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FORMAL SMME TAX COMPLIANCE SURVEY REPORT

PREPARED FOR NATIONAL TREASURY REPUBLIC OF SOUTH AFRICA

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This publication was produced for review by the United States Agency for International Development. It was prepared by Professor Rajen Govender and Citizen Surveys.

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EXECUTIVE SUMMARY

1. The purpose of this study was to investigate the overall costs of tax compliance for formal SMMEs in South Africa. Tax compliance costs were defined as all those costs incurred in the course of ensuring proper compliance with relevant tax regulations. These costs include the following:
 - The costs incurred in the course of record-keeping – this includes all the costs associated with the compiling and organization of receipts and records.
 - The costs incurred in the preparation and submission of all relevant tax returns.
 - The value of the time utilized by the small business staff in ensuring proper compliance, including visits to tax offices.
 - The costs incurred for the services of tax practitioners, accountants, and other consultants that may have been required to either ensure compliance and/or address disputes with SARS.
 - All other costs incurred in the course of ensuring compliance, including incidental and travel costs.

2. For the purposes of this study, a formal SMME was defined as a small business enterprise which was registered for and paying tax and which had an annual turnover of between R70 000 and R14 000 000.

3. The sample size for this study was fixed at 1000 cases, and the requirement was for this sample to be drawn in a manner that ensured an adequate basis for generalisability to the national population of formal SMMEs. To ensure the extraction of the sample with due consideration to the two key stratification variables (annual turnover and provincial location), a sampling cluster of 90 sample clusters was established, composed of a matrix of five turnover bands by nine provinces by two firm categories. The realised sample was extracted employing equal probability selection methods (EPSEM) for sampling of and within each cluster. Following the conclusion of the fieldwork, the obtained sample was reweighted to ensure national representivity.



4. It was apparent from the study that the assessment of advantages of tax registration by formal SMMEs was largely, and understandably, localised around business concerns, with just under half of all businesses (46.5%) providing a response in this cluster, with only under one-tenth indicating benefits to the wider community and society. Respondents were generally of the opinion that the primary advantage of being tax registered and compliant was the improved legal standing of the business, which in turn greatly facilitated business operations and offered the greatest prospects for business growth and success. In this regard, it was useful to note that campaigns to ensure better rates of compliance would probably be better served by focusing on direct benefits to the business rather than indirect benefits to society and the country.

5. Conversely, with respect to the disadvantages of tax registration and compliance, the greatest quantum of responses received related to the likely negative impact of compliance on the financial health of the business, and consequently, the possible negative impact on future growth prospects as a result of diminished levels of investment. Not surprisingly, the costs associated with tax compliance tasks and activities featured prominently in listed disadvantages of compliance. However, and reassuringly, almost one fifth (19.3%) of all respondents indicated that there were no real disadvantages to being tax registered, and this view was held regardless of entity type, sector of operation or size of the enterprise (turnover).

6. Formal small businesses were also quite consolidated in the view that being VAT registered was advantageous because it enabled the business to capitalise on the input tax credits through VAT refunds. This undoubtedly had a positive impact on cash flow and monies available for business growth and expansion. Nevertheless, many such formal SMME's are also worried about the relatively high costs associated with ensuring that they were fully compliant on this particular tax. Additionally, around one third of all those SMMEs who were registered for VAT at the time, indicated that there were no disadvantages to such registration. This group correlated strongly with those SMMEs who saw no disadvantages to be registered for Income Tax, indicating a more positive overall approach by these small businesses towards tax compliance.



7. In terms of the allocation and completion of tax- and compliance-related tasks within and without the small business, the survey found that the majority of small businesses relied on in-house expertise to attend to general record-keeping and bookkeeping, preferring to outsource primarily when the required tasks gravitated towards tax and specialised tax tasks. About one third of small businesses were entirely dependent on external expertise the remainder being partially dependent on this.



8. The principal reason for not outsourcing was the availability of appropriate expertise within the enterprise, with this being particularly true for proprietary limited enterprises. Sole proprietor and partnerships did not outsource as extensively as the other two types of enterprise because they reported being unable to afford such outsourcing. The primary reason for outsourcing was the highly specialised nature of the tax field. Close corporations were the most likely to outsource for this reason, while sole proprietor and partnerships businesses were likely to do so because of the difficulty in keeping abreast of changes in tax laws and rules.
9. Looking at all the different types of enterprise, it was clear that close corporations were the most dependent on the outsourcing of most tax and compliance tasks such as compiling financial statements and filing tax returns as well as engagement with SARS. In the case of proprietary limited businesses, the level of outsourcing was much lower because of the availability of in-house expertise. It was apparent that such enterprises actively limited the extent of outsourcing, achieving as much as possible internally and thereby allocating only the more critical tasks to external agencies.
10. In terms of the internal costs of compliance - the cost to enterprise in terms of the time required to prepare, complete and submit tax returns - the study revealed that income tax and provisional tax placed the lowest and second lowest burdens respectively on businesses in terms of the time requirement for their completion and filing. The highest burden was for employees' taxes (PAYE, UIF and SDL), which accounted for almost half of all time spent per annum on relevant taxes. VAT was the tax with the highest demand on time, consuming roughly one third of all the time taken per annum on all taxes.
11. Enterprises in the lowest turnover category (R70 000 per annum) spent a disproportionately greater amount of time to accomplish all the required activities for filing of returns for taxes for which they were registered. This corresponded to their low rates of outsourcing observed earlier, meaning that the burden of these tasks inevitably fell to resident capacity. Furthermore, given the small size of these businesses, it was likely that resident capacity was fairly low, thereby further increasing the amount of time needed to accomplish the required tasks.





12. The study also examined the role and costs of external consultants. In this regard, it was found that tax practitioners undoubtedly played an important role in the affairs of these small businesses, featuring in the tax and associated tasks of around 45% of small businesses, and that this role was that much more pronounced for tax matters than it was for general accounting and recordkeeping. The overwhelming majority of the tax practitioners were certified (as accountants, bookkeepers or tax consultants).
13. The reliance on tax practitioners was lowest in sole proprietor and partnership businesses, with a significant proportion of them getting by on their own even for specialised tax tasks, though dependency increased with correspondingly higher degrees of interaction with SARS, as in the case of the lodging of appeals and petitioning for waivers of interest and penalties
14. Close corporations were the most dependent on tax practitioners, mainly due to a greater tax requirement than sole proprietor and partnership businesses coupled with the lesser availability of in-house expertise as compared to proprietary limited businesses. Proprietary limited businesses were the least dependent on tax practitioners, preferring instead to absorb as many tax tasks and functions in-house before proceeding to outsourcing.
15. About half of small businesses which outsourced were unable to indicate the specific costs associated with this outsourcing. Small businesses were also unable to separate general accounting or bookkeeping costs from tax costs, though they believed that the bulk of the costs were aggregated at the tax end of the spectrum.
16. Only one-tenth of formal SMMEs lodged an appeal with SARS in the past year, with three-quarters of these lodging the appeals themselves, while the remainder used a tax practitioner to do so. The majority of appeals were lodged for Income Tax, and there were too few cases for all the other types of taxes to enable any meaningful analysis thereof.
17. The average cost of appeals in matters related to income tax was found to be around R1 750. This cost remained quite consistent regardless of whether the business or the tax practitioner lodged the appeal. Enterprises in the R1 million to R6 million turnover category



registered the highest average cost per appeal, consistently so regardless of who had lodged the appeal.

18. Perceptions of the appeals process were generally positive for most aspects of the process, particularly the deadline provided for the lodging of appeals and the nature of the appeal process. However, the single biggest complaint was the time taken for SARS to respond to appeals, with the majority of businesses being very unhappy with this.
19. Access to SARS was also examined in the survey. More than half of all surveyed businesses visited SARS last year, with the majority of these visiting SARS six times or less. On average, enterprises with the lowest turnover made the most number of visits to SARS, presumably because they could not afford to outsource tax matters and/or did not have sufficient in-house expertise to speedily address tax matters.
20. Three quarters of visitors to SARS took an hour or less to make the round trip from their place of business to SARS, while one-tenth took two hours and longer. Half of the visitors without appointments waited in queues for more than five minutes only about one-twentieth of the time. More than half of visitors without appointments were attended to within 15 minutes of joining the queue, which was well below the 95% target set out in the SARS charter. When visitors had made an appointment, they were kept waiting for a somewhat shorter period of time, with about two thirds having to wait for more than five minutes less than 5% of the time.
21. Less than 10% of businesses had interest and penalties applied due to late submission of tax returns. All of these businesses applied for relief from imposed sanctions, with two-thirds of them being successful in their bids. Moreover, applications for bids were generally made only once, except in a minority of cases when up to four applications were made.
22. The average cost for this appeals process was R850 for businesses which did so themselves and R1000 for businesses that used tax practitioners. The cost was highest for sole proprietor and partnership businesses and lowest for proprietary limited businesses. Close corporations were the most likely to use tax practitioners for such appeals.



23. In terms of improving overall levels of compliance, the survey found that about one third or 30% of small enterprises believed that there was nothing that SARS could do to improve compliance. This view corresponds to the high rates of compliance by these respondents, indicating well-established organisational routines for ensuring these levels of compliance.



24. The most frequently cited suggestions for improving compliance related to issues of access to SARS and the nature and quality of service provided by SARS to small businesses. Businesses prioritized the location of SARS offices, indicating a need to have them closer to where businesses were located. This was presumably to lower the time and travel costs associated with visiting SARS offices. In general, there was a need to increase overall levels of service from SARS, and specifically with respect to the efficiency of VAT refunds (the delays thereof undoubtedly had significant cash flow implications for SMMEs, particularly those in the lowest turnover categories).
25. One sixth of all businesses indicated that the procedures for registration and filing should be simpler and more easily accomplished, tax forms should be shortened to enable quicker completion thereof, and that forms should be simplified in terms of the language used and more explanatory notes should be provided.
26. Just under one tenth of businesses believed that there was a need for SARS to extend itself into the business community by way of providing education and training to SMMEs to help ensure better submission and overall general compliance, holding road shows to increase general understanding of tax and tax matters, and by directly helping businesses grow.
27. Finally, in terms of communication and media, formal small businesses indicated that SARS could improve compliance by increasing the amount of information on tax that it provided to SMMEs, improving its overall communication with small businesses, and by increasing the levels of advertising in the mass media.



CHAPTER ONE: INTRODUCTION, DEFINITIONS AND RESEARCH OBJECTIVES

I. I. PREAMBLE

There was general consensus that the SMME sector played a critical role in stimulating economic growth and promoting social development in South Africa. Amongst the attributes of this sector identified as being conducive to socio-economic development were the penetration of such types of businesses into previously disadvantaged communities, and the greater ability of such businesses to create jobs as compared to more capital-intensive larger enterprises.

However, notwithstanding the assessed value of SMMEs in promoting economic and social development, concerns have been expressed from various quarters about the constraints under which this sector has been compelled to operate. One such constraint has been identified as the relatively poor access to capital for such businesses when compared to larger more established enterprises. This was regarded as a key constraint.

Further key constraints have been identified as the regulations and bureaucracy which govern this sector and under which such businesses were compelled to operate. This was not simply a national trend, but has been identified globally as a key constraint to the continued growth and expansion of this sector. While regulations and bureaucracy were manifest in many forms, various studies have identified the regulations relating to tax compliance as being particularly onerous to small businesses. In South Africa, the impact of tax compliance regulation costs was also highlighted for special attention in the 2005 Budget Speech.

In addition to the cost of tax compliance, the complexity of ensuring such compliance was also identified as a significant challenge for SMMEs in South Africa. The cost and complexity of tax compliance was closely interconnected, with prior research indicating that greater degrees of complexity were invariably related to higher compliance costs. This trend was particularly true for small businesses because of their often poor or insufficient in-house capacity to accomplish such compliance, resulting in them having to increasingly outsource various tax functions to tax practitioners. This trend was identified and highlighted in the survey of tax practitioners undertaken by the Financial Investment Advisory Service in South Africa. The study also highlighted that the



costs of tax compliance were generally regressive for small businesses, with those with lower turnover expending greater proportions of their revenue to achieve such compliance¹.

Following from the 2005 budget speech, the cost and complexity of tax compliance for SMMEs in South Africa has been identified by both National Treasury (NT) and the South African Revenue Service (SARS) as a priority issue. To this end, both NT and SARS have since committed themselves to a multi-pronged approach to addressing this matter. The principal elements of this approach included promoting greater awareness and a culture of compliance amongst the country's small businesses, actively reducing the degree of complexity in compliance and the overall costs thereof, supporting small businesses in their business growth and development strategies, improving the capacity of small business to achieve compliance by identifying and providing requisite education and assistance in relevant taxation legislation and regulation and tax matters.

To facilitate these processes, a series of empirical research efforts were also identified as necessary for the accumulation of relevant information and the development of appropriate intervention strategies. The first of these was the aforementioned Survey of Tax Practitioners, which sought to obtain the views and assessments of practitioners in terms of their servicing of the SMME sector. The second and third research projects sought to assess a similar set of issues directly from small businesses themselves. One of these studies was undertaken for formal SMMEs, and the other for informal SMMEs. Collectively, these three empirical studies were intended to provide sufficient feedback for NT and SARS to consider and implement various tax policy and regulation reform initiatives.

The document that follows recorded and discussed the nature and primary findings of the survey of formal SMMEs. The study was undertaken in 2007 by an independent research agency contracted by the funders and who was accountable to NT and SARS.

1.2. DEFINITIONS

Before proceeding to the empirical research, it is useful to consider and clarify some of the issues around definitions.

¹ FIAS, "Tax Compliance Burden for Small Businesses: A survey of Tax Practitioners in South Africa", available at http://www.ifc.org/ifcext/fias_nfs/Content/FIAS_Resources_Country_Reports



1.2.1. Formal SMMEs

The first of these relates to the definition of an SMME. This report will not provide a detailed elaboration of this as much of this work has already been achieved (and approved) in the Survey of Tax Practitioners (STP). Hence this research employed definitions that ensued from that study (these definitions have subsequently been somewhat modified, but these modifications occurred after the current research had taken to field)

To clarify, for the purposes of these studies, a small business was defined as a business enterprise whose turnover was greater than R70 000 and less than R14 million per annum. Formal SMMEs were further defined as small business enterprises which were registered for and paying tax.

1.2.2. Tax Compliance Costs

For the purposes of these two studies, and once again proceeding from the STP, tax-compliance costs were defined as all those costs incurred in the course of ensuring proper compliance with relevant tax regulations. These costs include the following:

- The costs incurred in the course of record-keeping – this included all the costs associated with the compiling and organization of receipts and records.
- The costs incurred in the preparation and submission of all relevant tax returns.
- The value of the time utilized by the small business staff in ensuring proper compliance, including visits to tax offices.
- The costs incurred for the services of tax practitioners, accountants, and other consultants that may have been required to either ensure compliance and/or address disputes with SARS.
- All other costs incurred in the course of ensuring compliance, including incidental and travel costs.

Furthermore, as correctly identified in the STP, there was no error-free method for accurately assessing the full costs associated with tax compliance, particularly so as small businesses, by their very nature, were less likely to have on hand comprehensive documentation of all the activities, behaviours and personnel involved in ensuring compliance. However, while the STP focussed on the expertise of professional tax practitioners who had small businesses as their clients, this study



focused on the direct experience of the small businesses themselves regarding their costs, including their own staff time.

In this regard, it must be stated that the current method did not claim to be foolproof, but was instead employed as the best possible method to date for the estimation of the complete costs of tax compliance for small businesses. As such, the costs identified in this study should be regarded as indicative costs rather than “true” costs, which are impossible to assess completely and accurately with any single research methodology.



1.2.3. Tax Instruments

The tax instruments covered in this study followed directly from the tax regimen in South Africa, and were as follows²:

- Income Tax
- Value Added Tax (VAT)
- Pay As You Earn (PAYE)
- Skills Development Levy (SDL)
- Unemployment Insurance Fund contributions (UIF)

1.3. RESEARCH OBJECTIVES

As indicated in the original request for the proposal (RFP) supplied by the research funders, the research objective with respect to the survey of formal SMMEs was to investigate:

- The time and cost burdens to formal SMMEs for registering for Income tax, VAT and PAYE
- The time and cost burdens to formal SMMEs for filing returns for Income tax, VAT and PAYE
- Additional issues relating to:
 - access to SARS
 - the penalties and interest payable for non-compliance
 - and various aspects of formal SMME interaction with SARS

Additionally, in discussions with National Treasury, it was agreed that the study would also focus on identifying:

- How many of the formal SMMEs did their own books
- How many of them used formal/informal tax practitioners
- The importance of the relationship with the tax practitioner for the formal SMME
- The extent and level of involvement of the tax practitioner in the business
- Regarding a simplified tax regime for SMMEs –
 - what would it constitute?
 - what needed simplification?

² Note that CCs and PTY Ltds are automatically registered for provisional tax, along with income tax



- where it was most needed?
- Whether or not it was possible to separate accounting costs from tax costs
- What specifically could be done to lighten the compliance burden for formal SMMEs³

³ CCs, Pty, Ltds are automatically registered for provisional tax along with income tax



Finally, it was also agreed amongst all partners that the study would provide as much detail as possible on the population of formal SMMEs in the country, and specifically, the breakdown by:

- Region (province)
- Sector
- Tax instrument (VAT, Income Tax, PAYE, etc.)
- Any other significant available sub-category



CHAPTER TWO: RESEARCH METHODOLOGY

2.1. SAMPLING FRAME

To properly investigate issues relating to tax compliance and the costs associated with this, it was necessary to draw a sample of formal SMMEs that would ensure adequate generalisability to the population of formal SMMEs in the country. Furthermore, it was decided that the obtained sample should ensure sufficient number of cases according to the identified stratification variables to permit disaggregated analysis.

According to the Income Tax Act, the “gross income” of a resident entity was defined as “the total amount in cash or otherwise received by or accrued to or in favour of a resident.” For the purposes of this study, this “gross income” was deemed to be the most accurate proxy for the turnover of the formal SMMEs. Hence, and following from the definition of formal SMMEs as being small businesses registered for/ paying tax and with a turnover of R70 000 to R14 million per annum, it was decided that the SARS registry of tax filings by formal SMMEs would be employed to define the sampling frame. Furthermore, the 2005 tax year data was deemed to be the most complete and thus was employed for determining the sampling frame.

