

**FUNDING HIGHER EDUCATION AND TRAINING IN SOUTH AFRICA: A  
COMPARATIVE STUDY OF TAX INCENTIVE MEASURES, IN CONJUNCTION  
WITH A DEDICATED TAX**

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## ABSTRACT

Higher education and training in South Africa in the post-Apartheid era has never been more volatile than it is currently, some two decades into democracy. Despite the many advances and achievements of higher education, the student protests of 2015 and 2016 have given expression to underlying fault-lines, including increasing student expectations and frustrations with regard to access and funding.

This research was undertaken to document the underlying historical issues and models pertaining to funding within the higher education and training sector as well as the existing higher education and training taxation policies and incentives enacted in South Africa and selected international jurisdictions. This was done with a view to providing a framework for higher education and training tax policy formation in South Africa to assist in meeting its higher education and training “access and affordability” targets as set out in the National Plan on Higher Education and the Higher Education White Paper, while at the same time not hindering economic growth. A doctrinal research methodology was adopted in this study as it mainly analysed and interpreted legislation and policy documents and therefore the approach was qualitative in nature.

An extensive literature survey was done in order to document the various internationally selected legislated higher education and training tax policies and incentives. The literature indicated that there are widespread funding perspectives and initiatives, and that international tax policies enacted with the aim of ensuring that higher education and training is more accessible and affordable to the public, is stable and effective in certain jurisdictions. It is submitted that while a higher education dedicated tax may not be sufficiently effective in South Africa, a combination of broad-based tax incentives will help to promote the change to a more affordable and stable higher education funding system, whilst not preventing growth through sustainable development.

**Key words:** higher education and training, tax incentives, funding, government, international perspective

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## **CHAPTER 1: INTRODUCTION**

### **1.1 Context of the Research**

In October 2015, a protest by students of the University of the Witwatersrand against a proposed 10.5 percent increase in university tuition fees for 2016 rapidly spread to various other institutions across the country, developing into what is today known as the #FeesMustFall (FMF) movement (The University of the Witwatersrand, 2016). Since then, South African university students have been protesting vehemently – and somewhat violently – in mass action, advocating for free higher education. While the majority of students seem to want free higher education for all, others are demanding free education for the poor. There seems to be a misunderstanding, to a certain extent, on some crucial points, not least being that there is no such thing as free higher education - someone must always pay for it (Langa, Wangenge-Ouma, Jungblut and Cloete, 2016).

The Constitution of the Republic of South Africa, 1996 (the Constitution) sets out a description of the right to higher education. According to section 29(1) of the Constitution, “Everyone has the right - ... (b) to further education, which the state, through reasonable measures, must make progressively available and accessible.” The broadly nuanced interpretation of this right, and its implementation, is widely associated with the uncertainty and frustration of many South Africans seen today (South African Human Rights Commission, 2000).

Currently, the South African government spends a mere 4.7 percent of revenue, or 0.75 percent of gross domestic product, on the post-school education and training sector (University of the Witwatersrand, 2016). This includes universities, technical vocational education and training colleges and other post-school training institutions. The Organisation for Economic Co-operation and Development (OECD) on average spends 1.59 percent of gross domestic product on higher education, while the United Kingdom, for example, spends 1.23 percent and Germany 1.31 percent (University of the Witwatersrand, 2016).

In terms of actual cost, an amount of about 50 billion is spent on higher education in South Africa in the 2016 year of assessment (Pouris and Inglesi-Lotz, 2014; PricewaterhouseCoopers South Africa, 2016). South Africa subscribes to a funding framework in which costs are shared among the beneficiaries of university education (mainly government and students) (Phungo, 2015; PricewaterhouseCoopers South Africa, 2016). As a

percentage of total cost, the state contribution to university education has declined from 49 percent in 2002, to 40 percent in 2012, and is considered to be even lower, at between 35 and 40 percent, in 2016, while at the same time, the burden upon students has increased from 24 percent to approximately 37 percent during the same period (Ministry of Higher Education and Training, 2016a; PricewaterhouseCoopers South Africa, 2016; Phungo, 2015). With the increased financial burden on students, it is therefore not surprising that each calendar year is marked with student protests.

According to the Democratic Alliance's (DA) Shadow Minister of Higher Education and Training, Prof Belinda Bozzoli (2016), the department received information from the National Treasury stating that there are conspicuous shortfalls that pose a serious risk to the stability and ultimate future functionality of the sector. Bozzoli (2016) states that in order for the government to meet its goals as set out in the National Plan for Higher Education (which, as it relates to funding, is to provide access to higher education for all) the sector will experience a shortfall of over R120 billion in the next three financial years. This includes approximately R35 billion in the 2017/18 financial year, R40 billion in 2018/19 and R45 billion in 2019/20, taking into account the projected increase in enrolment of 1.6 percent (Bozzoli, 2016). The Technical and Vocational Education and Training Sector, which encompasses, but is not limited to, the Sector Education and Training Authorities, is said to be the most negatively affected area within the department as the baseline support is not sufficient for the current (and hence future) enrolment within the system (Bozzoli, 2016). The required state funding is said to be at 80 percent of the total cost ascribed to the Technical and Vocational Education and Training Sector (in terms of both tuition and living expenses) in order for a student to reasonably afford a higher education, yet the government is only able to fund students at 57 percent of the programme costs, excluding living costs (Bozzoli, 2016). This will result in the approximate estimated shortfall for the period of 2017 to 2020 being R38.5 million within this sector of the department alone. Furthermore, part of the total shortfall over the medium-term includes an amount of R23.2 billion required for the National Student Financial Aid Scheme (NSFAS) recipients who require full support with their tuition fees, accommodation, meals and transport (Bozzoli, 2016). Thus, the question as it relates to the National Plan for Higher Education and its proposed shortfall is: what constitutes access for all and how can this be achieved?

