 492	52 492	52 492	52 492
Dividend tax	20 247	20 247	20 247	20 247	20 247
Total tax payable	72 739	72 739	72 739	72 739	72 739
Average total tax for 5 years	72 739				

Figure 21: Summary of case study twenties total tax payable

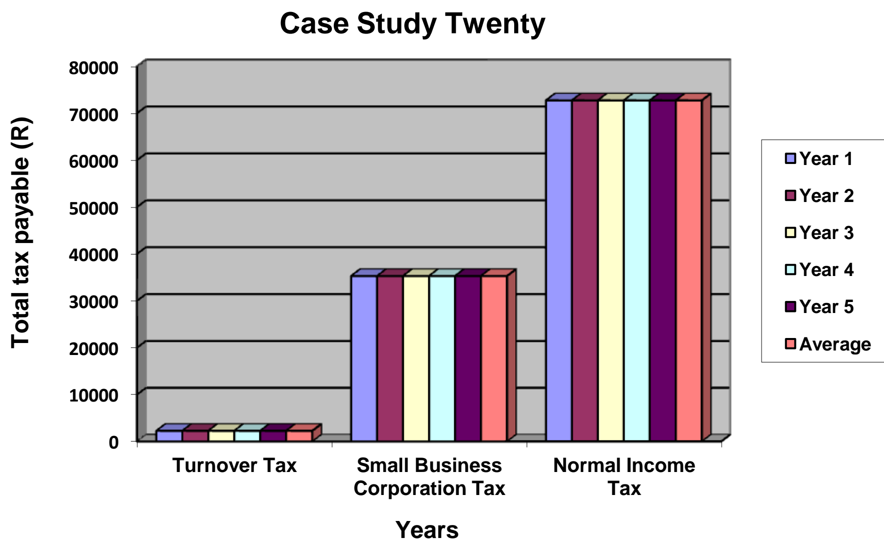


Figure 21 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Considering that there is no wear and tear allowance the same tax payable for years one to five.

5.3.4.4 Case Study Twenty One

Turnover tax liability

If the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R931 608 and 50% of proceeds R2 946 (50% x R5 892). Based on the sliding scale the tax liability would have been R26 573 (R15 500 + 6% x (R931 608 + R2 946) – R750 000).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. The dividends tax liability would have been R21 130 (((R367 439 – R26 573) –R200 000) x 15%). Case study twenty ones total tax liability under this option would therefore have been R47 703.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R367 439, with a tax liability of R21 364 (R20 852 + 21% x (R367 439– R365 000)). The dividends tax liability would have been R51 911 ((R367 439 – R21 364) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	367 439	367 439	367 439	367 439	367 439
Normal tax payable	21 364	21 364	21 364	21 364	21 364
Dividend tax	51 911	51 911	51 911	51 911	51 911
Total tax payable	73 275	73 275	73 275	73 275	73 275
Average total tax for 5 years	73 275				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R102 883 (R367 439 x 28%). The dividends tax liability would have been R39 683 ((R367 439 – R102 883) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	367 439	367 439	367 439	367 439	367 439
Normal tax payable	102 883	102 883	102 883	102 883	102 883
Dividend tax	39 683	39 683	39 683	39 683	39 683
Total tax payable	142 566	142 566	142 566	142 566	142 566
Average total tax for 5 years	142 566				

Figure 22: Summary of case study twenty ones total tax payable

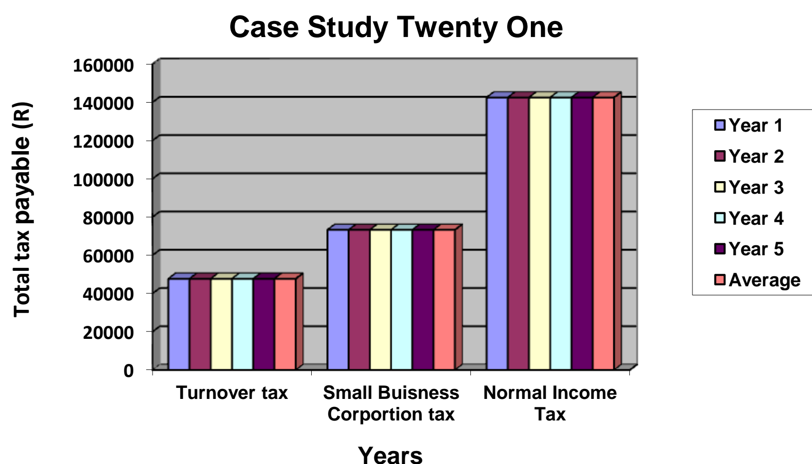


Figure 22 is a collation of the above total tax payable calculations for each tax system over a 5 year one to five because there is no wear and tear allowance.

5.3.4.5 Case Study Twenty Two

Turnover tax liability

If the turnover tax system had been chosen by the business, their tax liability would have been calculated based on its turnover of R789 023. Based on the sliding scale the tax liability would have been R17 841 (R15 500 + 6% x (R789 023 – R750 000)).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twenty twos total tax liability under this option would therefore have been R17 841.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R129 757, with a tax liability of R4 385 (7% x (R129 757 – R67 111)). The dividends tax liability would have been R18 806 ((R129 757 – R4 385) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	129 757	129 757	129 757	129 757	129 757
Normal tax payable	4 385	4 385	4 385	4 385	4 385
Dividend tax	18 806	18 806	18 806	18 806	18 806
Total tax payable	23 191	23 191	23 191	23 191	23 191
Average total tax for 5 years	23 191				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R36 332 (R129 757 x 28%). The dividends tax liability would have been R14 014 ((R129 757 – R36 332) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	129 757	129 757	129 757	129 757	129 757
Normal tax payable	36 332	36 332	36 332	36 332	36 332
Dividend tax	14 014	14 014	14 014	14 014	14 014
Total tax payable	50 346	50 346	50 346	50 346	50 346
Average total tax for 5 years	50 346				

Figure 23: Summary of case study twenty twos total tax payable

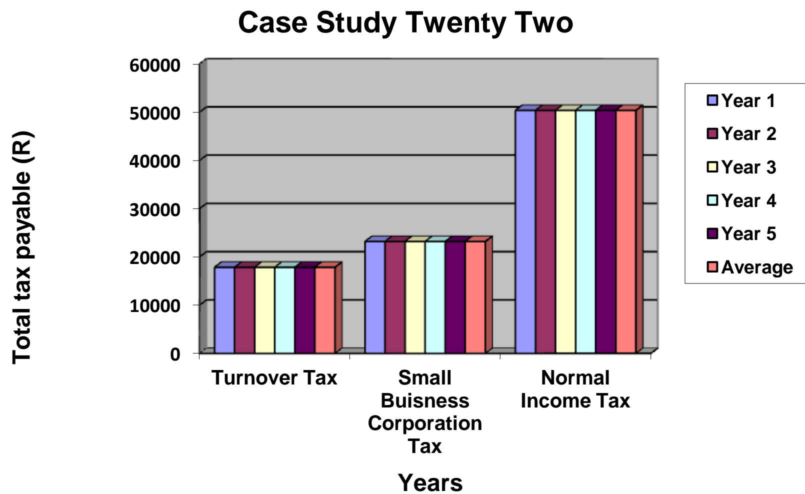


Figure 23 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. There is no wear and tear allowance therefore years one to five have the same tax payable.

5.3.4.6 Case Study Twenty Three

Turnover tax liability

The tax liability for case study twenty two would have been calculated based on its turnover of R185 333. Based on the sliding scale the tax liability would have been R353 (1% x (R185 333 – R150 000) if the business had chosen the turnover tax system,

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twenty threes total tax liability under this option would therefore have been R353.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R182 141, with a tax liability of R8 052 (7% x (R182 141 – R67 111)). The dividends tax liability would have been R26 113 ((R182 141 – R8 052) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	182 141	182 141	182 141	182 141	182 141
Normal tax payable	8 052	8 052	8 052	8 052	8 052
Dividend tax	26 113	26 113	26 113	26 113	26 113
Total tax payable	34 165	34 165	34 165	34 165	34 165
Average total tax for 5 years	34 165				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R50 999 (R182 141 x 28%). The dividends tax liability would have been R19 671 ((R182 141 – R50 999) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	182 141	182 141	182 141	182 141	182 141
Normal tax payable	50 999	50 999	50 999	50 999	50 999
Dividend tax	19 671	19 671	19 671	19 671	19 671
Total tax payable	70 670	70 670	70 670	70 670	70 670
Average total tax for 5 years	70 670				

Figure 24: Summary of case study twenty threes total tax payable

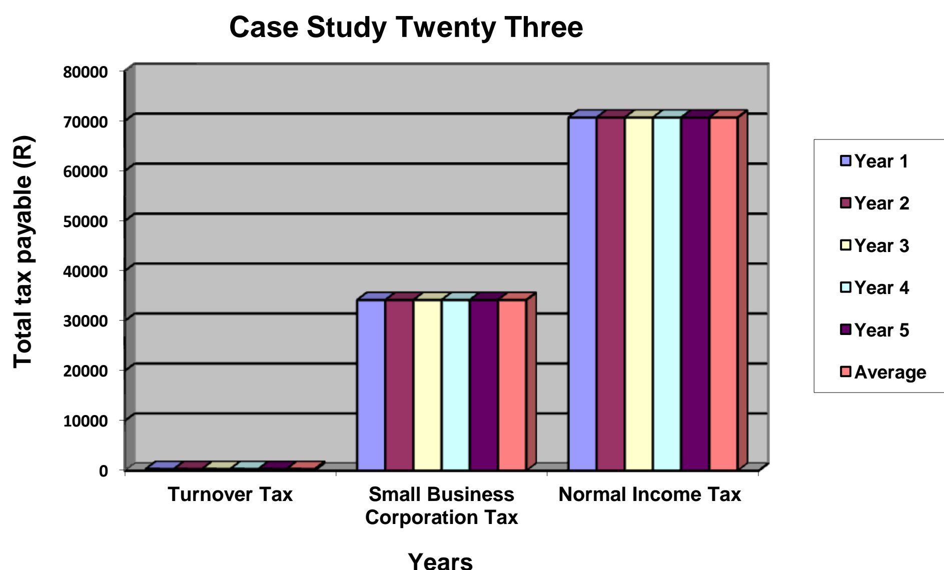


Figure 24 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. For the reason that there is no wear and tear allowance the same tax is payable for years one to five.