2.1.1. Gross Income

Based on this sampling methodology, SARS furnished the research team with an analysis of gross income for formal SMMEs. This analysis was disaggregated according to the entity type: 1) Sole Proprietors and Partnerships, and 2), PTY (Ltd) and Close Corporations. Of the 287,856 Sole Proprietors and Partners registered with SARS (where tax returns had been captured), 70,626 firms fell within the R70,000 to R14,000,000 turnover range, comprising both taxpayers and enterprises. Of the 493,058 PTY (Ltd) and Close Corporations, 173,192 fell within the stipulated gross income range.



Detailed tables showing gross income proportions by legal form and turnover follow here.

Table 2-1: Proportion of Legal Form within size of Business

Legal	Sole proprietorship	Partnership	Company (PTY LTD)	Close corporation	Other	Total
Less than R70 000	5.7%		1.2%	4.3%		3.5%
R70 000 to R300 000	32.8%	12.3%	4.5%	15.0%		15.3%
R300 001 to R1 000 000	17.8%	16.9%	12.2%	22.6%	33.3%	18.9%
R1 000 001 to R6 000 000	20.7%	35.4%	32.1%	33.1%	33.3%	30.9%
R6 000 001 to R14 000 000	7.5%	15.4%	17.9%	8.2%		10.9%
Over R14 million	4.6%	7.7%	21.1%	5.5%	33.3%	9.4%
Don't know/Unsure/Refusal	10.9%	12.3%	11.0%	11.3%		11.2%
Total	100%	100%	100%	100%	100%	100%

Table 2-2: Proportion of Business Turnover within Legal Form

Legal	Sole proprietorship	Partnership	Company (PTY LTD)	Close corporation	Other	Total
Less than R70 000	28.6%		8.6%	62.9%		100%
R70 000 to R300 000	37.3%	5.2%	7.2%	50.3%		100%
R300 001 to R1 000 000	16.4%	5.8%	15.9%	61.4%	0.5%	100%
R1 000 001 to R6 000 000	11.7%	7.4%	25.6%	55.0%	0.3%	100%
R6 000 001 to R14 000 000	11.9%	9.2%	40.4%	38.5%		100%
Over R14 million	8.5%	5.3%	55.3%	29.8%	1.1%	100%
Don't know/Unsure/Refusal	17.0%	7.1%	24.1%	51.8%		100%
Total	17.4%	6.5%	24.6%	51.2%	0.3%	100%

The quintiles for the Sole Proprietors and Partnership SMME gross income distribution were established as:

- Quintile 1: R70,000 to R99,206
- Quintile 2: R99,207 to R141,553
- Quintile 3: R141,554 to R211,518
- Quintile 4: R211,519 to R361,389
- Quintile 5: R361,390 to R14,000,000



The quintiles for the PTY (Ltd) businesses and Close Corporations gross income distribution were established as:

- Quintile 1: R70,000 to R225,824
- Quintile 2: R225,825 to R526,360
- Quintile 3: R526,361 to R1,225,956
- Quintile 4: R1,225,957 to R3,149,742
- Quintile 5: R3,149,743 to R14,000,000

2.1.2. Regional (Provincial) Distribution

A key requirement for this study was ensuring provincial distribution of formal SMMEs in accordance with the actual provincial distribution of such SMMEs in the country. SARS does not capture the provincial location of registered SMMEs, but does record the postal code in the address details for each SMME. These postal codes were thus used in order to establish the provincial location of the SMMEs.

Once the provincial distribution had been determined, the gross income bands were identified within each of the provinces, thereby ensuring the stratification framework for the drawing of the sample. The two stratification frameworks are provided below.



Table 2-3: Pty (Ltd) and CC - Number of Firms (Province by Gross Income Band)

Gross Income Band	Eastern Cape	Free State	Gauteng	KwaZulu-Natal	Limpopo	Mpumalanga	North West	Northern Cape	Western Cape	Grand Total
R70,000 to R225,824	1,750	1,296	15,714	3,590	796	1,568	1,413	599	7,731	34,457
R22,5825 to R526,360	1,856	1,298	15,830	3,392	770	1,700	1,369	550	7,849	34,614
R526,361 to R1,225,956	1,920	1,436	15,264	3,480	852	1,912	1,417	660	7,823	34,764
R1,225,957 to R3,149,742	2,157	1,441	14,921	3,628	842	1,959	1,441	694	7,711	34,794
R3,149,743 to R14,000,000	2,028	1,308	15,696	3,555	763	1,940	1,377	648	7,248	34,563
Grand Total	9,711	6,779	77,425	17,645	4,023	9,079	7,017	3,151	38,362	173,192

Table 2-4: Sole Proprietor and Partnerships – Number. Firms (Province by Gross Income Band)

Gross Income Band	Eastern Cape	Free State	Gauteng	KwaZulu-Natal	Limpopo	Mpumalanga	North West	Northern Cape	Western Cape	Grand Total
R70,000 to R99,206	1,116	1,142	3,590	2,118	425	737	865	784	3,338	14,115
R99,207 to R141,553	1,028	1,128	3,676	2,038	479	755	847	818	3,347	14,116
R141,554 to R211,518	1,043	1,162	3,840	1,959	466	726	854	773	3,276	14,099
R211,519 to R361,389	912	1,076	4,188	1,916	457	669	909	690	3,273	14,090
R361,390 to R14,000,000	677	832	5,564	1,767	256	561	712	500	3,337	14,206
Grand Total	4,776	5,340	20,858	9,798	2,083	3,448	4,187	3,565	16,571	70,626



2.2. SAMPLE EXTRACTION

The sample size for this study was fixed at 1000 cases. To ensure the extraction of this number of cases with due consideration to the two key stratification variables, a sampling cluster of 90 sample clusters was established, composed of a matrix of five turnover bands by nine provinces by two firm categories. The realised sample was extracted employing equal probability selection methods (EPSEM) for sampling of and within each cluster.

Given the difficulties experienced with securing respondent participation, the high number of incomplete questionnaires due to the length of the interview, and surveys that were spoilt due to incomplete/inaccurate information, it was anticipated that there would be some measure of discrepancy between the realised and obtained samples. Based on the final returns, this deviation rate was established as being less than 3%, which was wholly acceptable for a survey of this nature.

Finally, following the completion and vetting of all interviews, the final sample was then reweighted to ensure adequate national probability estimates and therefore, generalisability to the national population of formal SMMEs.

2.3. THE RESEARCH QUESTIONNAIRE

The research questionnaire was developed jointly by the research team and representatives from the funding agencies. The questionnaire drew upon global studies of a similar nature, with sufficient adaptation for local conditions. A copy of the final questionnaire as deployed in the field has been provided in Annexure A.

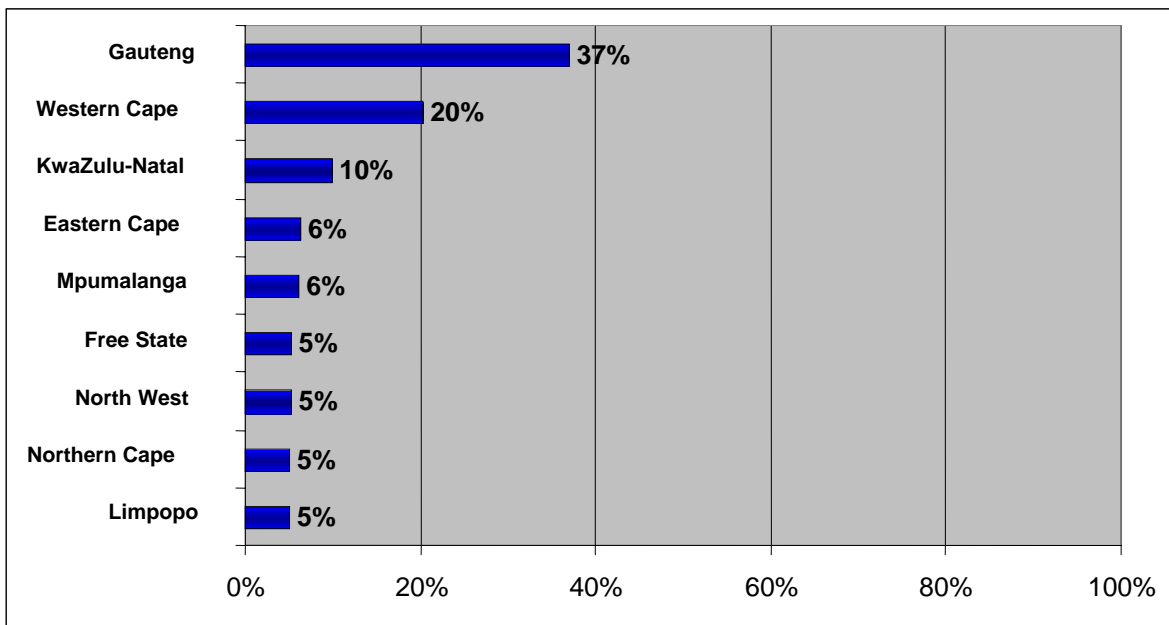
CHAPTER THREE: PROFILE OF THE SAMPLE

This chapter illustrates and discusses the core features and characteristics of the sample. In reviewing this chapter, it was useful to bear in mind that the sample was intended to be generalisable to the national population.

3.1. PROVINCIAL DISTRIBUTION

Given that the sample for the SMMEs was extracted from the relevant SARS databases employing a stratified sampling design with Probability Proportionate-to-Size (PPS) selection, the distribution of provincial location in the obtained sample was consistent with national distribution (see Figure 3-1).

Figure 3-1: Provincial Sub-Sample Distribution

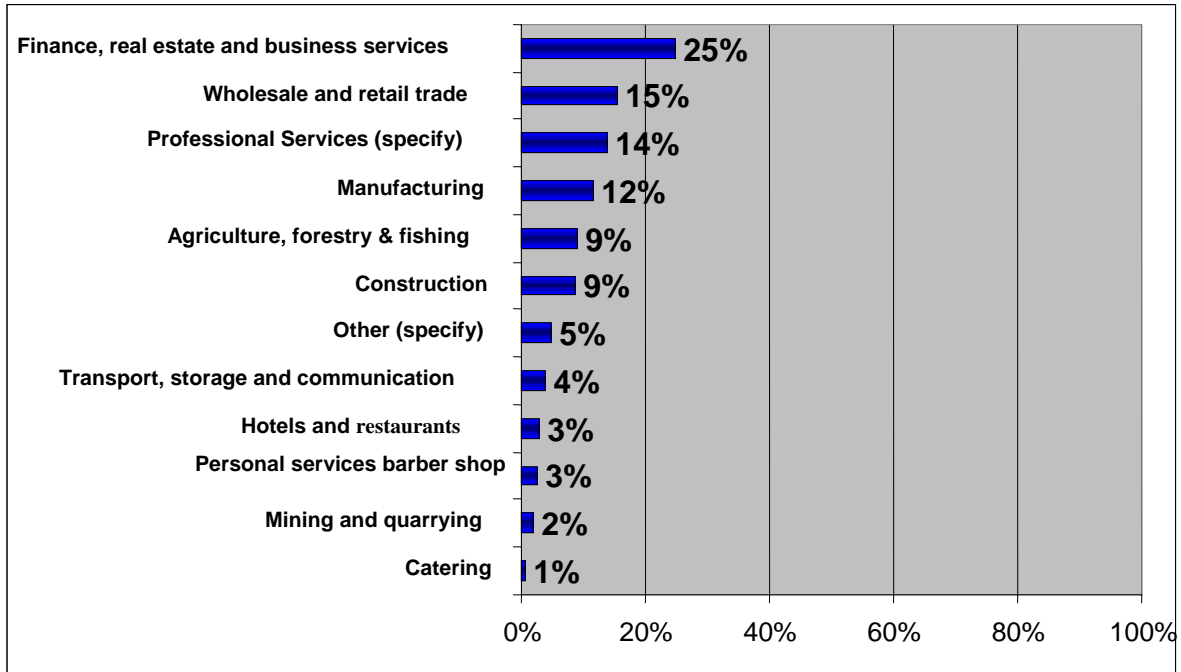


As can be seen in Figure 3-1, the largest sub-sample of formal SMMEs was resident in Gauteng, followed by the Western Cape and then KwaZulu-Natal. This trend was also observed in the survey of tax practitioners, with the exception being that in this study the formal SMMEs in the Northern Cape were deliberately over sampled to ensure a sufficient number of cases for meaningful provincial analysis.

3.2. SECTORS OF OPERATION

The distribution of formal SMMEs according to their sector of operation has been provided in Figure 3-2 below.

Figure 3-2: The distribution of Formal SMMEs



As can be seen in Figure 3-2, the highest proportion of surveyed SMMEs operate in the Finance, Real Estate and Business Services sector (24.8%), followed by Wholesale and Retail Trade (15.4%), Professional Services (13.9%) and Manufacturing (11.6%). Conversely, Personal Services (2.6%), Mining and Quarrying (1.8%) and Catering (0.6%) were the least represented sectors in the formal SMME population.

In terms of the distribution of key sectors across provinces, the noteworthy findings were:

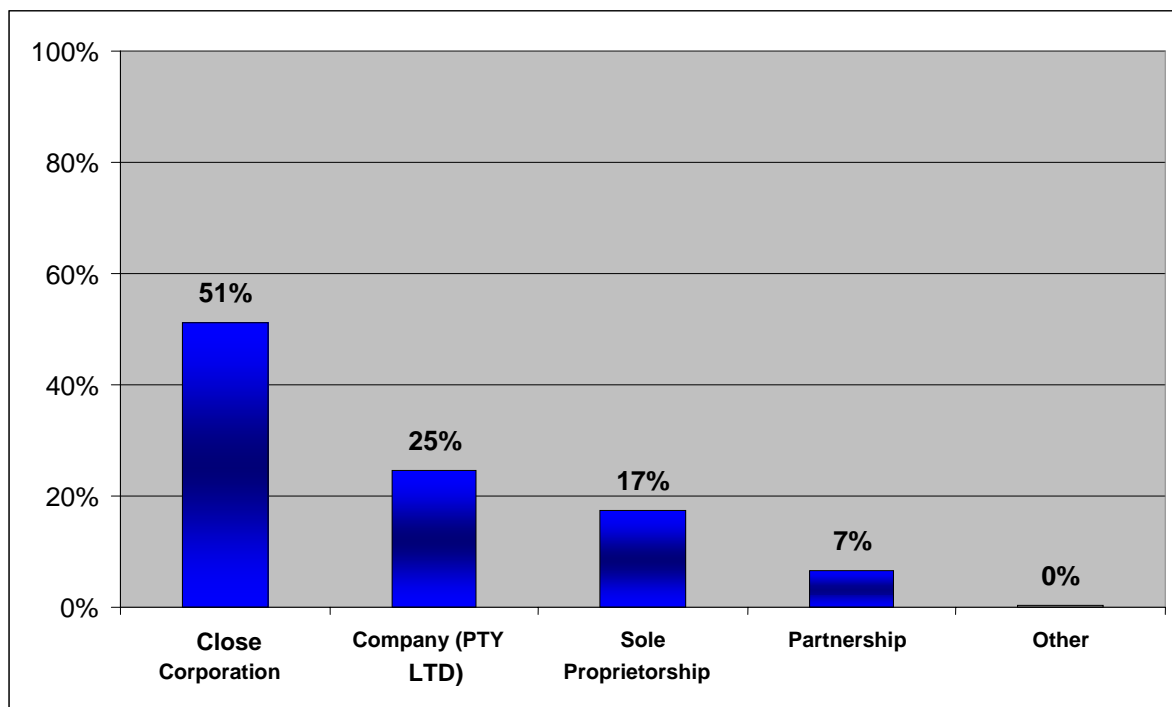
- The Wholesale and Retail sector was overrepresented in Mpumalanga and particularly so in Limpopo,
- Manufacturing was underrepresented in the North West, Mpumalanga, Limpopo and Northern Cape,
- Finance, Real Estate and Business Services were underrepresented in KwaZulu-Natal, and,

- Professional Services was underrepresented in Mpumalanga, Limpopo and Northern Cape.

3.3. ENTERPRISE TYPE

As can be seen in Figure 3-3, just over half of the SMMEs were close corporations (51.1%), with around a quarter being proprietary limited businesses (24.6%) and the remaining quarter being sole proprietorships and partnerships.

Figure 3-3: Enterprise Type



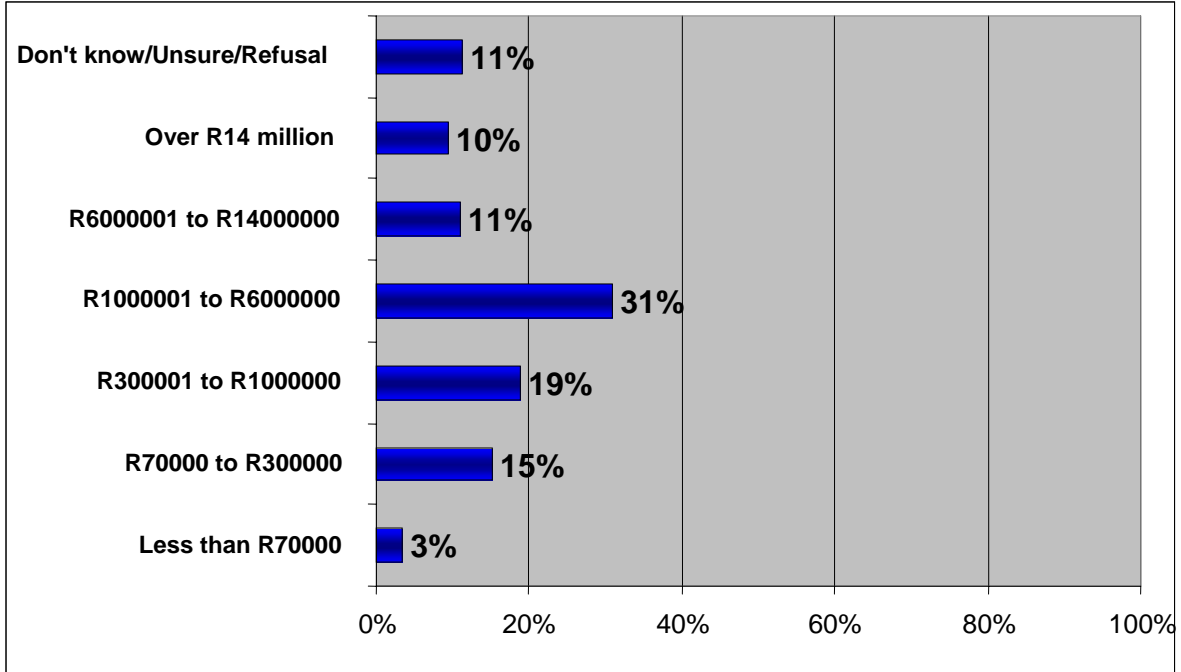
The distribution of type of enterprise across provinces was generally consistent with overall proportionate distribution in the sample, the noteworthy exceptions being:

- Gauteng had a disproportionately higher number of proprietary limited businesses
- The North West and Limpopo both had a disproportionately lower rate of proprietary limited businesses and a disproportionately higher rate of sole proprietor and partnership enterprises.