In comparison to other African countries, the South African investment (as a percentage of gross domestic product) in education is low, in fact, less than half of that which is spent by

countries like Ghana and Senegal, even though South Africa has the greatest number of public higher education institutions on the continent (Phungo, 2015). A more appropriate investment percentage for South Africa is suggested to be 2.5 percent of gross domestic product (Phungo, 2015). Furthermore, data produced show that a mere 5 percent of South African families, guardians or sponsors can afford university fees for their children (Phungo, 2015). Ensuring greater access to higher education and training will require a significant increase in the subsidy or grant awarded to these potential students by the government (and arguably the private sector). The question, however, is: how can this funding be raised?

It is important to note that government plays an important role in redressing certain historical disadvantages imposed upon the vast majority of the population. Through the power of taxation, government is able to assist those disadvantaged by the legacy of Apartheid by ensuring that those who qualify to attend university are able to do so (University of the Witwatersrand, 2016). The research set out in this thesis seeks to explore educational tax benefits and incentives that are currently available to the taxpayer.

It is also imperative to compare the challenges faced in funding higher education and training in South Africa with that of other countries. The issues faced in these countries may serve as important lessons for South Africa going forward. Many countries that once offered free higher education, such as China, Australia, Mozambique, Kenya and England, have since implemented cost-sharing policies and models of one form or another (Langa *et al*, 2016). This serves as one reason why a comparison between the funding of South African education from the perspective of international best practice is relevant. Furthermore, the research seeks to explore the application of international best practice in a South African context, with the possible imposition of a dedicated education tax.

## **1.2 Goals of the Research**

The overall goal of the research is to investigate how tax incentives and a dedicated education and training tax could assist in funding higher education and training in South Africa.

The sub-goals to be addressed in this thesis are the following:

- a brief overview of how higher education and training has been and is presently funded in South Africa;
- a brief overview of the challenges facing the funding of the South African higher education and training sector;

- an evaluation of current South African higher education and training tax incentives;
- the consideration of international examples of how higher education and training can be funded by way of tax incentives and/or a dedicated tax and the evaluation of such models in a South African content; and
- an evaluation and overall conclusion of what types of incentives and/or a dedicated tax could be considered for use in South Africa.

### **1.3 Methods, Procedures and Techniques**

An interpretative research approach will be adopted for the present research as it seeks to understand and describe (Babbie & Mouton, 2009). The research methodology to be applied can be described as a *doctrinal* research methodology. This methodology provides a systematic exposition of the rules governing a particular legal category (in the present case the legal rules relating to the funding of higher education through a dedicated tax or tax incentives), analyses the relationships between the rules, explains areas of difficulty and is based purely on documentary data (McKerchar, 2014).

The research is conducted in the form of an extended natural language argument, supported by documentary evidence.

In order to achieve the goals of the research a literature survey will be conducted, which will form the basis of the discussion in the thesis. The literature on educational taxing mechanisms is drawn from South African and international tax legislation, various documents issued by the Council of Higher Education and the South African Human Rights Commission, published books, articles published in journals, various reports on plenary sessions undertaken by universities, as well as selected popular articles and opinions accessed on-line or in the printed medium. Comparisons of selected international measures are drawn against the taxing statutes in South Africa, most notably the Income Tax Act No. 58 of 1962 (the Act) and the various reports issued by the South African Government and the South African National Treasury (National Treasury). The study focuses on higher education legislation enacted at federal and state levels in the United States of America, and higher education tax legislation in selected international jurisdictions, including the Finland, France, Germany, Ireland and the Netherlands. The international jurisdictions selected for the benchmarking in this research are examples of best practice from a taxation perspective in

relation to higher education funding sustainability. The broad-based nature of the state-level incentives in the United States of America is regarded as being valuable when analysing the options available to South Africa in terms of appropriate higher education tax legislation. Other countries were selected either because the literature indicates the positive results achieved in their higher education funding model or to showcase various lessons that are useful in a South Africa context.

The literature survey conducted in this research will not be exhaustive. The National Qualifications Framework Act No. 67 of 2008, the General and Further Education and Training Quality Assurance Act No. 58 of 2001, the Higher Education Act No. 101 of 1997 and the Skills Development Act No. 97 of 1998 are not considered, as the study intends to focus on the funding of higher education as opposed to the management of higher education.

The validity and reliability of the research and the conclusions will be ensured by:

- adhering to the rules of the statutory interpretation, as established in terms of statute and common law;
- placing greater evidential weight on legislation, case law which creates precedent or which is of persuasive value (primary data) and the writings of acknowledged experts in the field;
- discussing opposing viewpoints and concluding, based on a preponderance of credible evidence; and
- the rigour of the arguments.

#### **1.4 Ethical Considerations**

As the research only involves an analysis of documentary data, all of which are publicly available, no ethical considerations arise from their use. Interviews will not be conducted; opinions will be considered in their written form.

The researcher will not exaggerate or filter the data or results to support a particular viewpoint. Content will not be withheld or toned down. All sources of data will be appropriately acknowledged and full references provided.

## **1.5 Overview of Thesis**

Chapter two focuses on how higher education and training has been, and currently is, funded in South Africa. It is acknowledged that while it may be impossible for South Africa to fund higher education as a fully protected non-derogable right at this point in time, progress must be made in ensuring that all academically deserving students are provided with an opportunity to further their studies. In addition, in considering this, a brief overview of the historical and current challenges faced in the higher education and training sector in South Africa is provided. A pre-Apartheid and post-democracy analysis is made of the funding crisis and the previous deliberate exclusion of specific races, ethnicities and/or classes, with the aim of providing a full understanding of the issue.