5.3.4.7 Case Study Twenty Four

Turnover tax liability

Had the business chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R135 912. Based on the sliding scale the tax liability would be R0 (0% x R135 912).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act, consequently there would have been a R0 liability under this option for case study twenty four.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R132 248, with a tax liability of R4 560 (7% x (R132 248 – R67 111)). The dividends tax liability would have been R19 153 ((R132 248 – R4 560) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	132 248	132 248	132 248	132 248	132 248
Normal tax payable	4 560	4 560	4 560	4 560	4 560
Dividend tax	19 153	19 153	19 153	19 153	19 153
Total tax payable	23 713	23 713	23 713	23 713	23 713
Average total tax for 5 years	23 713				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R37 029 (R132 248 x 28%). The dividends tax liability would have been R14 283 ((R132 248 – R37 029) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	132 248	132 248	132 248	132 248	132 248
Normal tax payable	37 029	37 029	37 029	37 029	37 029
Dividend tax	14 283	14 283	14 283	14 283	14 283
Total tax payable	51 312	51 312	51 312	51 312	51 312
Average total tax for 5 years	51 312				

Figure 25: Summary of case study twenty fours total tax payable

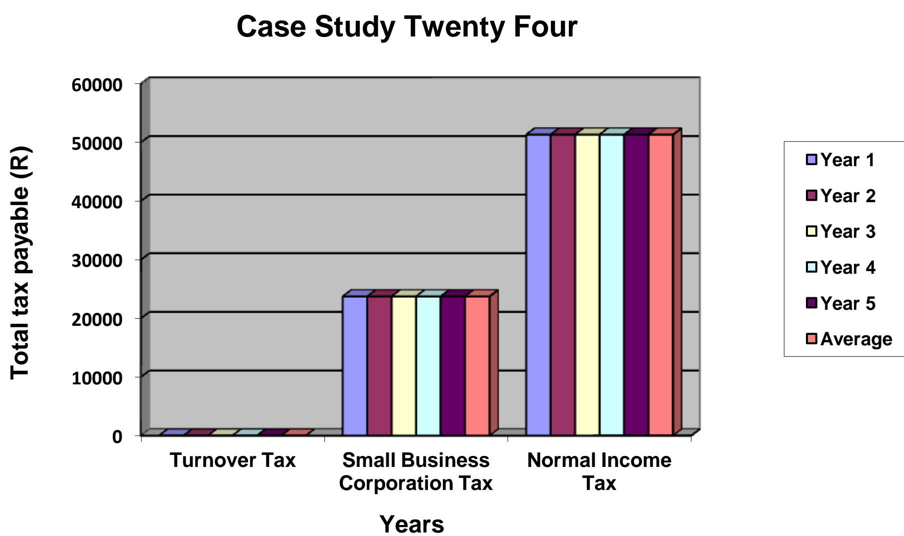


Figure 25 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Since there is no wear and tear allowance years one to five have the same tax payable.

5.3.4.8 Case Study Twenty Five

Turnover tax liability

If the turnover tax system had been the choice of this business, their tax liability would have been calculated based on its turnover of R786 981 and 50% of proceeds R2 946 (50% x R5 892) and interest received of R8 899. Based on the sliding scale the tax liability would have been R18 429 (R15 500 + 6% x (R786 981+ R2 946+ R8 899) – R750 000).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twenty fives total tax liability under this option would therefore have been R18 429.

Small business corporation normal tax liability

Since the business is had made a loss there will be no liability for small business corporation normal tax and no dividends tax liability as there is no income to be distributed.

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income/(loss) (refer above)	(118 787)	(118 787)	(118 787)	(118 787)	(118 787)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(118 787)				

Normal taxpayer normal tax liability

As the business had made a loss there will be no liability for normal tax, and no dividends tax liability as there is no income to be distributed.

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income/(loss) (refer above)	(118 787)	(118 787)	(118 787)	(118 787)	(118 787)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(118 787)				

Figure 26: Summary of case study twenty fives total tax payable

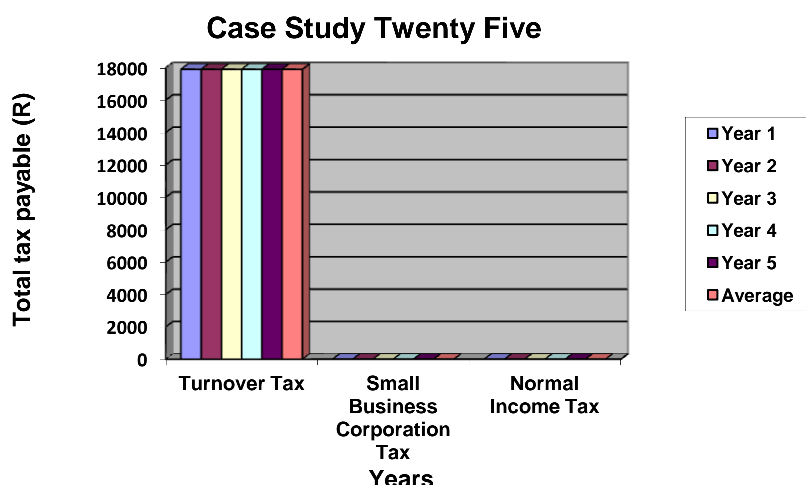


Figure 26 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Under both the small business corporation and normal income tax systems the business can offset the assessed loss against future income once all requirements are met. Seeing that there is no wear and tear allowance the same tax is payable from years one to five.

5.3.4.9 Case Study Twenty Six

Turnover tax liability

Had the business chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R688 150. Based on the sliding scale the R13 026 (R5 500 + 4% x (R688 150 – R500 000).

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twenty sixes total tax liability under this option would therefore have been R13 026.

Small business corporation normal tax liability

As the business had made a loss there will be no liability for small business corporation normal tax, and no dividends tax liability as there is no income to be distributed.

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income/(loss) (refer above)	(30 956)	(30 956)	(30 956)	(30 956)	(30 956)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(30 956)				

Normal taxpayer normal tax liability

Since the business had made a loss there will be no liability for normal tax and no dividends tax liability as there is no income to be distributed.

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income/(loss) (refer above)	(30 956)	(30 956)	(30 956)	(30 956)	(30 956)
Normal tax payable	0	0	0	0	0
Dividend tax	0	0	0	0	0
Total tax payable	0	0	0	0	0
Average total tax/(taxable loss) for 5 years	(30 956)				

Figure 27: Summary of case study twenty sixes total tax payable

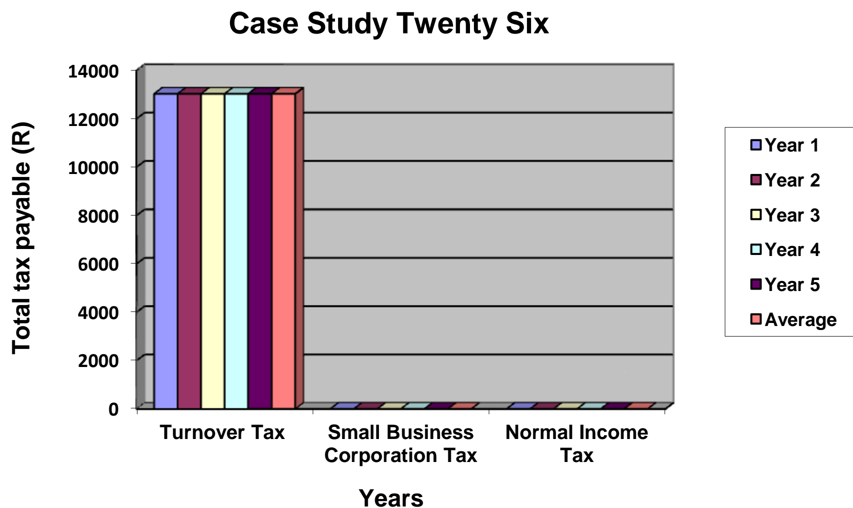


Figure 27 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Under both the small business corporation and normal income tax systems the business can offset the assessed loss against future income once all requirements are met. There is no wear and tear allowance therefore year one to five has the same tax payable.

5.3.4.10 Case Study Twenty Seven

Turnover tax liability

Their tax liability would have been calculated based on its turnover of R351 671. Based on the sliding scale the tax liability would have been R2 533 (R1 500 + 2% x (R351 671 – R300 000) had the business chosen the turnover tax system,

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Dividends tax liability R8 374 (((R258 358 - R2 533) – R200 000) X 15%). Case study twenty sevens total tax liability under this option would therefore have been R10 907.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R258 358, with a tax liability of R13 387 (7% x (R258 358 – R67 111)). The dividends tax liability would have been R36 746 ((R258 358 – R13 387) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	258 358	258 358	258 358	258 358	258 358
Normal tax payable	13 387	13 387	13 387	13 387	13 387
Dividend tax	36 746	36 746	36 746	36 746	36 746
Total tax payable	50 133	50 133	50 133	50 133	50 133
Average total tax for 5 years	50 133				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R72 340 (R258 358 x 28%). The dividends tax liability would have been R27 903 ((R258 358 – R72 340) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	258 358	258 358	258 358	258 358	258 358
Normal tax payable	72 340	72 340	72 340	72 340	72 340
Dividend tax	27 903	27 903	27 903	27 903	27 903
Total tax payable	100 243	100 243	100 243	100 243	100 243
Average total tax for 5 years	100 243				

Figure 28: Summary of case study twenty sevens total tax payable

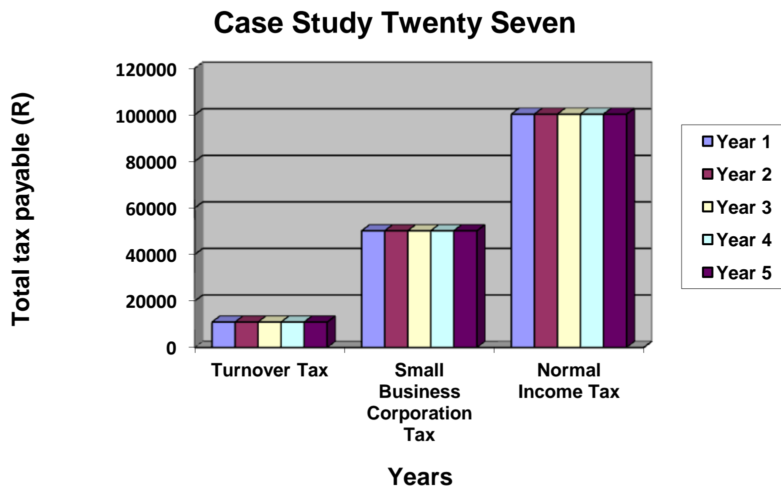


Figure 28 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. There is no wear and tear allowance therefore year one to five has the same tax payable.