3.4. ANNUAL TURNOVER/SALES

The distribution of annual turnover/sales for the surveyed SMMEs has been indicated below.

Figure 3-4: Annual Turnover/ Sales



The highest proportion of SMMEs was in the R1 million to R6 million bracket (30.8%), followed by the R300 000 to R1 million category (18.8%), and then the R70 000 to R300 000 category (15.3%).

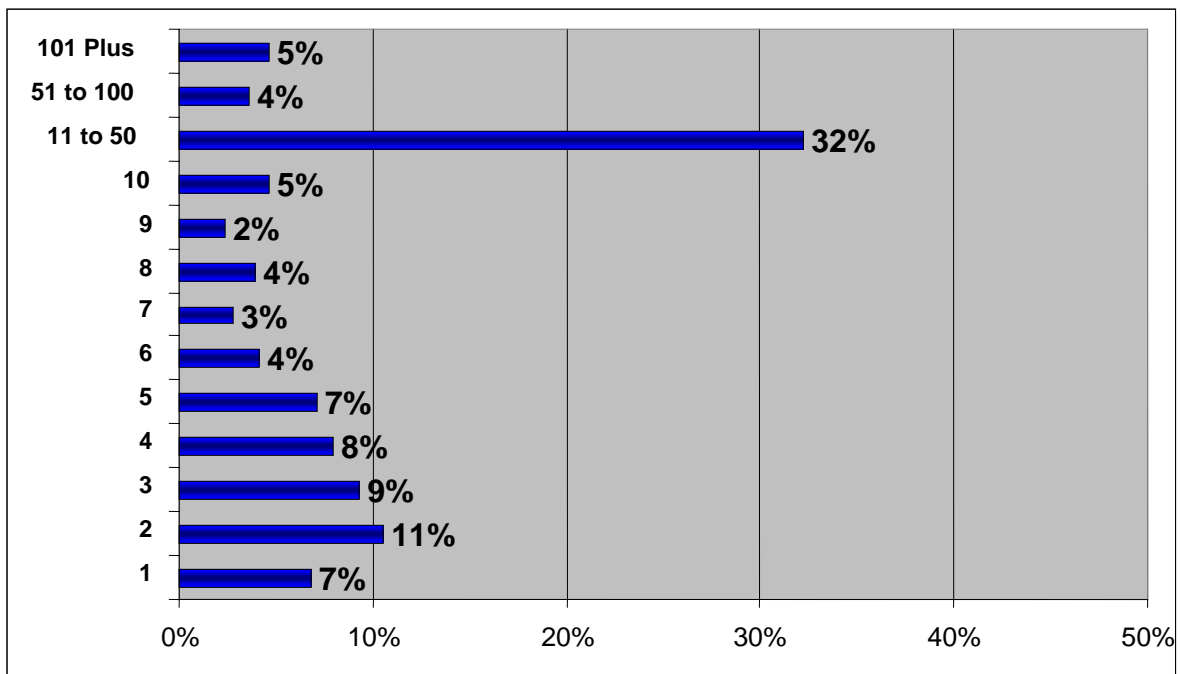
Almost one tenth of the sample indicated annual sales and turnover above R14 million, which was the revenue threshold for definition of an SMME. However, these SMMEs were nevertheless captured in the study as the sampling frame was developed using data for the 2005 year. While the realised sample based on this extraction ensured no SMMEs with annual sales or turnover above R14 million, the fact that these SMMEs were included was because these enterprises had experienced growth in the intervening 2-3 years. Given the difficulties associated with securing respondent cooperation for this study, it was elected to retain these SMMEs rather than filter them out and attempt to obtain other respondents. This was also true for those SMMEs who recorded annual turnover/sales of less than R70 000. Once again, these cases were retained in the final sample.



Finally, just over one tenth (11.2%) of respondents either refused to indicate or were unsure of their annual sales or turnover. An analysis of the distribution of these cases according to enterprise type, sector of operation and provincial location indicated no immediately discernible pattern, indicating that refusal to provide income detail was not related to or dependent on any specific enterprise demographic variable.

3.5. NUMBER OF FULL-TIME EMPLOYEES AND WORKERS

Figure 3-5: Number of Full-Time Employees and Workers

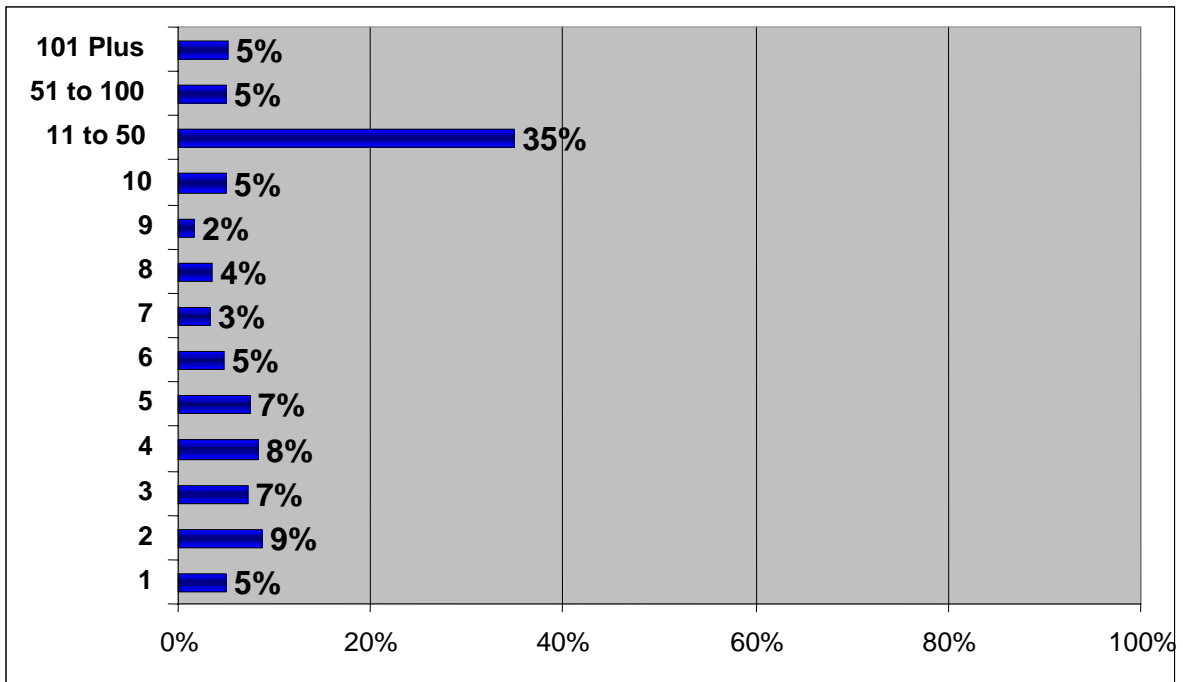


Consistent with the definition of this type of enterprise, over one-third of SMMEs (34.6%) was comprised of up to only 4 full-time employees, while just about a third (32.2%) employed 11 to 50 full time staff members. Furthermore, the majority of the small business enterprises (59.6%) comprised ten or fewer full-time employees, while the minority (less than five percent) employed more than 100 full-time employees. The distribution of number of employees according to sector of operation and provincial locations did not indicate any discernible trends or patterns.



The distribution for the total number of workers employed in the surveyed small business enterprises closely mirrored that established for the full-time employees (see Figure 3.6), with just over half (54.9%) having a total work force of 10 or less and just over 5% having a work force of 101 or more. The total number of workers was consistently distributed across the sectors of operation.

Figure 3-6: Total Number of Workers



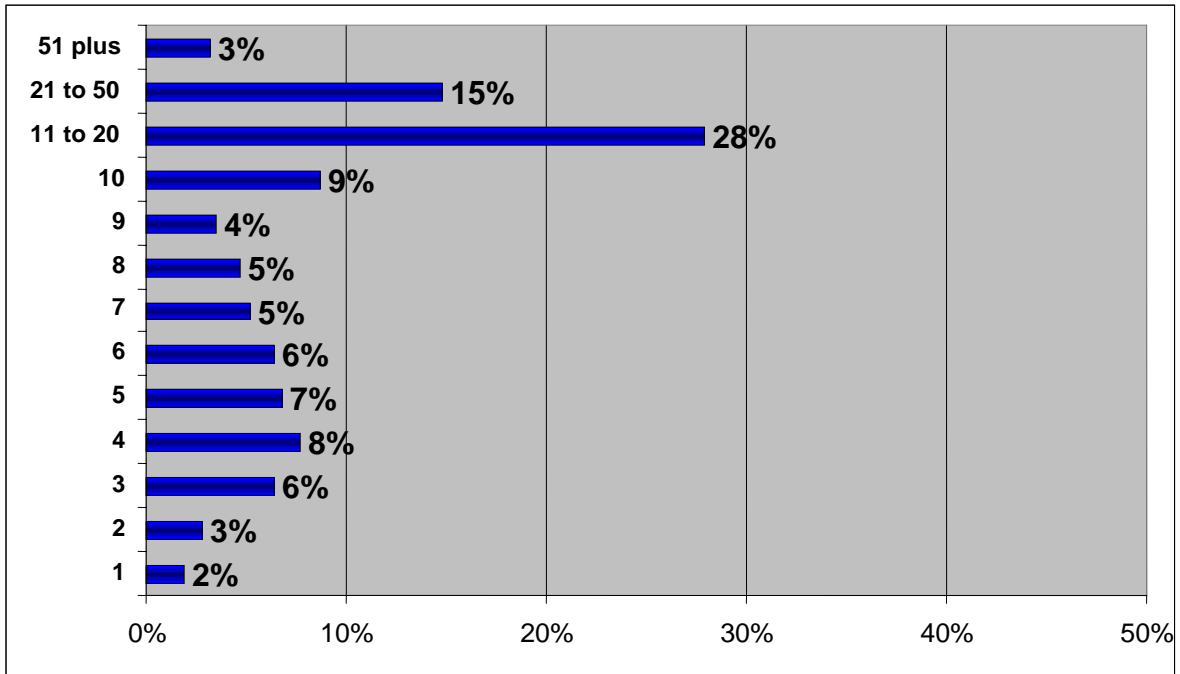
Overall, the distributions for full-time employees and total workforce were generally consistent with the definition of these businesses as SMMEs, with the overwhelming majority in both instances being below the 50 person mark (91.8% and 89.8% respectively).

3.6. LENGTH OF SMME OPERATIONS

More than half (54%) of small business enterprises surveyed had been in operation for ten years or less, while 27% had operated for between 11 and 20 years, and 14.8% for between 21 and 50 years. Less than 5% of the businesses were either two years or younger or older than 51 years. Overall, the average age of the SMMEs was 14.86 years, though given the distribution skew towards the lower end, the median of 10 years would be a more accurate reflection of enterprise age.

In terms of sector of operation, small businesses in manufacturing, personal services and agriculture and forestry were the oldest (median: 10 years). Conversely, SMMEs in the catering and hotel and restaurant sectors were the youngest in the sample (medians: 5 and 6 years respectively).

Figure 3-7: Length of SMME Operations



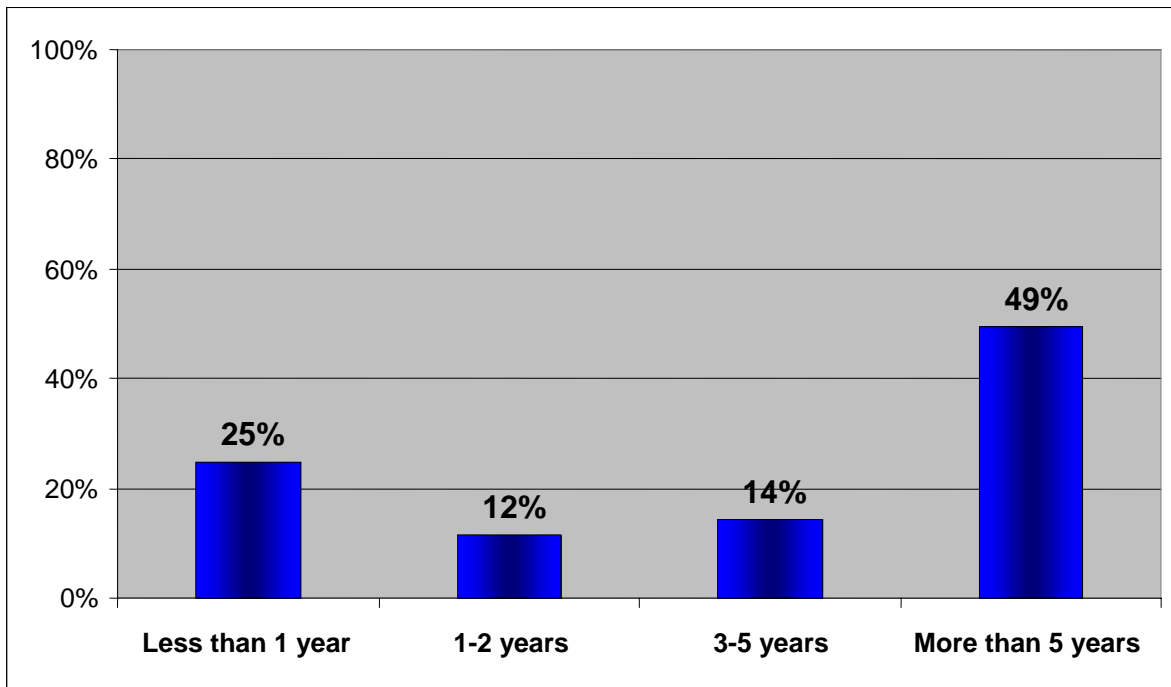
3.7. PERIOD OF OPERATION PRIOR TO TAX REGISTRATION

The survey assessed the length of time that the SMMEs operated before they were formally registered for tax purposes. Tax registration in this context referred specifically to income tax. 12% of the small businesses surveyed reported having operated for some period of time prior to registering for tax. Half of these small business enterprises had been conducting business for more than five years before registering for tax; one quarter operated for between one and five years, and the remaining one quarter registered for tax within the first year of their operation.



Analysis of the time between start of operations and registration for tax across the sectors indicated that SMMEs in the construction, finance, real estate and business services and wholesale and retail sectors were the slowest to register for tax (median: 4 years), while those in transport, storage and communications and personal services were the quickest (median: 1.5 years).

Figure 3-8: Period Operation Prior to Tax Registration



As the survey did not request the length of time taken after commencing business for registration for taxes other than income tax, no breakdown according to type of tax was possible.

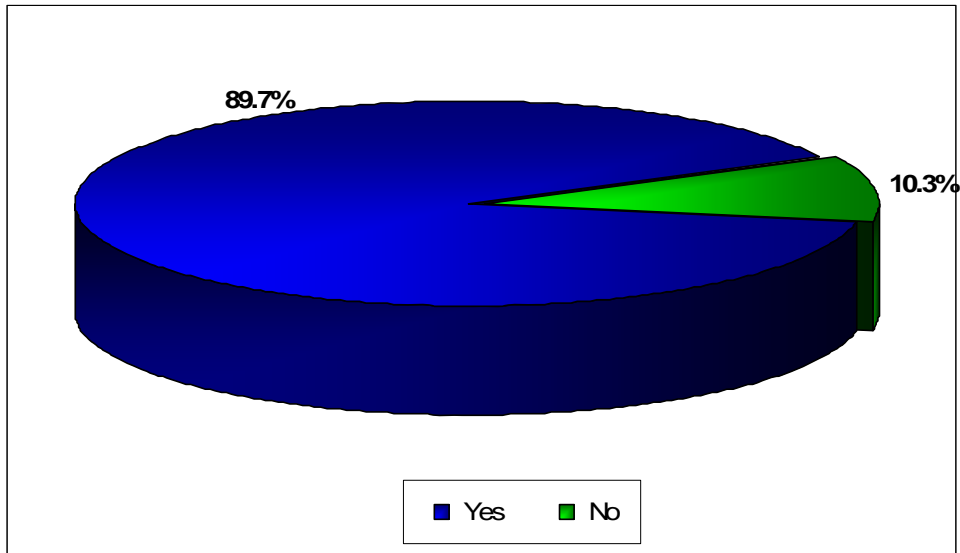
3.8. VAT REGISTRATION

The vast majority of the surveyed SMMEs (90.7%) were registered for VAT purposes (see Figure 3.9 below) . This high rate of VAT registration existed despite the fact that only 77.9% of the SMMEs were required to be registered for VAT based on turnover threshold requirements (R300 000 plus). Hence 12.8% of the sample, or 58% of those not required to register to VAT were in fact VAT registered. The largest proportion of these particular SMMEs was sole proprietor and partnerships.