Chapter three examines the South African taxing statutes and the provisions that have currently been enacted to facilitate and encourage the investment in higher education and training by both the state and the public sector. The existing tax incentives already legislated in the Income Tax Act, No.58 of 1962 (the Act). and the Value-Added Tax Act, No. 89 of 1991 (the VAT Act), are analysed, with the view of illustrating the present lack of an existing broad-based educational tax and, to a large extent, the limited scope of application of such incentives as there are.

Chapter four examines the implementation of market-based instruments, such as a higher education and training tax incentives and dedicated taxes, in selected international jurisdictions. The extent to which such incentives and taxes have been successfully implemented in the United States of America and various European countries, such as, Finland, France, Ireland, the Netherlands and Germany, is analysed, with particular focus on the feasibility of adopting such policies in a South African content.

Chapter five summarises the findings of the research in addressing the goals of the research. Furthermore, it reflects on the issues encountered in conducting the research and makes recommendations on areas of possible future research.

## **2 FUNDING THE CURRENT SOUTH AFRICAN HIGHER EDUCATION AND TRAINING SECTOR**

### **2.1 Introduction**

An understanding of the historical context of higher education in South Africa, and linking it to the funding demands of today, is necessary in order to fully grasp the situation and the associated challenges the country is currently facing. The root of the challenges is deeply entrenched in the deliberate educational divide and suppression of the black majority under Apartheid, culminating in years of under-funding and the lack of prioritisation (Cloete, Fehnel, Gibbon, Maassen, Moja and Perolds, 2001). The present apparent lack of leadership in the higher education sector in South Africa, particularly the perception that there is a lack of transformational leadership, is said to be directly at fault (Vinger and Cilliers, 2006). This has compromised the leaders' ability to manage change successfully. This chapter therefore seeks to explore the first goal of the research, namely, how higher education and training has been, and is presently, funded in South Africa, as well as the second goal of presenting a brief overview of the past and current challenges of funding as they relate to higher education and training in South Africa.

### **2.2 State Racial Structuring of the Higher Education Sector during Apartheid**

Since the early 1900s, higher education in South Africa has been skewed in a manner designed to entrench the privilege and power of the white minority (Cloete *et al*, 2001). Institutions of higher education were established and funded with the view of serving the ambitions, strategies and overall selective interests of the white minority (Cloete *et al*, 2001). Policy reflected discrimination to ensure that an affordable higher education and training sector was made impossible for the vast black majority.

Entrenched in the policy of the Apartheid government was that institutions had to be designated as being for the exclusive use of one of the four race groups, namely: African (or black), coloured, Indian and white (Reddy, 2004). By 1985, 19 higher education institutions had been designated as being “for the exclusive use of whites” (which were traditionally further divided into English and Afrikaans medium institutions), two as being “for the exclusive use of coloureds”, two “for the exclusive use of Indians”, and six as being “for the exclusive use of Africans” (Reddy, 2004). Apart from the six institutions for Africans, there were an additional seven institutions in the Transkei, Bophuthatswana, Venda and Ciskei

region that the National Party (even though not internationally recognised) declared independent “African” states (National Commission on Higher Education, 1996; Reddy, 2004). The National Party introduced stringent regulations to prevent institutions designated for the use of one race group from enrolling students from another race group (Reddy, 2004). Many black students sought entry into white-classified institutions in the hope of receiving a better quality and well-resourced education. Traditionally, white institutions were better equipped in terms of resources due to government’s prioritisation in terms of funding (Reddy, 2004).

Historically, white Afrikaans-medium institutions took their primary function to be that of acting in the service of the Apartheid government (Cloete *et al*, 2001). The support of these institutions for the government was a major aspect of their adaptive strategies and they saw their support of the Apartheid government as an essential aspect in ensuring their financial stability and longevity (Cloete *et al*, 2001). Their implementation of the government’s race-based policies is evident in their student enrolment patterns where, in 1990, 96 percent of their students were white and in 1993, this stood at 89 percent (Cloete *et al*, 2001; Reddy, 2004). Very little (if not nothing at all) was done to challenge the *status quo*. Jansen (2001:4) describes these institutions as, among other, having:

[a] lack of critical discourse in the disciplines as well as in more public spheres with respect to pressing social and human problems. There is a pervasive and narrow problem-solving, applications-based pedagogy and research, but not much of a standing back and posing of critical question in an attempt to understand, probe, disrupt official policy or standard practice.

Historically white English-medium institutions are said to have adopted a “liberal” approach to their daily functionality (Cloete *et al*, 2001). This encompassed their refusal to adopt the Apartheid government’s view that universities are simply “creatures of the state” (Cloete *et al*, 2001). Traditionally, these universities were committed to the universal values of academic freedom even though they, from time to time, accepted substantial sums of subsidy from the Nationalist government (Cloete *et al*, 2001).

In historically black institutions, the apartheid government kept strict control on the teaching material, student admissions, the selection of academics as well as the financial contributions of the state and any other funders (Cloete *et al*, 2001; Habib, 2001). The establishment of these institutions was overtly political; they were not established for reasons of academic

need, but rather that of state control (Cloete *et al*, 2001). These institutions were set up to train black people to “be useful” to the Apartheid state and to maintain the overall Apartheid socio-political agenda (Cloete *et al*, 2001). Due to minimal and highly regulated financial contributions to historically black institutions, the financial longevity of these institutions was highly uncertain with, in most cases, the majority of funding going towards salaries and operational costs, ultimately compromising the supply of quality educational resources (Cloete *et al*, 2001; Habib, 2001). The leadership of these institutions, from a council, management and academic staff perspective, comprised mostly of white Afrikaans-speaking individuals who had been trained at the historically white Afrikaans-medium universities (Cloete *et al*, 2001). Such institutional leadership absorbed the majority of the funding for salaries and their personal gain, resulting in the lack of prioritisation in terms of student needs as well as fees for black South Africans being unfordable for the most part (Cloete *et al*, 2001).

