

**INFORMAL SECTOR TAXATION: A LESSON FOR SOUTH
AFRICA**

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ABSTRACT

Most informal sector businesses in developing countries participate indirectly in the tax system through paying Value-Added Tax, as well as import and export duties, without being registered as taxpayers. This effectively results in the collection of lower tax revenue than the informal businesses would be liable for if they were registered as taxpayers. Additionally, the non-registration of informal sector businesses in the tax system perpetuates a culture of non-tax compliance.

Countries in sub-Saharan Africa have responded to this challenge by imposing direct taxes on revenue generated in the informal sector. This thesis discussed the informal sector taxation regimes adopted in Tanzania, Ghana and Zimbabwe, with the aim of identifying direct taxes that could be imposed in South Africa on the revenues generated in the informal sector.

The goal of the research was to determine the nature of direct taxes that could be imposed in South Africa on the revenues generated in the informal sector, taking lessons from the sub-Saharan countries of Tanzania, Ghana and Zimbabwe.

The research was based in the interpretivist paradigm. The data for the research consisted of documentary data dealing with the legislation and experiences of informal sector taxation in South Africa and the countries forming part of this research. The data were analysed using qualitative non-empirical research methods.

South Africa has a presumptive tax model in the form of the Turnover Tax system, and it was recommended that this direct tax could be adapted to integrate the informal sector businesses into the tax base. The study made several recommendations to integrate informal sector businesses into the tax base. These recommendations include the implementation of the tax stamp system to tax informal businesses other than minibus taxi businesses, and an income tax sticker specifically designed for the informal minibus taxi industry.

KEYWORDS: Informal sector taxation, South African Turnover Tax, presumptive taxes, presumptive taxes in Tanzania, Ghana and Zimbabwe

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LIST OF ABBREVIATIONS

ABBREVIATION	DESCRIPTION
BMS	Block Management System
CIPC	Companies and Intellectual Property Commission
GDP	Gross Domestic Product
GRA	Ghana Revenue Authority
IMF	International Monetary Fund
OECD	Organisation for Economic Co-operation and Development
Statistics South Africa	Statistics South Africa
SMMEs	Small Medium Micro Enterprises
SARS	South African Revenue Service
TRA	Tanzania Revenue Authority
VAT	Value-Added Tax
VIT	Vehicle Income Tax
ZIMRA	Zimbabwe Revenue Authority

CHAPTER ONE: INTRODUCTION

1.1 RESEARCH CONTEXT

The precise definition of what constitutes the informal sector differs from country to country but generally includes enterprises with productive activities at market value that are not registered with the relevant authorities (Allard, 2017). These enterprises are not subject to a variety of rules and regulations, including labour laws, environmental laws, and taxation laws (Joshi, Prichard, & Heady, 2014). Depending on the type of industry, these enterprises often operate as street vendors, small traders, independent producers, and subcontract workers, in a market with low barriers to entry, that is highly competitive, and is characterized by product homogeneity (Joshi *et al*, 2014). This thesis does not focus on the taxation of employees in the informal economy but on taxation of the informal sector businesses and their owners.

Most informal sector businesses in developing countries participate indirectly in the tax system through paying Value-Added Tax (VAT), as well as import and export duties, without being registered as taxpayers. Research has noted that this effectively results in the collection of lower tax revenue than the informal business would be liable for if they were registered as taxpayers (Joshi *et al*, 2014). Additionally, the non-registration of informal sector businesses in the tax system perpetuates a culture of non-tax compliance (Joshi *et al*, 2014). Certain developing countries in the Sub-Saharan Africa have responded to these challenges by implementing direct presumptive taxes for informal sector businesses.

Presumptive taxation uses indirect variables to ascertain tax liability. The word "presumptive" is used to indicate that there is a legal presumption that the taxpayer's income is no less than the amount resulting from the application of the indirect method (Thuronyi, 1996). The indirect variables that can be used to determine the tax base vary by country, and at the very basic level include turnover, number of employees, or cash generated (Joshi *et al*, 2014).

The presumptive tax models applied are not uniform across the developing countries. At the very basic level these tax models incorporate a simplified indicator of the tax base, such as profits, turnover, number of employees, or cash generated (Joshi *et al*, 2014). For example, Zimbabwe uses different indicators for different business sectors, where presumptive tax for transport operators is levied based on the model and the capacity of the type of transport operated, and for rental of premises the tax is levied at a percentage of the rental received (Dube, 2014). Tanzania levies presumptive taxes based on turnover, using a Block Management

System (Kundt, 2017). Under the Block Management System, tax collectors are assigned to geographical or sector blocks in which they identify small and medium businesses on which to levy presumptive tax (Kundt, 2017). A relatively similar system called “Identifiable Grouping Taxation” was applied in Ghana prior to moving to a “Tax Stamp and Vehicle Income Tax”, which requires transport operators to purchase tax compliance stickers from tax authorities on a quarterly basis (Kundt, 2017).

The revenue authorities in various African countries are faced with challenges in taxing the informal sector. Due to the informal sector being characterised by a lack of financial bookkeeping, the tax administrators face a major challenge in ascertaining a tax base indicator, such as profit or turnover (Dube & Casale, 2016). Additionally, a cost benefit analysis generally indicates that presumptive taxes have limited revenue potential and higher costs of collection (Joshi *et al*, 2014).

Despite these challenges, from a long-term perspective, the taxation of informal sector businesses encourages formalisation, which provides an opportunity for informal sector entities to access credit from financial institutions (Joshi *et al*, 2014). This debt leverage may ultimately lead to growth and higher revenue potential. The prospect of formalisation and growth, however, may not be appealing to all informal sector businesses as some firms have a small optimal size, and some firms are suitably structured for the goods and services they provide, and may not be able to compete in a formal market (Dube & Casale, 2016).

Arguments in favour of informal sector taxation have pointed out that there is an incentive for unregistered informal sector firms to enter the tax system as they are able to claim VAT refunds in instances where they are transacting with formal firms (Kundt, 2017). Furthermore, bringing the informal sector firms into the tax system builds a culture of tax compliance and promotes equity and fairness (Joshi *et al*, 2014). “Larger formal firms might consider it as unfair that small informal firms remain untaxed, which in turn potentially affects their own willingness to pay taxes” (Kundt, 2017:9). To achieve the objective of equity and fairness, the design of the informal sector taxation model must adhere to the principles of good tax policy as prescribed by the American Institute of Certified Public Accountants (AICPA).

The framework for evaluating tax policy as prescribed by the American Institute of Certified Public Accountants (2017), indicates that a good tax policy must provide certainty to the taxpayers of the taxes to be paid and provide convenient methods of paying the tax. The design

of the taxation model must be simple, neutral and collect revenue without impeding on the productive capacity of the economy.

Recently, there has been a growing awareness of the significance of the informal sector contribution in the South African economy. The informal sector was traditionally viewed as a low-productive and low-paid sector characterized by illegal business operations. This narrative is changing. Christensen (2020) explains that, in South Africa, revenues in the informal sector are generated from various lawful activities, for example, the African traditional “muti” market is estimated to be worth between R3 billion and R6 billion, spaza shop contributions are estimated to be worth R100 billion to R200 billion annually, and the township fast-food market is worth an estimated R80 billion per year.

The informal sector is an integral part of the labour markets in developing countries as it creates employment opportunities that stimulate economic growth (Christensen, 2020). Statistics South Africa (2019), in the 2019 Quarterly Labour Force Survey, revealed that 3 million people were working in the informal sector during the second quarter of 2019, and that represented 20% of total employment. It has been argued that this percentage may increase as those who lost their jobs in the formal sector due to the Covid 19 pandemic may choose to be self-employed (Rogan & Skinner, 2020). In 2015, Statistics South Africa (2015) estimated that the informal sector contributed 5.2% to the Gross Domestic Product (GDP) in South Africa. It is estimated that this contribution will grow to 23.59%, on average, in 2025 (Etim & Daramola, 2020).

In South Africa, informal businesses participate in the tax system by paying VAT when transacting with formal businesses. No direct taxes are levied on revenue generated by informal businesses. South Africa has a narrow tax base with personal income tax accounting for 38% of total revenue collected in 2019, 17% from corporate taxes, and 25% from VAT (National Treasury and SARS, 2019). Personal income tax was contributed by fewer than 3 million people, in a country with a population of about 56 million people (Kruger, 2020).

The government has undertaken various tax reform initiatives aimed at increasing tax revenue through expanding the tax base. According to Manuel (2002), as part of this strategy, Capital Gains Tax was introduced in 2001 to capture the tax on the appreciation of all investments, which previously went wholly untaxed, as the definition of “gross income” in the Income Tax Act, 58 of 1962 (the Income Tax Act), excluded capital gains, with no specific inclusions in taxable income to cater for capital gains. Manuel (2002) also explained that another reform to

broaden the tax base was changing the South African tax system from a source-based system, which only taxed income from a South African source, to a residence-based system, which taxes residents on their worldwide income and non-residents on income from a South African source. Manuel also noted that the removal of tax schemes such as the use of tax-free fringe benefits, and the limitation of deductions for salaried employees, also increased the tax base. The only presumptive tax in South Africa is the Turnover Tax levied in terms of the Sixth Schedule to the Income Tax Act, levied on the turnover of up to R1 million earned by micro businesses. These tax reforms have not, however, addressed the integration of informal sector businesses into the tax system.

This thesis discusses the informal sector taxation regimes adopted in Tanzania, Ghana and Zimbabwe, with the aim of identifying direct taxes that could be imposed in South Africa on the revenues generated in the informal sector. These countries are appropriate for this research as they have accessible information relating to their informal sector taxation regimes and are comparable to South Africa in the sense that economically they are in a developing stage and are characterised by the presence of informal business operations. This thesis aims to contribute to a growing literature on informal sector taxation, specifically in a South African context. The ultimate interest of this research is not, however, to advocate for or against direct income taxation in the informal sector.

1.2 GOALS OF THE RESEARCH

The goal of the research is to determine the nature of direct taxes that could be imposed in South Africa on the revenues generated in the informal sector, taking lessons from the sub-Saharan countries of Tanzania, Ghana and Zimbabwe.

This goal will be addressed by the following sub-goals:

- understanding the informal sector in South Africa and the countries forming part of the research - how the informal sector is defined, the causes of informality, and the estimated sizes of the informal sectors;
- analysing the methods and approaches used to tax informal sector businesses in Tanzania, Ghana and Zimbabwe;
- identifying the challenges and benefits of direct income taxation for the informal sector in Tanzania, Ghana and Zimbabwe; and

- recommending direct taxes that could be imposed in South Africa on the revenues generated in the informal sector.

1.3 RESEARCH METHODS, PROCEDURES AND TECHNIQUES

This research is based in the interpretivist paradigm; with an interpretivist perspective, researchers gain a deeper understanding of the subject under investigation, and its complexity in its unique context, instead of attempting to generalise the base of understanding for the whole population (Creswell, 2013). Hammersley (2013:26) also emphasises that interpretivist researchers should try to understand “the diverse ways of seeing and experiencing the world through different contexts and cultures and try to avoid the bias in studying the events and people with their own interpretations”.

The data for the research consist of documentary data dealing with the results and experiences of informal sector taxation in South Africa and the countries forming part of this research. Data will be analysed using qualitative non-empirical research methods. “Non-empirical research methods consist of conceptual analyses, theory-building studies, philosophical analyses and literature reviews” (Mouton, 2001, cited in Stander, 2013:61). This research will focus on literature. The purpose of the critical literature review is to establish the groundwork on which the research is built, and to develop a good understanding of, and insight into significant research conducted on the direct income taxation of informal sectors in the countries forming part of the research. To enhance the accuracy and reliability of the inputs into the research, a comprehensive review of literature, including propositions from both critics and advocates, will provide an opportunity for an unbiased discussion of the previous experiences of informal sector taxation in the countries. The data will be collected using reliable online search engines including those listed below:

- the Organisation for Economic Co-operation and Development (OECD) website: to obtain reports assessing the effectiveness of informal sector taxation as a revenue mobilization tool in developing countries;
- the Department of National Treasury website: to obtain reports of existing research conducted on tax reforms that inform the direction of future tax reforms; and
- various journal platforms, such as EBSCO Host databases and African Journals Online, to obtain relevant material discussing the experiences of adopting direct informal sector taxation in the countries involved in the research.

As only documentary data were used for the purposes of this research, no ethical considerations applied, and application for ethical approval on the Rhodes University ERAS platform, was not required.

1.4 OVERVIEW OF THE CHAPTERS

Chapter 1 outlines the background of the research, including the importance of broadening the tax base of developing countries, and challenges associated with levying direct presumptive taxes on the informal sector. It briefly identifies the types of presumptive taxes levied in South Africa, Ghana, Tanzania and Zimbabwe. It sets out the goals and subgoals of the research, and describes the research methodology applied.

Chapter 2 focuses on understanding the informal sector in South Africa and the countries of Ghana, Tanzania and Zimbabwe that were the subject of the research. It defines the concept of informality, and discusses the methods used to measure informality, as well as the trend of the informal sector in the sub-Saharan Africa. It discusses the estimated size and the reasons for the growth in the informal sector in Ghana, South Africa, Tanzania and Zimbabwe to facilitate the comparison of the informal sectors.

Chapter 3 analyses the methods and approaches used to tax informal sector businesses in Tanzania, Ghana and Zimbabwe, and discusses the challenges and benefits of direct income taxation for the informal sector.

Chapter 4 discusses the rationale for informal sector taxation in South Africa and recommends direct taxes that could be imposed in South Africa on the revenues generated in the informal sector.

Chapter 5 summarises the findings of the study and concludes by reviewing the extent to which the research goal and the sub-goals were achieved and suggests future areas of research.

CHAPTER TWO: UNDERSTANDING THE INFORMAL SECTOR

2.1 INTRODUCTION

Chapter 2 addresses the following goal of the research:

- understanding the informal sector in South Africa and the countries forming part of the research – how the informal sector is defined, the causes of informality, and the estimated sizes of the informal sectors.

The chapter first defines the concept of informality and the informal sector. The difficulty in measuring informality is then described. The slightly decreasing trend in the size of the informal sector in sub-Saharan Africa is referred to, and the causes leading to informality described. To facilitate the comparison, the estimated size and the reasons for the growth in the informal sector in Ghana, South Africa, Tanzania and Zimbabwe are discussed.

2.2 THE CONCEPT OF INFORMALITY

The concept of informality in the economy was first referred to in the 1970s and has since been widely debated around the world (Organisation for Economic Co-operation and Development (OECD), 2019). The distinction between formal and informal activities emerged from the attempts of scholars to apply the dualism framework to labour markets (Madhura, 1991). The traditional dual labour market theories suggested that jobs can be divided into two groups: those with low wages, poor working conditions, unstable employment, and little or no opportunity for advancement, and those with relatively high wages, good working conditions and opportunities for advancement (Uys & Blaauw, 2006). The term “informal sector” was able to incorporate a wide range of activities that were deemed to connote a poor standard of living conditions (Madhura, 1991).

In many developing countries, the informal economy has evolved from the generalised myths of being the illegal underground, shadow or black market (OECD, 2019). Research conducted at the World Bank (Oviedo, Thomas & Karakurum-ozdemir, 2009) indicates that this evolution of the informal economy covers a wide range of labour market activities that are different in nature and are motivated by different reasons. The market activities in the informal sector are motivated by coping behaviours of individuals and families in economic environments where

earning opportunities are scarce, and these families and individuals engage in subsistence farming, domestic casual jobs, and street vending, to earn a living. These activities are generally regarded as survivalist activities in the economy as they are motivated by a desire to earn a living. The informal economy can also be seen as a strategy to avoid labour regulations or other institutional regulations, and to evade tax.

The exact definition of the informal sector varies between countries. A common definition of the informal sector in developing countries includes entities that participate in the economic activities of a country without registering with the relevant authorities (OECD, 2019). In most countries the operational activities of these entities are not subject to a variety of rules and regulations, including labour laws, environmental laws, and taxation laws (Joshi *et al*, 2014). Characteristics that differentiate the informal sector from the formal sectors across various developed and developing countries include ease of entry into the market, and small-scale productions or operations that are highly labour intensive (OECD, 2019).

According to the international standards adopted by the 15th International Conference of Labour Statisticians, “the informal sector is a subset of unincorporated enterprises not constituted as a separate legal entity independently of their owners” (OECD, 2019:12). For the purposes of the present research, the informal sector includes market activities that would contribute to the Gross Domestic Product (GDP) of the country, if they were recorded, and excludes illegal activities and goods produced for household consumption.