While the specific reasons for VAT registration were not assessed, it was likely that this was done to secure the benefits of VAT input tax credits, despite the fact that such registration would necessarily require SMMEs to levy output VAT and ensure sufficient record keeping enabling submission of required VAT returns. SMMEs in the manufacturing, personal services,

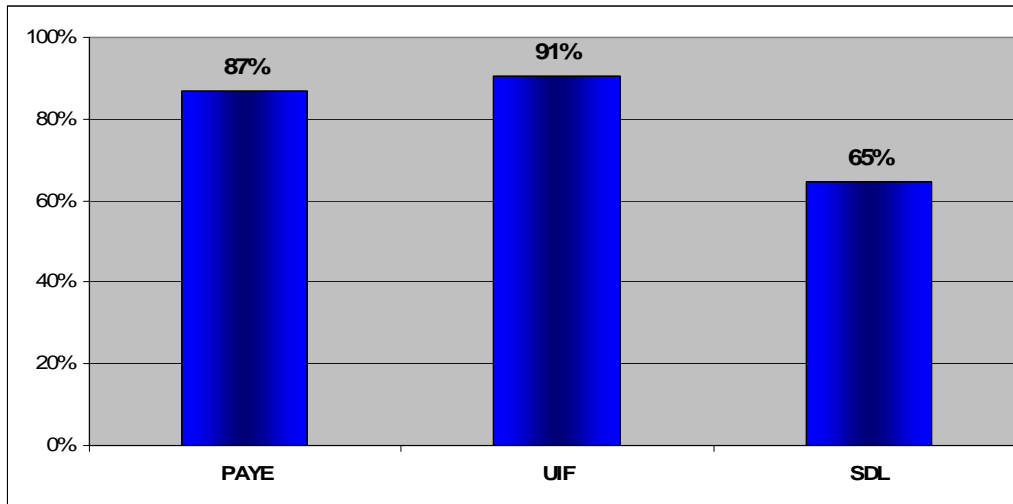
Figure 3-9: VAT Registration



3.9. REGISTRATION FOR OTHER TAXES

The distribution of SMMEs in terms of registration for the other types of tax was indicated in Figure 3-10. The data do not permit an assessment of the extent to which these rates do or do not correspond to the expected rates of registration for each type of tax given relevant enterprise characteristics.

Figure 3-10: Registration for other Taxes



3.10. ADVANTAGES AND DISADVANTAGES OF REGISTRATION FOR INCOME

TAX AND VAT

Small businesses were requested to provide their views on what they considered to be the primary advantages and disadvantages of registration for income tax and VAT. These views were assessed in an open-ended manner, meaning that respondents were free to provide any response that they chose to. Respondents were also asked to rank order the listed advantages and disadvantages of tax registration, to ensure that primary reasons take precedence over secondary and tertiary reasons. Once the responses had been received, they were subject to content analysis to ensure that similar responses were classified into similar categories. All response categories were discrete to ensure proper assignment of obtained responses. The overall responses were then analysed according to these cluster categories.



3.10.1. Advantages of income tax registration

According to respondents, the five primary advantages of income tax registration were, in ranked order, as follows:

1. Improvement of the legal standing of the business – 21% of all respondents believed that the biggest advantage to being registered for income tax was the proper legal standing of the business. The legal standing was deemed important because it facilitated the conducting of normalized business affairs and operations, and eliminated the possibility of legal sanctions in the event of detection and/or inspection by the relevant authorities. There was a slight relationship between the size of the enterprise and the tendency to view the legal standing as the primary advantage of registration, indicating that businesses which were larger tended to have greater profiles in their sector of operation, and were therefore less likely to continue operations without proper registration for any notable period of time. However, very small businesses were also likely to worry about the legal standing of the business, probably because they believed that they were too small to absorb the cost and implications of being found out for their illegal status. There were no noticeable trends to holding this position as a result of sector of operation.
2. Improved access to business opportunities – 12% of respondents believed that being registered for income tax improved their overall business prospects. The primary reasons for believing this were the confidence invested in them by their customers, clients and suppliers as a result of being formally registered (and conversely, the loss of this confidence should they be found out to be unregistered), and the improved access to financing for growth of the business. Respondents were also cognizant of the fact that they could engage with other businesses in their sector with greater confidence.
3. Impact of tax revenues on the country – 8.8% of respondents believed that a key advantage of being tax registered, and thus also tax compliant, was the numerous benefits that accrued to the country as a whole from tax revenue collected by the government. While half of these respondents simply indicated that being registered and paying tax generally improved the country, others provided more specific reasons. For instance, a portion believed that tax revenue was important for improving the lives of poor and disadvantaged people through the provision of better basic services in water, electricity, health and education, while others believed that tax revenue was important for improving social security in the country.



4. Trading with a larger number of businesses – 7.1% of respondents indicated that being tax registered enabled them to trade confidently with a wider circle of businesses, including suppliers, customers and clients. This was undoubtedly related to the fact that registered businesses were more likely to trade with other businesses which were themselves registered, as trading with non-registered businesses also created potential legal problems for registered businesses.
5. The ability to claim relief in the form of tax rebates - 6.4% of respondents indicated that the primary advantage of being tax registered was the ability to claim back some measure of relief in tax rebates. This relief was considered necessary to ensure proper growth and development of the business.

Other noteworthy results included the fact that only 2.5% of small businesses indicated that being tax registered was important for securing government tenders, indicating that this issue was not as much of a priority for these small business enterprises as was previously believed, and that employing the issue to promote tax registration may have limited effect. Finally, it was also noteworthy that at least one-tenth of all surveyed businesses believed that there were no advantages to being registered for income tax. This view prevailed despite the fact that all of them were already registered, indicating that many of them saw income tax registration as a “necessary evil” to be achieved merely to avoid negatively affecting the legal standing of the business.

Overall, it was apparent that the assessment of advantages of tax registration was largely, and understandably, localised around business concerns, with just under half of all businesses (46.5%) providing a response in this cluster, with only under one-tenth indicating benefits to the wider community and society. In this regard, it was useful to note that campaigns to ensure better rates of compliance would probably be better served by focusing on direct benefits to the business rather than indirect benefits to society and the country.



3.10.2. Disadvantages of income tax registration

The five primary disadvantages of being registered for income tax were indicated as follows:

1. High rates of taxation – 18.4% of respondents indicated that the rate at which small businesses was currently taxed was too high, and that this rate had many adverse consequences for the enterprises. Principal amongst these were the reduced levels of re-investment in the business, and the difficulties created for cash-flow by having to meet the required tax assessment.
2. The negative impact on profit-making – in addition to the assessment that the current tax rates were high and therefore removed money that the business would otherwise have considered using for re-investment, 10.8% of respondents believed that being registered and therefore paying tax impacted negatively as they were not able to ensure profit-taking. This diminished profit-taking in turn implied that people were less likely to either expand the business and/or start or grow other businesses.
3. The high cost of tax compliance – 13% of respondents believed that tax registration was onerous because of the costs associated with tax compliance and all the compliance-associated tasks and activities. Principal factors associated with this cost were the costs of contracting tax practitioners to complete and submit the necessary tax returns, and the costs of general recordkeeping and accounting throughout the year.
4. The time and effort required to complete and submit tax returns - 9.9% of respondents indicated that the requirements for tax compliance in terms of the labour and time of staff were high, and that this resulted in the business being adversely affected as staff were otherwise engaged in tax compliance matters.
5. No control over how government spent tax revenue – finally, 4.7% of respondents believed that being registered was not advantageous to them because they could exercise no control over how the collected revenue was spent by government. However, as taxpayers globally did not have direct control over revenue spent, respondents appeared resigned to this fact, though they were clearly dissatisfied with the lack of control.

Overall, then, as with the listed advantages of being tax registered, respondents were clearly inclined to view the disadvantages of tax registration primarily from the perspective of the general financial health and growth prospects of the business. Importantly, the costs associated with tax compliance tasks and activities also featured prominently in listed disadvantages.



However, and reassuringly, almost one fifth (19.3%) of all respondents indicated that there were no real disadvantages to being tax registered, and this view was held regardless of entity type, sector of operation or turnover size of the enterprise.

3.10.3. Advantages of being VAT registered

The primary advantages to being VAT registered were identified as follows:

1. Being able to obtain the benefit of input tax credits/VAT refunds - three-fifths (61.2%) of all small business enterprises believed that there were distinct benefits to being VAT registered, and foremost amongst these was the ability to benefit from input tax credits and VAT refunds. This was cited as having a salutary impact on the fiscal health of the business, particularly in terms of monthly cash flow. It was thus very apparent that obtaining input tax credits was a critical part of the financial strategies of these small businesses.
2. Being able to trade with a larger number of businesses – just under one tenth of SMMEs (8.4%) believed that being registered for VAT was essential in ensuring a wider circle of trading partners for the enterprise, both in terms of suppliers, customers and clients. This was undoubtedly a consequence of the established business practice of requiring suppliers/customers or clients to provide details of their VAT registration when preparing quotation, statements and invoices.
3. Improved prospects for business growth and expansion - 7.7% of the small businesses indicated that being VAT registered directly improved the overall prospects of the business.
4. The legal standing of the business – finally, just under five percent (4.5%) of respondents indicated that the single greatest advantage was the legal standing of the business, which arguably would then in turn impact upon business operations and business growth prospects.

Overall, small businesses were quite consolidated in the view that being VAT registered was advantageous because it enabled the business to capitalise on the input tax credits through VAT refunds. This undoubtedly had a positive impact on cash flow and monies available for business growth and expansion.

Finally, it bore noting that a minority (7.7%) of surveyed SMMEs believed that there were no advantages to being VAT registered. Only 40% of this latter category was not currently registered for VAT, meaning that the majority who held this view was currently VAT registered.

3.10.4. Disadvantages of being VAT registered

The primary disadvantages of being VAT registered were identified as follows:

1. A higher financial burden in terms of levying output tax and submission of returns - just under one-fifth (18.8%) of respondents indicated that the primary disadvantage was the financial costs associated with ensuring that VAT requirements were met in business transactions and that VAT returns were duly completed and filed.
2. The time needed to complete returns – in addition to the financial costs associated with VAT, the time taken to complete the regular VAT returns was cited as a major disadvantage by 15% of the respondents.
3. Potential for SARS prosecution/increased risk of audits – just under one-tenth, cumulatively 8.9% of small businesses, believed that being VAT registered was disadvantageous because it increased the prospect of being audited or inspected by SARS. Respondents did not venture specific reasons why they believed this, except to state that being VAT registered meant that SARS was always monitoring them through their VAT returns.

In summary, small businesses, while they saw distinct advantages to being VAT registered, were also clearly concerned about the costs to the business for ensuring proper compliance with the VAT regimen.

Finally, around 30% of all those SMMEs who were at the time registered for VAT indicated that there were no disadvantages to such registration. This group correlated strongly with those SMMEs who saw no disadvantages to be registered for Income Tax, indicating an overall more positive approach by these small businesses towards tax compliance.



3.11. CONCLUSION

Overall, the profile characteristics for the sample of formal SMMEs correspond in large part to that observed in other similar studies. Importantly, the data confirm that the distribution of surveyed formal SMMEs was generally consistent with that indicated by the SARS tax registry, particularly for type of enterprise, sector of operation and provincial location. The concordance on these three key stratification variables provided sufficient confidence in the data and therefore the results and conclusions obtained from the analysis. Having provided sufficient vetting of the sample, we now turned to the primary analysis and conclusions.

CHAPTER FOUR: TAX AND COMPLIANCE-RELATED TASKS

Turning to tax compliance and compliance-related tasks, the survey sought to establish the range and nature of tax compliance tasks that were undertaken by the small businesses, as well as the extent to which these tasks were divided between the SMME and external consultants such as accountants, bookkeepers and tax practitioners. We began by firstly examining recordkeeping in the small business enterprises.

4.1. GENERAL RECORDKEEPING

The returned results indicated that the vast majority of the SMMEs viewed recordkeeping as being a critical component of their business operations, and one that held significant value for the business if properly addressed, resourced and undertaken. Consequently, the majority of surveyed small businesses indicated that recordkeeping was a high priority for them and essential for the continued success and future growth of the business.

The prioritization of this task was clearly evident in the high rates of document management and electronic capture thereof and of other essential information. The overwhelming majority of the SMMEs (97.4%) achieved the minimum basis for recordkeeping by ensuring that they retained all physical documentation related to sales and purchases in an organised manner. A slightly smaller percentage (96.6%) further ensured that they practised some measure of physical bookkeeping to ensure that income and expenses were formally recorded. Finally, three quarters (75.3%) went one step further by transcribing income and expenses into an electronic format using a specialised accounting software package, although they did not necessarily do these themselves.

Unsurprisingly, the extent of recordkeeping, either in physical or electronic form, increased in accordance with the size of the small business as measured in terms of its turnover. SMMEs with higher turnovers, particularly in the R6 million plus categories, tended to undertake all three forms of recordkeeping with equal diligence, whereas SMMEs with turnover less than R300 000 were more likely to retain physical documentation related the sales and purchases than they were to transcribe such records into electronic format. Hence greater efficiencies in record keeping were as a consequence of better resources internally, or greater access to external resources as a result of having more funds available for this purpose.



These observed high rates of formal record keeping were to be expected given that all of these businesses were tax registered and hence regularly submitted the relevant returns on different taxes. This level of compliance would not be possible without a commensurate level of record keeping. Moreover, it was reassuring to note that the great majority of the small businesses were at the time utilising the appropriate means for electronic documentation, which undoubtedly facilitated provision of relevant information to tax practitioners for filing purposes and ensured that records, provided they were sufficiently backed up, were not easily susceptible to loss.

Furthermore, regardless of the level of recordkeeping achieved, it was instructive to note that the majority of the small businesses (91%) were of the opinion that such record keeping was not at all problematic, further confirming that these were already established and regular routines in the business operations. Once again, turnover played a key role in determining the extent to which such activities were problematic, with businesses with higher turnover perceiving it to be less problematic than those with smaller turnovers.

Finally, in terms of establishing who was responsible for the recordkeeping, the study indicated that about three-quarters of the small businesses (73%) regarded recordkeeping as the responsibility of the enterprise, and consequently, they elected to complete these tasks in-house. The designated person was generally the owner and/or a senior employee. About 15% of the SMMEs completely outsourced these tasks, while the remaining 12% achieved the tasks through a combination of in-house and outsourced assignments. The rate of outsourcing for general record keeping was disproportionately higher for close corporation enterprises (64%) than it was for proprietary limited businesses (12%).

Interestingly, the rate of outsourcing was highest in the smallest turnover band, decreasing as one moved up the turnover bands until the R14 million marks, at which point it started to increase again. The high rates of outsourcing at the lower end may be explained as a consequence of the lack of in-house expertise as outsourcing decreased as turnover, and hence more resident capacity, increased. The increase beyond turnover of R14 million was probably due to the complexity of operations at that annual sales figure.



Detailed tables showing outsource proportions by legal form and turnover follows here.

Table 4-1: Proportion - Business Legal Form, Outsourcing (Row percentages)

	Sole proprietorship	Partnership	Company (PTY LTD)	Close Corporation	Other	Total
Outsource	19.2%	3.3%	12.6%	64.9%		100%
Both Business Employee (Self), & Outsourced	14.3%	4.2%	22.7%	58.0%	0.8%	100%
Total	17.0%	3.7%	17.0%	61.9%	0.4%	100%

Table 4-2: Proportion - Business Legal Form, Outsourcing (Column percentages)

	Sole proprietorship	Partnership	Company (PTY LTD)	Close Corporation	Other	Total
Outsource	63.0%	50.0%	41.3%	58.7%		55.9%
Both Business Employee (Self), & Outsourced	37.0%	50.0%	58.7%	41.3%	100.0%	44.1%
Total	100%	100%	100%	100%	100%	100%

Table 4-3: Proportion - Business Turnover, Outsourcing (Row percentages)

	Outsource	Both Business Employee (Self), & Outsourced	Total
Less than R70 000	53.8%	46.2%	100%
R70 000 to R300 000	67.3%	32.7%	100%
R300 001 to R1 000 000	51.6%	48.4%	100%
R1 000 001 to R6 000 000	59.7%	40.3%	100%
R6 000 001 to R14 000 000	31.0%	69.0%	100%
Over R14 million	52.4%	47.6%	100%
Don't know/Unsure/Refusal	66.7%	33.3%	100%
Total	55.8%	44.2%	100%

Table 4-4: Proportion - Business Turnover, Outsourcing (Column percentages)

	Outsource	Both Business Employee (Self), & Outsource	Total
Less than R70 000	4.7%	5.0%	4.8%
R70 000 to R300 000	24.7%	15.1%	20.4%
R300 001 to R1 000 000	21.3%	25.2%	23.0%
R1 000 001 to R6 000 000	30.7%	26.1%	28.6%
R6 000 001 to R14 000 000	6.0%	16.8%	10.8%
Over R14 million	7.3%	8.4%	7.8%
Don't know/Unsure/Refusal	5.3%	3.4%	4.5%
Total	100%	100%	100%

4.2. DIRECT TAX AND TAX-COMPLIANCE TASKS

Moving beyond general record keeping, it became apparent that small businesses increased their reliance on external consultants as the tasks and activities more closely approximated those required for tax compliance purposes, particularly completing of submissions and filing.

Looking at the compilation of documentation for income tax, one third of SMMEs relied exclusively on outsourcing to ensure that the relevant documentation was compiled for tax submission, while a further 11% did so jointly with the external agency. The remaining 56% completed these tasks in-house, either through the owner (45%) or a senior employee (11%). In terms of entity type, 64% of close corporation enterprises outsourced completion of tax documentation as compared to 16% of proprietary limited businesses.

Looking at the compilation of company annual financial statements, we found that the rates of outsourcing for the compilation of annual company financial statements were roughly equivalent to that for compilation of necessary documentation for tax purposes, with 34% of small businesses completely outsourcing this task and a further 12% doing so jointly. In the remainder of small businesses these statements were compiled either by the owner (42%), or an employee (12%). The rate of outsourcing for compilation of annual financial statements was 66% and 17% for close corporation enterprises and proprietary limited businesses respectively.



Overall, it was very apparent that fewer of the close corporations, being small operations with small staff components, had the requisite expertise for these tasks, while the proprietary limited businesses were generally larger and thus had better in-house capacity. The rate of outsourcing in sole proprietor and partnership businesses was roughly equivalent to the incidence of these types of enterprises.



4.3. TAX FILING AND REFUNDS

We now examined the rates of outsourcing of tasks related specifically to the filing of different taxes.

4.3.1. Company Tax

Just over one third of small businesses (34%) relied entirely on external expertise to file the relevant business tax returns, while just over one-tenth (11%) used both in-house and outsourced expertise, and 46% completed the returns entirely in-house. Once again, close corporations were disproportionately more dependent on outsourcing (65%) than were proprietary limited businesses (17%).