### **2.3 The Political Struggle against Apartheid: Student Politics**

The main student organisation on campuses across South Africa during early Apartheid was the National Union of South African Students, founded in 1924 (Reddy, 2004; Davies, O’Meara and Dlamini, 1984). The National Union of South African Students consisted of English and Afrikaans speaking white pupils only, mainly because of the Apartheid restrictions on black people in organized political activity and, as a result, represented the minority interest of white students on campuses across South Africa (Reddy, 2004; Davies *et al*, 1984). However, due to ideological differences in terms of the state’s role in higher education and training, many Afrikaans students left the conservative-liberal organisation to form the Afrikaanse Nasionale Studentebond and later, the Afrikaanse Studentebond (Reddy, 2004). In the period of 1930 – 1950, the National Union of South African Students opened its membership to black students and adopted a non-racial stance, bringing it into direct conflict with the Nationalist government and its educational policies (Reddy, 2004; Davies *et al*, 1984).

The majority of the activism of both the National Union of South African Students and the Afrikaanse Nasionale Studentebond, during the Apartheid era, related to opposing views on the issue of state control of universities (Reddy, 2004). The National Union of South African Students believed that the role of the state was to ensure that universities are open to all current and academically deserving students, regardless of their race and as a result, ensure

equal state funding contributions to all universities based on their student intake (Reddy, 2004). The Afrikaanse Nasionale Studentebond, on the other hand, sought to maintain and enhance the agenda of the Nationalist government (Reddy, 2004). Neither of the student movements, however, saw it as part of their mandate to demand free higher education for all, or the poor, from the state (Reddy, 2004). While accurate data on the Apartheid state contribution towards higher education and training is limited, the contribution towards historically white universities was approximately twice that of historically black (including coloured and Indian) universities (Badat, 1999; Reddy, 2004). This funding model was adopted despite the fact that, in total at the time, there were 19 traditionally white universities and 17 traditionally black universities in South Africa (Reddy, 2004).

During the intensely repressive period of the mid-1960s, however, there were extensive limits within the National Union of South African Students when it came to the spearheading of issues of racial inequality, greater access to funding and education and unjust universal human rights violations (Reddy, 2004). Frustrated by the lack of progress, and after the break away of the South African Students Union from the National Union of South African Students (formed to serve white interests exclusively), Steve Biko (who was elected president of the organisation), together with various others, launched the South African Students Organisation (Badat, 1999; Reddy, 2004). The basic aims of the organisation, according to Badat (1999:178), were to:

- 1) [m]obilise black students by increasing contact nationally,
- 2) identify crucial issues/grievances that affected black students,
- 3) represent the interests of the black students,
- 4) establish a solid and strong identity and to boost black students' confidence in themselves,
- and 5) begin concrete programmes to respond to pertinent issues to get the majority of black students directly involved in SASO activities

In the execution of their aims, the South African Students Organisation sought free higher education for all (Badat, 1999). The organisation saw many great successes in the execution of their mandate, such as the 1972 boycotts, but did not realize their goal of free higher education for all, which they actively fought for since the inception of the movement (Badat, 1999; Reddy, 2004).

Currently, various student movements believe that, just like the South African Students Organisation, free higher education for all is possible (University of the Witwatersrand, 2016). Student movements are of the belief that this can be done through the mere re-

prioritisation and re-allocation of the state budget – despite government’s view that there is simply not enough funds available (University of the Witwatersrand, 2016). According to Keppler (2017), the Democratic Alliance Students Organisation, through the organisation’s leader, Yusuf Cassim, who serves as a Member of the South African Parliament in the Portfolio of Higher Education and Training, is calling for free quality higher education and training for the poor. Together with this, they are of the belief that there should be greater subsidies for the “missing middle”, while the rich, who can afford the exorbitant fees, should pay (Keppler, 2017). The Democratic Alliance Students Organisation believes that, as stated in Keppler (2017), students from disadvantaged backgrounds with a family income of up to R200 000 per annum should receive the full cost of studying free of charge. Parents earning between R200 000 and R350 000 per annum should receive 66 per cent funding towards their study costs and those with an income of R350 000 and R500 000 per annum 33 per cent aid towards their studies (Keppler, 2017).

## **2.4 Post-Apartheid Access and Opportunity in Higher Education**

### **2.4.1 The National Commission on Higher Education: A Framework for Transformation**

The National Commission on Higher Education (1996) was established with the broad mandate of advising the Minister of Education on the complete restructuring of higher education in South Africa. This document not only pioneered the legislation regulating higher education and training, but also highlighted various key issues, ideas and debates surrounding tertiary education, and the funding thereof, in a democratic state (National Commission on Higher Education, 1996). The work carried out by the National Commission on Higher Education was done under the central assumption that (at 35): “higher education can play a pivotal role in the political, economic and cultural reconstruction and development of South Africa.” The National Commission on Higher Education decided on the following principles to guide and direct the process of “transformation” (at 35):

- equitable distribution of resources and opportunities in higher education;
- redress historical inequalities;
- democratic, representative and participatory governance (of the system and individual institutions);
- balancing the development of ‘material and human resources’; and
- quality in higher education services and products.