5.3.4.11 Case Study Twenty Eight

Turnover tax liability

Based on the sliding scale the tax liability would have been R941 (1% x (R244 142 – R150 000)) if the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R244 142.

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Dividends tax liability R5 763 (((R239 358 – R941) – R200 000) X 15%). Case study twenty eights total tax liability under this option would thus have been R6 704.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R239 358, with a tax liability of R12 057 (7% x (R239 358 – R67 111)). The dividends tax liability would have been R34 095 ((R239 358 – R12 057) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	239 358	239 358	239 358	239 358	239 358
Normal tax payable	12 057	12 057	12 057	12 057	12 057
Dividend tax	34 095	34 095	34 095	34 095	34 095
Total tax payable	46 152	46 152	46 152	46 152	46 152
Average total tax for 5 years	46 152				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R67 020 (R239 358 x 28%). The dividends tax liability would have been R25 851 ((R239 358 – R67 020) x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	239 358	239 358	239 358	239 358	239 358
Normal tax payable	67 020	67 020	67 020	67 020	67 020
Dividend tax	25 851	25 851	25 851	25 851	25 851
Total tax payable	92 871	92 871	92 871	92 871	92 871
Average total tax for 5 years	92 871				

Figure 29: Summary of case study twenty eights total tax payable

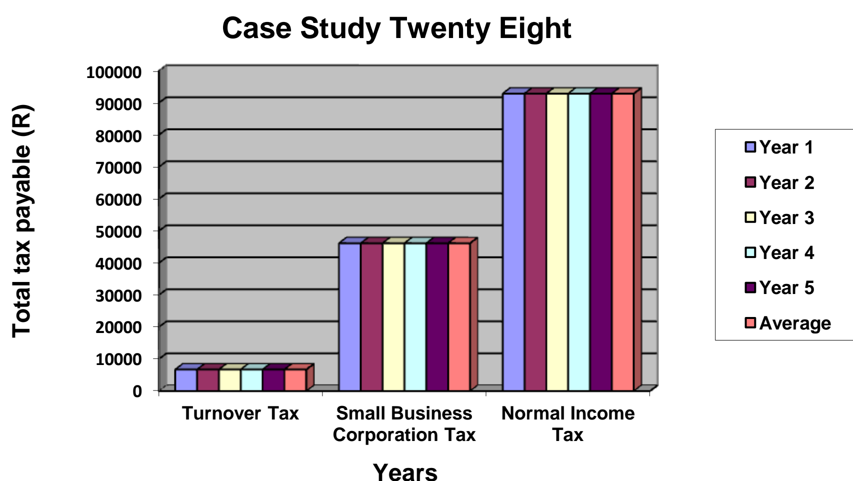


Figure 29 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. There is no wear and tear allowance therefore the same tax is payable for year one to five.

5.3.4.12 Case Study Twenty Nine

Turnover tax liability

Based on the sliding scale the tax liability would have been R0 (0% x R138 947), if the business had chosen the turnover tax system, their tax liability would have been calculated based on its turnover of R138 947.

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act. Case study twenty nine would therefore have had a R0 tax liability under this option.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R37 287, with a tax liability of R0 (0% x R37 287). The dividends tax liability would have been R5 593 (R37 287 x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	37 287	37 287	37 287	37 287	37 287
Normal tax payable	0	0	0	0	0
Dividend tax	5 593	5 593	5 593	5 593	5 593
Total tax payable	5 593	5 593	5 593	5 593	5 593
Average total tax for 5 years	5 593				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R10 440 (R37 287 x 28%). The dividends' tax liability would have been R4 027 ((R37 287 – R10 440) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	37 287	37 287	37 287	37 287	37 287
Normal tax payable	10 440	10 440	10 440	10 440	10 440
Dividend tax	4 027	4 027	4 027	4 027	4 027
Total tax payable	14 467	14 467	14 467	14 467	14 467
Average total tax for 5 years	14 467				

Figure 30: Summary of case study twenty nines total tax payable

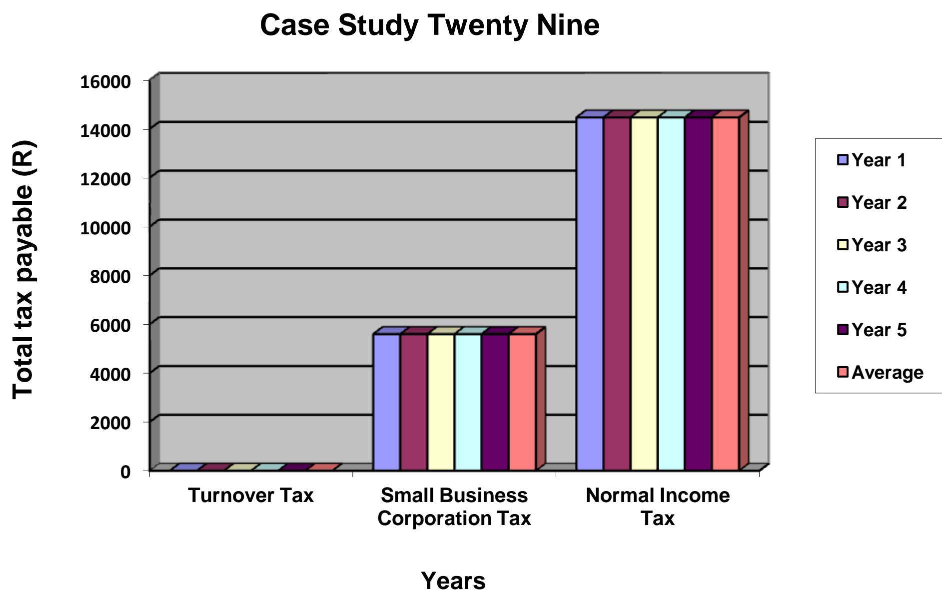


Figure 30 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. There is no wear and tear allowance consequently the same tax is due for years one to five.

5.3.4.13 Case Study Thirty

Turnover tax liability

Had the business chosen the turnover tax system, their tax liability would have been R0 (0% x R96 000) based on its turnover of R96 000, based on the sliding scale.

Businesses that are subject to turnover tax are not subject to dividends tax on the first R200 000 dividends in terms of section 64F(1)(*h*) of the Income Tax Act, therefore under this option, case study thirties total tax liability would therefore have been R0.

Small business corporation normal tax liability

The tax liability would have been calculated on its taxable income of R4 839, with a tax liability of R0 (0% x R4 839). The dividends tax liability would have been R726 (R4 839 x 15%).

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Taxable income (refer above)	4 839	4 839	4 839	4 839	4 839
Normal tax payable	0	0	0	0	0
Dividend tax	726	726	726	726	726
Total tax payable	726	726	726	726	726
Average total tax for 5 years	726				

Normal taxpayer normal tax liability

Under the normal income tax system, the business would have had a tax liability of R1 355 (R4 839 x 28%). The dividends tax liability would have been R523 ((R4 839 – R1 355) x 15%).

	Year 1	Year 2	Year 3	Year 4	Year 5
Taxable income (refer above)	4 839	4 839	4 839	4 839	4 839
Normal tax payable	1 355	1 355	1 355	1 355	1 355
Dividend tax	523	523	523	523	523
Total tax payable	1 878	1 878	1 878	1 878	1 878
Average total tax for 5 years	1 878				

Figure 31: Summary of case study thirties total tax payable

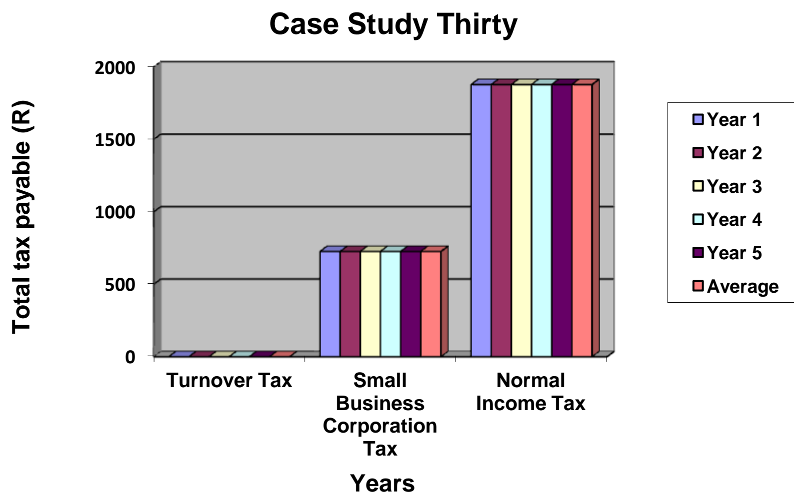


Figure 31 is a collation of the above total tax payable calculations for each tax system over a 5 year period to illustrate the time value of money. Because there is no wear and tear allowance the company is liable for the same tax for years one to five.