4.3.2. Provisional/Personal tax

Provisional/personal tax applicable to sole proprietors and partnerships collectively constituted 24% of the total sample. Of this type of enterprise, 42% relied on outsourcing either completely or partially to file the relevant returns, while the remaining 58% accomplished this in-house.

The overwhelming majority of in-house cases (80%) were undertaken by the owners themselves.

4.3.3. VAT

Of the small businesses that were registered for VAT, around one fifth completely outsourced the compiling of relevant VAT information and documentation (19%), while 11% employed a combination of in-house and outsourced expertise. Furthermore, in terms of the actual filing, 20% outsourced the filing of the returns, while 12% employed a combination of in-house and outsourced expertise. In the remainder of cases both tasks were achieved entirely in-house. Once again, close corporations were much more dependent on external expertise for accomplishment of these tasks than were proprietary limited businesses.



4.3.4. PAYE

The rates of outsourcing for PAYE were roughly equivalent to that found for VAT, both in terms of compilation of the necessary documentation and the filing of the returns, indicating that enterprises were likely to cluster both taxes together when considering how best to accomplish the tasks associated with each of them. The rate of dependency by close corporations on outsourcing for PAYE tasks was similar to that found for VAT, and likewise for proprietary limited businesses.

4.3.5. Obtaining Refunds

Although over a third of small businesses (34%) employed external expertise exclusively to formulate and submit tax returns; a smaller proportion relied exclusively on this external expertise to obtain the required refunds (28%). This was undoubtedly due to the fact that the refunds were not determined by the tax practitioners but by SARS, hence while practitioners were involved in compiling and submitting the returns, a lesser input was required from them when refunds were issued by SARS as refunds were made directly to the businesses themselves.

However, small businesses certainly depended greatly on tax practitioners to ensure that returns were completed in a manner that ensured the best possible refund, hence such practitioners were generally reported to be important in securing such refunds.

4.3.6. Engagement with SARS

31% of small businesses relied exclusively on external expertise to represent the enterprise during appeals to SARS, while a further 11% did so jointly. The rate of outsourcing for representing the enterprise in audits/inspections was 29% solely, and 12% jointly. Small businesses were slightly more dependent on external expertise when it came to the lodging of appeals with SARS, with 34% exclusively using external expertise while 13% did so using in-house and external expertise. Finally, a similar proportion of businesses used external expertise to petition SARS for the waiving of penalties and/or interest (31%).

Consistent with the trend observed for other tax tasks, close corporations were greater users of outsourcing than were proprietary limited businesses, while rates of outsourcing in sole proprietor and partnership enterprises were consistent with the incidence of such businesses in the sample.



4.4. CONCLUSION

In summary, then, certain key findings were evident with regard to the allocation and completion of tax and compliance related tasks:

1. The majority of small businesses relied on in-house expertise to complete general record keeping and bookkeeping, preferring to outsource primarily when the required tasks gravitated towards tax and specialised tax tasks.
2. About one third (34%) of small businesses were entirely dependent on external expertise to complete all relevant tax tasks,
3. Around 10% of small businesses employed a combination of in-house and external expertise to accomplish required tasks,



4. The principal reason for not outsourcing was the availability of appropriate expertise within the enterprise, with this being particularly true for proprietary limited enterprises. Sole proprietors and partnerships did not outsource as extensively as the other two types of business because they reported being unable to afford such outsourcing.
5. The primary reason for outsourcing was the highly specialised nature of the tax field. Close corporations were the most likely to outsource for this reason, while sole proprietors and partnerships were likely to do so because of the difficulty in keeping abreast of changes in tax law and rules.
6. Less than one tenth of all businesses outsourced because of the expertise of their current tax practitioner.
7. In general, reliance on outsourcing increased as the level of engagement with SARS increased,
8. The vast majority of businesses clustered different taxes together, with decisions to outsource being applied on a cluster basis for relevant taxes rather than differentiated in terms of individual taxes. Hence businesses did not generally always divide different tax tasks between themselves and outsourced agencies.
9. Sole proprietors and partnerships generally accomplished many of the tasks themselves, with only around 15% relying on outsourcing for most administratively related compliance tasks. However, when it came to interacting with SARS, particularly in terms of the lodging of appeals, obtaining of refunds and so forth, this proportion doubled to around 31%.
10. Just over two-fifths of close corporations (43%) relied exclusively on outsourcing for accomplishing the general administrative tax-related tasks, with a similar proportion doing so when there was the need for direct interaction and engagement with SARS for appeals, refunds and so forth.
11. Proprietary limited businesses were the least dependent on full outsourcing, with around 20% of them undertaking complete and exclusive outsourcing of the necessary tax tasks, and an equivalent proportion relying exclusively on outsourcing to ensure the lodging of appeals and petitions for refunds and waiving of penalties.
12. Looking at all the different types of businesses, it was clear that close corporation enterprises were the most dependent on the outsourcing of most tax and compliance tasks such as compiling financial statements and filing tax returns as well as for engagement with SARS.
13. In the case of proprietary limited businesses, the level of outsourcing was much lower because of the availability of in-house expertise, despite the greater compliance requirement when compared to close corporations. It was apparent that such businesses actively limited the extent



of outsourcing, achieving as much as possible internally and thereby allocating only the more critical tasks to external agencies.



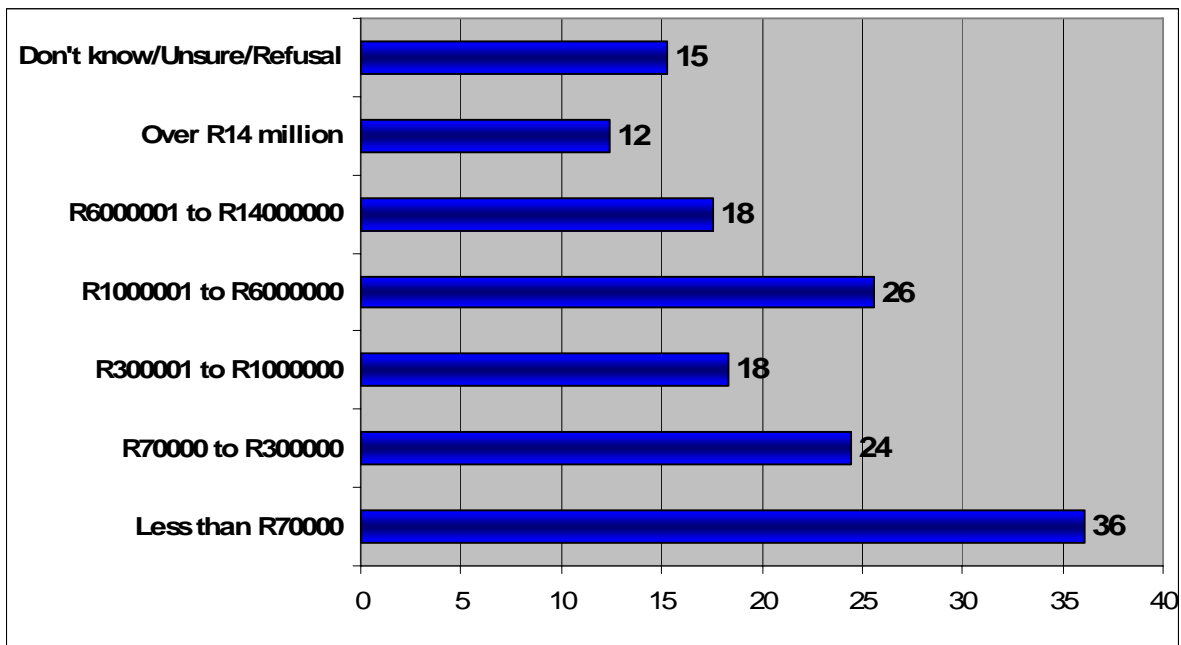
CHAPTER FIVE: NATURE AND EXTENT OF INTERNAL COSTS OF COMPLIANCE

The survey attempted to assess the costs associated with in-house completion of tax and tax compliance tasks and activities. However, while respondents were able to report on the costs to the small business in terms of the time taken by employees or the owner to achieve these, they were not able to attach a monetary value to these efforts. Hence we could only assess the costs in terms of time required to achieve the various activities and tasks.

5.1. TIME TAKEN FOR INCOME TAX

The Figure 5-1 below summarises the time taken to complete all tasks related to recordkeeping for and submission of Income Tax. The time taken covered the time spent by all employees per annum. The annual quantum was calculated by assessing the time taken per cycle/submission and then multiplying it by the number of submissions/cycles per annum. In the case of Income Tax this constituted one cycle/submission per annum.

Figure 5-1: Time Taken in Hours for Income Tax



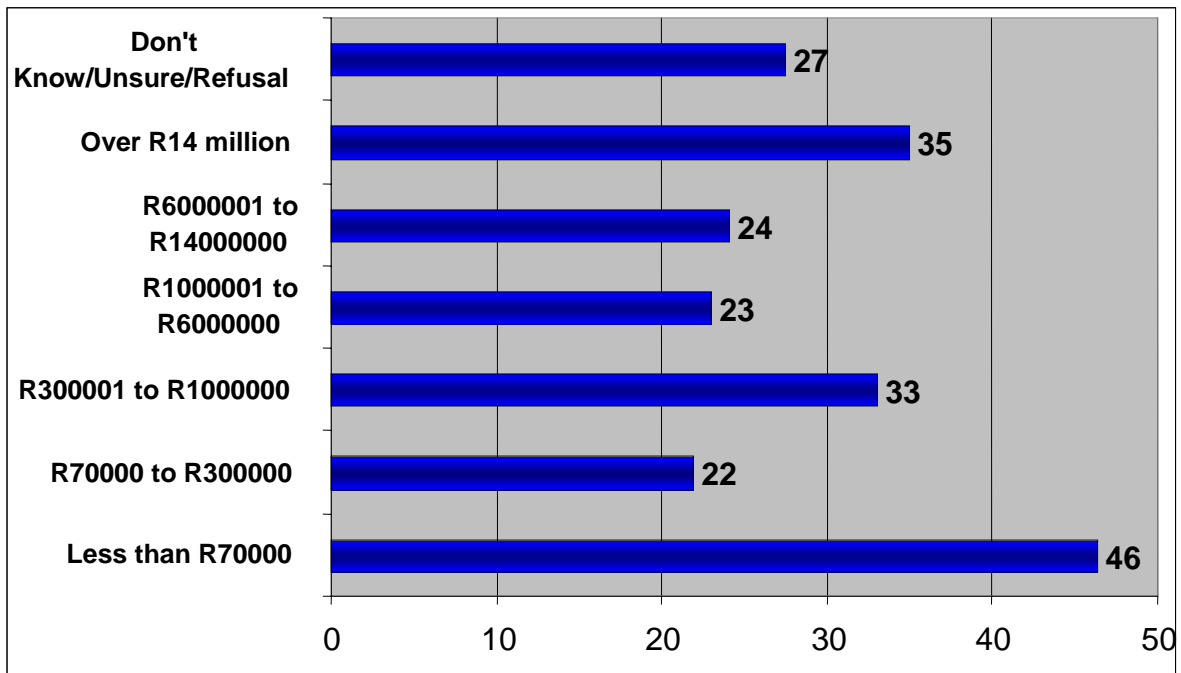


Unlike the findings of the tax practitioner study, the results here did not indicate an increase in time taken to prepare, complete and submit tax returns as a function of increasing income. Rather, the lowest category of turnover recorded the highest quantum of effort for such tasks. This was consistent with what had been found earlier in this study in respect of the very low rates of outsourcing of tax tasks by businesses in this category, meaning that most of these tasks were accomplished in-house due to the unaffordability of outsourcing. This, coupled, with the presumably lower rates of expertise and capacity in such enterprises, would explain the significantly higher amount of time taken to perform the necessary activities in respect of Income Tax.

5.2. TIME TAKEN FOR PROVISIONAL TAX

The time taken for provisional tax was assessed in the same manner as for Income Tax. That is, the annual quantum was calculated by assessing the time taken per cycle/submission and then multiplying it by the number of submissions/cycles per annum. For provisional tax, the number of cycles/submissions per annum was set at two, as per the tax practitioner study, and only businesses registered for this tax were included in the analysis. The time taken for provisional tax by businesses with different annual sales/turnover was indicated in the Figure 5-2 below.

Figure 5-2: Time Taken in Hours for Provisional Tax



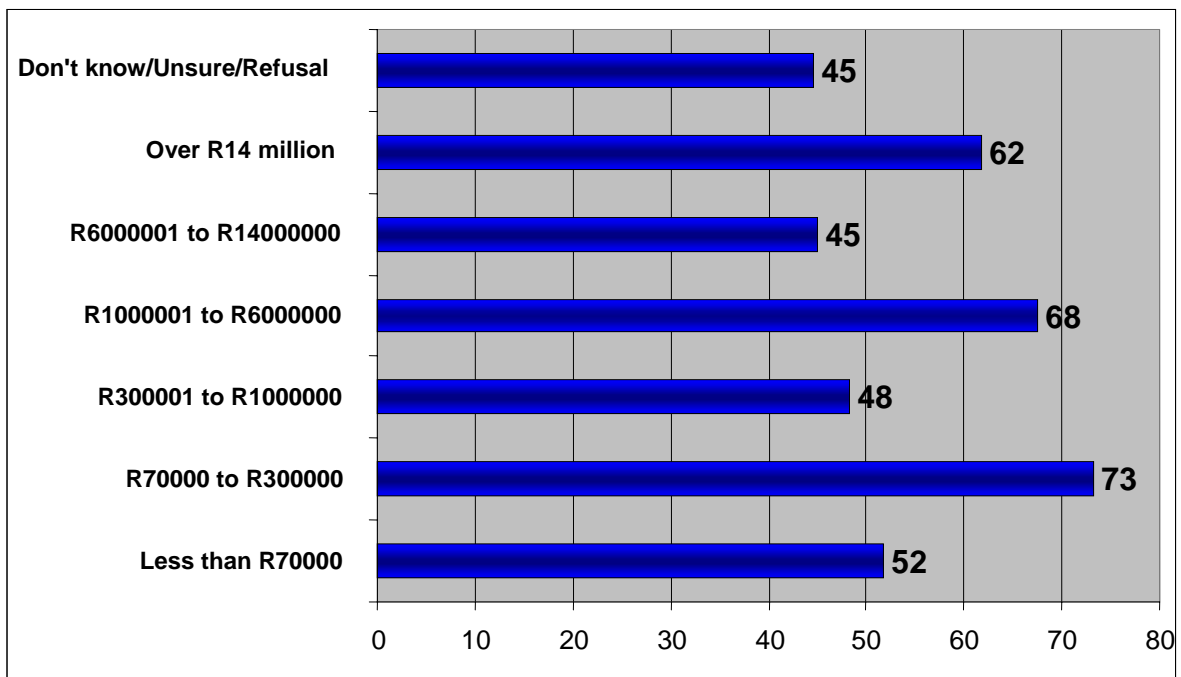


Once again, it was evident that businesses in the lowest turnover category spent significantly more time accomplishing tasks for the completion and submission of provisional tax returns, mainly as a result of a lower rate of outsourcing than enterprises in other turnover categories as well as lower rates of resident expertise.

5.3. TIME TAKEN FOR VAT

The total number of hours used to accomplish all tasks related to the completion and submission of VAT returns was computed from the number of hours per individual submission/cycle multiplied by the relevant number of submissions for the enterprise per year. The Figure 5-3 below indicates the average time taken in hours, and accounts only for businesses which were registered for VAT.

Figure 5-3: Time Taken in Hours for VAT



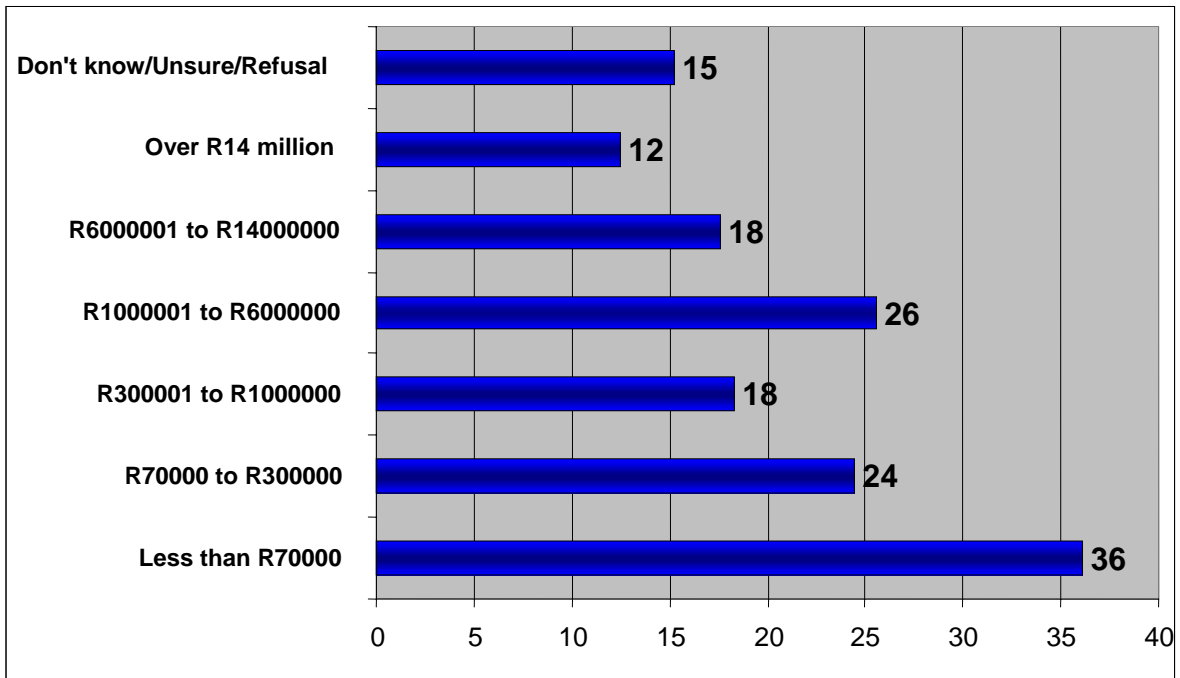
5.4. TIME TAKEN FOR ALL EMPLOYEES TAX

The small businesses were asked to indicate the time taken to complete all tasks necessary for the filing of PAYE, UIF and SDL. Once again, only businesses registered for these taxes were accounted



for, and the average time taken in hours, per annum, to complete and submit all returns for these taxes was reflected in the Figure 5-4 below.