2.3 MEASUREMENT OF INFORMALITY

According to Schneider and Buehn (2016) informality, by its complex nature and the inability of traders in the informal sector to maintain high quality financial records, is difficult to measure. This difficulty is exacerbated by the business cycles that affect the informal sector trading activities. Informal sector businesses, like all other businesses in the formal sector are not immune to recessions and expansions in the economy, and the output and employment in the informal sector fluctuates during each business cycle.

Research evidence from South Africa of the 2008/9 global economic crisis suggests that, contrary to the myth that the informal sector acts as a cushion and absorbs employees retrenched in the formal sector employment, the informal sector is often negatively impacted (Rogan & Skinner, 2020). The negative impact can be attributed to a decline in disposable income,

consumption and demand for goods and services during economic crises (Rogan & Skinner, 2020).

Despite the difficulties and complexities of measuring the size of the informal economy, researchers have developed a wide range of estimation methods and tools to estimate and capture the size of the informal sector (Schneider & Buehn, 2016). These measures can be categorised into indirect model-based estimates such as informal sector contribution to GDP, and direct measures gathered from surveys, such as labour force surveys and the physical input approach (Ohnsorge & Yu, 2021).

According to Echavarria (2015), economic studies explain that GDP can be calculated using either the income approach measure or the expenditure approach measure. In terms of the expenditure approach, GDP equals consumption, plus investment, plus government spending, plus exports, less imports. The income approach sums factor incomes to the factors of production. Theoretically the results of the expenditure approach and the income approach should be equal.

Due to the non-reporting of income by informal sector businesses, they are often included in the expenditure measurement of GDP and excluded from the income measurement, thus the difference between these two measures is an indicator of the size or contribution of the informal economy (Echavarria, 2015). The disadvantage of this method is that differences due to sampling and statistical errors, which cannot be disentangled from the amount that can be explained by the informal economy, can mistakenly be classified as the contribution of the informal economy into GDP (Schneider & Buehn, 2016).

The labour force survey measure estimates the size of the informal economy by the number of people employed in the informal sector at a certain point in time (Ohnsorge & Yu, 2021). Labour force surveys are widely used and are often comparable as they do not rely on complex assumptions, however over time methodologies may vary across countries, limiting the comparability of the data (Ohnsorge & Yu, 2021).

The physical input technique “measures the growth of the informal economy as the difference between the growth rate of GDP and the growth rate of electricity consumption” (Oviedo *et al*, 2009:7). This method suffers from limited data availability and the unrealistic assumption that all informal sector production requires the use of electricity (Ohnsorge & Yu, 2021).

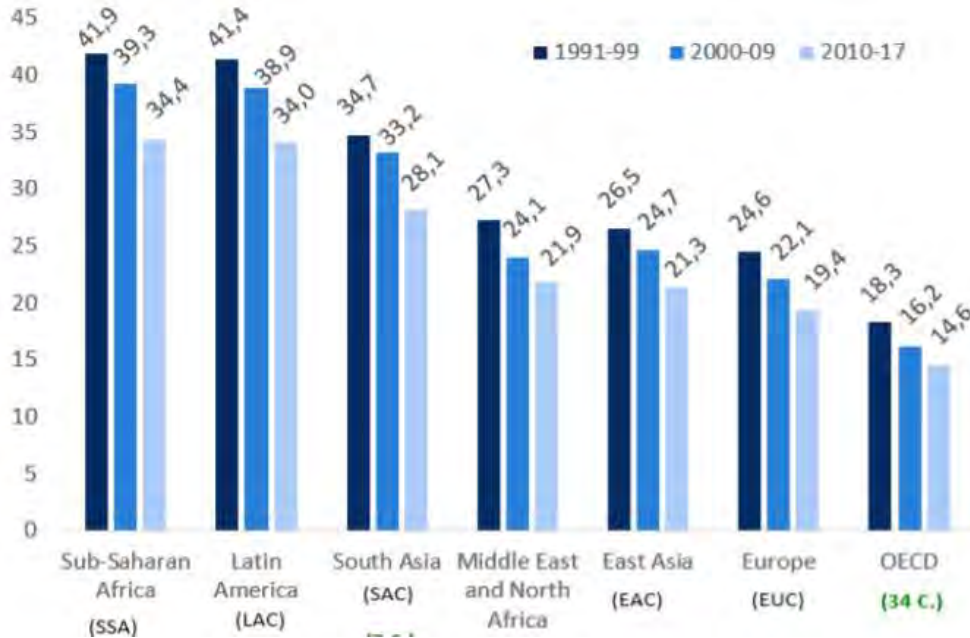
Due to the complexities of measuring the informal economy, there is no ideal method of measuring or estimating the size of the informal economy (Schneider & Buehn, 2016). The Multiple Indicator-Multiple Cause approach can also be used, due to its flexibility (Schneider & Buehn, 2016). “This model assumes that, while informal activity is not observable, its magnitude can be represented by a latent variable (in index form), and both its causes and effects can be observed and measured” (Oviedo *et al*: 2009:5).

Oviedo *et al* (2009) submit that the indirect methods of measuring informality, which include the labour force surveys and the discrepancy between aggregate income and expenditure, when applied in appropriate contexts, can mitigate their limitations and produce results that assist policy makers to institute appropriate macroeconomic policy for optimal economic performance. They can assist the relevant government institutions to measure the size of the informal sector and simplify the transition of informal businesses into the formal sector. Oviedo *et al*, claim that the results obtained from measuring the informal economy can also assist the government and other interested parties to tailor appropriate interventions to support the informal sector businesses. This can be in the form of financial support or the much-needed financial management skills, which is at the core of the survival of most informal sector businesses. Tax collection agencies can also use the results obtained from measuring the informal economy to quantify the tax leakage where informal sector revenues are not taxed, and to assess the effectiveness of tax policies where informal sector revenues are taxed.

2.4 TRENDS AND CAUSES OF INFORMALITY

Medina and Schneider (2019) have noted that the size of the informal economy, measured as a percentage of GDP, has gradually declined over years across many regions around the world. However, the informal economy still has a significant presence and contribution to the GDP in sub-Saharan countries compared to the more economically developed OECD region countries. The following graph indicates the trend of the informal economy by region, based on average percentage of GDP from 1991 to 2017.

Figure 2. 1: The Informal Economy by Region



Source: Medina and Schneider (2019:36)

A cross-country study (Loayza, Oviedo & Servèn, 2005) has indicated that the higher GDP contribution of the informal economy in developing countries is due to the high rates of unemployment, slow economic growth, high income inequality, and lack of formal skills and education prevalent in most developing countries. Other determinants of informal businesses include the excessive and strict regulatory compliance burden required to enter the formal sector, resulting in high compliance costs that firms in the informal sector cannot afford. It is submitted that these causes of informality extend beyond the government structures and institutional limitations, they extend to the entrepreneurs' choice of operating sector.

Chong and Gradstein (2004) constructed a theoretical model that studied the causes of informality. Among other determinants, the model also evaluated why entrepreneurs who have achieved sufficient profitability levels to afford the necessary resources required to formalise their businesses, such as Companies and Intellectual Property Commission (CIPC) registration, tax registration, and compliance with other labour regulations, still choose to remain in the informal sector. The results of the data analysis provided evidence that informality is the result of a rational choice of individuals. It is the result of a cost benefit analysis that consciously contemplates a number of aspects.

2.4.1 Flexibility of self-employment

In the first instance, self-employment in the informal sector may appear to be undesirable and may be associated with inferiority and not having the necessary education and skills to be employed in the formal sector (Rogan & Skinner, 2020). However, depending on the success of the business, most informal sector entrepreneurs create employment opportunities for others and enjoy a greater working flexibility of being self-employed (Oviedo *et al*, 2009).

Rogan and Skinner (2020) conducted a study of the economic impacts of the COVID-19 lockdown level five in South Africa, using the South African National Income Dynamics Coronavirus Rapid Mobile Survey data. The study suggests that just under a third (31%) of informal sector workers who did not lose their livelihoods completely were locked out of employment and could not trade or work due to Covid-19 restrictions. Average earnings for those who were able to work subsequently when restrictions were eased declined by 27% and typical earnings declined by 60%. Furthermore, informal sector employees' livelihoods were significantly affected as compared to formal sector employees, as most of informal sector employees are not registered with the Unemployment Insurance Fund, which was used to compensate employees for loss of income during the lockdown restrictions (Rogan & Skinner, 2020).

2.4.2 Costs of formalising

Oviedo *et al* (2009) explain that excessive business regulatory and compliance costs imposed by government legislation, and numerous regulations in developing countries, force many entrepreneurs to continue operating in the informal sector as they avoid the time, costs and effort associated with formalising. In many developing countries these costs include trading licences, registration, and annual renewals, registering with the Receiver of Revenue for taxes, keeping annual financial records in a manner accepted by the Receiver of Revenue, and submitting annual tax returns.

Depending on whether the income earned is above the taxable threshold, informal sector entrepreneurs also stay in the informal sector to avoid paying taxes (Oviedo *et al*, 2009). Most of the informal sector entrepreneurs operate in underdeveloped areas, and the poor state of public goods and service provision in their area is their justification to avoid paying taxes (Were, 2020). Ali, Fjeldstad and Sjørusen (2013) also support the view that there is a direct connection between tax compliance and the government provision of public goods and services.

“The greater the level of public satisfaction and trust in the quantity and quality of products and services the greater the tax morale and compliance” (Ali *et al*, 2013:829).

Williams (2014) also contends that the growth of informal entrepreneurship is positively related to high tax under standard tax regimes, and public sector corruption. The explanation is that, in developing economies where macro-economic conditions are characterised by government over-regulation, high taxes, public sector corruption and low-income distribution, informal businesses provide an opportunity to resist the government regulations, high taxes, and public sector corruption.

2.5 THE INFORMAL SECTOR IN GHANA

The estimated size of the informal sector in Ghana, and the reasons for its growth are described below.

2.5.1 Estimated size of the informal sector

Ghana is a developing economy with about two-thirds (67.6%) of the labour force employed, 9.1% percent unemployed, and 23.3% not part of the labour force (Ghana Statistical Service, 2016). The existence of the informal sector in Ghana’s economy can be traced back to the very beginnings of colonial capitalism, when the economy was characterised by low economic growth and political instability (Boateng & Ampratwum, 2011). According to Ocran (2018), throughout the expansion of the modern economy, the informal sector continued to exist in the urban and rural areas of Ghana.

The size of the informal sector in Ghana, measured by the percentage of employment, indicates that in 2015, 90% of the employed population (15 years and older) was in the informal sector (Ghana Statistical Service, 2016). In the rural areas the informal sector businesses consist mainly of small-scale gold and diamond miners, as well as small scale agricultural producers focusing on vegetable produce, and fishing and fish processing, which is predominant in the Ghana coastline areas.

Medium scale farmers focus on cocoa, oil palm, and coconut plantations. In the major urban centres of Ghana, the informal sector businesses include shoe-manufactures, private taxi services, hawkers, market traders, hairdressers, domestic workers, and construction workers. The 2015 labour force survey also indicated that sectors making the highest contribution to

informal employment were agriculture, forestry and fishing, at 37.5%, and the wholesale and retail industry at 31.3% (Ghana Statistical Service, 2016).

It appears from these statistics that the informal sector in Ghana provides a unique opportunity to increase employment opportunities and contribute meaningfully to the socio-economic development of the Ghanaian citizens. However, the government is striving to formalise the informal sector in order to widen the tax base and provide social protection to promote financial stability and economic growth (Ghana Business News, 2019). Despite these efforts, the trajectory of informal sector growth is still evident in the Ghanaian economy with the sector contributing 73.3 billion Ghanaian Cedis (GHC) to the GDP of Ghana in 2017, which represented 28.6 % of the country's total GDP (Ghana Business News, 2019).

2.5.2 Determinants of the informal sector in Ghana

There are a number of reasons for the existence and growth of the informal sector in Ghana, including restrictive government regulation, low levels of education, and a lack of confidence in the banking system.

Restrictive government regulation

The existence and growth of the informal sector in Ghana is attributed to the restrictive business regulatory environment and lack of government support for entry level businesses (Boateng & Ampratwum, 2011). In the World Bank Doing Business Survey (World Bank, 2020), Ghana ranks 118th out of 190 economies in terms of the ease of starting a business. The survey is a series of annual studies that investigates the regulations that enhance business activity and those that constrain it in an economy (World Bank, 2020). The 118th position indicates a deteriorating rate from the position of 114th in 2019 (World Bank, 2019a).

Low levels of education

The majority of the population in Ghana do not have the necessary skills and education required to compete for jobs in the formal sector. The 2015 Labour Force Survey indicates that the highest qualification attained by 32.8% of the population is primary education, 23.9% have attained junior secondary education, and only 3.1% and 0.7% have attained a bachelor's degree and postgraduate degree respectively (Ghana Statistical Service, 2016).

Work aspiration results also included in the 2015 Labour Force Survey indicated that 36.7% of the population who have no educational qualification would want to work as service- or salespersons in the agricultural and fishery industry, and 21.1% as craft and related trades workers, plant machine operators and assemblers, where they can easily become self-employed (Ghana Statistical Service, 2016). The convenience of self-employment, coupled with lack of education, perpetuates the growth of informal sector entrepreneurship, as often the entrepreneurs do not have the relevant skills and knowledge to keep quality financial records (Ocran, 2018).

Lack of confidence in the banking system

In 1982 Ghana undertook a currency reform by demonetizing its 50 Sedi currency to fight against corruption and manage liquidity (Ocran, 2018). The reform was unsuccessful and resulted in a loss of faith in the banking system and led to the preference for conducting cash transactions outside the banking system, which remains at the core of informal entrepreneurship (Ocran, 2018).

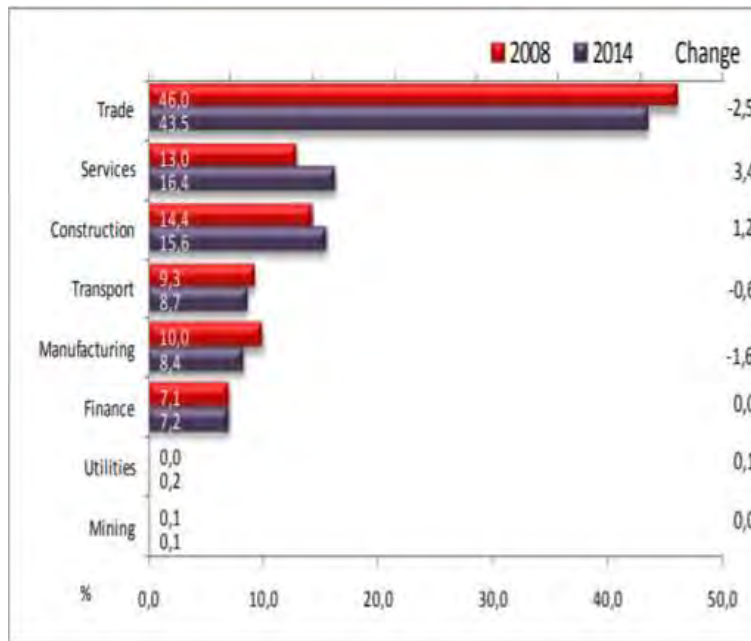
2.6 THE INFORMAL SECTOR IN SOUTH AFRICA

As is the case in Ghana, South Africa has a large informal sector, for reasons very similar, including unemployment, low levels of education, and structural constraints and burdensome regulations.

2.6.1 Estimated size of the informal sector

Initially, informal sectors in South Africa were a product of the apartheid system, which denied the oppressed population groups quality education and reduced their chances of employment in the formal sector. The marginalised population resorted to self-employment, servicing the communities' needs as a means of survival. Twenty-seven years after democracy, the graph below shows that although there is a slight declining trend of informality in South Africa, it is still prevalent. Informality in the South African economy is firmly established in the townships and inner-city environments, where there is a high population density. Statistics South Africa (2015) indicates that in 2014 the dominant informal sector businesses were in the trade sector, which constituted 43,5% of the market share, and the services sector, which constituted 16,4% of the market, as reflected in the graph below.

Figure 2. 2: Percentage Change of Informal Businesses by Sector in South Africa



Source: Statistics South Africa (2015:10)

Charman, Petersen and Govender (2020) explain that, in South Africa the prominent business examples in the trade sector include liquor retailers (Shebeens), grocery shops (Spazas), street vendors, African products and muti shops, fast food restaurants, as well clothing shops. Businesses in the services sector include hair salons, car workshops, residential accommodation rental (back-room rental), tailors, and child day care services.