In its attempt to accomplish these goals, the state recognised that its role in so doing is of a “steering and co-ordinating” nature (National Commission on Higher Education, 1995). While institutional autonomy is paramount, the affairs of institutions must be monitored within the limits of accountability and transparency (National Commission on Higher Education, 1995). It was proposed that, in order to ensure that this is accomplished, financial incentives and other financial steering mechanisms are used, instead of a commanding measure of control of finances from the state (National Commission on Higher Education, 1995). The proposed funding model would be based on a “goal oriented” funding framework for public higher education, with two core elements as follows (National Commission on Higher Education, 1995: 8-23):

- (1) [f]ormula funding component – will generate block grants for institutions based on the number of full-time students and fields of study.
- (2) [e]armarked funding component – will be allocated in line with specific policy, and for targeted programmes and activities, address “unacceptable inequalities and to serve as a means of redress in higher education.” (p.21) The NCHE suggests the following areas for earmarked funding: research, student financial aid, academic development, staff development, information technology, library capacity building, curriculum development, equipment, institutional development, new buildings and new land. It states that earmarked funds should be allocated according for three types of redress: (a) institutional redress (to disadvantaged institutions; need to apply; allocated on the basis of “comprehensive institutional audits and institutional missions, programme mixes and needs assessments”); (b) individual redress (in the form of student financial aid schemes such as NSFAS); and (c) any other specific redress purposes.

This report further highlights that, in 1995, state funding of higher education and training amounted to 1.7 percent of gross domestic product (which has decreased to 0.75 percent in the 2016/17 tax year), an amount equivalent to the average budgeted spending in countries that are members of the Organisation for Economic Cooperation and Development (National Commission on Higher Education, 1995; University of the Witwatersrand, 2016). The report highlights that the avenues of access, as it relates to funding, for white students, in comparison to other race group’s remains significantly higher (National Commission on Higher Education, 1995). A further breakdown of access demonstrates that class is (additionally) a contributing factor and that race alone does not provide a comprehensive enough picture of a student’s ability to afford university costs (National Commission on

Higher Education, 1995; Reddy, 2004). According to Statistics South Africa (2016), as from 2015, approximately 10 percent of the population of South Africa own at least 90 – 95 percent of all assets. The unequal access to higher education and training, due to the unaffordability of higher education and training for many, serves as an added reason as to why the earmarked funding component, which seeks to address these inequalities, is important in the hope of realizing (if not free education) an affordable higher education and training sector for all.

Moja and Hayward (2005) recognised the immense contribution that the National Commission on Higher Education had in identifying the challenges in higher education in South Africa, but continue to criticise it for not developing any proposals on curriculum development, racial imbalances and a comprehensive implementation plan for its proposed funding models.

#### **2.4.2 The Higher Education White Paper and Related Policy Developments**

The key challenges facing the South African education system (and recommended proposals following on from the National Commission on Higher Education) are outlined in The Higher Education White Paper, as adopted in December of 1998 (Department of Education, 1997). The goal of the document is “to redress past inequalities and to transform the higher education system to serve a new social order, to meet pressing national needs, and to respond to new realities and opportunities” (Department of Education, 1997). More specifically, the Department of Education (1997:06) indicates that the role of higher education in a knowledge-driven world is three-fold, namely:

- human resource development: the mobilisation of human talent and potential through lifelong learning to contribute to the social, economic, cultural and intellectual life of a rapidly changing society;
- high-level skills training: the training and provision of person power to strengthen this country’s enterprises, services and infrastructure, and
- production, acquisition and application of new knowledge: the growth and competitiveness of a nation is dependent on continuous technological improvement and innovation that is driven by a well-organized, vibrant research and development system, which integrates the research and training capacity of higher education with the needs of industry and of social reconstruction.

In achieving these goals, as the White Paper states, it is necessary for the redress funds (as discussed in the earmarked funding component) to be facilitated in a manner in which the needs of the institutions are linked to performance and efficiency measures (Department of Education, 1997). Among other things, the White Paper highlights targets for the size and shape of the higher education system, including overall growth and varied participation rates, institutional and programme mixes and equity and efficiency goals (Department of Education, 1997). In achieving this, the effective use of funding, through the continuous development of the funding formula, based on the funding principles and framework outlined in the White Paper, is crucial to the success of such a project (Department of Education, 1997).

Furthermore, it is noted that these challenges must be understood in a worldwide content in which the phenomenon of globalisation is recognised (Department of Education, 1997). At the centre of the changes brought about by globalization is the notion that, in the 21<sup>st</sup> century, knowledge and the possession of information will be the key driving forces in wealth creation and thus social and economic development, all of which is supplemented through a highly effective, well-funded and inclusive education system (Department of Education, 1997).

Although, today, the vision of the White Paper continues to remain compelling, the goal remains unachieved (Centre for Higher Education and Training, 2001; Ministry of Higher Education and Training, 2016b). It is clear that the implementation vacuum has given rise to a number of highly significant issues, including the unintended and unanticipated consequences which, if continued to be left unattended, threaten the development (and ultimate realization) of a single, national, co-ordinated, higher education funding model (Centre for Higher Education and Training, 2001).

The institutional planning process, which was initiated in 1998 through the development of the White Paper, forming the basis of a valuable contribution to the debate on the need and basis for the restructuring of the higher education system, led to (in 2001 and still relevant today) the establishment of the Council on Higher Education (Centre for Higher Education and Training, 2001). The Council on Higher Education report, which builds on the White Paper, further highlights the National Plan for Higher Education (Centre for Higher Education and Training, 2001).

## **2.5 Government's Funding Framework for South African Higher Education**

Since 2007, the total Medium-Term Expenditure Framework budget for higher education and training, up until the 2011/2012 tax year, had risen by approximately R20.7 billion (Ministry of Higher Education and Training, 2012). While this amount sounds substantial, the portion of funding for higher education as a percentage of the budget has decreased substantially from 1987 (De Villiers and Steyn, 2007). In 1987, the state spent 3.03 percent of its revenue on higher education, but in 2015 this figure stood at 0.64 percent (De Villiers and Steyn, 2007; Department of Higher Education and Training, 2016a). This represents a decrease of almost three percentage points in the past 20 years. State funding forms a large portion of the total income of almost every higher education institution (De Villiers and Steyn, 2007) and it is thus important for senior management, staff in general as well as students and their sponsors to be aware of and understand the details of state funding and the challenges with which it is faced.