5.3.4.14 Summary and Conclusion of Case Studies Eighteen to Thirty

The results for case studies eighteen to thirty can be summarised as follows:

Table 11: Total tax liability/ (taxable loss) for case studies eighteen to thirty for year one

Case Study	Turnover Tax (R)	Small Business Corporation Tax/ (Taxable Loss) (R)	Normal Tax/ (Taxable Loss) (R)
18	0	7 424	19 205
19	8 689	44 066	89 007
20	2 262	35 282	72 739
21	47 703	73 275	142 566
22	17 841	23 191	50 346
23	353	34 165	70 670
24	0	23 713	51 312
25	18 429	(118 787)	(118 787)
26	13 026	(30 956)	(30 956)
27	10 907	50 133	100 243
28	6 704	46 152	92 871
29	0	5 593	14 467
30	0	726	1 878

Table 11 is a summary of the total tax liability/ (taxable loss), includes dividend tax for case studies eighteen to thirty on each of the three tax systems. This data was collated from above case study calculations.

Stemming from the above tax calculations the most beneficial tax system for case studies eighteen to twenty four, twenty seven to thirty would be the turnover tax system. In terms of this tax system no tax or the lowest tax would have been payable and the tax expense would be based on the turnover of the business, however, all the criteria of the Sixth Schedule and section 48 of the Income Tax Act have to be satisfied in order to qualify as a micro business for this tax system to be used. The qualifying turnover for the year of assessment does not exceed R1-million, however, an exclusion per the Sixth Schedule of the Income Tax Act (South Africa 1962:260) is applicable. A professional service provider is disqualified from the turnover tax system as per paragraph 3 of the Sixth Schedule to the Income Tax Act. The Income Tax Act states that a professional service is any service in the field of accounting,

actuarial science, architecture, auctioneering, auditing, broadcasting, consulting, draftsmanship, education, engineering, financial service broking, health, information technology, journalism, law, management, real estate broking, research, sport, surveying, translation, valuation or veterinary science (South Africa 1962). These case studies do not meet the requirements of a micro business as they are real estate brokers.

The next best tax system for these businesses is the small business corporation tax system, again all the criteria of section 12E(4)(*a*) of the Income Tax Act have to be satisfied. As per the Income Tax Act gross income does not exceed R20 million, none of the members should hold any shares in other companies and not more than 20 percent of total receipts and accruals should consist of personal services or investment income. This business meets the criteria however, provides personal services and therefore does not meet the prerequisites of a small business corporation (section 12E(4)(a) of the Income Tax Act).

For case studies twenty five and twenty six the most beneficial tax system would have been the small business corporations tax as the least amount of tax would be payable, however, once again all the criteria of section 12E(4)(*a*) of the Income Tax Act have to be satisfied before a business can apply this tax system. Yet again, these case studies provide real estate services which are included in the definition of a personal service.

The only choice for case studies eighteen to thirty is to apply the normal income tax system as they do not meet the requirements of the turnover tax and small business corporation tax systems, being real estate brokers. The results were the same over a five year period as there was no wear and tear allowance, therefore the results are not presented here. A summary of the thirty case studies follows.

5.3.5 Summary of the Thirty Case Studies

Overall it appeared that the small business corporation tax system would have been the most beneficial tax system for fifteen of the thirty case studies and the turnover tax system for the other fifteen case studies. In the long term the small business corporation tax system would have been the most beneficial tax system for fourteen of the thirty case studies and the turnover tax system for the other sixteen case studies. The difference over the longer term, being case study ten, due to the lower tax rates and dividend tax exemption on the first R200 000 dividends in terms of section 64F(1)(*h*) in respect of micro businesses.

If the business had made a loss the turnover tax system would not have been ideal as the business would have been liable for taxes as the tax liability is based on the business turnover that exceeds the exempt threshold. The small business corporation or normal income tax is a better option as the assessed loss may be carried over to the next financial year and offset against future income, if all the criteria are satisfied. What may be inferred from above is that the turnover tax system is most beneficial to businesses with a turnover of R500 000 and below and that do not have much tax deductible expenditure. Businesses with high expenditure do not benefit from the turnover tax system because tax is levied on taxable turnover that exceeds the exempt threshold, which is before deducting expenditure. Operating as a sole proprietor might be most beneficial if the business has a low profit and no other income. Emanating from above discussion it is apparent that small business corporations generally have a cash flow advantage especially with respect to the wear and tear allowances and other tax deductible expenditure and lower tax rates.

The mean for the fifteen small business corporations of 63% (median is 53%, range is 76%, mode is 33%) of revenue was to cover expenditure of which at least (mean) 2% (median is 1%, range is 3%, mode is 1% and 2%) covered accounting fees, this is a third of the revenue of the business. These expenses relate to water and electricity, wages, advertising and other expenses as seen above in the thirty case studies.

The mean for the fifteen turnover tax of 40% (median is 39%, range is 93%, there is no mode) of revenue covered expenditure of which the mean of 2% (median is 1%, range is 5%, mode is 1%) covered accounting fees. From this it may be perceived that the turnover tax system would not benefit these businesses, as the tax expense would be incurred on turnover before the business expenditure. Therefore these businesses would incur a tax expense before allowable expenses are deducted.

For businesses in an assessed loss position (taxable income before capital allowances), the mean of 75% (median is 67%, range is 55%, there is no mode) of revenue, covered expenditure of which 2% (mean) (median is 2%, range is 3%, mode is 2%) covered accounting fees. The reason why these businesses have an assessed loss is due to the fact that on average (mean), 75% contribute to expenditure and the allowable deductions/allowances exceed the revenue of the business. Proposals have been made to change the small business corporation tax and turnover tax systems.

5.4 DAVIS TAX COMMITTEE PROPOSAL

The Davis Tax Committee was established in 2013 by the former Minister of Finance, Pravin Gordhan to examine the role of South Africa's tax system in order to promote growth, job creation, sustainable development and fiscal self-reliance. The top priority of the committee is growth of small businesses. After having examined the role of the South African tax system, the Committee was expected to make recommendations to the Minister of Finance, the decision was announced as part of the budget and legislative process.

The interim report was issued by the Davis Tax Committee (2014) and the following statistics were presented: 7 827 active micro businesses, 139 with addresses unknown, 59 dormant, 74 in estates, 345 in-active and 49 suspended. The committee has proposed that small business corporations tax be replaced with a flat corporate rate of 28% and that small businesses receive a refundable compliance

rebate of R15 000 (Davis Tax Committee 2014). This rebate would also be received by small business corporations in a loss making position. What does this mean for small businesses? Instead of being taxed on lower rates on a sliding scale, small businesses will be taxed at a fixed rate of 28% and receive a R15 000 rebate, which is currently the normal income tax system rate. This rebate will not be permitted to small businesses with turnover less than R335 000 per annum (Davis Tax Committee 2014:21) and in addition, the turnover tax system should amend its thresholds (assuming a net profit percentage of 20% of turnover) as follows:

Turnover (R)	Rate of Tax (R)
0 – 335 000	0% of turnover
335 001 - 500 000	2% of the amount above R335 000
500 001 - 750 000	R3 300 + 4% of the amount above R500 000
750 001 - 1 000 000	R13 300 + 5% of the amount above R750 000

(Davis Tax Committee 2014:28)

Table 12: Davis committee proposal impact on total tax on the selected thirty case studies for year one

Case Study	Turnover	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax and Dividend Tax Proposed Change
1	357 916	(88)	(15 000)	458
2	352 100	4 764	(10 236)	342
3	202 464	(31 923)	0	0
4	925 580	41 336	26 336	22 079
5	271 236	12 812	12 812	0
6	768 645	4 020	(10 980)	14 232
7	425 869	29 721	14 721	1 817
8	983 891	14 189	(811)	24 995

Case Study	Turnover	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax and Dividend Tax Proposed Change
9	215 650	(503)	0	0
10	300 600	3 794	3 794	0
11	282 134	(321 141)	0	0
12	892 710	32 671	17 671	20 436
13	298 332	(26 216)	0	0
14	383 195	11 564	(3 436)	964
15	275 569	20 094	20 094	0
16	996 367	13 125	(1 875)	25 618
17	907 127	11 548	(3 452)	21 156
18	140 125	19 205	19 205	0
19	473 750	89 007	74 007	6 769
20	338 108	72 739	57 739	62
21	931 608	142 566	127 566	44 139
22	789 023	50 346	35 346	15 251
23	185 333	70 670	70 670	0
24	135 912	51 312	51 312	0
25	786 981	(118 787)	(15 000)	15 149
26	688 150	(30 956)	(15 000)	10 826
27	351 671	100 243	85 243	9 037
28	244 142	92 871	92 871	5 904
29	138 947	14 467	14 467	0
30	96 000	1 878	1 878	0

Table 12 is the impact the Davis Committee's proposal has on the total tax (together with dividend tax) for the selected thirty case studies. The turnover and normal

income tax/ (taxable loss) was collated from each of the above thirty case studies. The small business proposed change was calculated at 28% on the normal taxable income/ (loss) plus dividend tax, less R15 000 compliance rebate, noting small businesses with turnover less than R335 000 do not qualify for the rebate. Lastly, the turnover tax proposed changes were calculated using the proposed amended thresholds (assuming a net profit percentage of 20% of turnover) above plus dividend tax. Refer to Annexure D for more information.