The trends in the graph above indicate that the lowest contributing sectors were finance and manufacturing, while utilities and mining remained insignificant. The data excludes agriculture and household work. Christensen (2020) explains that in South Africa, revenues in the informal sector are generated from various lawful activities, for example, the African traditional “muti” market is estimated to be worth between R3 billion and R6 billion, spaza shop contributions are estimated to be worth R100 billion to R200 billion annually, and the township fast-food market is worth an estimated R80 billion per year. Alcock (2020) also adds that the backroom rental market in the informal sector is worth more than R30 billion a year. In 2015, Statistics South Africa (2015) estimated that the informal sector contributed 5.2% to the GDP in South Africa. It is estimated that this contribution will grow to 23.59%, on average, in 2025 (Etim & Daramola, 2020).

Informal employment in South Africa

According to the Statistics South Africa Quarterly Labour Force Survey (Statistics South Africa, 2020a), 2,5 million people were employed in the informal sector during the 4th quarter of 2020 (excluding agriculture). Due to the impact of Covid-19, Statistics South Africa reduced face to face contact interviews and changed the survey mode of collection to telephonic conversations; as a result, the 2020 estimates are not based on a full sample and caution should be applied when compared with prior years (Statistics South Africa, 2020). The share of informal sector total employment in 2019 was estimated at 20% (Statistics South Africa, 2019).

According to Francis, Valodia and Ramburuth-Hurt (2020), during the COVID-19 pandemic formal employment in South Africa contracted by 4%, while informal employment contracted by 7%. Contrary to expectations, the informal sector did not absorb employees who had lost their formal jobs, but rather it was disproportionately affected. Furthermore, compared to the global average informal sector employment of 60% (Ohnsorge & Yu, 2021), it appears that South Africa has relatively low informal sector employment.

2.6.2 Determinants of the informal sector in South Africa

The main reasons for the existence of the informal sector in South Africa are elaborated on below.

High rate of unemployment

With South Africa's unemployment at 32,5% in the 4th quarter of 2020, the reality is that many people are running informal business due to a lack of job opportunities (Statistics South Africa, 2020a). In the latest Survey of Employers and the Self Employed (Statistics South Africa, 2017), 63.5% of the participants mentioned that unemployment was the main reason they started an informal business. A small percentage of the participants stated that they started an informal business because they had the required skills and passion to deliver the services required in the business, and the income they earned was better than in their previous jobs. Another small percentage of participants had informal businesses because they inherited them from their families.

Low levels of education

Many people working in the informal sector do not have the necessary skills and educational qualifications to compete for jobs in the formal sector. The Survey of Employers and the Self Employed also revealed that 67.8% of the participants running their own businesses had less than matric as their highest qualification, and 30,9% had matric and other higher education qualifications (Statistics South Africa, 2017).

Structural constraints and regulatory burdens

Although unemployment is the leading cause of informality in South Africa, research conducted by Trade and Industrial Policy Strategies (2017) found that other factors that hinder the transition of informal businesses to formal business in South Africa include structural constraints and regulatory burdens. Structural constraints for the majority of the population are described as the legacy of apartheid laws that contributed to the high inequality in South Africa, lack of capital, and access to other assets such as land.

In the 2020 World Bank Doing Business Survey (World Bank, 2020), South Africa ranked 84th out of 190 countries, a ranking better than Ghana (118), Tanzania (141) and Zimbabwe (140), indicating the South African government's somewhat greater ability to set regulations that encourage efficiency and support freedom to do business in South Africa. However, the impact on South African small businesses is not yet significant, as research still finds the cost of the regulatory burden as the main reason for entrepreneurs to remain in the informal sector (Trade & Industry Policy Strategies, 2017).

2.6.3 Income earned in the informal sector

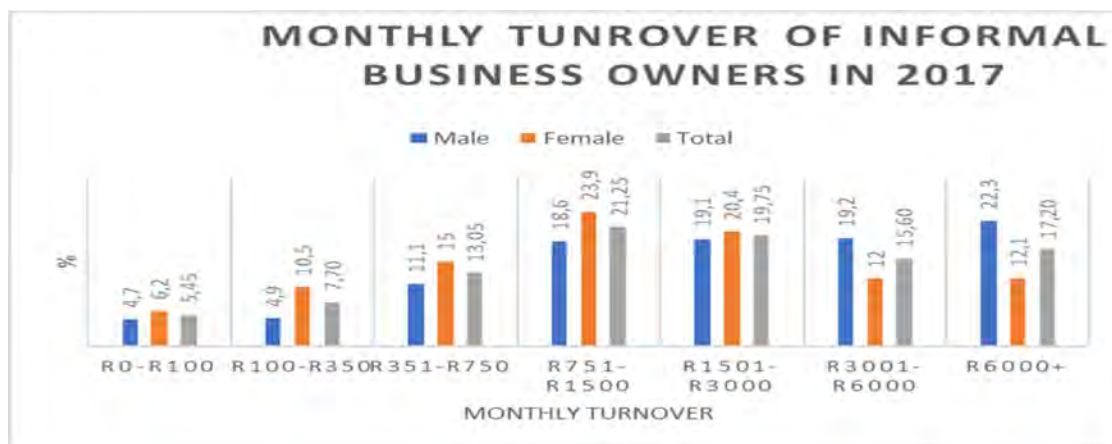
Alcock (2018) wrote a book "KasiNomic Revolution", in which he discussed interviews with different types of self-employed entrepreneurs in the informal sector operating their businesses in the townships of Gauteng. The results of the interviews revealed that a woman who was selling snacks and lunch time meals at a local township school for R2, R5 and up to R10 an item was able to make profits of between R350 and R500 per day. In a school calendar of 200 days pre-pandemic, the woman made profits of between R70 000 to R100 000 a year. A fresh

vegetable stall hawker made profits of between R20 000 and R40 000 a month, while a woman selling vetkoek made on average R30 000 profit a month.

Other informal entrepreneurs interviewed were not able to quantify their profits, however they were certain that they make enough money to afford to have employees, support their families and send their children to universities. Interestingly the vegetable vendor, when asked if he would consider paying tax, responded that he does not see the need to do so. Alcock (2018) submits that these highly profitable informal businesses do not represent the majority of the informal businesses, but they represent a sizeable proportion, which can be as high as one in every four businesses

The data collected in the Gender Series Volume V11: Informal Economy 2013-2019 ((Statistics South Africa, 2020b), as reflected in the graph below, revealed that the majority of the informal business owners surveyed, 21,25 %, generated a monthly turnover between R751 to R1 500. About one fifth of the business owners, 19,5%, generated a monthly turnover between R1 501 and R3 000, and 17,2% of the business owners generated a monthly turnover greater than R6 000 (Statistics South Africa, 2020b).

Figure 2. 3: Monthly Turnover of Informal Business Owners -2017



Source: Adapted from Statistics South Africa (2020b:31)

2.7 THE INFORMAL SECTOR IN TANZANIA

The estimated size of the informal sector in Tanzania, and the determinants of its size, are discussed below.

2.7.1 Estimated size of the informal sector

Doing business in the informal sector in Tanzania gained popularity in the mid-eighties during the structural adjustment programmes, which were implemented to redirect some of the provision of health services, sanitary and water supply, public security, and educational services from the government to the private sector (Lema, 2013). The population affected by retrenchment programmes started small and medium scale businesses, which constitute the informal sector in Tanzania (Lema, 2013).

According to the 2014 Integrated Labour Force Survey, the informal sector employed 6.2 million people, which represents 31.2 % of the labour force employed in Tanzania (National Bureau of Statistics, 2015). In Tanzania, similar to the trend in other sub-Saharan countries, the majority of the people with the lowest level of education are employed in the informal sectors. The Integrated Labour Force Survey indicated that, in 2014, of the people employed in the informal sector, 70% had attained primary level education as the highest level of education (National Bureau of Statistics, 2015).

The 2014 Integrated Labour Force Survey (National Bureau of Statistics, 2015) further revealed that the two significant industries in the informal sector in Tanzania are the wholesale and retail industry, which includes the repair of motor vehicles and motorcycles, and the accommodation and food services industry. The wholesale and retail industry accounts for 47.9% of the people employed in the informal sector, while the accommodation and food services industry accounts for 14.5%. The informal sector in Tanzania is dominated by self-employed entrepreneurs. Sixty-eight-point-one percent of the participants surveyed in 2014 were self-employed, without employees, in non-agricultural activities, and 9% were self-employed with employees. Sixteen percent were paid employees.

Research conducted by the World Bank (Ohnsorge & Yu, 2021) indicates that the contribution of the informal sector in Tanzania is estimated to be 50% of the GDP for the period between 2010 to 2018. Although this contribution remains significant, it reflects a decline from a 60% contribution for the period between 1990 and 1999.

2.7.2 Determinants of the informal sector in Tanzania

As in Ghana and South Africa, the determinants of the informal sector are very similar in Tanzania.

Unemployment

The unemployment rate of 10.3%, as reported in the 2014 Integrated Labour Force Survey (National Bureau of Statistics, 2015) was relatively low compared to the rate of unemployment in South Africa. People who engaged in informal sector activities because they were not able to find employment opportunities anywhere else only amounted to 28.4% of the total population (National Bureau of Statistics, 2015).

Additional income

Many people surveyed (37.8%) indicated the need for additional income as the reason to engage in informal sector activities (National Bureau of Statistics, 2015). The need for additional income is to supplement lower formal sector earnings, or mainly because the informal activities yield more turnover than the salary of the participants at previous jobs (Aikaeli & Mkenda, 2015).

Low start-up capital and restrictive government regulations

The regulatory environment in Tanzania is not conducive for start-up businesses and even worse for small medium enterprises (Aikaeli & Mkenda, 2015). Further evidenced of this is its rating of 141 out of 190 countries in the 2020 World Bank Doing Business Survey (World Bank, 2020). Twenty-nine-point-seven percent of the informal business owners surveyed in the 2014 Integrated Labour Force Survey (National Bureau of Statistics, 2015) mentioned that they joined the informal sector because entry into the informal sector does not require much capital and there are no regulatory requirements to start a business. This is also associated with the lack of financial support for small medium enterprises in the informal sector. According to the 2014 Integrated Labour Force Survey (National Bureau of Statistics, 2015), 10.6% of the informal sector business owners surveyed reported that they received financial assistance in a form of a loan or credit facility in their business, and 89.4% did not have access to financial assistance.

2.8 THE INFORMAL SECTOR IN ZIMBABWE

The discussion below indicates the similarity of the informal sector in Zimbabwe with those in Ghana, Tanzania and South Africa.

2.8.1 Estimated size of the informal sector

The Zimbabwean economy has experienced numerous economic shocks, including hyperinflation in the early 2000s, which shrunk the economy and job opportunities in the formal sector, leaving the informal sector as the official backbone of the economy (Mbiriri, 2010). The large agricultural sector, policy disruptions, and the hyperinflation has negatively affected the production of accurate economic statistics in Zimbabwe (Mbiriri, 2010). Using the Multiple Indicator-Multiple Cause indirect approach to measuring informal economies in a study of 158 countries, Medina and Schneider (2018) measured the informal economy of Zimbabwe as the third largest economy after Bolivia and Georgia. This estimation is for the period between 1991 and 2015. It is estimated that the informal workforce in Zimbabwe is about 85% of the total workforce (Kedem, 2020).

2.8.2 Determinants of the informal sector in Zimbabwe

Unemployment and poor economic growth are the main contributors to the existence and growth in the informal sector in Zimbabwe. Although there is no literature to support this, it is submitted that lack of access to capital, regulation and a low level of education may also play a part in the growth of the informal sector.

Unemployment

Due to the economic crisis in Zimbabwe, foreign investment declined, consequentially manufacturing output declined and, in 2000, 400 companies were closed (Mbiriri, 2010). The structural adjustment programme introduced by the government further exacerbated the level of retrenchments (Sakuhuni, 2014). In 2013 unemployment remained significantly high at 50% and as a result many people resorted to the informal sector to find employment opportunities (Sakuhuni, 2014).

Poor economic growth

The poor economic growth in Zimbabwe is attributable to various reasons, including the land reform programme that resulted in a decline in food production, trade sanctions imposed on the government, and hyperinflation (Mbiriri, 2010). The real economic growth declined on average from 2.8% between 1991 to 1996 to -4.5% between 2000 and 2007 (Sakuhuni, 2014).

2.9 CONCLUSION

The literature review revealed that the exact definition of the informal sector varies between countries. A common definition of the informal sector in developing countries includes entities that participate in the economic activities of a country without registering with the relevant authorities (OECD, 2019). According to the international standards adopted by the 15th International Conference of Labour Statisticians, “the informal sector is a subset of unincorporated enterprises not constituted as a separate legal entity independently of their owners” (OECD, 2019:12). For the purposes of the present research, the informal sector includes market activities that would contribute to GDP if they were recorded, and excludes illegal activities and goods produced for household consumption.

Despite the difficulties and complexities of measuring the size of the informal sector, researchers have developed a wide range of estimation methods and tools to estimate and capture the size of the informal sector.

The size of the informal sector in Ghana, measured by the percentage of employment, indicates that in 2015, 90% of the employed population was in the informal sector (Ghana Statistical Service, 2016). The significant industries in the informal sector are mainly forestry and fishing, at 37.5%, and wholesale and retail industry at 31.3% (Ghana Statistical Service, 2016). The causes of the informal sector in Ghana include restrictive government regulations, low levels of education and a lack of confidence in the banking system.

In South Africa, the dominant informal sector businesses were in the trade sector, which constituted 43,5% of the market share, and the services sector, which constituted 16,4% in 2014. (Statistics South Africa, 2015). Christensen (2020) explains that, in South Africa, revenues in the informal sector are generated from various lawful activities. For example, the African traditional “muti” market is estimated to be worth between R3 billion and R6 billion, spaza shop contributions are estimated to be worth R100 billion to R200 billion annually, and the township fast-food market is worth an estimated R80 billion per year. The share of informal sector total employment in 2019 was estimated at 20% (Statistics South Africa, 2019). The results of the informal business owners’ interviews in KasiNomic Revolution (Alcock, 2018) indicates that there are highly profitable informal businesses in South Africa, and although these businesses do not represent the majority of the informal businesses, they represent a sizeable proportion, which can be as much as one in every four businesses. The data collected in the

Gender Series Volume V11: Informal Economy 2013-2019 (Statistics South Africa, 2020b) revealed that 17.2% of the informal business owners generated a monthly turnover greater than R6 000 in 2017. The causes of the informal sector in South Africa include low levels of education, structural constraints and regulatory burdens.

Research conducted by the World Bank (Ohnsorge & Yu, 2021) indicates that the contribution of the informal sector in Tanzania is estimated to be 50% of the GDP for the period between 2010 to 2018. The informal workforce in Tanzania is estimated to be 31.2% of the total workforce (National Bureau of Statistics, 2015). The significant industry in the Tanzanian informal sector is the wholesale and retail industry which is measured at 47.9%. The causes of the informal sector in Tanzania include unemployment, lack of access for start-up capital and restrictive government regulations.

The informal sector in Zimbabwe contributed 60.6% to GDP between 1991 and 2015 (Medina & Schneider, 2018). The informal workforce in Zimbabwe is estimated to be 85% of the total workforce (Kedem, 2020). Zimbabwe's informal sector is driven, *inter alia*, by high unemployment and poor economic growth.

There are high levels of similarity between the size and contribution to GDP of the informal sectors in Ghana, South Africa, Tanzania, and Zimbabwe, and there is a great deal of correspondence between the reasons for the existence and growth of the informal sector in these countries. This makes it appropriate to discuss and compare the direct presumptive taxes levied in these countries, with a view to recommending presumptive taxes to be applied in South Africa.

The next chapter therefore analyses the methods and approaches used to tax informal sector businesses in Ghana, Tanzania, and Zimbabwe, and identifies the challenges and benefits of direct income taxation in the informal sector

CHAPTER THREE: PRESUMPTIVE TAXATION IN TANZANIA, GHANA AND ZIMBABWE

3.1 INTRODUCTION

Chapter 3 addresses the following goals of the research:

- analysing the methods and approaches used to tax informal sector businesses in Tanzania, Ghana and Zimbabwe; and
- identifying the challenges and benefits of direct income taxation for the informal sector.

According to the World Bank (2019b), sub-Saharan Africa remains the region with the largest number of economies below the minimum desirable tax-to-GDP ratio of 15%. At that low level, revenues are inadequate to finance basic government service provision. As a result, informal sector taxation has become an inescapable component of the tax systems in most developing countries. “More than 25 countries in sub-Saharan Africa and 14 countries in Latin America have a special tax regime for small enterprises (which includes the informal sector)” (IMF, 2007, cited in Dube & Casale, 2016:670). Over time researchers have analysed the benefits and challenges of informal sector taxation.

This chapter therefore first discusses the benefits and challenges of informal sector taxation, and presumptive taxes in general, and then describes the presumptive taxes applied in Ghana, Tanzania and Zimbabwe.