Figure 5-4: Time Taken in Hours for PAYE, UIF, SDL

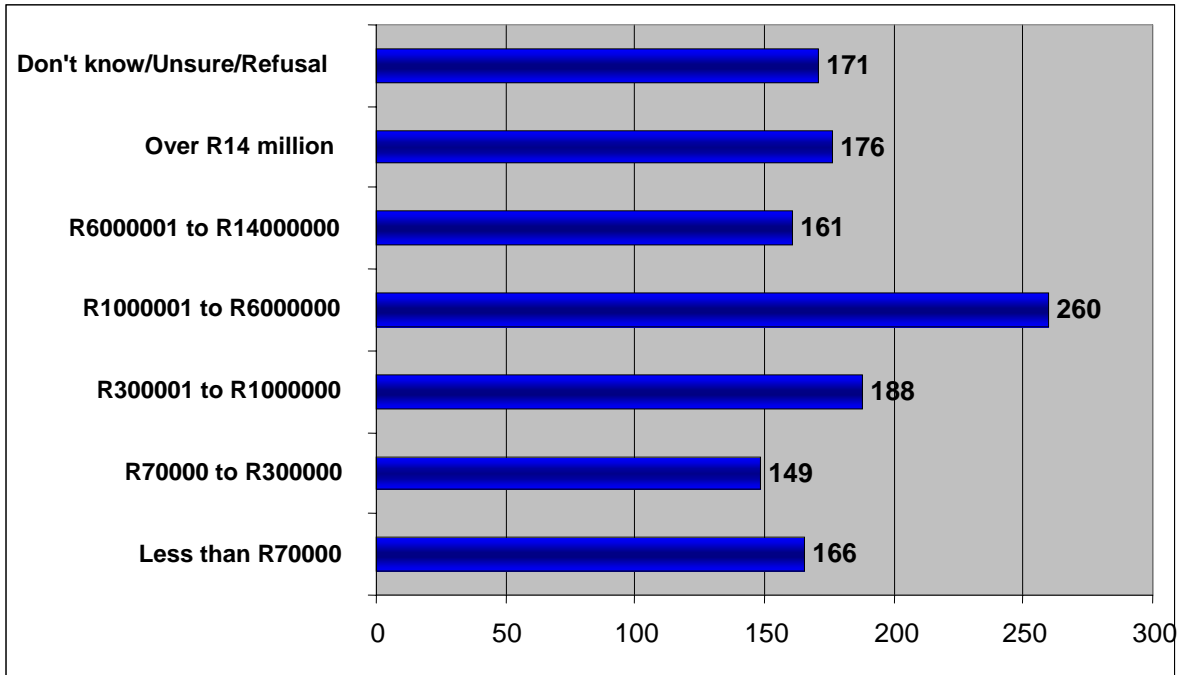


In general, as found in the tax practitioners study, more time was needed for the completing and filing of these tax returns as a function of the increased size and complexity of the business. That study also found that beyond the R1 million-R6 million turnover categories, time and costs tended to drop. The trend was observed in this study as well, though it was not immediately clear why this was so. The drop in time/cost of firms with higher turnover might be explained by their greater likelihood to make use of accounting/tax software.

5.5. TOTAL TIME TAKEN PER ANNUM FOR ALL TAXES

Finally, it was useful to examine the total time taken for businesses to submit all relevant taxes for which they were registered. This was done by summing the time taken for all relevant taxes per enterprise, and the average time taken to prepare, complete and submit all relevant tax returns as is reflected in the graph below.

Figure 5-5: Total Time Taken in Hours for all Taxes



There were very few benchmarks against which these results could be compared. The one that did exist was the Doing Business 2007 study, which estimated the total time taken to be around 350 hours per annum, which was much higher than the average times found in this study. However, there were critical differences between the two studies that must be accounted for:

- The Doing Business Study provided the benchmark of 350 hours for what was ostensibly a large company in the context of South Africa, and hence was not readily applicable to enterprises of the size surveyed in this study.
- The benchmark provided in that study included all time taken on tax and tax-related matters, including time spent in consultations with SARS, and so forth. The time provided in this analysis only accounted for the tasks directly related to compilation of information and filing.



5.6. CONCLUSION

Overall, the following may be observed about the cost to enterprise in terms of the time required to prepare, complete and submit tax returns:

1. Income tax and provisional tax placed the lowest and second-lowest burdens respectively on enterprises in terms of the time requirement for their completion and filing.
2. The highest requirement was for employees taxes (PAYE, UIF and SDL), which accounted for almost half of all time spent per annum on relevant taxes.
3. VAT was the individual tax with the highest demand on time, consuming roughly one third of all the time taken per annum on all taxes.
4. Enterprises in the lowest turnover category (less than R70 000 per annum) spent a disproportionately greater amount of time to accomplish all the required activities for filing of returns for taxes for which they were registered. This corresponded to their low rates of outsourcing observed earlier, meaning that the burden of these tasks inevitably fell to resident capacity. Furthermore, given the small size of these enterprises, it was likely that resident capacity was fairly low, thereby further increasing the amount of time needed to accomplish the required tasks.
5. The total cost to enterprise in terms of time taken for individual taxes as well as all taxes summatively indicated an increase until the turnover category R1million to R6 million, after which the time taken tapered off. A similar effect was observed in the tax practitioner study, with a tapering off after the R6 million turnover threshold, though the decrease was much slighter than that observed in this study. The data from this study did not allow for a proper examination of the reasons for this, and it remains an issue for future examination.



CHAPTER SIX: ROLE AND COSTS OF TAX PRACTITIONERS

Chapter five highlighted the dependency on small businesses on external consultants, noting that this reliance increased as a near linear function of the increased relevance of the task to tax and tax-compliance activities. In this chapter, we examine the role of the external consultant in the life of these small businesses, and assess the cost of these consultants to the businesses.

6.1. PROFILE OF THE TAX PRACTITIONER/EXTERNAL CONSULTANT

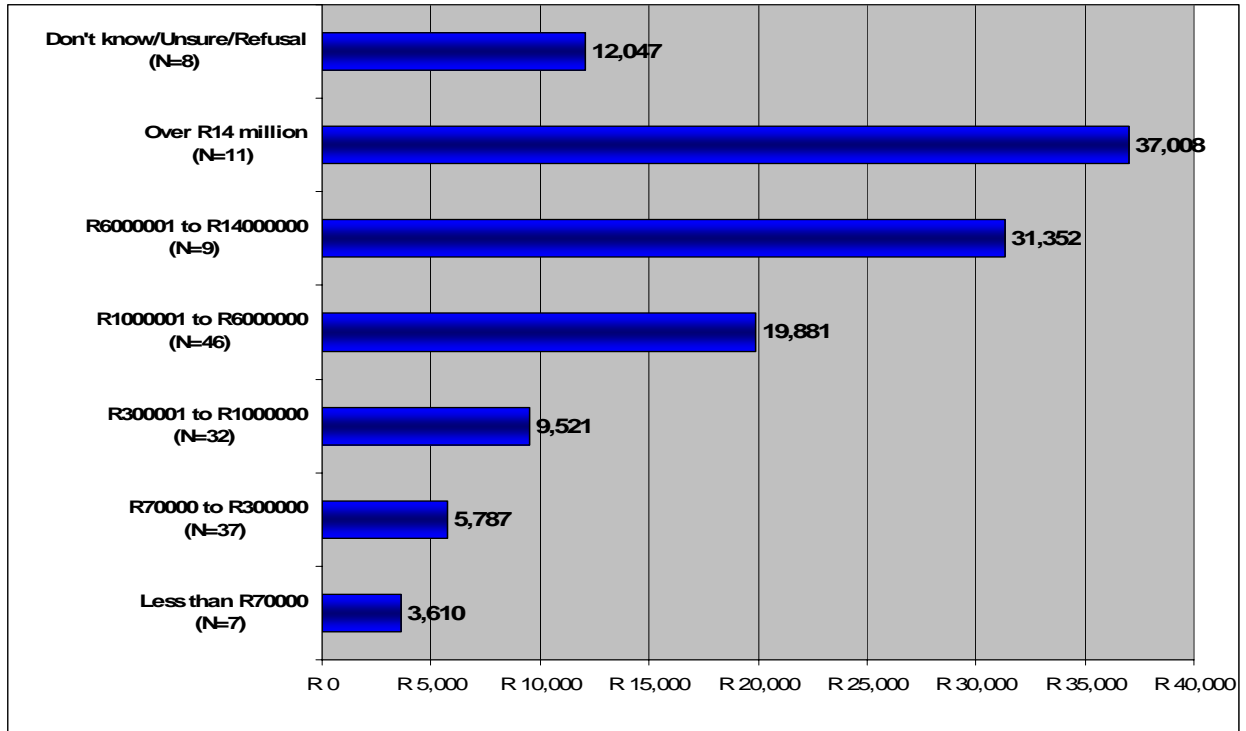
Looking specifically at those small businesses which did outsource their record-keeping and tax-related tasks, the data revealed that that the majority of SMMEs (58%) outsourced to independent certified accountants, 26% outsourced to independent certified bookkeepers, 8% outsourced to independent certified tax consultants, and the remaining 8% outsourced to a range of certified and non-certified bookkeepers, accountants and tax consultants who were either independent or related to them through friendship or family.

Importantly, half of the lattermost category was certified, implying that 96% of all businesses were outsourcing to a practitioner who was certified (regardless of whether or not the practitioner was completely independent or associated to the SMME in some manner). This indicated that SMMEs were fully cognizant of the importance of certification and, hence, the need to engage the services of such certified individuals.

6.2. COSTS ASSOCIATED WITH TAX PRACTITIONERS/EXTERNAL CONSULTANTS

Only slightly more than half (53%) of those businesses which did outsource record-keeping and tax tasks were able to report on the costs associated with such outsourced tasks. The distribution of the outsourced costs across turnover bracket is indicated in Figure 6-1 below.

Figure 6-1: Costs Associated with Tax Practitioners/ External Consultants



As can be seen in the Figure 6-1, while actual costs were generally progressive, the proportionate costs of outsourcing were regressive, with enterprises with smaller turnovers spending disproportionately more than those with higher annual sales/turnover. The caveat here was that this cost did not reflect the total cost to an enterprise for ensuring completion of tax and compliance tasks, which would be undoubtedly higher for proprietary limited businesses because of their propensity to rely more on in-house expertise than outsourcing.

The figures below indicate the costs associated with outsourcing for the different enterprise types.

Figure 6-2: Sole Proprietors and Partnerships

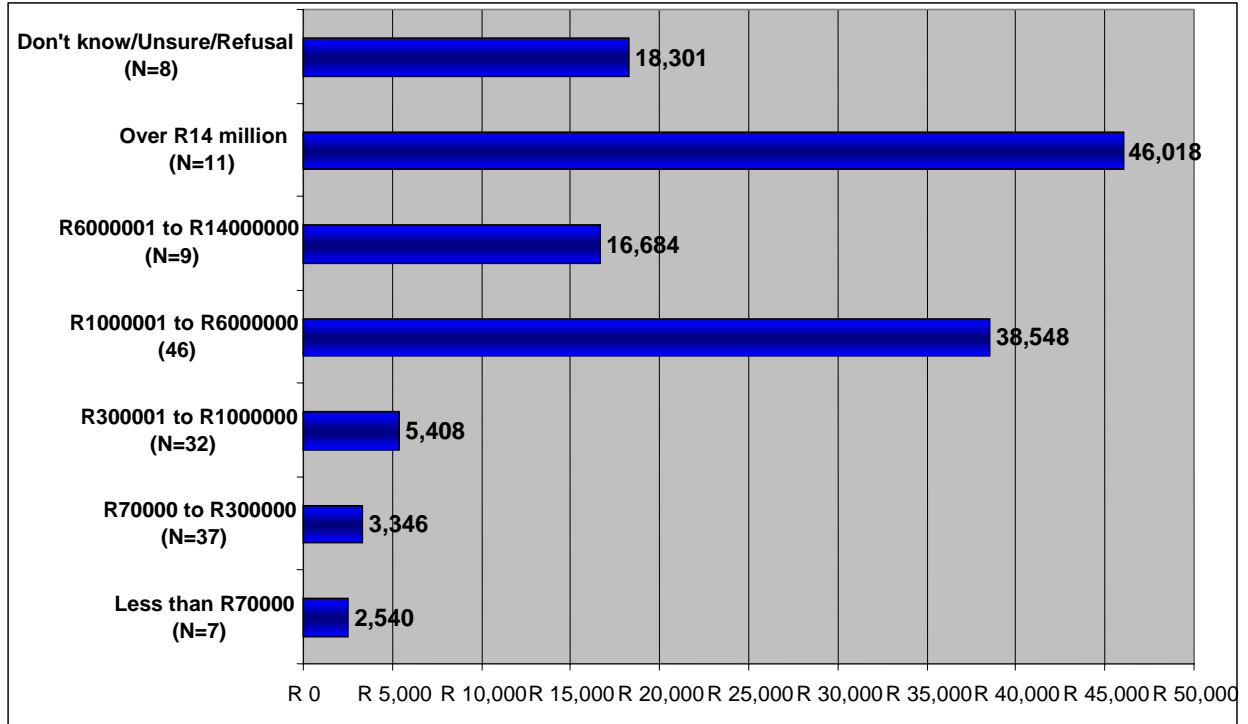




Figure 6-3: Close Corporations

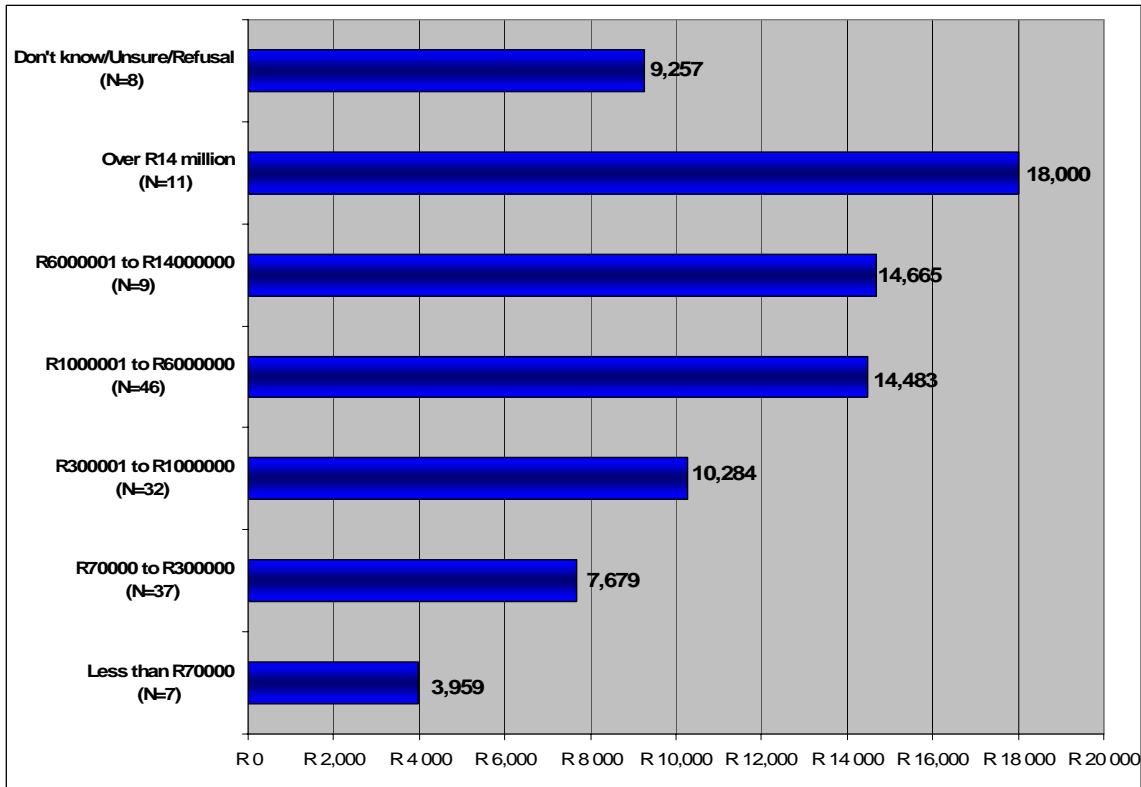
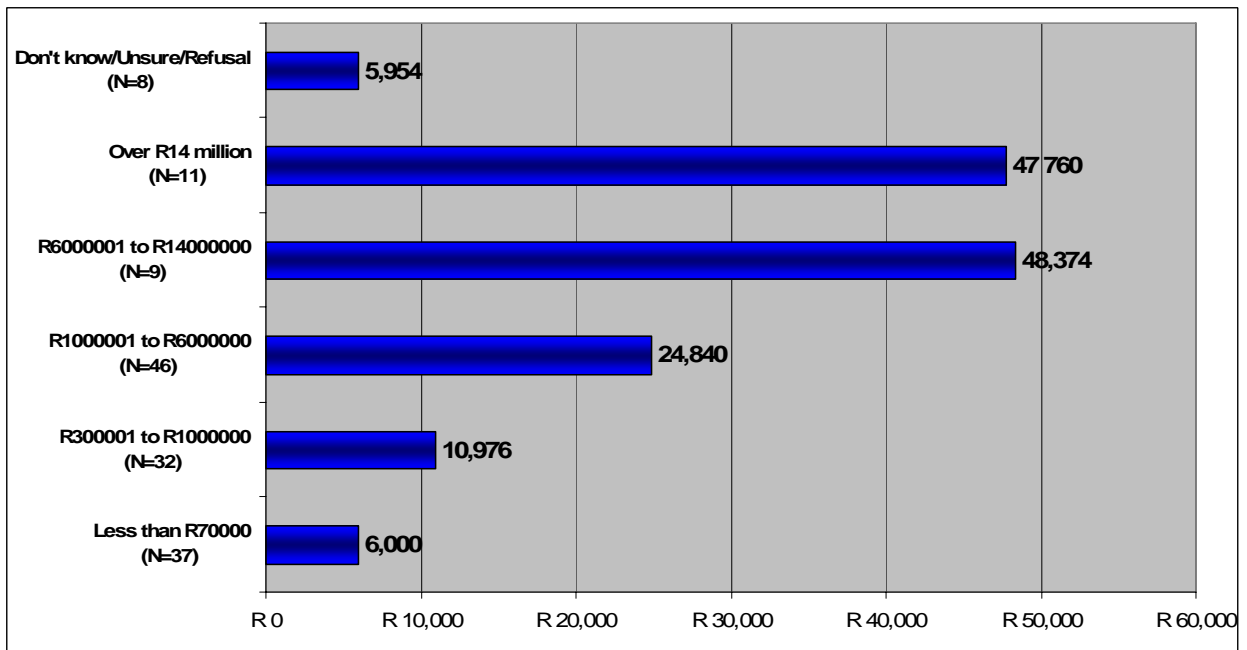


Figure 6-4: Proprietary Limited Businesses





The respondents believed that the total cost of outsourcing was divided almost equally between costs for completion of tax and bookkeeping tasks collectively (49%) and costs for completion of tax tasks exclusively (51%). No further breakdown was provided by the data, hence it was not possible to separate tax costs from accounting costs.