The Treasury allocation (excluding National Student Financial Aid Scheme loans) to the university sector, in the 2015/16 tax year, amounted to approximately R26.2 billion (Ministry of Higher Education and Training, 2016a; Universities South Africa, 2016). Furthermore, a 0.3 percent decrease in the total funding allocation from the previous year of assessment (namely 2014/15), has also been experienced (Universities South Africa, 2016).

There have only been four frameworks for funding since the 1950s, starting with the Holloway formula for universities in 1953 (De Villiers and Steyn, 2005). Since then, the framework has been changed and updated, resulting in the New Funding Framework, which could be seen as the result of an evolution of funding by means of formulae (De Villiers and Steyn, 2005). The calculation of state funding by means of formulae is said to yield a number of advantages, including a fair distribution of funds, and the fact that the details of funding are known in advance allows for medium- and long-term planning (De Villiers and Steyn, 2005). A disadvantage of any formula-based framework, however, is that a beneficiary will inevitably seek out and exploit loopholes in either the definition or calculation of input elements (De Villiers and Steyn, 2005). Thus, the continuous review of any formula, taking into account the economic environment, may be beneficial in ensuring ultimate fairness.

### **2.5.1 1953: The Holloway Formula**

In 1951, the government appointed the Holloway Commission to investigate university funding (De Villiers and Steyn, 2005). The Commission produced a report, the recommendations of which were implemented in 1953, forming the basis of state funding until the early 1970s (De Villiers and Steyn, 2005). The formula, according to De Villiers and Steyn (2005:30), was based on three elements:

$$F(H) = Sb + Ss + A$$

where:

*Sb* = basic teaching determination (not related to student numbers)

*Ss* = standard teaching determination (partially related to student numbers)

*A* = staff living costs compensation (on an additional basis from 1959).

The salaries of academic staff in academic departments and librarians are represented by the “*Sb*” component (De Villiers and Steyn, 2005). The “*Ss*” component represents the sum of the salaries of any remaining academic staff (such as those in management positions outside of academic departments), a predetermined contribution for each full-time student, the cost of laboratory modules (to fund laboratory machinery) and a certain predetermined percentage for administration expenses (De Villiers and Steyn, 2005). Lastly, “*A*” represented the living costs (in terms of housing) for all staff members who reside on campus (De Villiers and Steyn, 2005).

From 1953 to 1977, for over 20 years, this formula determined the subsidy to universities across South Africa, with small adjustments in 1959, 1964 and 1969 (De Villiers and Steyn, 2005). The problem was that certain universities discovered a loophole, ultimately allowing them to divide their courses into smaller units in order for them to increase their government subsidy (De Villiers and Steyn, 2005). The formula also lacked adjustability for inflation – a relevant element in the finance world during the 1970s and beyond (De Villiers and Steyn, 2005).

### **2.5.2 1977: The Van Wyk de Vries Formula**

After the government discovered that universities were exploiting a loophole, the order to revise the subsidy formula was given (De Villiers and Steyn, 2005). The Van Wyk de Vries Commission was appointed in 1968 and oversaw an in-depth review of the Holloway Formula (De Villiers and Steyn, 2005). After a substantial period (approximately six years), a

final report was produced (De Villiers and Steyn, 2005). The result of this report was a funding formula with much needed new principles, but still keeping the most important elements of the Holloway Formula intact (De Villiers and Steyn, 2005). The Van Wyk de Vries Formula was then adopted and implemented in 1977 (De Villiers and Steyn, 2005).

One of the major changes was the use of a “weighted number for students” as opposed to a predetermined set contribution per full-time student (De Villiers and Steyn, 2005). Undergraduate students received a weighting of one unit each, two units for honours and three units each for masters and doctoral students (De Villiers and Steyn, 2005). A weighted approach was further applied to the method of delivery on an undergraduate level, for example, for full-time students, a weighting of one applied, 0.75 for part-time students and 0.33 for students in non-university residential accommodation (De Villiers and Steyn, 2005). The disadvantage was that this model, like that of the Holloway Formula, did not make provision for annual inflation increases or prevent the possible division of courses for extra funding purposes (De Villiers and Steyn, 2005).

### **2.5.3 1984: The SAPSE Formula**

The South African Post-Secondary Education (SAPSE) information system was comprehensive, yet instrumental in its use during the 1980s (De Villiers and Steyn, 2005). The formula made the important assumption that the students were best capable of determining their own welfare and that they have the best knowledge in deciding which course to enrol for (De Villiers and Steyn, 2005). The formula was based on student enrolments and funded as such (De Villiers and Steyn, 2005). Students could enrol at any university or technikon as they saw fit and the formula was seen as being market driven (De Villiers and Steyn, 2005).

To consider inflation, an annual increase was incorporated into the cost formula (De Villiers and Steyn, 2005). The increase was based on indicators and, to prevent escalation at universities, a national indicator was used (De Villiers and Steyn, 2005). Another important element was that – for the first time – the subsidy was not only based on student and other inputs, but on output parameters per institution (De Villiers and Steyn, 2005). Output was mainly determined by the module credits completed by students and the research published by senior students and/or academic staff (De Villiers and Steyn, 2005).

From 1986 to 1992, student enrolment at institutions increased substantially (De Villiers and Steyn, 2005). As a result, government had to decrease the value assigned to the number of enrolments per institution (De Villiers and Steyn, 2005). The government acknowledged that the South African Post-Secondary Education formula had the unintended disadvantage of allowing for the unrealistic increase in student numbers (De Villiers and Steyn, 2005). As a result of this flaw (as well as other negative aspects of certain elements of the formula) the Advisory Council for Universities and Technikons revised the formula in 1991 (De Villiers and Steyn, 2005). The newly approved formula, which was used from 1993 through to 2003, took into account a number of adjustments relating to the student intake and the weighting of specific courses (De Villiers and Steyn, 2005).