3.2 BENEFITS OF DIRECT TAXATION OF THE INFORMAL SECTOR

There are a number of benefits for informal sector businesses and the *fiscus* that flow from direct taxation. These include the benefits of formalisation, a Value-Added Tax incentive, promoting a culture of tax compliance, and increased equity.

From a long-term perspective, the taxation of informal sector businesses encourages formalisation, which provides an opportunity for informal sector entities to access credit from financial institutions (Joshi *et al*, 2014). This debt leverage may ultimately lead to growth and higher revenue potential. The prospect of formalisation and growth, however, may not be appealing to all informal sector businesses, as some firms have a small optimal size, and some

firms are suitably structured for the goods and services they provide and may not be able to compete in a formal market (Dube & Casale, 2016).

Arguments in favour of informal sector taxation have pointed out that there is an incentive for unregistered informal sector firms to enter the tax system as they are able to claim Value-Added Tax (VAT) refunds in instances where they are transacting with formal firms (Kundt, 2017).

Bringing the informal sector firms into the tax system builds a culture of tax compliance and promotes equity and fairness (Joshi *et al*, 2014). “Larger formal firms might consider it as unfair that small informal firms remain untaxed, which in turn potentially affects their own willingness to pay taxes” (Kundt, 2017:9).

Horizontal equity means treating people on the same economic level equally for tax purposes, while vertical equity means treating people on different economic levels differently, and informal sector taxation is an optimal way of ensuring that people with the same level of income do not escape the tax net simply because they are unregistered (Mpofu, 2021).

3.3 CHALLENGES OF DIRECT TAXATION OF THE INFORMAL SECTOR

Opponents of informal sector taxation have argued that, from a cost benefit analysis perspective, presumptive taxes have limited revenue potential and higher costs of collection (Joshi *et al*, 2014). Pimhidzai and Fox (2011) have argued that informal sector taxation is regressive to the growth of small firms. However, viewed differently, the contribution of small firms to tax revenue increases the government’s capacity to provide social services and eliminates the distortion arising from “free riding” taxable persons in the allocation and access to social services (Deloitte, 2015).

3.4 PRESUMPTIVE TAXATION

Informal sector businesses are not commonly taxed through the standard tax regime due to their complex nature and difficulty in maintaining quality financial records to accurately measure the taxable income generated, which is used as a base in determining the tax liability under the standard tax regime (Dube & Casale, 2016). Loeprick (2009) also argues that the standard tax regime approach requires tax return filing, which increases compliance costs and makes it difficult for informal sector businesses to comply.

Presumptive taxation is the use of indirect variables to ascertain tax liability. The word "presumptive" is used to indicate that there is a legal presumption that the taxpayer's income is no less than the amount resulting from the application of the indirect method (Thuronyi, 1996). The indirect variables that can be used to determine the tax base vary by country, and at the very basic level includes turnover, number of employees, or cash generated (Joshi *et al*, 2014).

Loeprick (2019) explains that presumptive taxes provide a simplified tax model that reduces tax compliance costs for informal businesses, as they often do not require formal tax filing. Presumptive tax is a tool used to fight tax evasion by bringing into the tax net informal businesses that have the potential to pay taxes but would otherwise have remained invisible to the tax authorities (Deloitte, 2015). Presumptive tax models determine tax payable based on a presumption of turnover or other bases that in some instance results in violating vertical equity by treating taxpayers with different levels of income in the same way (Mpofu, 2021).

The experiences of Ghana, Tanzania and Zimbabwe, as detailed below, provide more insight into the presumptive tax models that are used to tax direct income in the informal sector.

3.5 PRESUMPTIVE TAX IN GHANA

Ofori (2009) explains that Ghana's informal sector presumptive tax model has undergone several changes since its inception. The first attempt at taxing the informal sector in Ghana was through the Standard Assessment Act, Act 205 of 1963, which required a fixed lump sum tax to be levied on individuals and businesses based on the level of business activity they engage in. The system was discontinued as it violated vertical equity by imposing the same tax liability on high- and low-income earners.

In 1986 the Standard Assessment System was abolished and replaced with an associational taxation system, where the informal sector associations with knowledge of the members' income earnings were able to negotiate the affordable standard rates of tax per association (Ampaabeng, 2018). This system was successful in raising additional revenue as it facilitated bargaining and cooperation between informal sector associations, businesses, and the government, and through enhancing amendments it transitioned into the identifiable grouping taxation (Joshi *et al*, 2014).

Under the identifiable grouping system, the Internal Revenue Service tasked the informal sector associations to collect revenue from the informal businesses with the idea that the association

agencies can more easily collect revenue from its members (Ampaabeng, 2018). This system enhanced horizontal equity as it captured small businesses and the self-employed who had previously escaped the standard tax system (Ofori, 2009). However, the challenge of this system was that the agencies failed to properly account for taxes collected from their members. As a result of the high level of corruption, the system was replaced with the small business tax stamp and the vehicle income tax stamp administered by the Ghana Revenue Authority (GRA) (Ampaabeng, 2018).

3.5.1 Tax stamp system

Under the tax stamp system informal businesses are categorised according to the size, turnover and business activities to determine the quarterly tax payable (Danquah & Osei-Assibey, 2016). The quarterly tax rate ranges from a minimum of GHC3 to a maximum of GHC45 as indicated in the table below.

Table 3. 1: Tax Stamp Rates

Category	Types of business	Size	Rate per quarter (GHC)
Category A	Businesses engaged in commercial and retail trading activities such as susu collectors, pub and chop bar owners, bakeries, business centres, estate and accommodation agents, block and terrazzo manufacturers, sand and stone winners, and contractors and licensed diamond and gold winners and buyers.	Large	45
		Medium	30
		Small	10
		Table-top	3
Category B	Businesses engaged in vocational activities such as dress makers and tailors, hairdressers, beauticians and barbers, artisans and hiring services, freelance photographers and car washing bays.	Large	35
		Medium	20
		Small	5
		Table-top	3
Category C	Businesses engaged in agricultural-related activities such as butchers, corn and other millers, charcoal and firewood vendors, traditional healers and other businesses as determined by the Ministry.	Large	25
		Medium	15
		Small	3
		Table-top	3

Source: Ghana Income Tax Regulations (2006: L.I. 2244)

The Ghana Revenue Authority (2021a) explains that the tax stamp targets low-income informal businesses with turnover between GHC20 000 and GHC90 000 that are not registered for VAT and Corporate Income Tax and often operate in temporary structures. The tax stamps must be

purchased quarterly in advance and displayed in the business premises or carried by the taxpayers while operating their business.

The tax stamp is not a final tax, as businesses purchasing the tax stamps are still required to file returns at the end of the year of assessment (Ghana Revenue Authority, 2021a). However, Iddrisu, Warwick, Abrokwah, Conron, Kamara and Nuer (2021) noted that, because filing behaviour is haphazard among small traders (and the cost to the Ghana Revenue Authority of enforcing filing obligations among small traders may outweigh potential tax collections), in practice the quarterly payments may often act as a final tax on small traders. In terms of the Ghana 2016 Income Tax Regulations, failure to produce the stamp results in a penalty of between GHC20 and GHC50.

Revenue collection

Ofori (2009) explains that due to the required visibility of the stamps, the tax stamp system was able to reduce the level of corruption and increase compliance rates. The increased compliance rates were accomplished by continuous efforts of performing on-the-spot verification of the stamps to enforce tax compliance.

The implementation of the tax stamps was enabled by the strong support from the national government by enacting the legislation that allows for the funding of the tax stamp system by the revenue authority, even when the implementation affected a politically sensitive group (African Tax Administration Forum, 2014).

Danquah and Osei-Assibey (2016) warned that a successful implementation was merely a step in the right direction, and a lot of effort is still required to increase revenue collections, as the informal sector has the potential to generate annual tax revenue of GHC327 million. It appears that there are a number of challenges to be addressed in order for the Ghana Revenue Authority to make a serious breakthrough when it comes to revenue collection.

3.5.2 Challenges of the tax stamp system

Three main challenges face the Ghana Revenue Authority in increasing revenue collection.

Defining the enterprise size in the legislation

Danquah and Osei-Assibey (2016) explain that the parameters defining the size of the enterprise are not clearly stipulated in the legislation and, as a result, the tax officials, based on experience, subjectively classify the informal business as either large, medium or small. The subjective classification may lead to over- or under-estimation of the actual tax payments required. To prevent this, it is imperative for the Ghana Revenue Authority to devise a standard measure for assessing the size of the informal businesses.

Poor data quality hampering the monitoring regime of the system

In a case study of the Ghana tax stamp project, the African Tax Administration Forum (2014) noted that the Small Tax Office that is responsible for the collection of the tax stamp revenue does not have a data monitoring system that is designed to trace the change in the size of the informal businesses, for example, when the informal business has grown from small to a medium size. Furthermore, most of the revenue administration processes are executed manually, which results in inefficiencies. Figures relating to the cost of collection were not readily available, but it was noted that, whilst the compliance cost on the part of the taxpayer is low, the administrative cost for the revenue authority can be high if the system's implementation relies heavily on manual processing.

Inefficient tax education programmes

Danquah and Osei-Assibey (2016) revealed that the educational level of the taxpayer contributed to the informal sector tax gap in Ghana. The tax gap was found to be higher for informal business owners with no educational background (GH¢302,840) as compared to those with at least primary education (GH¢293,509). Education has a chance of improving the individual's understanding of the importance and contribution of paying tax to the government; accordingly, tax education should be vigorously pursued.

3.5.3 Vehicle income tax stamps

The vehicle income tax stamp is designed to collect income tax from commercial vehicle owners. The owners are required to purchase a quarterly Vehicle Income Tax (VIT) sticker,

which is pasted on the front windscreen of the vehicle. The purchase price of the sticker is determined by the tonnage and the vehicle capacity as illustrated in Table 2.

Table 3. 2: Ghana's Vehicle Income Tax

Vehicle description	Annual Rate (GHC)
Tractors, power tillers and tankers	40
Taxis/private taxis	48
One pound, one pound/Peugeot cars/fork-lift, recovery towing trucks	60
Trotro (up to 15 persons)	64
Hiring cars (saloon, caravan)	320
Hiring cars (4x4) four wheels	480
Trotro (up to 19 persons)	80
Trotro (20–23 persons)	88
Trotro (24–32 persons and above)	120
Commuter (up to 15 persons)	80
Commuter (16–19 persons)	100
Buses, commuter (up to 23 persons)	80
Tour operator (up to 15 persons)	320
Commuter (up to 38 persons)	160
Tour operator (16–23 persons)	400
Commuter (39–45 persons)	200
Tour operator (24–38 persons)	280
Tour operator (above 45 persons)	600
Commuter (46 and above persons)	240
Dry cargo (below 2 tons) pay loaders/pickups 2–3.5 tons	140
Dry cargo (2–4 tons) tankers 2000 gallons/sewage tankers/garbage trucks/cranes	256
Tankers above 2000 gallons/graders/bulldozers	404
Dry cargo (4–7 tons)	480
Tipper trucks (single axle)	320
Tipper trucks (double axle)	480
Articulated truck trailers (18 cubic metres)/timber trucks	800
Tipper trucks (12–14 wheelers)	600
Ambulance/motor hearse	88
Articulated truck trailers (single axle)	800

Source: Ghana Income Tax Regulations (2016: L.I. 2244)

The VIT sticker is not a final tax; vehicle owners are required to file an annual income tax return (African Tax Administration Forum, 2014). However, in practice, similar to the tax stamp, the VIT payment often becomes final tax payment, as the cost to the Ghana Revenue

Authority of enforcing filing obligations among small traders may outweigh potential tax collections (Iddrisu *et al*, 2021). Compliance with the VIT stickers is monitored with the assistance of the Ghana Police Services (Ghana Revenue Authority, 2021b). Commercial drivers who fail to purchase or renew the VIT stickers are faced with a fine of not less than 25 penalty units and not more than 50 penalty units, or to a term of imprisonment of not less than 2 months (Ghana Income Tax Regulations, 2016). A penalty unit “refers to such units established by the Fines (Penalty Units) Act 2000 (Act 572). The monetary value of a penalty unit stands at GH¢12.00” (Ghana Revenue Authority, 2021b: Online).

The African Tax Administration Forum (2014) noted that the VIT system is more successful than the tax stamp system as the compliance rate is reasonably high. In 2010 average quarterly VIT stickers sold amounted to 187,349, which equates to a compliance rate of 85.5%. A similar conclusion was also reached in the study by Oppong (2015). In this study it was further explained that the high level of payment can be attributed to the strict implementation and monitoring by the Motor Traffic and Transport Unit of the Ghana Police Services.

3.5.4 Challenges of the vehicle income tax

Oppong (2015) explains that, despite the high compliance rates in the VIT system, there are some pertinent challenges faced by the commercial vehicle owners in their attempt to comply with the VIT. These challenges include a shortage of the VIT stickers and long queues, which result in revenue losses for the drivers. The stickers are printed by the Controller and Accountant General division, which is not within the Ghana Revenue Authority, and that makes it challenging for the Ghana Revenue Authority to ensure that the stickers are printed in a timely manner.

3.6 PRESUMPTIVE TAX IN TANZANIA

Tanzania adopted presumptive taxes in 2001 to broaden its tax base (Dube & Casale, 2016). The presumptive income tax is managed and administered by the Department of Domestic Revenue, which forms part of the Tanzania Revenue Authority (TRA) (Dube & Casale, 2016). In July 2004, the Tanzania Revenue Authority formalised the presumptive taxation scheme by incorporating a new simplified taxation schedule into the Income Tax Act of 2004, as amended in 2006, which was thereafter referred to as the Income Tax Act 2004 (Haji, 2015). Haji explains that the First Schedule of the Income Tax Act 2004 provides definitions, content, and structure for imposing presumptive income tax in Tanzania, and was introduced to facilitate

and formalise the registration in the tax system of informal sector operators, including start-up businesses, to ensure that they start paying taxes.

3.6.1 Institutional framework

Joshi *et al* (2014) explain that, to capture more informal businesses in the tax net and to increase tax compliance, the Tanzania Revenue Authority uses the Block Management System (BMS). The BMS maps informal businesses on a geographical basis, where a combination of a few streets or trading areas forms a block. The Tanzania Revenue Authority A allocates staff to each block, who are delegated to operate the tax administration functions of identifying informal businesses eligible for registration, executing the registration processes, assessing the annual tax payable, and accounting for the revenue collected. To mitigate the impact of corruption, the staff is rotated between the blocks after a certain period. Each block team is assigned a team leader who reports to the assistant manager and takes responsibility for the performance of the team. For performance management purposes each team is allocated revenue collection targets.

The BMS allows the revenue authority to closely monitor the informal business sector activities, which improves its capacity fight to tax evasion. The BMS offers simplified registration processes for informal traders and can easily identify non-registered businesses and bring them into the tax net (Haji, 2015). Despite the strategic set up of the BMS with its inherent potential to broaden the tax base, there are views that the system has not been optimally utilized or effectively implemented in Tanzania due to limited financial and human resources (Tanzania Revenue Authority, 2011). It appears that, for a revenue mobilisation system to achieve its intended purpose, both the design and implementation of the system are equally important.

3.6.2 Presumptive tax payable

The determination of presumptive tax payable in Tanzania includes two taxable categories targeting low-income informal businesses (PricewaterhouseCoopers, 2021). The following table stipulates the tax rates applicable in terms of the level of annual turnover for taxpayers who compile financial records, and for taxpayers who do not compile financial records (PricewaterhouseCoopers, 2021). The distinction was made to reduce the administrative burden on informal businesses and to improve taxpayer compliance. Haji (2015) contends that the distinction can also perpetuate the culture of poor-quality financial records or, in some instances, failing to report transactions. Taxpayers with an annual turnover of at least TZS 100

million are required to submit audited financial statements to the tax authority (PricewaterhouseCoopers, 2021).

Table 3. 3: Tanzanian Presumptive Tax Rates

(TZS)	Tax liability (Tanzanian Shillings (TZS))	
	Section 35 of the Tax Administration Act, 2015 is not complied with (i.e. taxpayer does not maintain records)	Section 35 of the Tax Administration Act, 2015 is complied with (i.e. taxpayer maintains records)
Less than 4 million	0	0
4 million to 7 million	100,000	3% of amount in excess of 4 million
7 million to 11 million	250,000	90,000 plus 3% of amount in excess of 7 million
11 million to 14 million	450,000	230,000 plus 3% of amount in excess of 11 million
14 million to 100 million	N/A	450,000 plus 3.5% of amount in excess of 14 million

Source: PricewaterhouseCoopers (2021)

3.6.3 Revenue collection trends

The following table displays the revenue collection trends for the presumptive tax in Tanzania.