For the thirty case studies analysed for this study as presented in table 12 above, it would indicate that twenty six of the thirty cases would benefit from the proposed tax changes. From those twenty six, ten (case studies 1, 2, 6, 8 12, 14, 16, 17, 25 and 26) were said to benefit from electing the proposed small business tax system and sixteen (case studies 4, 5, 7, 10, 15, 18 to 24, 27 to 30) from the changes to the turnover tax system. Based on the analysis performed using the proposed changes businesses with a lot of tax deductible expenditure generally benefited the most from the proposed small business tax system and the other businesses generally benefited from the changes to the turnover tax system. The majority of the cases that benefited from the small business proposed tax system were retailers and service providers, while most real estate brokers benefited from the proposed turnover tax rates. Real estate brokers are personal service providers and as previously mentioned do not qualify as micro businesses. Businesses in an assessed loss position and whose turnover is less than R335 000, could choose either the proposed small business corporation or turnover tax system, this was applicable for four of the case studies (3, 9, 11 and 13). Other factors should be considered by it when choosing a tax system, for example administrative expenses.

Table 13: Davis committee proposal impact on total tax on the selected thirty case studies over five years

Case Study	Turnover	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax and Dividend Tax Proposed Change
1	357 916	(264)	(15 000)	458
2	352 100	4 764	(10 236)	342
3	202 464	(95 769)	0	0
4	925 580	41 336	26 336	22 079
5	271 236	12 812	12 812	0
6	768 645	4 020	(10 980)	14 232
7	425 869	29 721	14 721	1 817
8	983 891	14 189	(811)	24 995
9	215 650	(1 509)	0	0
10	300 600	3 794	3 794	0
11	282 134	(963 423)	0	0
12	892 710	32 671	17 671	20 436
13	298 332	(78 648)	0	0
14	383 195	11 564	(3 436)	964
15	275 569	20 094	20 094	0
16	996 367	13 125	(1 875)	25 618
17	907 127	11 548	(3 452)	21 156
18	140 125	19 205	19 205	0
19	473 750	89 007	74 007	6 769
20	338 108	72 739	57 739	62
21	931 608	142 566	127 566	44 139
22	789 023	50 346	35 346	15 251

Case Study	Turnover	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax and Dividend Tax Proposed Change
23	185 333	70 670	70 670	0
24	135 912	51 312	51 312	0
25	786 981	(118 787)	(15 000)	15 149
26	688 150	(30 956)	(15 000)	10 826
27	351 671	100 243	85 243	9 037
28	244 142	92 871	92 871	5 904
29	138 947	14 467	14 467	0
30	96 000	1 878	1 878	0

Table 13 is the impact the Davis Committee's proposal has on the total average tax (together with dividend tax) over a 5 year period for the selected thirty case studies. The turnover and normal income tax/ (taxable loss) was collated from each of the above thirty case studies. The small business proposed change was calculated at 28% on the normal taxable income/ (loss) plus dividend tax less R15 000 compliance credit, noting small businesses with turnover less than R335 000 do not qualify for the rebate. Lastly, the turnover tax proposed changes were calculated using the proposed amended thresholds (assuming a net profit percentage of 20% of turnover) above plus dividend tax. Refer to Annexure E for more information.

Twenty six of the thirty cases would benefit from the proposed tax changes. From those twenty six, ten were said to benefit from electing the proposed small business tax system and sixteen from the changes to the turnover tax system. The majority of the cases that benefited from the small business proposed tax system were retailers and service providers, while most of the real estate brokers benefited from the proposed turnover tax rates. Real estate brokers are personal service providers and as previously mentioned do not qualify as micro businesses. Businesses in an

assessed loss position and whose turnover is less than R335 000, could choose either the proposed small business corporation or turnover tax system, this was applicable for four of the case studies (3, 9, 11 and 13). Other factors should be considered by it when choosing a tax system, for example administrative expenses. The same results were obtained over a 5 year period and year one because no accelerated allowance is received under the proposed changes and this eliminates the benefits of the time value of money. The summary of this chapter is presented here under.

5.5 SUMMARY

This chapter presented the results gained from analysing the financial statements of the thirty case studies. Each financial statement was analysed and discussed in depth presenting the actual figures from the financial statements. A quantitative approach was used to analyse the financial statements of each case study. The analysis of each financial statement was performed to identify the type of business, the tax expense for all three tax systems were recalculated, namely turnover tax, small business corporation tax and the normal income tax system for companies and lastly the most beneficial of the three tax systems was identified for each of the businesses once all the criteria as per the Income Tax Act were satisfied. This was followed by the Davis Tax Committee proposal. The next chapter presents the conclusion and recommendations for this study.

Chapter 6 : CONCLUSION AND RECOMMENDATIONS

6.1 INTRODUCTION

The turnover tax system was implemented in South Africa with effect from 1 March 2009. This study investigated the working of this system when compared to the small business corporation tax system.

In this chapter the conclusions and recommendations emanating from this study were discussed. The results will be discussed based on the research questions developed in Chapter 1. Initially the limitations of this study are presented in section 6.2. Thereafter the conclusions arrived at from the interviews are dealt with in section 6.3 and case studies are discussed. This is followed by the recommendations in section 6.4 for the use of the two tax systems, namely turnover tax and small business corporation tax systems and recommendations for future studies follow. Finally the contribution of this study to the knowledge on both turnover tax and small business corporation tax systems are discussed in 6.5. The limitations experienced while conducting this study are presented below.

6.2 LIMITATIONS OF THE STUDY

As with any study of this nature there are certain limitations that must be considered when evaluating the results and recommendations. In this study one of the major limitations was the process of identifying tax practitioners who were willing to be interviewed. Several tax practitioners did not want to be interviewed for various reasons, including time constraints due to large workloads. The practitioners who participated in this study were therefore selected using a convenience sample.

Another limitation was obtaining financial statements of businesses that could be used due to the confidential client information and unwillingness of businesses to supply financial information. Although the researcher had requested depersonalised

financial statements which were to be used in an ethical manner, tax practitioners were not willing to share their clients' financial information due to the confidentiality agreement with clients as well as for ethical reasons. Those tax practitioners who had originally agreed to participate in the study, requested the permission of several of their clients, however, their clients refused to participate in the study although they were assured that anonymity would be observed. Consequently, those practitioners withdrew from participating in the study. Another obstacle encountered was that some of the tax practitioners who were approached to participate in the study did not have many clients with a turnover of R1 million and below.

Additionally, it was difficult to identify businesses whose turnover was less than a million rand and located in various sectors in industry. The tax practitioners although willing to provide financial statements were not in a position to provide financial statements for particular industries requested.

Since time was a constraint the tax practitioners who participated in this study provided financial statements that were accessible. Despite these limitations the study makes a valuable contribution to the field being studied by using actual financial statements (case study) information to evaluate the effectiveness of the different tax systems. Having pointed out the limitations experienced, a discussion of the conclusions emanating from the findings follow.

6.3 CONCLUSIONS OF THE STUDY

The aim of this study was to identify which tax system provides the most beneficial tax dispensation to small business corporations and micro businesses. A literature review was undertaken to determine the tax legislation requirements and benefits applicable to micro and small business corporations. The research was followed by conducting face-to-face interviews with tax practitioners and a tax representative, in order to gain the opinions on the benefits and limitations regarding small business corporations and micro businesses. The next phase of the study involved an analysis

of thirty financial statements which were referred to as case studies to identify the tax payable using the different tax systems in the selected case studies, namely turnover tax, small business corporations tax and the normal income tax system and lastly to identify which of the three tax systems is most beneficial to the business once all the criteria as per the Income Tax Act were met. The findings and analysis of the interviews were presented in Chapter 4 and the findings and analysis of the case studies were presented in Chapter 5. From the analysis of the two phases of the research certain conclusions were reached and a discussion of these conclusions follows. The themes identified in Chapter 4 are presented and the first theme that emerged was the knowledge of the tax systems available for small and micro businesses.

6.3.1 Knowledge of the tax systems in terms of which small and micro businesses will be taxed

All the participants were aware that the turnover tax system is available to micro businesses and the small business corporation tax system to small business corporations and micro businesses. From the face-to-face interviews it was evident that the participants have not kept abreast with the changes to the tax legislation which states that the gross income limitation is now R20 million and below for a small business corporation. The participants were only aware of the old gross income requirement of R14 million and below as the criteria for a small business corporation. This lack of knowledge regarding the tax legislation questions the participants' ability to make sound decisions and advise their clients accordingly and may be viewed as a contravention of the Tax Administration Act 28 of 2011. The Act discusses ways to 'enhance' tax compliance so that every person pays their fair portion of tax (South Africa 2011).

This also begs the question "could this be the reason why the participants do not have any micro businesses registered for turnover tax?" In addition, the fact that Mr Khan continuously used the terms sole proprietor and partnership to describe the tax systems indicates his lack of knowledge of the tax systems. According to tax legislation there are three tax systems which may be applied to small business

corporations and micro businesses, namely the turnover tax system, the small business corporation tax system and the normal income tax system. Participants could advise their clients of the benefits and limitations of these systems if they keep abreast with the current changes made to the tax legislation. Benefits and limitations of the turnover tax and small business corporation tax systems will be discussed next.

6.3.2 Benefits and Limitations of the Turnover Tax and Small Business Corporation Tax Systems

The participants in this study found that the turnover tax system is an easy tax system to use because the tax expense is based purely on the turnover of the business as the turnover of the business is taxed according to the relevant tax bracket (see Annexure A). Further, some of the participants pointed out that the client would provide his/her monthly turnover figure and by August of the current financial year the tax practitioner would estimate the turnover for that financial year, this estimate would be revisited towards the end of the year when provisional tax payments are made in August and February each financial year for turnover tax. They also mentioned the fact that no records of purchases and expenses have to be maintained, however, SARS require records of amounts received, dividends declared, all assets with a cost price of more than R10 000 each and records of all liabilities that exceed R10 000 at the end of the year of assessment.

From the participants' understanding of the turnover tax system, all the participants concurred that this tax system is a simpler tax system to apply however, they are of the opinion that the small business corporation tax system is more beneficial to small business corporations and micro businesses.

Another advantage identified by the participants for applying the turnover tax system is that micro businesses do not have to register for VAT and the tax rates applicable for micro businesses are lower depending on the turnover (see Annexure A).