#### **2.5.4 Earmarked Funding (1993 – 2003)**

In order to subsidise any specific area of need at the various institutions, earmarked funding was available (De Villiers and Steyn, 2005). Earmarked funding was used at the same time as the South African Post-Secondary Education formula and included the following (De Villiers and Steyn, 2005:47):

- i. [f]ixed asset projects: this included land acquisitions and property development,
- ii. [m]unicipal rates: government would fund the municipal assessment rates, given that the receipts were provided,
- iii. [t]he National Financial Aid Scheme (NSFAS): in 1991, the Tertiary Education Fund of SA (TEFSA) was established as a non-profit organization with the mandate of assisting students through the awarding of loans for higher education. From 1995, NSFAS was known as and administrated through TEFSA until 2000, when TEFSA became legally known as NSFAS,
- iv. [r]edress: funding for purposes of redress at universities and technikons, which were classified as, impaired by historical inequalities benefited from this allocation in the 1998/9 year of assessment. Although such funding was meant to be available up until the end of the 2000/1 year of assessment, the distribution of such funds was not published in the official budget documents of the Department of Education for the years in question,
- v. Teacher Training Colleges: during the 2000/1 and 2001/2 years of assessment, *ad hoc* funds were allocated for the merging of these colleges with various universities, and
- vi. [o]ther earmarked funds: in order to fund vehicle schemes, medical specialists and other gratitude payments, funds, titled *inter alia*, were allocated.

During the tax year of 1996/7, earmarked fund allocations for higher education constituted 15.6 percent of the total funding for higher education (De Villiers and Steyn, 2005). In the

following tax year, this percentage dropped to 10 percent, mostly because of the discontinuation of funding allocations towards capital projects (De Villiers and Steyn, 2005). After this, some increases in specific areas were evident in the following three years, but a drop in the 2003/4 tax year, to 10.3 percent, was again seen (De Villiers and Steyn, 2005). Following on from this, earmarked funding, as it relates to the abovementioned criteria, ended altogether (De Villiers and Steyn, 2005).

### **2.5.5 The New Funding Framework**

The New Funding Framework (introduced in the 2003/4 tax year and formally established in the 2004/5 tax year) was the result of a highly collaborated and difficult process (De Villiers and Steyn, 2005). The framework was first proposed and published by the National Commission on Higher Education in 1996, followed by an extensive review and fine-tuning process, resulting in the Education White Paper 3 (WP3) in 1997 (De Villiers and Steyn, 2005). In the following six years (after the initial proposal), various experts and stakeholders worked on a proposed model of funding (set within the framework of the Education White Paper 3) (De Villiers and Steyn, 2005). A funding framework was first published by the Department of Education (DoE) in March 2001, followed by three “migration” years after which the final new Funding Formula was implemented in 2004 (De Villiers and Steyn, 2005).

#### **2.5.5.1 The New Funding Formula as a Structure: Block Grants**

The New Funding Formula (which is still used today as the primary form of funding) comprises two important elements, namely; block grants and earmarked grants (De Villiers and Steyn, 2005; and Ministry of Higher Education and Training, 2016b). The first refers to funds that are aimed at covering operational costs at universities and technikons, determined by teaching and research activities (Ministry of Higher Education and Training, 2016b). Block grants for a specific year  $n$  are determined by student numbers and graduates per institution (which includes research publications) in year  $n - 2$  and is divided into the Classification of Educational Subject Matter (CESM) categories as per [Table 1](#) and [Table 3](#) below (Ministry of Higher Education and Training, 2016b).

The total budget (including that of the National Student Financial Aid Scheme), awarded to higher education and training in South Africa in the 2016/17 tax year, equates to approximately R37 billion (Ministry of Higher Education and Training, 2016b). This

represents a 21.5 percent increase from the 2015/16 tax year, with a proposed further increase of 19.3 percent in the 2017/18 tax year (Ministry of Higher Education and Training, 2016b).

### 2.5.5.1.1 Block Grants: Teaching Input Grants

Teaching input grants are determined by the full-time student enrolments (FTE) for year  $n - 2$  (Ministry of Higher Education and Training, 2016b). The full-time student enrolment units are weighted by qualification type and funding group as indicated in the funding grid in [Table 1](#) (Ministry of Higher Education and Training, 2016b). The funding groups are determined by the aggregations of the “Classification of Educational Subject Matter” (CESM) categories in [Table 2](#) and [Table 3](#) (Ministry of Higher Education and Training, 2016b).

The total number of teaching input units per institution is determined by the approved number of full-time enrolment students per qualification type (course) and the funding group for year  $n - 2$  (Ministry of Higher Education and Training, 2016b). The total grant is then divided per institution in accordance with their teaching input units (Ministry of Higher Education and Training, 2016b). The teaching input grant for the 2017/18 year amounted to R16 220 201 000, an increase of 17 percent from the previous year, with an expected increase of 6.4 percent in 2018/19 (Ministry of Higher Education and Training, 2016b).

**Table 1:** Funding weightings for teaching inputs: 2004/05 – 2018/19

Funding group	Undergraduate & equivalent		Honours & equivalent		Master’s & equivalent		Doctoral & equivalent	
	Contact	Distance	Contact	Distance	Contact	Distance	Contact	Distance
1	1.0	0.5	2.0	1.0	3.0	3.0	4.0	4.0
2	1.5	0.75	3.0	1.5	4.5	4.5	6.0	6.0
3	2.5	1.25	5.0	2.5	7.5	7.5	10.0	10.0
4	3.5	1.75	7.0	3.5	10.5	10.5	14.0	14.0

Source: (Ministry of Higher Education and Training, 2012:8 and 2016b:7)

**Table 2:** Funding groups for 2004/05 – 2006/07

<b>Funding group</b>	<b>CESM categories included in funding group</b>
1	07 education, 13 law, 14 librarianship, 21 social service/public administration.
2	04 business/commerce, 05 communication, 06 computer science, 12 languages, 18 philosophy/religion, 22 physical education.
3	02 architecture/planning, 08 engineering, 10 home economics, 11 industrial arts, 16 mathematical sciences, 19 physical education.
4	01 agriculture, 03 fine and performing arts, 09 health sciences, 15 life and physical sciences.