Table 3. 4: Revenue Collection Trends in Tanzania

	2012/13	2013/14	2014/15	2015/16	2016/17
% of presumptive taxpayers to total Tanzania Revenue Authority taxpayers	31%	30.2%	29.2%	28.5%	27.1%
Growth rate of presumptive taxpayers	8.4%	8.0%	8.0%	8.0%	8.0%
Growth rate of total Tanzania Revenue Authority taxpayers	5.5%	10.8%	11.6%	10.5%	13.7%

% of presumptive to total individual revenue collections	43.0%	43%	46%	46%	46%
% of total individual revenues to total Tanzania Revenue	0.9%	0.9%	1.0%	1.1%	1.3%
% of presumptive revenues to total Tanzania Revenue	0.4%	0.4%	0.5%	0.5%	0.6%

Source: University of Dar Es Salaam (2018:36)

The table above indicates that in 2016/17 presumptive taxpayers constituted a significant portion (46%) of the individual taxpayers in Tanzania, which appears to be representative of the large number of people employed in the informal sector. This achievement is due to the implementation of tax compliance measures such as the BMS, tax audits and patrols (African Tax Administration Forum, 2014). Although the BMS has been successful in increasing the number of presumptive taxpayers, the presumptive tax revenue collected at 0.6% in 2016/17, and at less than 1% for the five-year period between 2012/13 to 2016/17, appears to be significantly low.

3.6.4 Administrative challenges

The results of the Tanzania Revenue Authority research (Tanzania Revenue Authority, 2011) indicate that the major challenges of administering the presumptive taxes in Tanzania include human resource capacity constraints. The report indicates that there were areas that were operating at 20% of the required capacity, which negatively influenced the quality of service provided. Another challenge highlighted in the report is the high concentration of tax functions of identification, registration, and assessment, under one tax officer, which may circumvent internal controls, increase corruption, and result in the abuse of power. The report recommends that the effective implementation of the BMS requires strengthening the human resource capacity of the TRA to allow for proper functioning of internal controls.

The African Tax Administration Forum (2014) explains that, in an attempt to increase tax revenue collections and to reduce the costs of tax collections, Tanzania launched the use of electronic fiscal devices in 2010. Through the system of electronic fiscal devices, the retailers are obliged to issue a receipt for every transaction, which is then stored in the fiscal memory of the electronic fiscal printer. The stored financial transactions increase tax administration efficiency as it becomes easier to verify the turnover generated by the enterprise. The use of electronic fiscal devices was implemented in two phases. The first phase covered VAT

registered taxpayers and the second phase covered non-VAT registered taxpayers with annual turnover ranging from 14 million Tanzanian Shillings and above.

According to a survey conducted by the University of Dar es Salaam (2018) on the effective use of electronic devices in the informal sector, 85.5% of the informal sector entrepreneurs in 2017 did not use the electronic fiscal devices and only a few participants (14.5%) were using the electronic fiscal devices. It was submitted that the results of the survey suggest that the use of modern technology to enhance tax collections in the informal sector was not yet effective (University of Dar es Salaam, 2018). This was mainly because most informal sector entrepreneurs cannot afford to acquire and maintain the high costs of operating electronic fiscal devices. Also, due to the lower level of education in the informal sector, some entrepreneurs resist the use of electronic fiscal devices as a result of misunderstanding modern technology and a high preference for manual processes. Despite these challenges, the tax administrators expect that over time the use of electronic fiscal devices will improve efficiencies in the tax collection system and improve audit outcomes.

3.7 PRESUMPTIVE TAX IN ZIMBABWE

Informal sector presumptive tax in Zimbabwe was introduced in 2005, targeting selected sectors of the economy to broaden the tax base (Zimbabwe Revenue Authority, 2021). According to Dube (2014), the introduction of informal sector taxation in Zimbabwe commenced in 2003, with research on public passenger transport operators. The research estimated the public transport operators' profits using simulations of estimated number of trips per day and fares charged. Based on the results of the research, in 2005 the Finance Minister announced the list of informal sector activities to be included in the presumptive tax schedule. Table 3.5 reveals that currently the presumptive tax schedule includes the following informal sector activities.

Table 3. 5: Informal Sector Activities in Zimbabwe

Description of informal sector activities	Applicable tax rates (Zimbabwe Dollar (ZWL))
Transport Operators' Presumptive tax	Vehicle capacity and applicable rates are included in Table 3.6 below
Informal Traders' Presumptive tax (for the receipt of rental income for residential accommodation or commercial premises)	10% of rental income
Hairdressing Salon Operator's Presumptive tax	Zimbabwean dollar (ZWL)100.00 per chair per month

Cross Boarder Traders Presumptive Tax	10% of the value for duty of commercial goods (excluding taxpayers registered for Corporate Income Tax)
Operators of Restaurants or Bottle-stores	ZWL700 per month
Cottage Industry Operators (includes furniture making, upholstery trade, metal fabrication, regardless of being licenced)	ZWL 700 per month
Commercial Waterborne Vessels (used for commercial passenger carriage and fishing rigs)	ZWL 800 per month

Source: Zimbabwe Revenue Authority (2021)

Table 3.6 below provides vehicle capacity and applicable rates at which the transport operators are taxed.

Table 3. 6: Zimbabwe Transport Operator's Presumptive Tax

Operators of:	Description	Presumptive tax (Zimbabwe Dollar (ZWL)) per month with effect from 31/12/2019)
Omnibuses	8 to 14 Passengers	400
	15 to 24 Passengers	450
	25 to 36 Passengers	700
	From 37 Passengers and above	1000
Taxi-Cabs	All	250
Driving Schools	Class 4 vehicles	1000
	Class 1 and 2 Vehicles	1300
Goods Vehicles	More than 10 tonnes but less than 20 tonnes	2000
	More than 20 tonnes	5000
	10 Tonnes or less but with combination of truck and trailers of more than 15 but less than 20 tonnes	5000
Ship, Cruiser, Boat, Houseboat, Speedboat, Canoe	Less than 5 Passengers	600
	Less than 16 Passengers	1000
	Less than 26 Passengers	2000
	Less than 50 Passengers	3500
	50 or More passengers	4500

Source: Zimbabwe Revenue Authority (2021)

3.7.1 Administration of taxes

Presumptive taxes in Zimbabwe are administered and collected by the Zimbabwe Revenue Authority (ZIMRA), except for the transport operators' tax, which since January 2015 is collected by the Zimbabwe National Roads Administration (ZIMARA) (Zimbabwe Revenue Authority, 2021). Presumptive taxes are collected through ZIMRA large taxpayer offices, as there is no small taxpayer's office dedicated to the collection of taxes for medium-size enterprises, including informal sector businesses (Dube, 2014).

3.7.2 Monitoring and enforcement

Presumptive income tax is currently enforced through the Zimbabwe Income Tax Act (2011) Chapter 23:06, read with the 26th Schedule, which places the onus on the informal sector entrepreneurs to comply voluntarily with the tax regulations (Dube, 2014). The Act also stipulates penalties for non-compliance (Zimbabwe Revenue Authority, 2021). For informal traders and public transport operators these penalties amount to 100% of the tax due (Zimbabwe Revenue Authority, 2021).

Dube (2014) explains that ZIMRA does not have proper procedures in place to monitor informal sector turnover, identify non-registered taxpayers, and enforce payments for those who are registered. Payment is mainly induced by *ad hoc* methods such as raiding for hairdressing salons and roadblocks for public transport operators, which are conducted with the assistance of the police.

Public transport operators are required to carry a tax clearance certificate as evidence of compliance (Mpofu & Mususa, 2019). Failure to produce a compliance tax clearance certificate results in a fine equal to the amount of tax payable (Zimbabwe Income Tax Act, 2011). Failure to pay taxes in time attracts interest and ultimately if taxpayers continuously fail to settle their accounts, they can face six months imprisonment (Zimbabwe Income Tax Act, 2011). Other informal businesses such as hairdressers, cross border traders and restaurant operators are asked to provide proof of payment for quarterly taxes due during the raids, and failure to provide the evidence attracts a penalty (Dube, 2014).

3.7.3 Presumptive tax revenue collection trends

The following table indicates that there has been limited success in the structural administration as well as implementation and collection of the presumptive taxes in the informal sector, as the revenue contribution of less than 1% for the period set out below is not representative of the extent of informality in Zimbabwe (Dube & Casale, 2016). Zivanai, Manyani, Hove, Chirisei and Mudzura (2014) also concur that at a 60% contribution to GDP in 2011, the informal sector in Zimbabwe has the potential to contribute more to total tax revenue.

Table 3. 7: Tax Collections in Zimbabwe

Year	Total tax revenue (\$)	Presumptive tax (\$)	Presumptive tax as a percentage of total revenue
2009	988 478 184	1 391 153,70	0.14%
2010	2 238 240 232	5 220 196,66	0.23%
2011	2 816 378 834	13 143 213,53	0.47%

Source: Dube (2014:141)

Dube (2014) explains that the significant increase in revenue in 2010 is attributable to the economic stability experienced after the dollarization in 2009, while the increase in 2011 was due to higher presumptive tax collections at the border. In anticipation of the change in legislation to ban second-hand car imports from Japan, there was an increase in imports to secure the cars before the new legislation was implemented.

The latest ZIMRA annual reports disclose presumptive tax revenue in a common grouped account described as “Other Taxes” and as a result the latest tax statistic relating to the collection of presumptive taxes are not readily available (Mpofu, 2021).

3.7.4 Taxpayer compliance challenges

The informal sector legislation categorises of informal sector activities for the purpose of levying presumptive tax, and the compliance challenges are analysed below in terms of each category.

Public transport operators’ tax

In a study assessing the impact of presumptive tax on the profitability of transport operators, Zivanai *et al.*, (2014) found that taxpayers who are non-compliant indicated that transport

operators' presumptive tax is an additional expense that hampers their business growth as they already have to pay route licences to ZINARA, radio licences and tollgate fees. Dube (2014) further elaborates that costs incurred by minibus taxis and taxi cabs, for example, include registration and licencing estimated at \$200 once-off, route authority costs at \$75 once-off, rank disc costs at \$100 (renewable per quarter), vehicle insurance at 75\$ per quarter, and passenger insurance at \$300 annually.

Zivanai *et al* (2014) further noted that some transport operators were simply not aware of how to comply with their transport operators' presumptive tax obligations. Other reasons for non-compliance included a lack of consultation with the informal sector transport associations in determining the tax rates, as well corruption and a lack of transparency by the government on how the revenue collected is used towards the development of the informal transport operators' businesses.

Cross-broader traders

Dube (2014) explains that for cross-broader traders the presumptive tax increases the costs of acquiring the inventory and ultimately the selling price. The main challenge in complying is the difficulty to compete in setting the prices, as those that have decided not to comply are able to sell similar items at a lower cost.

Hair dressing salons and cottage industries

Informal entrepreneurs in the hair dressing and cottage industry sectors interviewed were not aware of presumptive tax and also indicated that, even if they wanted to comply, given the low levels of income, they are not in a position to afford the tax (Dube, 2014).

3.7.5 Administrative and structural challenges

In addition to the taxpayer non-compliance reasons discussed above, there are the following loopholes in the structural design, implementation and administration of presumptive taxes that perpetuate the non-compliance.

Commitment to enforce presumptive taxes

Dube (2014) noted from the ZIMRA officials interviewed that there is a palpable lack of commitment to enforce the presumptive tax payments from informal sector entrepreneurs, as these officials perceive the presumptive tax rates to be too high. This lack of commitment is also evidenced by ZIMRA's failure to use available databases to detect taxpayer non-compliance, such as the list of public transport operators from the Ministry of Transport.

Lack of human resource capacity

Due to human capacity constraints ZIMRA does not have officials dedicated to the collection of presumptive tax. Officials who deal with large taxpayers are also tasked to service informal taxpayers, which results in large taxpayers taking priority over informal taxpayers in terms of tax compliance, tax education support, monitoring and evaluation (Mpofu & Mususa, 2019).

3.8 CONCLUSION

A distinguishing characteristic of informal sector businesses is their lack of proper financial record systems, which renders them difficult to tax. As a result, certain countries in sub-Saharan Africa have implemented direct income tax on the informal sector for various reasons, which include broadening the tax base and collecting more tax revenue, incentivising formalisation, fostering a culture of tax compliance, and promoting tax equity and fairness. The possibility of formalisation encompasses access to financial credit facilities. These benefits are accompanied by challenges such as high costs of administration and low revenue collection. A good tax regime for small firms is, however, a key policy tool to pave the way out of the “informality trap” of low growth, limited access to markets, and exclusion from formal financial services. Presumptive taxation is an effective tool to achieve this as it simplifies the tax compliance process and reduces the compliance cost for informal businesses. The presumptive tax models are not uniform across the countries researched.

Ghana's informal sector presumptive tax model includes a tax stamp and vehicle income tax. The tax stamp system categorises informal businesses according to size, turnover and business activity to determine the quarterly tax payable. The tax stamps must be purchased quarterly in advance and be displayed in the business premises or be carried by the taxpayers while operating their business. Challenges experienced in the implementation of the tax stamp system

include defining the parameters that determine the size of the enterprise for categorisation purposes, poor data quality hampering the monitoring regime of the system, and inefficient tax education programmes.

The vehicle income stamp requires owners to purchase a quarterly Vehicle Income Tax (VIT) sticker which is pasted on the front windscreen of the vehicle. The purchase price of the sticker is determined by the tonnage and the vehicle capacity. Compliance with the VIT stickers is monitored through the assistance of the Ghana Police Services. Challenges experienced in the implementation of VIT include shortages of the VIT stickers and long queues, which results in revenue loss for the drivers.

The determination of presumptive tax payable in Tanzania includes two taxable categories, taxpayers who maintain financial records and taxpayers who do not maintain financial records. The distinction was made to reduce the administrative burden on informal businesses and to improve taxpayer compliance. Tax compliance is implemented through the Block Management System (BMS). As part of the BMS, the Tanzania Revenue Authority allocates staff to each block, who are delegated to identify and collect presumptive taxes from eligible informal sector businesses.

The BMS closely monitors the informal business sector activities, which increases its capacity to fight tax evasion. However, challenges such as corruption and the lack of human resource capacity has affected the optimal functioning of the system. Accordingly, the government has responded to this challenge by launching the use of electronic fiscal devices, which over time are expected to improve efficiencies in the tax collection system and improve audit outcomes.

Informal sector presumptive tax in Zimbabwe is targeted at selected sectors of the economy to broaden the tax base. The applicable tax rates differ per sector. Presumptive taxes are collected through ZIMRA large taxpayer offices, as there is no small taxpayer's office dedicated to the collection of taxes for medium enterprises, including informal sector businesses. The common compliance challenges among the various tax categories include lack of taxpayer education poor structural administration, implementation, and collection of taxes.

The tax revenue collection trends in the countries forming part of the present research do not reflect significant revenue collections from presumptive taxes. According to Loeprick (2009) when informal sector taxation is considered solely from a revenue perspective, the benefits are

often overlooked. The benefit of a broader tax base in the medium to long term may not, however, offset the comparatively high cost of administering small contributors. Informal sector taxation should be seen as an entry point to formality.

The success of presumptive taxes cannot solely be evaluated by tracking revenues collected from presumptive taxes, as the impact may be noticeable in the increased culture of overall tax compliance. The presumptive tax regime should be introduced to achieve various goals, and in the short to medium term the focus should be to broaden the tax base, to eliminate the distortion arising from “free riding” taxable persons in the allocation, and access to social services.

The next chapter explains the reasons for implementing presumptive taxes in the South African context and provides recommendations for a presumptive tax model that could be adopted in South Africa.

CHAPTER FOUR: TAXING THE INFORMAL SECTOR IN SOUTH AFRICA

4.1 INTRODUCTION

Chapter 4 addresses the following goal of the research:

- recommending direct taxes that could be imposed in South Africa on the revenue generated in the informal sector.

South Africa does not have a specific income tax regime to deal with revenue generated in the informal sector (Kgatle, 2016). Currently informal business in South Africa participate indirectly in the tax system through paying Value-Added Tax (VAT), as well as import and export duties, without being registered as taxpayers. Research has noted that the indirect participation of informal businesses in the tax system effectively results in the collection of lower tax revenue than the informal business would be liable for if they were registered as taxpayers (Joshi *et al*, 2014). The non-registration of informal sector businesses in the tax system, also encourages a culture of non-tax compliance (Joshi *et al*, 2014). The selected sub-Saharan countries of Tanzania, Ghana and Zimbabwe that have been the subject of the present research, have responded to these challenges by implementing direct presumptive taxes on the revenue generated in the informal sector.