The main limitation identified by participants for the turnover tax system is that application must be made before the beginning of the year of assessment or at a later date during the year of assessment as the Commissioner may prescribe in the Gazette and new businesses within two months of commencement of the business. If a micro business does not meet this deadline for turnover tax, they will have to remain on their current tax system or in the case of a new business they will have to register on the normal income tax system or the small business corporation tax system.

All the participants agreed that the benefits of the small business corporation tax system are the lower tax rates and the accelerated wear and tear allowance on assets. Mr Khan pointed out that for small business corporations no tax is due to SARS for a turnover less than R150 000. The general consensus among participants was that the small business corporation tax system is easy to apply and is based on the information supplied by the client. This is based on the experience of tax practitioners and not taxpayers, it will add to the businesses compliance cost as taxpayers outsource this function to tax practitioners. Based on the fact that the case studies were all small businesses and all the financial statements were prepared by the tax practitioners, it is obvious that many small businesses outsource this function. However, in Ms Essop's opinion there are three limitations to the small business corporation tax system, the first being that a provider of personal services does not qualify as a small business corporation, a trust cannot register as a small business corporation and the turnover requirements for a small business corporation are low. The reason she offered for identifying these limitations is that small businesses are unable to survive.

6.3.3 The Benefits of SARS E-Filing

The general consensus among the participants once again, regarding the general benefit of SARS e-filing is that it is a productive and progressive system since it obviates manual submissions and enables small and micro businesses to file income tax returns and pay taxes online. Apart from the challenges that small and micro businesses face regarding taxation, they also encounter other challenges.

6.3.4 Challenges Faced by Small and Micro Businesses

In general small and micro businesses face many non-tax related challenges due to their size, the first being the economic situation in South Africa. In the opinion of the participants competition is a major challenge faced by small business corporations and micro businesses, with the corporates, conglomerates and the new malls small businesses are suffering due to the decrease in turnover and the loss of clients. Mr Moosa also added that finance plays a significant role in the survival of small businesses. Small businesses are unable to obtain financial assistance and invariably suffer the consequences of a lack of finance.

6.3.5 Compliance Costs for Small and Micro Businesses

The participants concurred that small business corporations and micro businesses experience similar compliance costs to large businesses and because of their size they are forced to outsource the accounting and taxation function, this is a financial burden to the small business corporation or micro business. Micro businesses face lower compliance costs due to the size of their business. Added to the requisite compliance costs are the costs of outsourcing the accounting and taxation functions. Ms Essop suggested that SARS and the Labour Department should be consolidated, however, she conceded that consolidating the departments would not be ideal as these departments function efficiently on their own, for example, SARS and the Labour Department function effectively because they are separate. Having presented the conclusions derived from the qualitative phase of the study, conclusions emanating from the case studies are presented below.

6.3.6 Case Study Analysis

Based on the IMF (2007) theoretical framework discussed in Chapter Two, this section uses the hierarchy identified by them to discuss the conclusions emanating from the case studies. The hierarchy is as follows, the turnover tax system then the small business corporation tax system and finally the normal income tax system.

A spread sheet (a summary of this spread sheet for year 1 is presented in Annexure B and the average of years 1 to 5 in Annexure C) was used to collate the analysis of the thirty financial statements by entering turnover, tax expense, taxable income, accounting fees, expenditure, type of business, the identified tax system based on the analysis referred to in Chapter 5 and lastly the tax system applied by the tax practitioner for each of the case studies. This spread sheet was used to group the businesses into the most beneficial tax system for each case study before the criteria of the Income Tax Act were met.

For each of the case studies a summary of the information available was provided, this took the form of a description of the business activities as well as the basic financial information for the business. This was followed by a discussion of the total tax liability (includes dividend tax) of the case study under each of the different tax systems investigated in Chapter 5. In order to ensure comparability of the tax liability under the different tax systems it was assumed that all profits, after normal tax was distributed and constituted a dividend or deemed dividend subject to the provisions of Part VIII of the Income Tax Act.

For the purpose of this study, it was assumed that each case study would qualify to be taxed under each of the tax systems. The tax liability of each case was calculated despite the fact that the description of the business indicated that it might for example not qualify as a small business corporation due to the fact the owner owns shares in more than one company. After performing all the calculations a conclusion was reached as to which tax system was the best for the business was based on the description of the business and the information contained in the financial statements.

The calculations revealed that the small business corporation tax system was the most beneficial tax system for fifteen of the thirty case studies and the turnover tax system for the other fifteen case studies. Over a five year average, small business corporation tax would have been the most beneficial for fourteen of the thirty case studies and turnover tax for the remaining sixteen. Many factors had to be considered when calculating the tax, such as, type of business, turnover, taxable

income, allowable deductions to determine the most suitable tax system for the case study.

If the business has low profit and no other income, operating as a sole proprietor might be most beneficial. On the other hand, the turnover tax system was identified as the most beneficial to businesses with a turnover of R500 000 and below and these case studies were real estate agents that do not meet the criteria of a micro business. The biggest benefit of the turnover tax system is the reduced administration burden. Amongst other benefits micro businesses do not have to hire a tax consultant to deal with tax issues and turnover tax obviates the time spent on completing the number of different tax returns. As mentioned in Chapter 5, a provider of professional/personal services does not qualify as a micro business or a small business corporation. They all had no choice but to apply the normal income tax system. Fifteen of the thirty businesses would benefit from the turnover tax system. On average 40% of revenue generated by these businesses was to cover expenditure of which at least 2% covered accounting fees, this is a third of the revenue of the business. These expenses relate to water and electricity, wages, advertising and other expenses as seen in the thirty case studies presented in Chapter 5. Small business corporation tax was identified as the most beneficial for fifteen of the cases as mentioned in Chapter 5.

Fifteen of the thirty case studies would benefit most from the small business corporation tax system. Five of the fifteen were sole proprietors and not companies or close corporations and therefore were not eligible to apply the small business corporation tax system. As a result the owners of these businesses were taxed in their personal capacity. The case studies were a combination of service providers, retailers and real estate brokers. From the analysis presented in Chapter 5 it was suggested that it is more beneficial for these five case studies to register as companies and apply the small business corporation tax system. However, it might be more beneficial for sole proprietors to remain as such if their taxable income is low and they do not receive any other income. On average 53% of the revenue generated by these businesses was to cover expenditure of which about 1% covered

accounting fees. Based on the fact that turnover tax is levied on the turnover of the business, these businesses would not benefit as this would be before business expenditure. As discussed in Chapter 5 turnover tax does not benefit businesses with high expenditure and loss making businesses.

In conclusion, five cases studied had assessed losses (taxable income before capital allowances), based on the quantitative analysis performed in Chapter 5 the most appropriate tax system for these cases is the small business corporations tax system. The assessed loss arose from the fact that the allowable deductions were more than the business income. These businesses were located in different industries, such as, real estate, service providers and retailers. On average 75% of the revenue generated by these businesses was to cover expenditure of which 2% covered accounting fees. Although only 69% contributed to expenditure, the assessed loss resulted from the fact that allowable deductions exceeded gross income.

The following was identified when applying the Davis Tax Committee proposals to the thirty case studies, for year one, twenty six of the thirty cases would benefit from the proposed tax changes. From those twenty six, ten (case studies 1, 2, 6, 8 12, 14, 16, 17, 25 and 26) were said to benefit from electing the proposed small business tax system and sixteen (case studies 4, 5, 7, 10, 15, 18 to 24, 27 to 30) from the changes to the turnover tax system. Based on the analysis performed using the proposed changes businesses with a lot of tax deductible expenditure generally benefited the most from the proposed small business tax system and the other businesses generally benefited from the changes to the turnover tax system. The majority of the cases that benefited from the small business proposed tax system were retailers and service providers, while most real estate brokers benefited from the proposed turnover tax rates. Real estate brokers are personal service providers and as previously mentioned do not qualify as micro businesses. Businesses in an assessed loss position and whose turnover is less than R335 000 (noting that the compliance rebate will not be permitted to small businesses with turnover less than R335 000 per annum) could choose either the small business corporation or turnover

tax system, this was applicable for four of the case studies (3, 9, 11 and 13). Other factors should be considered by businesses when choosing a tax system, for example administrative expenses.

The Davis Committee's proposal was applied to the selected thirty case studies over a five year period. Twenty six of the thirty cases would benefit from the proposed tax changes. From those twenty six, ten were said to benefit from electing the proposed small business tax system and sixteen from the changes to the turnover tax system. The majority of the cases that benefited from the small business proposed tax system were retailers and service providers, while most of the real estate brokers benefited from the proposed turnover tax rates. Real estate brokers are personal service providers and as previously mentioned do not qualify as micro businesses. Businesses in an assessed loss position and whose turnover is less than R335 000, could choose either the small business corporation or turnover tax system, this was applicable for four of the case studies (3, 9, 11 and 13). Other factors should be considered by it when choosing a tax system, for example administrative expenses, compliance cost, advisory and bookkeeping costs. The same results were obtained over a five year period and year one because no accelerated allowance is received under the proposed changes and this eliminates the benefits of the time value of money. Stemming from the above conclusions, recommendations for the use of the turnover tax and small business corporation tax system follow.

6.4 RECOMMENDATIONS OF THE STUDY

6.4.1 Recommendations for National Treasury on the Turnover Tax and Small Business Corporation Tax System

This study submits that the gross income and turnover threshold for small and micro businesses are too low and National Treasury should consider increasing these thresholds. The analysis of the financial statements revealed that real estate brokers benefited the most from the turnover tax system, however, they are personal service providers and do not qualify as micro businesses. SARS should modify the requirements of personal service providers, to attract more small businesses. The

scope of the definition of a ‘professional service and personal service provider’ is too wide and not to the point. Straightforward parameters should be used to remove any uncertainty regarding its meaning and scope. The requirements for a micro business should also be modified in order for all micro businesses to benefit from the turnover tax system. The disqualification criteria is arbitrary and needs to be simplified. It is unfair for an individual that belongs to a certain profession to be automatically prohibited from the turnover tax system.