However, it was apparent that the bulk of the costs were allocated towards the tax end rather than the bookkeeping/accounting end of the spectrum, confirming the trend observed earlier that small businesses, in order to reduce costs, tried to accomplish as much as possible in-house and outsourced primarily when requirements progressed closer towards tax tasks and specialised tax matters.

Detailed tables showing costs for completion of tax and bookkeeping tasks collectively and exclusively follow here.

Table 6-1: Average Spend, Business Turnover, Completion of Tax and Bookkeeping Tasks

Business Turnover	Only tax documentation and information requirements	Both the tax and bookkeeping	Other
Less than R70 000	R1,942	R3,143	
R70 000 to R300 000	R3,541	R3,479	R3,000
R300 001 to R1 000 000	R3,216	R4,458	R99
R1 000 001 to R6 000 000	R9,549	R13,873	R18,969
R6 000 001 to R14 000 000	R16,292	R18,337	
Over R14 million	R600,842	R11,894	R30,000
Don't know/Unsure/Refusal	R7,983	R3,658	R6,000
Total	R65,908	R8,700	R12,718

Table 6-2: Proportion - Business Turnover, Cost of Completion of Tax and Bookkeeping Tasks

Business Turnover	Only tax documentation and information requirements	Both the tax and bookkeeping	Other	Total
Less than R70 000	2.6%	4.7%		3.6%
R70 000 to R300 000	14.7%	20.9%	16.7%	17.8%
R300 001 to R1 000 000	23.4%	21.6%	16.7%	22.4%
R1 000 001 to R6 000 000	30.4%	30.9%	33.3%	30.7%
R6 000 001 to R14 000 000	13.2%	7.9%		10.4%
Over R14 million	9.9%	7.6%	16.7%	8.8%



Don't know/Unsure/Refusal	5.9%	6.5%	16.7%	6.3%
Total	100%	100%	100%	100%

Table 6-3: Proportion - Business Turnover, Cost of Completion of Tax and Bookkeeping Tasks

	Only tax documentation and information requirements	Both the tax and bookkeeping	Other	Total
Less than R70 000	35.0%	65.0%		100%
R70 000 to R300 000	40.4%	58.6%	1.0%	100%
R300 001 to R1 000 000	51.2%	48.0%	0.8%	100%
R1 000 001 to R6 000 000	48.5%	50.3%	1.2%	100%
R6 000 001 to R14 000 000	62.1%	37.9%		100%
Over R14 million	55.1%	42.9%	2.0%	100%
Don't know/Unsure/Refusal	45.7%	51.4%	2.9%	100%
Total	49.0%	49.9%	1.1%	100%

Table 6-4: Average Spend - Business Legal Form, Completion of Tax and Bookkeeping Tasks

Business Legal Form	Only tax documentation and information requirements	Both the tax and bookkeeping	Other
Sole proprietorship	R8,484	R2,688	R6,000
Partnership	R1,035,406	R35,878	
Company (PTY LTD)	R18,454	R16,436	R27,513
Close corporation	R4,898	R7,040	R5,331
Other	R99		
Total	R65,908	R8,700	R12,718

Table 6-5: Proportion - Business Legal Form, Cost of Completion of Tax and Bookkeeping Tasks

	Only tax documentation and information requirements	Both the tax and bookkeeping	Other	Total
Sole proprietorship	15.0%	19.0%	16.7%	17.0%
Partnership	5.5%	3.9%		4.7%
Company (PTY LTD)	22.3%	15.4%	33.30%	19.0%
Close corporation	56.8%	61.6%	50.0%	59.1
Other	0.4%			0.20%
Total	100%	100%	100%	100%

Table 6-6: Proportion Business Legal Form, Cost of Completion of Tax and Bookkeeping Tasks

	Only tax documentation and information requirements	Both the tax and bookkeeping	Other	Total
Sole proprietorship	43.20%	55.80%	1.10%	100%



Partnership	57.70%	42.30%		100%
Company (PTY LTD)	57.50%	40.60%	1.90%	100%
Close corporation	47.00%	52.10%	0.90%	100%
Other	100.00%			100%
Total	48.90%	50.00%	1.10%	100%



6.3. CONCLUSION

The following conclusions were apparent from the analysis of the role and costs of external consultants:

1. Tax practitioners undoubtedly played an important role in the affairs of these small businesses, featuring in the tax and associated tasks of around 45% of small businesses.
2. SMMEs are more likely to hire professional services in matters relating to tax than it was for general accounting and recordkeeping.
3. The reliance on tax practitioners was lowest in sole proprietor and partnership businesses, with a significant proportion of them getting by on their own even for specialised tax tasks, though dependency increased with correspondingly higher degrees of interaction with SARS, as in the case of the lodging of appeals, petitioning for waivers of interest and penalties and the like.
4. Close corporations were the most dependent on tax practitioners, mainly due to a greater tax requirement than sole proprietary businesses, coupled with the lesser availability of in-house expertise as compared to proprietary limited businesses.
5. Proprietary limited businesses were the least dependent on tax practitioners, preferring instead to absorb as many tax tasks and functions in-house before proceeding to outsourcing.
6. The overwhelming majority of the tax practitioners were certified (as accountants, bookkeepers or tax consultants).
7. About half of small businesses which outsourced were unable to indicate the specific costs associated with this outsourcing.
8. Small businesses were also unable to separate general accounting/bookkeeping costs from tax costs, though it was evident that they believed the bulk of the costs were aggregated at the tax end of the spectrum.

CHAPTER SEVEN: OBJECTIONS AND APPEALS

A critical tax issue for small businesses related to the effort, costs and difficulties associated with the lodging of objections and appeals with SARS. In this chapter, some of the core issues relating to objections and appeals are examined and discussed. To begin with, we found that only 8.8% of all small businesses surveyed lodged an objection with respect to a SARS assessment. 75% of these appeals were lodged by the businesses, while 25% of appeals were lodged by tax practitioners on behalf of the businesses.

7.1. COST OF APPEALS AND OBJECTIONS

The survey assessed the cost to enterprise of each of these appeals. The cost of the appeal was defined to include the cost of employees' time and that of a tax specialist but excluded the actual penalties/interest that the enterprise was required to pay. The breakdown of costs per tax across the different turnover categories was reflected in the following table, Table 7-1 and Table 7-2, firstly for appeals lodged by the enterprise and then for appeals lodged by tax practitioners on behalf of the enterprises.

Table 7-1: Cost Appeals When Undertaken By the Enterprise

Turnover	Cost For Income Tax	Cost For Provisional Tax	Cost For VAT	Cost For PAYE
R70000 to R300000 (N=10)	R 1,433.33			
R300001 to R1000000 (N=8)	R 330.00		R 200.00	
R1000001 to R6000000 (N=35)	R 2,599.93	R 5,724.75	R 80.00	R 25.00
R6000001 to R14000000 (N=5)	R 675.00			
Over R14 million (N=14)	R 1,674.88	R 1,900.00	R 4,000.00	R 99.00
Mean	R 1,796.12	R 3,814.14	R 657.14	R 34.80

Table 7-2: Cost Appeals When Undertaken By Tax Practitioners

Turnover	Cost For Income Tax	Cost For Provisional Tax	Cost For VAT	Cost For PAYE
Less than R70000 (N=3)	R 800.00			
R70000 to R300000 (N=6)	R 387.50			
R300001 to R1000000 (N=9)	R 487.50			
R1000001 to R6000000 (N=8)	R 5,200.00	R 300.00	R 1,000.00	R 15,000.00
R6000001 to R14000000 (N=2)	R 150.00			



Don't know/Unsure/Refusal (N=2)		R 3,000.00		
Total (N=30)	R 1,693.33	R 1,650.00	R 500.00	R 7,500.00

The small number for the appeals in this sample restricted the extent of comparison for all taxes, with the exception of appeals for income taxes, which comprised roughly two thirds of all appeals lodged. As was evident from both tables, the average cost to enterprise for appeals regarding income tax was around R1 750, irrespective of whether the enterprise lodged the appeal or whether it was lodged by a tax practitioner. Interestingly, businesses in the R1million to R6million turnover category registered the highest costs in both instances for income tax appeals. However, given the small number of cases for this particular analysis, we could not read too much into this finding.

7.2. PERCEPTIONS OF THE APPEALS PROCESS

The majority of businesses which lodged an appeal reported being satisfied with some aspects of the appeals process and dissatisfied with other aspects. 70% of those who did appeal were satisfied to very satisfied with the time provided by SARS to lodge an appeal; 55% were satisfied to very satisfied with the appeals process, and just over half (52%) were satisfied to very satisfied with the cost of the appeal process.

However, in terms of the time taken by SARS to respond, the businesses were split, with more than half being displeased with the time taken by SARS, while only 40% were satisfied to very satisfied with this time.

Overall, businesses were generally happy with the appeals process, which was quite positive when one considered that appeals were generally not viewed with much enthusiasm by taxpayers because of, inter alia, the costs associated with it. However, it was also apparent from the study that small businesses would clearly appreciate a quicker turnaround time from SARS on the appeals process.



7.3. CONCLUSION

The following conclusions may be drawn from the analysis of the perceptions and costs of objections and appeals:

1. Overall, less than 10% of businesses lodged an appeal with SARS in the past year.
2. 75% of businesses lodged the appeals themselves, while 25% used their tax practitioners to do so.
3. The majority of appeals were lodged for Income Tax (68%), and there were too few cases for all the other types of taxes to enable any meaningful analysis thereof.
4. The average cost of appeals in matters related to income tax was found to be around R1 750.
5. This cost remained quite consistent regardless of whether the business or the tax practitioner lodged the appeal.
6. Enterprises in the R1 million to R6 million turnover category registered the highest average cost per appeal, consistently so regardless of whom had lodged the appeal.
7. Perceptions of the appeals process were generally positive for most aspects of the process, particularly the deadline provided for the lodging of the appeals and the nature of the appeals process.

However, the single biggest complaint of the majority of businesses was the time taken for SARS to respond to appeals.

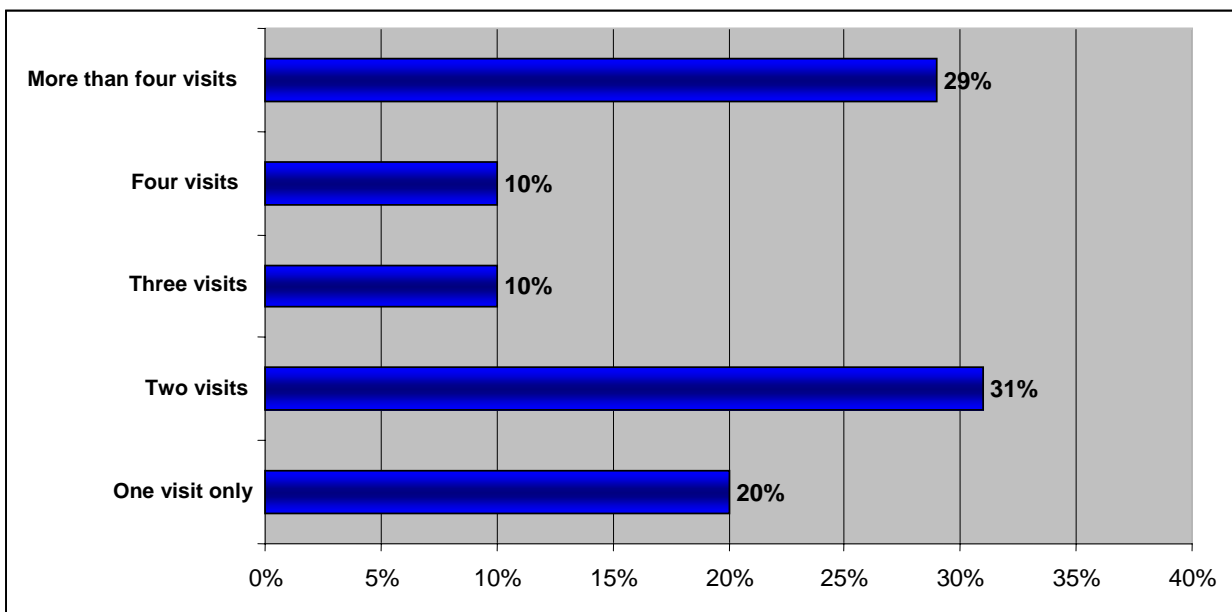
CHAPTER EIGHT: ENGAGEMENT WITH SARS – PHYSICAL VISITS

A key aspect of the extent to which small businesses were satisfied with the level of service received from SARS related to the quality of the service received when such businesses made physical visits to a SARS office. In this chapter, various aspects of physical visits to SARS offices are analysed.

8.1. NUMBER OF SARS VISITS

Just over half (53%) of the small businesses surveyed visited a SARS office in the past year, with the majority of these (71%) doing so four or fewer times in the year. The distribution of the number of visits to SARS offices in the past year is reflected in the Figure 8-1 below

Figure 8-1: Number of SARS Visits



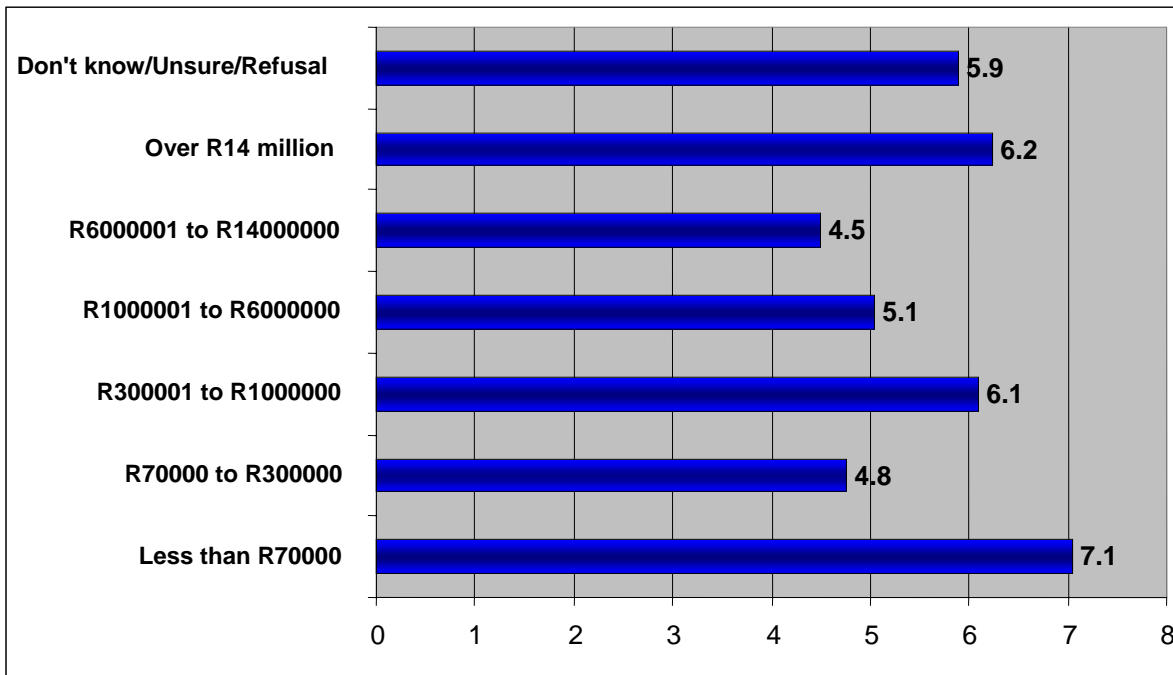
The data did not allow an analysis of why the remaining businesses did not visit SARS, and it was difficult to speculate whether this was due to their use of intermediaries and/or if they had no reason to do so.



8.2. SARS VISITS AND TURNOVER

Looking at visits to SARS in terms of business turnover (see Figure 8-2 below), it was apparent that the smallest businesses made the most number of trips to SARS. Again, this could have been as a result of the low rate of outsourcing, which placed the burden of these visits directly on the business itself.