4.2 RATIONALE FOR INFORMAL SECTOR TAXATION IN SOUTH AFRICA

There are two important reasons for introducing measures to tax revenue generated in the informal sector – expanding the tax base and encouraging a culture of tax compliance.

4.2.1 Expanding the tax base

According to the National Treasury Tax Revenue Statistics (National Treasury and SARS, 2020), tax revenue collected by SARS amounted to R1 355.8 billion for the 2019/2020 fiscal year. Thirty-nine percent of the revenue was collected from Personal Income Tax, 25.6% from Value-Added Tax (VAT), 15.6% from Corporate Income Tax, and the other taxes contributed 19.2%. The number of individual taxpayers registered for personal income tax was 22.9 million for the 2019/2020 fiscal year, of whom six million individual taxpayers were expected to submit tax returns, and only 4.3 million individual taxpayers submitted tax returns, resulting in 19% of individual registered taxpayers being assessed. These tax revenue collection statistics suggest that a very small proportion of the personal income taxpayers is responsible for personal income

tax revenue collected. Therefore, bringing informal business owners into the tax net has potential to spread the tax burden across a wider spectrum (BusinessTech, 2021a).

The government has undertaken various tax reform initiatives aimed at increasing tax revenue through expanding the tax base. According to Manuel (2002), as part of this strategy, Capital Gains Tax was introduced in 2001 to capture the tax on the appreciation of all investments, which previously went wholly untaxed as the definition of “gross income” in the Income Tax Act excluded capital gains, with no specific inclusions in taxable income to cater for these gains. Manuel also explains that another reform to broaden the tax base was changing the South African tax system from a source-based system, which only taxed income from a South African source, to a residence-based system, which taxes residents on their worldwide income and non-residents on income from a South African source. Manuel also notes that the removal of tax schemes such as the use of tax-free fringe benefits, and the limitation of deductions for salaried employees, also broadened the tax base.

The tax reforms undertaken by the government in South Africa also included incentives aimed at reducing the tax burden of Small, Medium and Micro Enterprises (SMMEs) in South Africa (Davis Tax Committee, 2016). These incentives were introduced principally through the tax on Small Business Corporations, which is provided for in section 12E of the Income Tax Act, and the Turnover Tax in terms of the Sixth Schedule to the Income Tax Act (Davis Tax Committee, 2016). These tax reforms have not, however, addressed the integration of informal sector businesses into the tax system (Kgatle 2016).

4.2.2 Building a culture of tax compliance

According to the SARS Compliance Programme 2012/13-2016/17 (SARS, 2012), small businesses are a high-risk sector when it comes to tax compliance, as tax registration is particularly low within the small businesses sector. For example, for the minibus taxi industry, it was recently reported that despite generating an annual revenue of about R90 billion, SARS only collected tax revenue of R5 million from this industry for the 2019/2020 year of assessment (Claasen, 2021). The National Treasury has indicated that the lower collections are due to the majority of the minibus taxi owners in the industry declaring a nil return or having a refund due to them (Claasen, 2021). It appears that a culture of tax compliance is not present in this industry.

4.3 RECOMMENDING DIRECT TAXES ON THE INFORMAL SECTOR

Based on the approaches adopted in the selected African countries, recommendations are made for direct taxes in the informal sector.

4.3.1 Presumptive tax model

It appears from the analysis of the methods and approaches used to tax informal sector businesses in Tanzania, Ghana, and Zimbabwe, that the appropriate tax model that could be implemented in the South African informal sector is a presumptive tax model. The presumptive tax model is appealing in the South African context as it is simple to administer, resulting in low tax compliance costs for informal businesses. The low compliance cost is aligned with the SARS strategic objective, as stated in the SARS 2020/2021 Annual Report, of making tax compliance affordable and easy for SMMEs in South Africa (SARS, 2021a).

South Africa already has a presumptive tax model in the form of turnover tax which could be used to tax direct revenue generated in the informal sector.

4.3.2 Turnover tax system

In terms of Sixth Schedule to the Income Tax Act, turnover tax is a simplified tax system for micro businesses with a qualifying turnover of not more than R1 million per annum, where turnover tax takes the place of VAT, provisional tax, income tax, capital gains tax, and dividends tax. Under the turnover tax system, qualifying businesses pay a single tax instead of various other taxes. Turnover tax is available to sole proprietors (natural persons), companies, close corporations, partnerships, and co-operatives that qualify and elect to register as a micro business.

Where the SMME has registered as a micro business it is taxed according to the tax rates reflected in Table 4.1 below, based on the level of turnover for the years of assessment between 1 March 2021 and 28 February 2022.

Table 4. 1: Turnover Tax Rates

Turnover (R)	Rate of tax (R)
0 – 335 000	0%
335 001 – 500 000	1% of each 1 above 335 000
500 001 – 750 000	1 650 + 2% of the amount above 500 000
750 001 and above	6 650 + 3% of the amount above 750 000

Source: SARS (2021b: Online)

4.3.3 Incorporating the informal sector into the turnover tax system

The turnover tax system is a suitable measure to tax the informal sector business, for several reasons.

Reducing the tax administrative burden

According to Alabede, Zaimoh, and Kamil (2011), the choice to pay tax or remain untaxed in the informal sector is simple for many small entrepreneurs in Africa, considering the tax compliance costs both financially and in time. These entrepreneurs choose to remain in the informal sector. It is therefore imperative to provide for an informal sector tax policy tool to reduce the tax compliance costs. In South Africa the turnover tax system is suitably designed to address this need.

The turnover tax system requires taxpayers to comply with only one simplified tax that replaces, *inter alia*, VAT and provisional tax. This aspect of the design of turnover tax is important in order to encourage informal businesses to register for tax, as it resolves the complexities of complying with more than one form of tax. Using one simplified tax reduces tax compliance costs as, for example, the taxpayer does not need to incur costs to comply with VAT and income tax; this is incorporated under one system.

The simplified tax approach is appropriate for informal businesses as most informal business owners lack formal education and financial expertise, and do not have sufficient financial resources to outsource their tax compliance requirements. It was noted in chapter 2 that low levels of education are one of the reasons for the existence of the informal sector in South Africa. Sixty-seven percent of the participants running their own businesses who were

interviewed in the Survey of the Employers and the Self Employed, had less than matric as their highest qualification, and 30.9% had matric and other higher education qualification (Statistics South Africa, 2017).

Paragraph 14 of the Sixth Schedule of the Income Tax Act reduces the requirement to maintain accounting records to only recording amounts received, dividends declared, a list of assets with a cost price of more than R10,000, and liabilities exceeding R10,000 at the end of the year of assessment. Informal sector businesses are not set up as companies, as this would require registration, and would therefore not be declaring dividends. Very few of these businesses are likely to own assets with a cost price of R10 000 or more, or have liabilities exceeding R10 000 at the end of the year of assessment.

The simplified record keeping requirement is therefore appropriately structured to benefit the informal sector as it does not require informal business owners to incur the cost of outsourcing to accountants to prepare financial statements. It is also acknowledged in the Davis Tax Committee Report (Davis Tax Committee, 2014), that the turnover tax system is an important component of the tax dispensation for SMMEs due to its major benefit of reducing the administrative and compliance burden to make tax compliance easier.

No formal registration required

Turnover tax is a simplified tax system aimed at micro businesses. According to paragraph 2 of the Sixth Schedule to the Income Tax Act, a micro business includes a natural person. This requirement makes the turnover tax system appealing for the informal sector as it is characterised by natural persons who operate unregistered businesses and who will therefore be able to participate in the tax system without formally having to register their businesses with the Companies and Intellectual Property Commission (CIPC).

Flexibility to accommodate business growth

One of the benefits of turnover tax is that it replaces VAT, however taxpayers are not prohibited from registering for VAT. Where a business is generating income of more than R50 000 within a 12-month consecutive period, a voluntary registration for VAT purposes is permitted (SARS, 2021b). The relevance of this for informal businesses is that the turnover tax system provides the flexibility to promote business growth and provides an opportunity for informal businesses

to prepare to graduate into the standard tax system by registering for VAT, while still within the constraints of the turnover tax requirement of generating qualifying turnover of not more than R1 million per annum. To the extent that informal businesses are interested in formalising, they will still have an opportunity to enjoy the benefits of turnover tax as persons that qualify as micro businesses also include companies (paragraph 2 of the Sixth Schedule to the Income Tax Act).

Another element that is incorporated in the design of the turnover tax system to accommodate business growth is allowing micro business owners to participate in a partnership. This flexibility establishes an environment in which informal business owners are not constrained by a tax regime to explore growth opportunities beyond sole proprietorship. Informal business owners will be able to enjoy this benefit to the extent that the qualifying turnover of the partnership does not exceed R1 million and provided the partner is not a partner in more than one partnership during the year of assessment (paragraph 3(g) of the Sixth Schedule to the Income Tax Act). The Davis Tax Committee (2016) also supports the view that SMMEs should be permitted to make use of any business structure when it makes sound sense to do so in the pursuit of a commercial justification, without experiencing adverse tax implications.

Exclusions from turnover tax

The Sixth Schedule to the Income Tax Act lists different circumstances where persons do not qualify to register as micro businesses:

- where more than 20 percent of the natural person's total receipts during the year of assessment consists of income from the rendering of a professional service (paragraph 3(b)(i));
- where persons are members of more than one partnership during the year of assessment, and where the qualifying turnover of a partnership exceeds R1 million (paragraph 3(g)); and
- persons providing professional services (paragraph 3(b)(ii)).

These requirements are not prohibitive for the informal businesses as informal businesses seldom undertake the listed business activities. For example, in chapter 2 it was noted that only 7% of informal businesses are in the professional services sector. Generally, it does not appear

that the exclusions in the Sixth Schedule to the Income Tax Act compromise the potential of the turnover tax system to integrate the informal sector into the tax base.

4.4. TURNOVER TAX STRUCTURAL CHALLENGES

Despite the above-mentioned benefits of the turnover tax system, which strategically positions it as a suitable taxation tool to integrate the informal sector into the tax base, there are structural challenges that need to be addressed for the system to be effective and achieve the intended purpose. These challenges are discussed below.

4.4.1 High exemption threshold

The turnover tax system has a high exemption threshold, where turnover below R335 000 is exempt. This high exemption threshold may potentially result in a nil tax liability for most informal sector businesses, as it was noted in chapter 2 that turnover generated in the South African informal sectors is not generally high. However, to ensure that all informal sector businesses are registered for tax purposes, the turnover tax system is ideal, as many of these registered businesses may later start to generate a higher turnover. A taxation model used to tax informal sector businesses will not be effective in addressing its objectives if it still leaves a large number of informal businesses outside the tax net (Prichard, 2010). To improve the effective use of turnover tax and to integrate the informal sector businesses into the tax base, certain recommendations are made in section 4.5 below.

4.4.2 Interim payments

Paragraph 11(1) of the Sixth Schedule requires taxpayers registered under the turnover tax system to estimate taxable turnover for the year of assessment and pay 50% of the amount calculated within six months of the first day of the year of assessment, which is similar to the requirements of the provisional tax system in the standard income tax system. Non-compliance with this requirement in the form of late submission of the interim return, late payment, and the understatement of turnover, attract interest and penalties.

The Davis Tax Committee (2014) noted that the requirement for an interim payment is confusing and increases the administrative burden and compliance costs for the taxpayer. The interim payment requirement in its current form is not conducive to the integration of informal sector businesses into the tax base.

4.5 RECOMMENDED MEASURES TO TAX THE INFORMAL SECTOR

In this section of the thesis, recommendations are made to improve the uptake of the turnover tax system by informal sector businesses. Based on the research on presumptive taxes in Ghana, Tanzania and Zimbabwe, and the similar problems faced in South Africa, a number of other recommendations are also made to tax the informal sector.

4.5.1 Changes to the turnover tax system

As informal sector businesses with a turnover of less than R335 000 (in terms of the 2021-2022 tax rates) would not be liable for tax and would not carry on their businesses in the form of a company, this makes the turnover tax system ideal for these businesses. They would, however, need to register with SARS for turnover tax and keep the records necessary to determine their turnover for the year of assessment, and formally declare that they do not have assets with a cost price of more than R10 000 and liabilities exceeding R10 000 at the end of the year of assessment. This would require the simplest bookkeeping system. The advantage of this is that when these businesses begin to earn turnover exceeding the threshold, they would become liable for tax.

At a maximum marginal rate of tax of 3% (refer to Table 4.1), removing the requirement to make an interim payment would make very little difference to tax collections. Deleting this requirement from the Sixth Schedule to the Income Tax Act would be one measure that could make the turnover tax system more attractive to informal sector operators with a turnover of more than R335 000.

Informal sector businesses with a turnover of more than the threshold rate would be liable for the turnover tax. The problem with the turnover tax system is that it does not take account of expenditure or tax allowances. This would mean that many businesses would be liable for the tax that have made very little profit, or even generate a loss. A possible amendment could be suggested, allowing businesses that keep the necessary records and have a turnover not exceeding R1 million to base their tax liability on their profit. In terms of the 2021-2022 normal rates of tax, the threshold at which tax becomes payable for individuals (who are not yet 65 years old) at the rate of 18% on taxable income, is R87 300. The turnover tax system would therefore be attractive to these business owners.

A further recommendation is that the upper turnover limit of R1 million could be adjusted annually in line with inflation. This, coupled with the other recommended changes, would draw more micro businesses into the tax net.

A distinguishing characteristic of the informal sector is non-registration with SARS. The Davis Tax Committee report (2016) contends that the fear of arrear taxation claims is a major cause of non-registration by SMMEs. To alleviate the fear of arrear tax liabilities, informal sector businesses that were previously not registered for tax and would qualify for Turnover Tax, could be provided with a temporary tax amnesty on the basis that they voluntarily register with SARS within the period stipulated in a tax amnesty. The tax amnesty could forgive arrear tax liabilities. A critical benefit of a voluntary disclosure programme is that it may lead to an increase in revenue collection (Rukundo, 2020). It is estimated that since 2009 voluntary disclosure programmes in 40 jurisdictions resulted in the collection of an additional €102 billion in tax revenue (Rukundo, 2020).

To promote registration with SARS and the turnover tax system, a dedicated campaign would need to be launched to raise awareness of the benefits of the system. A taxpayer education programme could be provided by SARS, both online and in person and this could be linked with the Block Management System (see below) to target areas where informal businesses are found.

4.5.2 Tax stamps

Taking lessons from the Ghana's informal sector taxation system, an alternative approach aimed at satisfying the tax compliance requirements for informal sector businesses in South Africa could be the tax stamp system approach. This requirement could be extended to all informal sector businesses that do not register for Turnover Tax in terms of the Sixth Schedule to the Act. This recommendation is intended to allow the informal business owners to contribute to tax revenue with absolute minimum compliance burden.

Under the tax stamp system informal businesses that are not registered for Turnover Tax, will be required to purchase a tax stamp as a way of discharging their tax obligation. The tax stamp targets informal businesses in the trade, services, manufacturing, and construction industry, excluding informal transport operators. Informal transport operators can be accommodated

under a different system due to the uniqueness of their business model. The tax stamp must be purchased annually in advance and be displayed in the business premises or be carried by the taxpayer while operating their business. The tax stamp approach is appealing in the South African context due to the required visibility of the stamps that enhances the facilitation of tax compliance.

Determining the tax payable

To calculate realistic purchase prices for the tax stamps for each type of informal business, it is important to consider the levels of income of the businesses, and the difference in the nature of business activities within the trade, services, manufacturing, and construction informal sectors. To accommodate this, it would be suitable for South Africa to consider the approach applied in Zimbabwe, where informal businesses were categorised by the nature of business activity to determine the tax payable. For example, the number of chairs in a hair dressing salon and the number of rooms in a guest house indicate the businesses' revenue generation capacity. Other indicators in manufacturing and construction industries include the number of employees of the business. A fixed percentage of turnover could be applied where other revenue drivers cannot be used.

The process of determining the tax payable is challenging and requires research and an extensive consultation process. The tax payable must be determined in consultation with the relevant stakeholders and other civil society organisations, and the tax must be consistently applied. It must be affordable and must not financially hinder the growth of informal businesses. Non-participation of informal sector businesses and associations in setting taxes can result in a low level of tax compliance.

Taxpayer identification

Due to non-registration with the relevant authorities, the informal sector is often outside the purview of government and the tax authorities (Joshi *et al*, 2014). The successful integration of the informal business sector into the tax base therefore requires a mechanism that can be used to identify the informal sector businesses. It is recommended that South Africa could use the Block Management System (BMS) to identify informal sector businesses that need to be registered for tax. A BMS is a system that was implemented by Tanzania in its presumptive tax model to map informal businesses on a geographical basis, where a combination of a few streets or trading areas forms a block (Joshi *et al*, 2014).