The automatic disqualification from turnover tax for capital disposals greater than R1500 000 in a three year period should be increased and also the disqualification should be effective the following financial year, as no transaction records would have been retained for the current financial year. A provision should be included in the turnover tax system for loss making entities to not have to pay taxes on their turnover and also an assessed loss provision should be implemented. The limitation of a February year ends should be amended, micro businesses should not have to change their financial year end to use the turnover tax system. Turnover tax should replace all taxes, currently it only replaces income tax, dividend tax and CGT.

All sectors are taxed at the same rate, international best practice suggests different tax rates for trade and services. Gluckman (2012) recommends that the tax payable should be logical and understandable to the taxpayer and the government. Small business corporation tax is complex to understand as there are many inclusions and exclusions to taxable income and does not incorporate any of the other taxes. Du Toit (2012) recommended that South Africa implement a limit of R40 000 on the movement in stock levels from the opening to closing balance for small businesses and implement a manufacturing and processing profit deduction for small manufacturing companies.

A recommendation by one of the participants is that an audit trail (records be maintained of all income, expenses and purchases) should be a prerequisite for the turnover tax system. The value of documents to be retained should be increased annually. There was general consensus among the participants that the tax

thresholds should be increased and overall tax burden lowered for both the turnover tax and small business corporation tax systems.

A recommendation from the researcher is that tax practitioners should attend training with the aim of providing them with an in-depth understanding of the tax systems applicable to small and micro businesses. Also, the Tax Administration Act 28 of 2011 should be applied strictly. Additionally, constant support needs to be provided through call centres and easier access provided to SARS offices for individuals and businesses. The OTS (2012) suggests guidance, tips and tools should be provided from the early stages of the small business registration process, two way email communication with a set time frame for responses, updates and impact of tax changes, an option to choose an accounting period, allow all forms to be submitted online, and lastly to choose language on forms, statements and all correspondence that would be easier to understand and to complete for taxpayers.

The literature identified OECD guidelines to which 44 governments adhere, South Africa does not adhere to these guidelines nor do they have similar guidelines; it would be worthwhile for South Africa to consider implementing such guidelines. In addition the OTS issued recommendations for small businesses, these recommendations could be considered by South Africa to educate and assist small businesses in complying with the tax regulations and will give small businesses the confidence and encourage them to comply with tax regulations. These recommendations will assist with compliance of tax regulations and growth and development of small and micro businesses. Recommendations for future research are discussed below.

6.4.2 Recommendations for Future Research

To reiterate this study included five participants and thirty financial statements, this is not representative of the small and micro businesses and the tax practitioner population however, it provided a good indication of the experiences and opinions of tax practitioners as well as a tax representative towards the turnover tax and small business corporation tax systems. To enhance the quality of future studies it is

recommended that a larger sample of tax practitioners who are involved in the tax calculations of small and micro businesses be identified for the collection of data using in-depth face-to-face interviews. In addition a sizeable sample of financial statements should be analysed. The financial statements should be the most recent, preferably from the last financial year. If possible, the financial statements requested for a larger study that should be those of the same industry.

The researcher's recommendation is that face-to-face interviews be conducted with a focus group on small and micro businesses and those employees of SARS who are involved with the turnover tax and small business corporation tax systems. Further insight needs to be gained into the perceived reason for the implementation of the turnover tax system and the perceived benefits and limitations of both the turnover tax and small business corporation tax systems. Interviews could also be conducted with business owners to gain further insight into their knowledge and opinions of the tax systems available to small and micro businesses. Finally the contribution of this study to the knowledge on both turnover tax and small business corporation tax systems is discussed.

6.5 CONTRIBUTION OF THIS STUDY

Tax practitioners may find the information from this study valuable when deciding which tax system to use for clients who own micro or small businesses. The information may also be used as it would assist in providing them with some information to advise their clients on the most appropriate tax system for their businesses. Additionally, the information obtained from this study may also be used by small and micro businesses to highlight which tax system is most beneficial for their business. Furthermore, the results of this study could contribute to the debate on legislation for small and micro businesses prepared by National Treasury.

6.6 SUMMARY

This study aimed to investigate which of the two tax systems, namely the small business corporation tax or turnover tax is more beneficial to the selected small and micro businesses. This chapter presented limitations, conclusions and lastly recommendations for the turnover tax and small business corporation tax system as well as recommendations for future studies.

The conclusions arrived at in this study indicate that the tax practitioners do not keep abreast with changes in legislation and practical problems in the use of the turnover tax system as none of the tax practitioners have applied for this system. The turnover tax system was intended to assist micro businesses to register for taxes however, based on this study it is evident that the turnover tax system is not the most beneficial tax system for the selected micro businesses. This study provided evidence that many factors such as type of business, turnover, taxable income, allowable deductions and the Income Tax Act criteria have to be considered before choosing a tax system. However, it needs to be borne in mind that the tax system chosen may be dictated by the turnover and taxable income of that particular business. Overall this study highlighted very important aspects of taxation that could have an impact on the type of tax system used for small and micro businesses.

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Annexure A: Tax Rates

Small business corporations (financial years ending on any date between 1 April 2013 and 31 March 2014)

Taxable Income (R)	Rate of Tax (R)
0 – 67 111	0% of taxable income
67 112 – 365 000	7% of taxable income above 67 111
365 001 – 550 000	20 852 +21% of taxable income above 365 000
550 001 and above	59 702 +28% of taxable income above 550 000

Turnover tax for micro businesses (financial years ending on any date between 1 April 2013 and 31 March 2014)

Turnover (R)	Rate of Tax (R)
0 – 150 000	0% of taxable turnover
150 001 – 300 000	1% of taxable turnover above 150 000
300 001 – 500 000	1 500 + 2% of taxable turnover above 300 000
500 001 – 750 000	5 500 + 4% of taxable turnover above 500 000
750 001 and above	15 500 + 6% of taxable turnover above 750 000

There rates were obtained from the SARS 2013/2014 Tax Guide (www.treasury.gov.za)

Annexure B: Case Study Analysis (Year 1)

Case Study	Location of business	Type of business	Turnover	Net Profit before Tax	Tax expense as per Financial Statements	Taxable Income/ (loss) (before capital allowance)	Total Turnover Tax (including Dividend Tax)	Total Small Business Corporations Tax Expense (including Dividend Tax	Total Normal Income Tax (including Dividend Tax
1	Lenasia	Retailer	357 916	1 404	-	3 639	2 658	0	-
2	Lenasia	Retailer	352 100	12 279	-	15 822	2 542	1 045	4 764
3	Lenasia	Retailer	202 464	(39 512)	-	(5 817)	525	-	-
4	Mayfair	Retailer	925 580	99 925	2 737	116 378	26 035	15 233	41 336
5	Benoni	Retailer	271 236	33 020	-	35 079	1 212	4 490	12 812
6	Benoni	Retailer	768 645	10 361	-	19 395	16 619	-	4 020
7	Benoni	Retailer	425 869	76 600	2 348	76 959	4 017	12 022	29 721
8	Benoni	Farmer	983 891	36 570	-	43 000	29 533	5 485	14 189
9	Lenasia	Service Provider	215 650	(502)	-	1 993	657	-	-
10	Lenasia	Service Provider	300 600	9 779	-	19 400	1 512	-	3 794
11	Mayfair	Service Provider	282 134	(321 148)	-	(312 457)	1 321	-	-
12	Mayfair	Service Provider	892 710	79 775	2 002	122 504	24 063	4 002	32 671
13	Sandton	Service Provider	298 332	(33 417)	-	(19 015)	1 483	-	-
14	Benoni	Service Provider	383 195	29 805	11 365	30 034	3 164	4 419	11 564
15	Benoni	Service Provider	275 569	51 788	1 918	54 503	1 256	7 157	20 094
16	Ormonde	Service Provider	996 367	33 828	-	79 293	30 282	-	13 125
17	Ormonde	Service Provider	907 127	29 763	-	80 955	24 928	-	11 548
18	Mayfair	Real Estate	140 125	49 488	14 353	49 497	-	7 424	19 205
19	Fordsburg	Real Estate	473 750	305 703	74 209	229 401	8 689	44 066	89 007
20	Fordsburg	Real Estate	338 108	204 707	57 057	187 472	2 262	35 282	72 739
21	Fordsburg	Real Estate	931 608	589 977	134 260	367 439	47 703	73 275	142 566

Case Study	Location of business	Type of business	Turnover	Net Profit before Tax	Tax expense as per Financial Statements	Taxable Income/ (loss) (before capital allowance)	Total Turnover Tax (including Dividend Tax)	Total Small Business Corporations Tax Expense (including Dividend Tax	Total Normal Income Tax (including Dividend Tax
22	Fordsburg	Real Estate	789 023	150 915	38 581	129 757	17 841	23 191	50 346
23	Fordsburg	Real Estate	185 333	183 265	50 999	182 141	353	34 165	70 670
24	Fordsburg	Real Estate	135 912	132 248	37 029	132 248	-	23 713	51 312
25	Fordsburg	Real Estate	786 981	187 013	35 884	(118 787)	18 429	-	-
26	Fordsburg	Real Estate	688 150	179 027	18 692	(30 956)	13 026	-	-
27	Fordsburg	Real Estate	351 671	258 358	72 340	258 358	10 907	50 133	100 243
28	Fordsburg	Real Estate	244 142	239 358	67 020	239 358	6 704	46 152	92 871
29	Kempton Park	Real Estate	138 947	37 287	10 440	37 287	-	5 593	14 467
30	Springs	Real Estate	96 000	4 839	1 355	4 839	-	726	1 878

Annexure C: Case Study Analysis (Average tax liability over 5 year period)