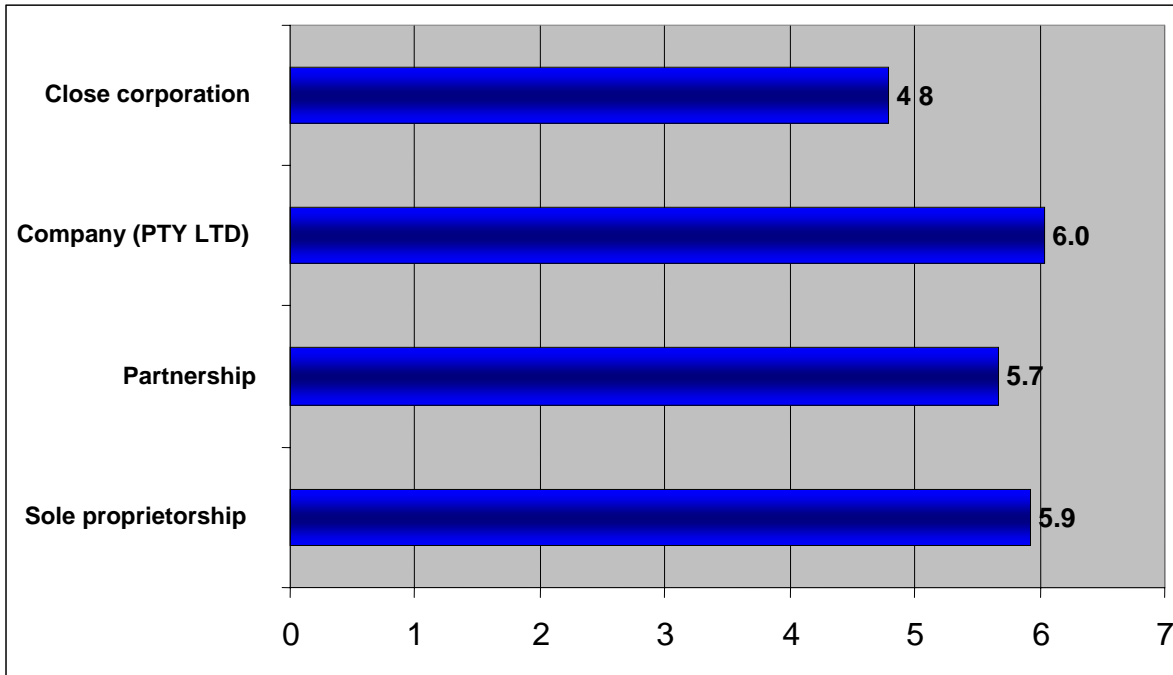
Figure 8-2: Number of Trips Taken To SARS by Turnover



8.3. SARS VISITS AND ENTITY TYPE

The breakdown of visits to SARS according to entity type is reflected in the Figure 8-3 below.

Figure 8-3: Number of Trips taken To SARS by Entity Type



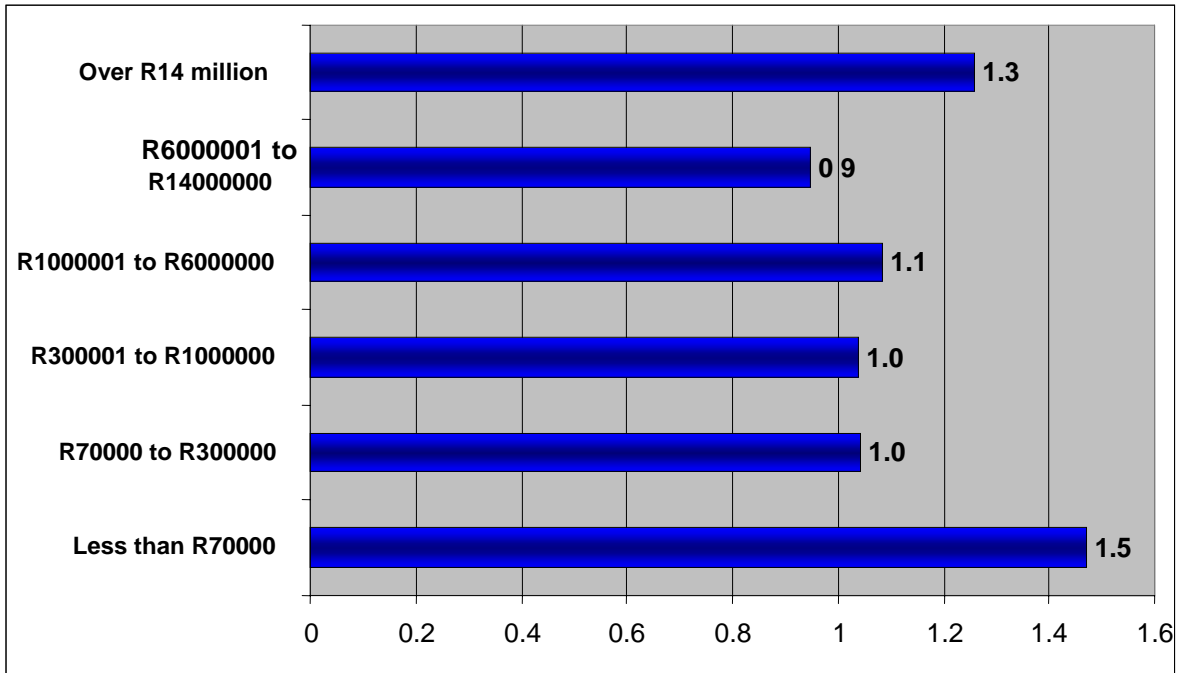
As can be seen in Figure 8-3, there were no statistically significant differences in the number of trips made to SARS as a function of the type of enterprise, though close corporations did make the least number of trips in the past year. This was consistent with the higher than average rates of outsourcing seen in these types of enterprise, meaning that the number of visits associated with these businesses could be higher when one took into account that visits could have been undertaken on their behalf by the tax practitioners.

8.4. TRAVEL TIME TO AND FROM SARS

Of those businesses that visited a SARS office in the past year, the majority (73%) took an hour or less to travel to and from the SARS office; 17% took between one and two hours; 5% took between two and three hours, and the remaining 5% took longer than 3 hours.

The average time taken by all businesses who visited SARS was approximately one hour for the round trip, and there were no significant differences across different categories of business turnover, as seen in Figure 8.4 below.

Figure 8-4: Time Taken For Round Trip to SARS (In Hours)





8.5. CONCLUSION

The study did not examine the specific nature of the visits to SARS, nor did it assess what the reasons were for some businesses not visiting SARS. Nevertheless, it did extract some useful information about visits in general:

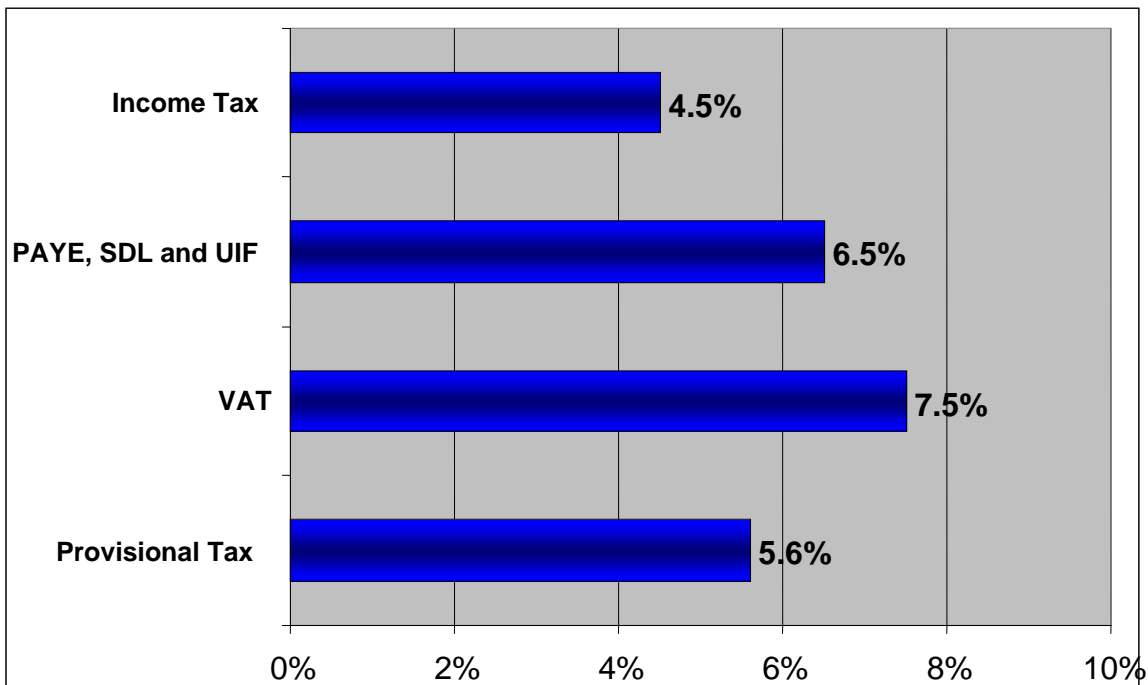
1. 53% of businesses visited SARS last year,
2. 71% of those visiting SARS did so four times or less.
3. On average, enterprises with the lowest turnover made the most number of visits to SARS, presumably because they could not afford to outsource tax matters and/or did not have sufficient in-house expertise to speedily address tax matters.
4. The number of visits to SARS was not dependent on the type of enterprise, though close corporations did register the lowest number of visits, which was consistent with the earlier finding that such businesses were the most likely to outsource tax tasks.
5. Three quarters of visitors to SARS took an hour or less to make the round trip from their place of business to SARS.
6. 10% of visitors took two hours and longer for the round trip.
7. Half of the visitors without appointments waited in queues for more than five minutes only about one-twentieth of the time.
8. 58% of visitors without appointments were attended to within 15 minutes of joining the queue, which was well below the 95% set out in the SARS charter.
9. When visitors had made an appointment, they were kept waiting for a somewhat shorter period of time, with about two thirds having to wait for more than five minutes less than 5% of the time.

CHAPTER NINE: PENALTIES AND INTEREST

9.1. INCIDENCE OF PENALTIES AND INTEREST

Overall, less than 10% of small businesses surveyed reported suffering sanctions in the form of penalties and/or interest for the late submission of various tax returns. The proportion of businesses which suffered these sanctions according to the specific tax is reflected in the Figure 9-1 below.

Figure 9-1: Type of Tax which incurred sanctions



Not surprisingly, the rate of sanctions was almost linearly dependent on the frequency of cycles/submissions for the different taxes. 65 VAT submissions and employees tax were submitted most frequently (up to twelve submissions per annum), followed by provisional tax (2 submissions per annum), and then income tax (one submission per annum). There were no discernible trends in terms of penalties suffered according to the entity type or annual turnover.



9.2. INCIDENCE OF APPEALS AND RATES OF SUCCESS

All of the businesses which had these sanctions applied, requested that the applicable penalties and/or interest be waived. This was a reassuring result, as it did indicate a measure of confidence in the appeals process by small businesses.

The vast majority (80%) of all small businesses which made requests to SARS to have penalties waived did so once or twice, while less than 5% of businesses appealed four times or so (on average?). Additionally, just under two-thirds (63%) of businesses that appealed to SARS, to have penalties waived, were successful in their bids. Turning to interest levied, 69% of businesses which applied to SARS to waive interest did so once or twice, with a minority appealing more often, while 66% of those who appealed were successful in their bid to have the interest waived.

9.3. COST OF PENALTY AND INTEREST WAIVING APPEALS

The cost of appeals was differentiated in terms of whether the SMME undertook the appeals themselves or whether they had contracted a tax practitioner to do so. Securing the waivers for penalties and/or interest cost businesses on average approximately R850 when the appeal was undertaken by themselves and approximately R1000 when the appeal was undertaken by the tax practitioner. However, given the small number of cases for appeals lodged by the tax practitioner, these results should be interpreted with caution. The breakdown of these costs by the type of company has been indicated in the Table 9-1 below.

Table 9-1: Cost of Appeals by Entity Type

Type Of Business	Business Appeals	Tax Practitioner Appeals
Sole proprietorship	R 1,875.00	
Partnership	R 1,433.00	
Company (PTY) Ltd	R 499.56	
Close corporation	R 929.36	R 1,000.00



Sole proprietor and partnership businesses appeared to incur the greatest costs, mainly due to the high incidence of sanction-incurring instances on their part, as well as relatively lower rates of in-house expertise, which necessitated a greater number of visits to SARS (as was seen earlier) and hence the higher costs. Conversely, proprietary limited businesses registered the lowest (rated) cost, arguably due to the greater reliance on in-house expertise (employees' time was not accounted for in this cost calculation). Finally, consistent with the trend observed earlier on in this report, close corporations were most reliant on tax practitioners to accomplish tasks related to direct engagement with SARS.

9.4. CONCLUSION

In summary, the following were found regarding penalties and interest:

1. Less than 10% of businesses had these sanctions applied due to late submission of tax returns.
2. All of the businesses affected applied for relief from imposed sanctions.
3. The majority of businesses that applied for relief did so either once or twice, with less than 5% having to do so four times or more.
4. About two thirds of appeals were successful both in respect of penalties and interest.
5. The average cost for this appeals process was R850 for businesses which did so themselves and R1000 for businesses which used tax practitioners.
6. The cost was highest for sole proprietor and partnership businesses and lowest for proprietary limited businesses.
7. Close corporations were the most likely to use tax practitioners for such appeals.



CONCLUSION: RECOMMENDATIONS FOR IMPROVING COMPLIANCE

Finally, and most pertinent with regard to recommendations on regulation and policy, the study surveyed the opinions of small business corporations with respect to the measures that may be undertaken to achieve greater degrees of tax compliance in their sector. In gathering this information, the survey phrased the questions in a general rather than a specific manner; that is, it was directed to businesses in terms of formal SMMEs in general, and was not intended specifically for them. Hence the responses received should be read as being applicable to the sector as a whole, and not merely for the specific SMME. Moreover, it was likely that businesses rated these measures with a view to non-compliant small businesses as well. Table 9-2 below summarises the ranking by businesses of the various measures that SARS may take in order to improve compliance in SMMEs. These measures were provided to the respondents, and they were simply asked to rate each of them.

Table 9-2: Measures that may be taken by SARS

Measures That May Be Taken By SARS	Ranking
Direct access to SARS assessors via e-mail, telephone, or in person	1
Reduced penalties and interest charges	2
Simplified tax registration procedures	3
A higher turnover threshold for compulsory VAT registration	4
A community-based person or ombudsman to assist confidentially with tax matters	5
Facility to allow SMMEs to register and change personal/company details online using the Internet	6
Ensure that most of the SARS decision-making powers are decentralised to SARS regional offices to make access and communication easier	7
Provide more SARS offices in remote areas	8



Probing deeper, respondents were requested to provide suggestions on the specific measures that SARS may undertake to improve compliance. These responses were completely unprompted, and hence respondents were free to provide whatever responses they chose to. Moreover, the questions were furnished with multiple response items; hence they did not add up to 100%. In analyzing the responses, content analysis was undertaken to organise the responses into increasingly higher order clusters. This process was undertaken through a series of iterations before the final five clusters were identified as follows:

1. SARS Access And Service Levels
2. Tax Policy, Thresholds And Penalties
3. Simplification Of Rules, Procedures And Materials
4. SARS Outreach And Facilitation
5. Communication And Media

Before proceeding to the tables, it is important to note that:

- Almost one third (29.8%) of businesses indicated that there was nothing that SARS could do to improve compliance. Not surprisingly, this view was held predominantly by enterprises which were already fully tax compliant, meaning that they had established the necessary organisational routines for compliance and these were institutionalised to the point where there was no longer a need for further SARS intervention.
- About 5% of the businesses did not have any suggestions as to how SARS could improve compliance levels, in that they could not think of anything specific that SARS could do. This view was generalised across the sample.
- The figures for the following tables reflect percentages only for those businesses which did provide suggestions (65.4% of sample)

Table 9-3: SARS Access and Service Levels

Have more SARS offices closer to business locations	8.7%
Improve overall levels of service, particularly by being more helpful to small businesses	6.9%
Be quicker with VAT refunds	5.7%
Employ more staff to provide more direct relationships with small business	4.9%
Ensure direct access to SARS assessors via telephone	3.1%
TOTAL	29.3%



**Table 9-4: Tax Policy, Thresholds and Penalties**

Reduce tax rates	17.0%
Reduce penalties and interest	6.4%
Do not tax small business	3.1%
TOTAL	26.5%

Table 9-5: Simplification of Rules, procedures

Simplify procedures and processes - for tax registration, submission, queries and appeals, e-filing and online applications procedures, including speeding up such processes so businesses spend less time on them	7.9%
Shorten the tax forms to allow better completion rates – make forms easier to complete in one session	7.5%
Make the tax forms simpler to understand and complete – by using simpler language and provide explanatory notes written in “layman’s terms”	6.1%
TOTAL	21.5%

Table 9-6: Outreach and Facilitation

Send staff out to help educate and train small businesses, including training in general tax compliance and how to complete forms	5.5%
Arrange workshops to help increase understanding on tax issues	5.3%
Directly help businesses grow	2.1%
TOTAL	12.9%

Table 9-7: Communication and Media

Increase the quota of information provided to businesses on critical tax issues	4.4%
Improve overall levels of communication directly with businesses	3.7%
Advertise more in the mass media (electronic and print, including pamphlets) and via road shows	1.7%
TOTAL	9.6%



9.5. CONCLUSION

The following were the overall conclusions in terms of improving levels of tax compliance in the sector:

1. 30% of small business corporations believed that there was nothing that SARS could do to improve compliance. This view corresponded to the high rates of compliance by these respondents, indicating well-established organisational routines for ensuring these levels of compliance.
2. 5% could not think of anything specific to suggest, and this view was generalised across the sample.
3. The most frequently cited suggestions for improving compliance related to issues of access to SARS and the nature and quality of service provided by SARS to small businesses:
 - a. Businesses prioritized the location of SARS offices, indicating a need to have them closer to where businesses were located. This was presumably to lower the time and travel costs associated with visiting SARS offices.
 - b. In general, there was a need to increase overall levels of service from SARS, and specifically with respect to the efficiency of VAT refunds (the delays thereof undoubtedly had significant cash flow implications for SMMEs, particularly those in the lowest turnover categories).
 - c. Businesses also requested more SARS officials to be on hand to address their issues, and wanted direct access to assessors (this latter issue was also identified in the tax practitioner study)
4. SMMEs made various suggestions with regard to tax policy and penalties and interest:
 - a. One tenth indicated a need for reducing current tax rates
 - b. Just under 5% suggested reducing rates for penalties and interest
5. One sixth of all businesses indicated the need to simplify rules, procedures and materials:
 - a. Procedures for registration and filing should be simpler and more easily accomplished
 - b. Tax forms should be shortened to enable quicker completion thereof



- c. Forms should be simplified in terms of the language used and more explanatory notes should be provided



6. Just under one tenth of businesses believed that there was a need for SARS to extend itself into the business community by way of:
 - a. Providing education and training to SMMEs to help ensure better submission and overall general compliance
 - b. Having road shows to increase general understanding of tax and tax matters
 - c. Directly helping businesses grow

7. Finally, in terms of communication and media, SARS could also improve compliance by
 - a. increasing the amount of information on tax that it provided to SMMEs
 - b. improving its communication with small businesses
 - c. Increasing levels of advertising in the mass media



ANNEXURE A: RESEARCH QUESTIONNAIRE