A BMS in South Africa could perform the administrative function of registering taxpayers, assessing the annual tax payable and collecting the tax payable (Joshi *et al*, 2014). The BMS teams could be responsible for selling the tax stamps, which could be printed by the Government Printer. Each tax stamp could be allocated a unique tax number and have a print style that cannot be easily duplicated. Social media platforms should also be used to identify eligible taxpayers as many businesses now operate profitably without having a physical location. The tax stamps could also be displayed on the online platforms for the informal businesses that operate online.

The BMS is an attractive model due to its capacity to fight tax evasion. This unique capacity comes from the structural design of the system, which enhances its ability to closely monitor the informal business sector activities (Haji, 2015).

In Tanzania the BMS function was set up within the Tanzanian Revenue Authority (Tanzania Revenue Authority, 2011). Despite the strategic set up of the BMS with its inherent potential to broaden the tax base, it was noted in chapter 3 that the optimal utilisation and the effective implementation of the system was hindered by human resource capacity constraints (Tanzania Revenue Authority, 2011).

Institutional framework

In South Africa, SARS is in the process of building its human resource capacity to service the existing revenue collection streams (Arnoldi, 2021). Thus, there is a risk that setting up the BMS function within SARS will over-burden the system and interfere with optimal utilisation and effective implementation, in a way similar to the challenges experienced in Tanzania. It is therefore recommended that to address these challenges in South Africa, the BMS could be outsourced to local governments. Within the local government sphere the set-up of the BMS function should be delegated to municipalities that will execute all the tax administration functions.

According to Joshi *et al* (2014) the strategy of ceding the responsibility for the collection of taxes from the informal sector to local government has been used in Ethiopia. Bodin and Koukpaizan, 2008 (cited in Joshi *et al*, 2014:1340) explain that the benefits of ceding tax collection responsibility to local governments are the following:

- local governments have a greater need of resources, and will have stronger incentives to pursue taxation in the informal economy;
- tax collection will be closer to, and thus responsive to, local conditions;
- local governments are better placed to negotiate productively with informal sector actors...

The State of City Finances Report (Mahlalela, Msomi, & Walsh, 2020) explains that South African cities are increasingly finding it difficult to raise sufficient revenue to deliver basic services according to their mandates, mainly due to the deteriorating macro-economic conditions. The report notes that although cities can improve their fiscal effort through expenditure efficiencies, the deteriorating macro-economic conditions have negatively affected their capacity to raise additional revenue. The need for cities in South Africa to raise additional revenue provides them with an incentive to pursue taxation in the informal economy.

In South Africa the local government's ability to achieve service delivery goals is also hindered by financial mismanagement (Mahlalela *et al*, 2020). Stringent accountability and transparency controls are required to mitigate the challenges of financial mismanagement. It is therefore recommended that the transparency should be in the form of earmarking revenue collected from the informal sector presumptive tax to improve infrastructure and the provision of basic services in the areas where the informal sectors operate. Most taxpayers experience the benefits of taxation at the local level and therefore earmarking informal sector tax revenue to finance local developments has potential to build public support for informal sector taxation (Prichard, 2010).

According to Alabede *et al* (2011), taxpayer compliance in the informal sector is a function of the perceived quality of service delivery. If taxpayers perceive that the quality of services meet their expectations, their compliance rate is high, and if not, their compliance rate is low. A similar pattern was also observed in Guinea where Korsun and Meagher 2004, (cited in Joshi *et al*, 2014:1340), found that "the collection of market taxes doubled after they were linked explicitly to construction of new market facilities". Other measures that can be enforced to promote transparency measures includes publishing tax statistics information explicitly linking tax collection to public expenditure by location and purpose (Prichard, 2010).

Monitoring and compliance

Similar to the process followed in Tanzania, the BMS could map informal businesses on a geographical basis where a combination of a few streets or trading areas forms a block. Online businesses could be grouped together under a separate block. Each block team should be assigned a manager who takes responsibility for the performance of the team. For performance management purposes each team should be allocated revenue collection targets and other non-financial key performance indicators could be used, such as satisfaction surveys to ensure that harassment is not used by the officials in the tax revenue collection processes to meet revenue collection targets (Joshi *et al*, 2014).

The block team should have sufficient human resource capacity to allow for the proper functioning of segregation of duties as a way of preventing corruption. The block teams should perform site verifications of the tax stamp, and a tax compliance certificate as evidence of compliance with turnover tax should be requested. This interaction with taxpayers can also be used as an opportunity to provide tax education.

The quality of the data collected during the monitoring process enhances the monitoring regime in the long run. In Ghana it was noted that the poor quality of data collection hampers the monitoring regime of the system in the long run, as the changes in the size of the informal businesses were not tracked to identify when the categorization should change, or when the businesses have met the requirements to register under the normal income tax regime (African Tax Administration Forum, 2014). In this regard it is recommended that an information technology strategic plan should be developed with appropriate applications designed to ensure that the database of informal businesses is constantly updated. The use of technological payments systems in the informal sector should also be encouraged to phase out the cash payments. as the use of digital payment systems simplify financial record keeping in a business (BusinessTech, 2021a).

4.5.3 Vehicle income tax system

The recommendations above focused on the integration of informal businesses in the trade, services, manufacturing, and construction informal sectors. The integration of the transport informal sector is addressed below.

SARS's investigation into the high level of non-tax compliance noted in the minibus taxi industry revealed that minibus taxi owners are not declaring taxable income in their corporate income returns or they are incorrectly having a refund due to them (Claasen, 2021). This is an indication that an alternative tax regime is required to address the challenges of levying direct income taxes on revenue generated in the minibus taxi industry. The lesson learnt from the literature review of the presumptive tax models introduced in Ghana, and Zimbabwe is that a specific presumptive tax regime designed for the minibus taxi industry can foster compliance.

The literature review in chapter 2 revealed that the informal transport industry represented 7% of the informal businesses in South Africa in 2014 (Statistics South Africa, 2015). Although the size of this industry appears small, the estimated annual income generated in this sector of R90 billion is significant (Claasen, 2021). The minibus taxi industry also appears to be profitable with estimated operator profits of R25 000 a month for shorter distances in Johannesburg and R37 000 for longer trips between Durban and Johannesburg (BusinessTech, 2021b). It is recommended that South African could adopt a similar approach to the Vehicle Income Tax system (VIT) system used in Ghana. In Ghana the vehicle income tax stamp tax is designed to collect tax from commercial vehicle owners who are required to purchase a quarterly VIT sticker, which is pasted on the front windscreen of the vehicle. The purchase price of the sticker is determined by the tonnage and the vehicle capacity.

In South Africa the vehicle tax regime could be adopted as a minibus taxi income tax to focus on the minibus taxi industry to encourage income tax compliance in this sector. The minibus taxis in South Africa are the largest and most commonly used form of transport, with the number of minibus taxis estimated at 250 000, completing 15 million daily trips for about 69% of the households (Transaction Capital, 2020). Similar to the VIT system in Ghana, under the minibus taxi tax system, minibus taxi operators should be required to purchase an annual minibus taxi tax sticker to be displayed on the front windscreen of the minibus.

Institutional framework

SARS has previously adopted a number of targeted interventions to encourage voluntary tax compliance in the taxi industry, including the Small Business Tax Amnesty that was introduced in 2006 (Rukundo, 2020). The amnesty was introduced to deal with the non-tax compliance in the taxi industry, which, due to its informal nature, remained outside the tax base despite being valued as a multi-billion-rand industry (Rukundo, 2020). Due to the lower tax revenue collected

from minibus taxis and the lack of human resource capacity at SARS it is recommended that the collection of minibus taxi income tax could be outsourced to the Department of Transport in South Africa.

The Department of Transport has sufficient information in relation to the minibus taxi operations obtained during the operating license issue and renewal processes. An operating license provides authority for the use of a road-based public transport service (Department of Transport, 2021). The information obtained by the Department of Transport during this process includes identity documents of the vehicle owner and the registration certificate of the vehicle (Department of Transport, 2021). This information can be used to compile a database of minibus taxi drivers who are liable for minibus taxi tax, and it can also be used to identify minibus taxis that are non-tax compliant during the compliance monitoring process.

Currently the control in place used by the Department of Transport to ensure that minibus taxi drivers are tax compliant is to require a tax clearance certificate as part of the supporting documents required for the application of issuing or renewing an operating license. However, this control does not prevent minibus taxi owners from escaping tax liability as a tax clearance certificate can be obtained in instances where the minibus taxi owner has duly submitted an income tax return, but incorrectly declared a nil taxable income in the income tax return.

Structural implementation

The functions of the Department of Transport through the Road Traffic Management Corporation agency could be extended to include the mandate to print and sell the minibus taxi tax stickers as a way of collecting income tax from the taxi drivers. The Road Traffic Management Corporation is a corporation established within the Department of Transport for the provision of road traffic service, including safety, security, discipline, and mobility on the roads, as well the protection of roads infrastructure (Road Traffic Management Corporation Act, 20 of 1999).

The Road Traffic Management Corporation is suitably positioned to collect income tax from minibus taxi drivers due to its vehicle licensing platforms that provide an opportunity for interaction with minibus taxi drivers. The vehicle licensing platforms include traffic departments, post offices and specific supermarkets where vehicle licensing discs can be purchased annually (Department of Transport, 2021). These platforms are appropriately

positioned to sell minibus taxi tax stickers, due to the ease of access and the mandatory annual interaction that has already been established with the minibus taxi drivers. The purchase date of the minibus taxi sticker should be aligned with the renewal date of the vehicle licenses and minibus taxi drivers should be required to have a valid tax sticker prior to renewing their vehicle licenses.

Determining the tax payable

The purchase price of the minibus taxi tax stickers should be determined by the minibus taxi capacity. The profitability of minibus taxi routes and operational locations should be factored into determining the purchase price. For example, minibus taxis that operate in rural areas may not achieve profits similar to minibus taxis operating in urban areas. The purchase price should be determined in consultation with minibus taxi drivers through key stakeholders such as the South African National Taxi Association and other taxi associations.

The latest technological developments could also be used to gather relevant data to provide accurate profitability estimations in the minibus taxi industry. Research on attractive methods for tracking minibus taxis in South Africa for public transport regulatory purposes that was carried out by Van Zyl and Labuschagne (2008) indicated that technological developments such as passenger counting software, GPS tracking and LCD monitor linked security cameras can provide useful information, such as minibus taxi route adherence, as well as disclosing the average number of passengers transported per day for profitability estimation purposes. In this research a pilot programme was run on ten taxis in the Western Cape, where the operational effectiveness of the technological equipment was tested, as well as the willingness of the taxi drivers and owners to be regulated. It was noted that the use of the LCD screens can generate additional income for taxi owners through paid advertising. It was emphasized that taxi drivers and owners are entrepreneurs and were willing to be regulated to the extent that they could also benefit from the regulation process.

Electronic fare collection systems such as the fairpay system could also be leveraged to provide a reliable profitability estimation in the minibus taxi industry. Fairpay is an electronic fare collection system that was piloted in Pretoria by the Gauteng Department of Roads and Transport to allow commuters to load cash into a fairpay card that uses the same technology as chip bank cards (Shezi, 2016). The commuters settle the taxi fare by scanning their fairpay cards when entering the taxi (Shezi, 2016).

Monitoring and enforcement

The Road Traffic Management Corporation has metropolitan police departments that, among other responsibilities, enforce compliance with road traffic regulations (Department of Transport, 2021). The metro police are suitably positioned to ensure compliance with the minibus taxi tax sticker due to their visibility on the roads, which will provide them with an opportunity to check whether a valid minibus tax sticker is visible on the minibus taxis. Fines could be issued by the metro police for non-tax compliance.

Apart from the regular spot checks of the minibus taxi tax sticker, compliance could be encouraged by earmarking the income tax revenue collected for the development of the taxi industry. A lesson learnt in Zimbabwe was that the lack of compliance with the transport operators' tax was attributed *inter alia* to the lack of consultation with the informal sector transport associations in determining the tax rates, as well as the lack of transparency on the part of the government regarding how the revenue collected was used to develop the informal transport operators' businesses (Zivanai *et al*, 2014).

It is recommended that the minibus income tax revenue collected should be used for the development of road infrastructure in South Africa, including taxi rank infrastructure for the benefit of taxi owners and the public. Minibus taxi owners should also be consulted to identify how they would prefer to benefit from the minibus taxi tax revenue collected. The choice of whether or not to pay tax is often a function of cost-benefit analysis, therefore in encouraging compliance it is essential that taxpayers understand how they will benefit from paying tax (Pfister, 2009).

4.6 GENERAL RECOMMENDATIONS

Apart from the design and implementation of the presumptive tax models, there are a number of other actions pertinent to the success of an informal sector tax regime that South Africa should take into consideration in developing its models.

4.6.1 Government support

The implementation of informal sector taxation requires government support, despite the potential political conflict that could arise from taxing the informal sector, which in most cases

includes most of the voters (Joshi *et al*, 2014). In Ghana, the successful implementation of the tax stamps was enabled by the strong support from the national government in enacting legislation that allowed for the funding of the tax stamp system by the revenue authority, even when the implementation affected a politically sensitive group (African Tax Administration Forum, 2014).

The South African government would need to allocate sufficient funds to ensure that the costs of developing and operating the systems recommended, together with publicising the systems and providing the necessary education for informal sector operators.

4.6.2 Taxpayer education

In all the countries forming part of this research a positive relationship was noted between taxpayer education and tax compliance, where lack of tax knowledge was cited as a reason for non-tax compliance. Education has a chance of improving the individual's understanding of the importance of paying tax to the government; accordingly, tax education should be vigorously pursued (Joshi *et al*, 2014).

4.7 CONCLUSION

South Africa does not have a specific income tax regime dealing with tax revenue generated in the informal sector (Kgatlé, 2016). The government has taken various tax reform initiatives aimed at increasing tax revenue through expanding the tax base. These tax reforms include small-business tax-relief initiatives, such as the introduction of a turnover tax (in the Sixth Schedule to the Income Tax Act) and Small Business Corporation taxation (in section 12E of the Income Tax Act). These reforms have, however, not addressed the integration of informal sector businesses into the tax system.

The lessons learnt from the literature review of the presumptive tax models introduced in Tanzania, Ghana, and Zimbabwe suggest that a presumptive tax model is an appropriate tax model that could be implemented in the South African informal business sector. South Africa already has a presumptive tax model in the form of turnover tax that could be used to tax revenue generated in the informal sector.

The turnover tax system is an important component of the tax dispensation for SMMEs due to its major benefit of reducing the administrative and compliance burden to make tax compliance

easier. Despite these benefits, there are challenges that require attention for the system to be effective and achieve the intended purpose of integrating the informal sector into the tax base. Recommendations were made for the removal of the interim tax payment, taking account of expenditure and tax allowances, adjusting the upper turnover limit of R1 million annually in line with inflation, and providing a tax amnesty for unregistered informal sector business owners.

The turnover tax system has a high exemption threshold where turnover below R335 000 is exempt. This higher exemption threshold may potentially result in a nil tax liability for most informal sector businesses. A taxation model used to tax informal sector businesses will not be effective if it still leaves a large number of informal businesses outside the tax net (Prichard, 2010). Therefore, a recommendation has been made for informal sector operators to have the option to be subject to the turnover tax system, or alternative tax measures. Taking lessons from the informal sector taxation system in Ghana, an alternative approach aimed at satisfying the tax compliance requirements for informal sector businesses in South Africa could be the tax stamp system approach.

Under the tax stamp system informal businesses will be required to purchase a tax stamp as a way of discharging their tax obligation. The tax stamp must be purchased annually in advance and be displayed in the business premises or be carried by the taxpayer while operating their business. The tax stamp approach is appealing in the South African context due to the required visibility of the stamps that enhances the facilitation of tax compliance.

Due to non-registration with the relevant authorities the informal sector is often outside the purview of government and the tax authorities (Joshi *et al*, 2014). It is recommended that South Africa should implement a BMS as a tool to identify and register informal businesses for presumptive tax. The BMS could map informal businesses on a geographical basis where a combination of a few streets or trading areas forms a block, and online businesses could form another block. The BMS is an attractive model due to its capacity to closely monitor the informal business sector activities and fight tax evasion. The BMS in South Africa could perform the administrative function of registering taxpayers, assessing the annual tax payable and collecting the tax payable.