Case Study	Location of business	Type of business	Turnover	Net Profit before Tax	Tax expense as per Financial Statements	Taxable Income/ (loss) (before capital allowance)	Total Turnover Tax (including Dividend Tax)	Total Small Business Corporations Tax Expense (including Dividend Tax	Total Normal Income Tax (including Dividend Tax
1	Lenasia	Retailer	357 916	1 404	-	3 639	2 658	-	-
2	Lenasia	Retailer	352 100	12 279	-	15 822	2 542	1 842	4 764
3	Lenasia	Retailer	202 464	(39 512)	-	(5 817)	525	-	-
4	Mayfair	Retailer	925 580	99 925	2 737	116 378	26 035	18 326	41 336
5	Benoni	Retailer	271 236	33 020	-	35 079	1 212	4 953	12 812
6	Benoni	Retailer	768 645	10 361	-	19 395	16 619	1 554	4 020
7	Benoni	Retailer	425 869	76 600	2 348	76 959	4 017	12 054	29 721
8	Benoni	Farmer	983 891	36 570	-	43 000	29 533	5 485	14 189
9	Lenasia	Service Provider	215 650	(502)	-	1 993	657	-	-
10	Lenasia	Service Provider	300 600	9 779	-	19 400	1 512	1 467	3 794
11	Mayfair	Service Provider	282 134	(321 148)	-	(312 457)	1 321	-	-
12	Mayfair	Service Provider	892 710	79 775	2 002	122 504	24 063	14 154	32 671
13	Sandton	Service Provider	298 332	(33 417)	-	(19 015)	1 483	-	-
14	Benoni	Service Provider	383 195	29 805	11 365	30 034	3 164	4 471	11 564
15	Benoni	Service Provider	275 569	51 788	1 918	54 503	1 256	7 768	20 094
16	Ormonde	Service Provider	996 367	33 828	-	79 293	30 282	5 364	13 125
17	Ormonde	Service Provider	907 127	29 763	-	80 955	24 928	4 638	11 548
18	Mayfair	Real Estate	140 125	49 488	14 353	49 497	-	7 424	19 205
19	Fordsburg	Real Estate	473 750	305 703	74 209	229 401	8 689	44 066	89 007
20	Fordsburg	Real Estate	338 108	204 707	57 057	187 472	2 262	35 282	72 739
21	Fordsburg	Real Estate	931 608	589 977	134 260	367 439	47 703	73 275	142 566
22	Fordsburg	Real Estate	789 023	150 915	38 581	129 757	17 841	23 191	50 346

Case Study	Location of business	Type of business	Turnover	Net Profit before Tax	Tax expense as per Financial Statements	Taxable Income/ (loss) (before capital allowance)	Total Turnover Tax (including Dividend Tax)	Total Small Business Corporations Tax Expense (including Dividend Tax	Total Normal Income Tax (including Dividend Tax
23	Fordsburg	Real Estate	185 333	183 265	50 999	182 141	353	34 165	70 670
24	Fordsburg	Real Estate	135 912	132 248	37 029	132 248	-	23 713	51 312
25	Fordsburg	Real Estate	786 981	187 013	35 884	(118 787)	18 429	-	-
26	Fordsburg	Real Estate	688 150	179 027	18 692	(30 956)	13 026	-	-
27	Fordsburg	Real Estate	351 671	258 358	72 340	258 358	10 907	50 133	100 243
28	Fordsburg	Real Estate	244 142	239 358	67 020	239 358	6 704	46 152	92 871
29	Kempton Park	Real Estate	138 947	37 287	10 440	37 287	-	5 593	14 467
30	Springs	Real Estate	96 000	4 839	1 355	4 839	-	726	1 878

Annexure D: Davis Committee Proposal (Year One)

Case Study	Type of business	Turnover	Small Business Corporations Taxable Income/ (Taxable Loss)	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Rebate	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax Proposed Change	Dividend Tax	Turnover Tax and Dividend Tax Proposed Change
1	Retailer	357 916	(88)	(88)	(15 000)	(15 000)	458	-	458
2	Retailer	352 100	12 279	4 764	(15 000)	(10 236)	342	-	342
3	Retailer	202 464	(31 923)	(31 923)	-	-	-	-	0
4	Retailer	925 580	106 537	41 336	(15 000)	26 336	22 079	-	22 079
5	Retailer	271 236	33 020	12 812	-	12 812	-	-	0
6	Retailer	768 645	10 361	4 020	(15 000)	(10 980)	14 232	-	14 232
7	Retailer	425 869	76 600	29 721	(15 000)	14 721	1 817	-	1 817
8	Farmer	983 891	36 570	14 189	(15 000)	(811)	24 995	-	24 995
9	Service Provider	215 650	(503)	(503)	-	-	-	-	0
10	Service Provider	300 600	9 779	3 794	-	3 794	-	-	0
11	Service Provider	282 134	(321 141)	(321 141)	-	-	-	-	0
12	Service Provider	892 710	84 204	32 671	(15 000)	17 671	20 436	-	20 436
13	Service Provider	298 332	(26 216)	(26 216)	-	-	-	-	0
14	Service Provider	383 195	29 805	11 564	(15 000)	(3 436)	964	-	964
15	Service Provider	275 569	51 788	20 094	-	20 094	-	-	0
16	Service Provider	996 367	33 828	13 125	(15 000)	(1 875)	25 618	-	25 618
17	Service Provider	907 127	29 763	11 548	(15 000)	(3 452)	21 156	-	21 156
18	Real Estate	140 125	49 497	19 205	-	19 205	-	-	0
19	Real Estate	473 750	229 401	89 007	(15 000)	74 007	2 775	3 994	6,769
20	Real Estate	338 108	187 472	72 739	(15 000)	57 739	62	-	62
21	Real Estate	931 608	367 439	142 566	(15 000)	127 566	2 380	21 759	44 139

Case Study	Type of business	Turnover	Small Business Corporations Taxable Income/ (Taxable Loss)	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Rebate	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax Proposed Change	Dividend Tax	Turnover Tax and Dividend Tax Proposed Change
22	Real Estate	789 023	129 757	50 346	(15 000)	35 346	15 251	-	15 251
23	Real Estate	185 333	182 141	70 670	-	70 670	-	-	0
24	Real Estate	135 912	132 248	51 312	-	51 312	-	-	0
25	Real Estate	786 981	(118 787)	(118 787)	(15 000)	(15 000)	15 149	-	15 149
26	Real Estate	688 150	(30 956)	(30 956)	(15 000)	(15 000)	10 826	-	10 826
27	Real Estate	351 671	258 358	100 243	(15 000)	85 243	333	8 704	9 037
28	Real Estate	244 142	239 358	92 871	-	92 871	-	5 904	5 904
29	Real Estate	138 947	37 287	14 467	-	14 467	-	-	0
30	Real Estate	96 000	4 839	1 878	-	1 878	-	-	0

Annexure E: Davis Committee Proposal (Average over 5 year period)

Case Study	Type of business	Turnover	Small Business Corporations Taxable Income/ (Taxable Loss)	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Rebate	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax Proposed Change	Dividend Tax	Turnover Tax and Dividend Tax Proposed Change
1	Retailer	357 916	-264	(264)	(15 000)	(15 000)	458	-	458
2	Retailer	352 100	12 279	4 764	(15 000)	(10 236)	342	-	342
3	Retailer	202 464	(95 769)	(95 769)	0	-	-	-	0
4	Retailer	925 580	106 537	41 336	(15 000)	26 336	22 079	-	22 079
5	Retailer	271 236	33 020	12 812	0	12 812	-	-	0
6	Retailer	768 645	10 361	4 020	(15 000)	(10 980)	14 232	-	14 232
7	Retailer	425 869	76 600	29 721	(15 000)	14 721	1 817	-	1 817
8	Farmer	983 891	36 570	14 189	(15 000)	(811)	24 995	-	24 995
9	Service Provider	215 650	(1 509)	(1 509)	0	-	-	-	0
10	Service Provider	300 600	9 779	3 794	0	3 794	-	-	0
11	Service Provider	282 134	(963 423)	(963 423)	0	-	-	-	0
12	Service Provider	892 710	84 204	32 671	(15 000)	17 671	20 436	-	20 436
13	Service Provider	298 332	(78 648)	(78 648)	0	-	-	-	0
14	Service Provider	383 195	29 805	11 564	(15 000)	(3 436)	964	-	964
15	Service Provider	275 569	51 788	20 094	0	20 094	-	-	0
16	Service Provider	996 368	33 828	13 125	(15 000)	(1 875)	25 618	-	25 618
17	Service Provider	907 127	29 763	11 548	(15 000)	(3 452)	21 156	-	21 156
18	Real Estate	140 125	49 497	19 205	0	19 205	-	-	0
19	Real Estate	473 750	229 401	89 007	(15 000)	74 007	2 775	3 994	6 769
20	Real Estate	338 108	187 472	72 739	(15 000)	57 739	62	-	62
21	Real Estate	931 608	367 439	142 566	(15 000)	127 566	22 380	21 759	44 139

Case Study	Type of business	Turnover	Small Business Corporations Taxable Income/ (Taxable Loss)	Normal Income Tax and Dividend Tax/ (Taxable Loss)	Rebate	Small Business Proposed Change Normal Income Tax and Dividend Tax/ (Tax Credit)	Turnover Tax Proposed Change	Dividend Tax	Turnover Tax and Dividend Tax Proposed Change
22	Real Estate	789 023	129 757	50 346	(15 000)	35 346	15 251	-	15 251
23	Real Estate	185 333	182 141	70670	0	70 670	-	-	0
24	Real Estate	135 912	132 248	51312	0	51 312	-	-	0
25	Real Estate	786 981	(118 787)	(118 787)	(15 000)	(15 000)	15 149	-	15 149
26	Real Estate	688 150	(30 956)	(30 956)	(15 000)	(15 000)	10 826	-	10 826
27	Real Estate	351 671	258 358	100 243	(15 000)	85 243	333	8 704	9 037
28	Real Estate	244 142	239 358	92 871	0	92 871	-	5 904	5 904
29	Real Estate	138 947	37 287	14 467	0	14 467	-	-	0
30	Real Estate	96 000	4 839	1 878	0	1 878	-	-	0