To avert the challenges of lack of human resource capacity in SARS to execute the BMS functions, it is recommended that the collection of tax through the BMS could be outsourced to

municipalities. The benefits of ceding informal sector tax collection to local government is that local governments are financially constrained and will be motivated to pursue informal sector taxation in return for raising additional revenue. Local governments are located close to the informal sector and able to understand the nature of business and negotiate the appropriate tax rate (Joshi *et al*, 2014).

In South Africa the local government's ability to achieve service delivery goals is also hindered by financial mismanagement (State of City Finance Report, 2020). It is recommended that, to increase taxpayer compliance and to mitigate the challenge of financial mismanagement, stringent transparency controls should be applied. Transparency could be in a form of earmarking revenue collected from the informal sector presumptive tax to improve infrastructure and the provision of basic services where the informal sectors operate.

SARS's investigation into the high level of non-tax compliance noted in the minibus taxi industry revealed that minibus taxi owners are not declaring taxable income in their corporate income returns, or they are incorrectly having a refund due to them (Claasen, 2021). It is recommended that a specific presumptive tax regime designed for the minibus taxi industry in the form of vehicle income tax could promote compliance. Minibus taxi drivers could be required to purchase a minibus taxi tax sticker annually that is displayed in the windscreen of the minibus taxi. The purchase and term of the minibus income tax sticker could be aligned with the renewal of the vehicle license disc and be sold at a similar location. Minibus taxi operators should be required to discharge their tax liabilities prior to renewing their vehicle licenses

Ceding the collection of the vehicle tax to the Department of Transport will enhance taxpayer compliance due to the interaction platforms that the department already has with the minibus taxi drivers, and the department already has metro police officers who can assist in enforcing compliance. The purchase price of the minibus taxi tax stickers should be determined by the minibus taxi capacity. The profitability of minibus taxi routes and operational locations should be factored into determining the purchase price, and the purchase price should be determined in consultation with the minibus taxi drivers through the South African National Tax Association, or other taxi associations. The latest technological developments could also be used to gather relevant data that can provide accurate profitability estimations in the minibus taxi industry.

It is recommended that to increase taxpayer compliance, minibus taxi tax revenue could be used for the development of road infrastructure in South Africa, including taxi rank infrastructure for the benefit of taxi owners and the public. The choice of whether or not to pay tax is a function of a cost-benefit analysis, therefore in encouraging compliance it is essential that taxpayers understand how they will benefit from paying tax (Pfister, 2009).

The implementation of informal sector taxation requires government support, despite the potential political conflict of taxing the informal sector, which in most cases includes most of the voters (Joshi *et al*, 2014). Furthermore, tax education should be vigorously pursued to educate the taxpayers about their tax obligations and the benefits of tax compliance.

The next chapter provides an overall conclusion and the summary of how the research objectives were achieved.

CHAPTER FIVE: CONCLUSION

5.1 INTRODUCTION

Joshi *et al* (2014) explain that most informal sector businesses in developing countries participate indirectly in the tax system through paying Value-Added Tax (VAT), as well as import and export duties, without being registered as taxpayers. This effectively results in the collection of lower tax revenue than the informal business would be liable for if they were registered as taxpayers. Additionally, the non-registration of informal sector businesses in the tax system perpetuates a culture of non-tax compliance.

Countries have responded to this challenge by imposing direct taxes on revenue generated in the informal sector. This thesis discussed the informal sector taxation regimes adopted in Tanzania, Ghana and Zimbabwe, with the aim of identifying direct taxes that could be imposed in South Africa on the revenues generated in the informal sector.

5.2 REVIEW OF THE RESEARCH FINDINGS

The overall goal of this research was to determine the nature of direct taxes that could be imposed in South Africa on the revenues generated in the informal sector, taking lessons from the sub-Saharan countries of Tanzania, Ghana and Zimbabwe. To achieve this main goal the research was guided by the following sub-goals:

- understanding the informal sector in South Africa and the countries forming part of the research – how the informal sector is defined, causes of informality and the estimated sizes of the informal sectors;
- analysing the methods and approaches used to tax informal sector businesses in Tanzania, Ghana and Zimbabwe;
- identifying the challenges and benefits of direct income taxation on the informal sector; and
- recommending direct taxes that could be imposed in South Africa on the revenues generated in the informal sector

5.2.1 The first research objective

The first research objective was to understand the informal sector in South Africa and the countries involved in the research. Chapter 2 focused on this objective. The literature review revealed that the definition of the informal sector varies between countries. A common definition of the informal sector in developing countries includes entities that participate in the economic activities of a country without registering with the relevant authorities (OECD, 2019). According to the international standards adopted by the 15th International Conference of Labour Statisticians, “the informal sector is a subset of unincorporated enterprises not constituted as a separate legal entity independently of their owners” (OECD, 2019:12). For the purposes of the present research, the informal sector includes market activities that would contribute to GDP if they were recorded, and excludes illegal activities and goods produced for household consumption.

Despite the difficulties and complexities of measuring the size of the informal sector, researchers have developed a wide range of estimation methods and tools to estimate and capture the size of the informal sector. The informal sector in Zimbabwe contributed 60.6% to GDP between 1991 and 2015 (Medina & Schneider, 2018). The informal workforce in Zimbabwe is estimated to be 85% of the total workforce (Kedem, 2020). Zimbabwe’s informal sector is driven by high unemployment and poor economic growth.

Research conducted by the World Bank (Ohnsorge & Yu, 2021) indicates that the contribution of the informal sector in Tanzania was estimated to be 50% of the GDP for the period between 2010 and 2018. The informal workforce in Tanzania is estimated to be 31.2% of the total workforce (National Bureau of Statistics, 2015). The significant industry in the Tanzanian informal sector is the wholesale and retail industry, which accounts for 47.9% of the people engaged in the informal sector. The causes of the informal sector in Tanzania include unemployment, lack of access to start-up capital, and restrictive government regulations.

The size of the informal sector in Ghana, measured by the percentage of employment, in 2015, was estimated at 90% of the employed population (Ghana Statistical Service, 2016). The significant industries in the informal sector are mainly forestry and fishing, at 37.5%, and the wholesale and retail industry at 31.3% (Ghana Statistical Service, 2016). The causes of the informal sector in Ghana include restrictive government regulations, low levels of education, and a lack of confidence in the banking system.

In South Africa the dominant informal sector businesses are in the trade sector, which in 2014 constituted 43,5% of the market share, and the services sector, which constituted 16,4% (Statistics South Africa, 2015). Christensen (2020) explains that, in South Africa, revenues in the informal sector are generated from various lawful activities, for example, the African traditional “muti” market is estimated to be worth between R3 billion and R6 billion, spaza shop contributions are estimated to be worth R100 billion to R200 billion annually, and the township fast-food market is worth an estimated R80 billion per year. The share of informal sector total employment in 2019 was estimated at 20% (Statistics South Africa, 2019).

The results of the informal business owners’ interviews documented in the book, *KasiNomic Revolution*, indicated that there are highly profitable informal businesses in South Africa, and although these businesses do not represent the majority of the informal businesses, they represent a sizeable proportion, which could be one in every four businesses (Alcock, 2018). The data collected in the Gender Series Volume V11: Informal Economy 2013-2019 (Statistics South Africa, 2020) revealed that 17.2% of the informal business owners generated a monthly turnover greater than R6 000 in 2017. The causes of the informal sector in South Africa include low levels of education, structural constraints and regulatory burdens.

5.2.2 The second and third research objectives

The second and third objectives were to analyse the methods and approaches used to tax informal sector businesses in Tanzania, Ghana and Zimbabwe, and identify the challenges and benefits of direct income taxation on the informal sector. Chapter 3 dealt with these objectives. It was established that the benefits of direct income tax in the informal sector include formalisation, tax incentives, promoting a culture of tax compliance, and contributing to horizontal and vertical equity. These benefits were, however, accompanied by challenges such as regressivity and an adverse cost-benefit analysis on the part of informal business owners.

This chapter established that the method used to tax informal sector businesses in Tanzania, Ghana and Zimbabwe is a presumptive tax model. This method was adopted as it is simple and reduced tax compliance costs and is effective in bringing informal businesses into the tax net that would have otherwise remained invisible to the tax authorities. The presumptive taxes in Tanzania, Ghana and Zimbabwe are structured differently. Tanzania uses a Block Management System (BMS) to identify informal businesses that are eligible for tax registration, to execute

the tax administrative activities of assessing the tax payable, and to account for the revenue collected. The BMS staff are employed by the revenue authority and are located within the informal business operating areas to be able to easily monitor and enforce compliance with the presumptive tax. The presumptive tax payable in Tanzania is based on an estimated level of turnover.

Ghana has two approaches to applying presumptive tax in the informal sector – the tax stamp system and Vehicle Income Tax (VIT) sticker system. Both systems require the taxpayer to purchase a sticker as a way of paying tax. The determination of the purchase price of the tax stamp considers the nature of business activities and the size of the business, and the purchase price of VIT stickers is based on the vehicle capacity and tonnage.

Zimbabwe targeted specific economic sectors to be included in the presumptive tax schedule. The presumptive tax schedule determines the tax payable, considering the nature of the business activities and the revenue drivers. Similar to Ghana, Zimbabwe uses a transport operators tax system that determines the tax payable based on vehicle capacity and tonnage.

Chapter 3 noted that the success of presumptive taxes cannot be evaluated solely by tracking revenues collected from presumptive taxes, as the impact may be noticeable in the increased culture of overall tax compliance. The presumptive tax regime should be introduced to achieve various goals and, in the short to medium term the focus should be to broaden the tax base, to eliminate the distortion arising from “free riding” taxable persons in the allocation and access to social services.

5.2.3 The fourth research objective

The fourth research objective was to recommend direct taxes that could be imposed in South Africa on the revenue generated in the informal sector. Recommendations for the direct taxes that could be imposed in South Africa on the revenues generated in the informal sector were made in chapter 4. It was noted in this chapter that the tax reforms implemented to reduce the tax burden of Small, Medium and Micro Enterprises (SMMEs) in South Africa were made in terms of the Small Business Corporation provisions in section 12E of the Income Tax Act, and the Turnover Tax in terms of the Sixth Schedule to the Income Tax Act. It was established that these reforms are not structured to address the integration of informal sector businesses into the tax system.

Based on the lessons learnt from the literature review of the presumptive tax models introduced in Tanzania, Ghana, and Zimbabwe, this chapter confirmed that a presumptive tax model is also an appropriate tax model that could be implemented in the South African informal sector, on the basis that it is simple to administer, resulting in low tax compliance costs for informal businesses. South Africa already has a presumptive tax model in the form of turnover tax which could be used to tax direct revenue generated in the informal sector.

The turnover tax system is an important component of the tax dispensation for SMMEs due to its major benefit of reducing the administrative and compliance burden. Despite this benefit, there are structural challenges that need to be addressed for the system to be effective and achieve the intended purpose of integrating the informal sector into the tax base. Recommendations were made to remove the requirement for an annual interim tax payment, for taking expenditure and tax allowances into account where micro business owners maintain a suitable set of accounts, adjusting the upper turnover limit of R1 million annually in line with inflation, and providing a tax amnesty for unregistered businesses that qualify for the turnover tax system.

The turnover tax system has a high exemption threshold in terms of which turnover below R335 000 (for the 2021-2022 year of assessment) is exempt. This exemption threshold would result in a nil tax liability for most informal sectors. A taxation model used to tax informal sector businesses will not be effective if it still leaves a large number of informal businesses outside the tax net. It was proposed that informal businesses that do not register for turnover tax should be taxed according to an alternative presumptive tax system.

Taking lessons from the informal sector taxation system in Ghana, an alternative approach aimed at achieving the tax compliance requirements for informal sector businesses in South Africa could be the tax stamp approach. Under the tax stamp system informal businesses will be required to purchase a tax stamp as a way of discharging their tax obligation. The tax stamp must be purchased annually in advance and be displayed in the business premises or be carried by the taxpayer while operating their business.

It is recommended that South Africa should implement a Block Management System (BMS) as a tool to identify and register informal businesses for presumptive tax. The BMS should map informal businesses on a geographical basis, where a combination of a few streets or trading

areas forms a block, with a separate block comprising online businesses. It is recommended that the collection of tax through the BMS should be outsourced to municipalities. The benefits of ceding informal sector tax collection to local government is that most local governments in South Africa are financially constrained and will therefore be motivated to pursue informal sector taxation in return for raising additional revenue. Local government is uniquely positioned relative to the informal sector taxation to understand the nature of their businesses and negotiate the appropriate tax rate.

It is recommended that, to increase taxpayer compliance and to reduce the challenge of financial mismanagement in local government, stringent transparency requirements should be applied. Transparency could also be in a form of earmarking revenue collected from the informal sector presumptive tax to improve infrastructure and the provision of basic services where the informal sectors operate.

SARS's investigation into the high level of non-tax compliance noted in the minibus taxi industry revealed that minibus taxi owners are not declaring taxable income in their corporate income returns or they are incorrectly having a refund due to them (Claasen, 2021). It is recommended that a specific presumptive tax regime designed for the minibus taxi industry in the form of vehicle income tax could be introduced to promote voluntary compliance. Minibus taxi businesses should purchase a minibus taxi tax sticker annually that is displayed on the windscreen of the minibus taxi. The purchase of the minibus taxi tax sticker could be aligned with the renewable of the vehicle licence and could be sold at similar locations. Minibus taxi operators should be required to discharge their tax liabilities prior to renewing their vehicle licence.

Ceding the collection of minibus taxi tax to the Department of Transport will enhance taxpayer compliance due to the interactive platforms that the department already has with the minibus taxi drivers, and the department also has metro police officers who can assist in enforcing compliance. The purchase price of the minibus taxi tax stickers should be determined by the minibus taxi capacity. The profitability of minibus taxi routes and operational locations should be factored in when determining the purchase price, and the purchase price should be determined in consultation with the minibus taxi businesses through the South African National Taxi Association and other taxi associations.

The latest technological developments could also be used to gather relevant data to provide accurate profitability estimations in the minibus taxi industry. It is recommended that, to increase taxpayer compliance, minibus taxi tax revenue could be used for the development of road infrastructure in South Africa, as well as taxi rank infrastructure for the benefit of taxi owners and the public. The choice of whether or not to pay tax is a function of a cost-benefit analysis, therefore in encouraging compliance it is essential that taxpayers understand how they will benefit from paying tax (Pfister, 2009).

The implementation of informal sector taxation requires government support, despite the potential political conflict of taxing the informal sector, which in most cases includes most of the voters (Joshi *et al*, 2014). Furthermore, tax education should be vigorously pursued to educate the taxpayers about their tax obligations and the benefits of tax compliance.

5.3 CONCLUDING REMARKS

This study was limited to recommending certain direct taxes that could be imposed in South Africa on the revenues generated in the informal sector.

Effective taxation of the informal sector has the potential to broaden the tax base in South Africa. It is, however, imperative that the legislation introduced to implement the recommended presumptive taxes adheres to the twelve principles of good tax policy as listed by the American Institute of Certified Public Accountants (AICPA) (2017:3) in the framework for evaluating tax policy. The twelve principles are as follows:

1. Equity and Fairness: similarly situated taxpayers should be taxed similarly.
2. Certainty: the tax rules should clearly specify when the tax is to be paid, how it is to be paid, and how the amount to be paid is to be determined.
3. Convenience of Payment: a tax should be due at a time or in a manner that is most likely to be convenient for the taxpayer.
4. Economy in Collection: the costs to collect a tax should be kept to a minimum for both the government and taxpayers.
5. Simplicity: the tax law should be simple so that taxpayers understand the rules and can comply with them correctly and in a cost-efficient manner.
6. Neutrality: the effect of the tax law on a taxpayer's decisions as to how to carry out a particular transaction or whether to engage in a transaction should be kept to a minimum.

7. Economic Growth and Efficiency: the tax system should not impede or reduce the productive capacity of the economy.
8. Transparency and Visibility: taxpayers should know that a tax exists and how and when it is imposed upon them and others.
9. Minimum Tax Gap: a tax should be structured to minimize noncompliance.
10. Appropriate Government Revenues: the tax system should enable the government to determine how much tax revenue will likely be collected and when.
11. Accountability of taxpayers: tax education should be pursued to ensure that taxpayers understand to which extent the tax legislation will be enforced.
12. Appropriate government revenues: an effective tax should generate revenue for the government

This study recommended the tax stamp approach as an alternative approach aimed at achieving the tax compliance requirements for informal sector businesses in South Africa with turnover below R335 000. Under the tax stamp system informal businesses will be required to purchase a tax stamp as a way of discharging their income tax obligations. Future research on the South African informal sector taxation can offer policy makers guidance on the appropriate pricing of the tax stamps that will enhance adherence to the twelve principles of good tax policy as listed by the American Institute of Certified Public Accountants.

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