Source: (Ministry of Higher Education and Training, 2012:8)

**Table 3:** Funding groups for 2008/09 to 2018/19

<b>Funding group</b>	<b>CESM categories included in funding group</b>
1	07 education, 12 law, 18 psychology, 19 public administration and services.
2	04 business, economics & management studies, 05 communication & journalism, 06 computer & information science, 11 languages, linguistics & literature 17 philosophy, religion & theology, 20 social sciences
3	02 architecture & the built environment, 08 engineering, 10 family ecology & consumer sciences, 15 mathematics and statistics.
4	01 agriculture & agricultural operations, 03 visual and performing arts, 09 health professions & related clinical sciences, 13 life sciences, 14 physical sciences.

Source: (Ministry of Higher Education and Training, 2012:8 and 2016b:8)

#### **2.5.5.1.2 Block Grants: Research Output Grants**

An institution can calculate their research output unit for year  $n - 2$  by using the following formula (Ministry of Higher Education and Training, 2016b):

Research output units = publication units approved by the DoHE (Department of Higher Education and Training) + research master's degrees awarded + 3\*doctoral degrees awarded.

The grant is then divided per institution, based on their research output unit as a percentage of the total research output unit for all universities.

In order to determine whether an institution over- or under-performs, a ministerial statement, which provides for a norm ranging from 1.1 to 2.5 units (as indicated in [Table 4](#) below), per permanent staff member at each institution, is developed (Ministry of Higher Education and Training, 2016b). The research output grant awarded to each institution is based on their ability to perform as compared to their expected norm (Ministry of Higher Education and Training, 2016b). Whether or not a university receives the grant, is largely based on their ability to perform in accordance with their expected norm. For the 2013/14 year and thereafter, the research development grant is no longer calculated as part of the block grants, but under earmarked grants (Ministry of Higher Education and Training, 2016a). The research output grant for the 2017/18 tax year amounted to R3 346 481 000, an increase of 5 percent from the previous year, with an expected further increase of 5.8 percent in the 2018/19 tax year (Ministry of Higher Education and Training, 2016b).

**Table 4:** Research output norms for 2013/14 – 2015/16

	<b>Norm 2012/13</b>	<b>Norm 2013/14 – 2015/16</b>
Cape Peninsula University of Technology	0.565	1.1
Central University of Technology	0.565	1.1
Durban University of Technology	0.565	1.1
Mangosuthu University of Technology	0.565	1.1
Tshwane University of Technology	0.565	1.1
Vaal University of Technology	0.565	1.1
Walter Sisulu University	0.8249	1.1
Nelson Mandela Metropolitan University	1.0509	1.7
University of Johannesburg	1.0961	1.7
University of South Africa	1.3108	1.1
University of Cape Town	1.4125	2.4
University of Fort Hare	1.4125	2.1
University of Free State	1.4125	1.7
University of KwaZulu-Natal	1.4125	1.7
University of Limpopo	1.4125	1.1
North-West University	1.4125	1.7
University of Pretoria	1.4125	2.2

Rhodes University	1.4125	2.5
University of Stellenbosch	1.4125	2.5
University of Venda	1.4125	1.1
University of the Western Cape	1.4125	2.0
University of Witwatersrand	1.4125	2.1
University of Zululand	1.4125	1.1

Source: (Ministry of Higher Education and Training, 2012:13)

### 2.5.5.1.3 Block Grants: Teaching Output Grants

In order to calculate the number of teaching output units for an institution in year  $n - 2$ , the number of graduates per qualification for year  $n - 2$  is weighted by using the weights in [Table 5](#) (below) and then summed (Ministry of Higher Education and Training, 2016b). The total grant is divided relative to the summed amount per institution (Ministry of Higher Education and Training, 2016b).

Again, in order to determine whether an institution over- or under-performs, the normative output can be calculated by taking the norms per qualification type given in the ministerial statement (as shown in [Table 6](#)) multiplied by the number of students enrolled in that particular qualification (Ministry of Higher Education and Training, 2016b). The sum of the grant is uniquely dependent on the performance of the institution against its norms (Ministry of Higher Education and Training, 2016b).

According to the Ministry of Higher Education and Training (2016b), the 2017/18 tax year budget for this grant amounted to R4 310 654 000, an increase of 22.7 percent from the previous year with an additional expected increase in the 2018/19 tax year of 6.4 percent.

**Table 5:** Funding weightings for contact and distance teaching outputs: 2015/16

Teaching outputs	Fund weightings
1 <sup>st</sup> certificates and diplomas of 2 years of less	0.5
Postgraduate and post-diploma diplomas	0.5
Honours degree/higher diplomas/post-graduate diplomas approved under the new HEQF	0.5
Non-research master's degrees and diplomas	0.5
1 <sup>st</sup> diplomas and bachelor degree: 3 years	1.0
Postgraduate bachelor degrees	1.0
Professional 1 <sup>st</sup> bachelor degree: 4 years and more	1.5

Source: (Ministry of Higher Education and Training, 2016a:12)

**Table 6:** Norms for graduation rates

Qualification type	Contact	Distance
Undergraduate: up to 3 years	22.5%	13.5%
Undergraduate: 4 years or more	18.0%	9.0%
Postgraduate: up to honours	54.0%	27.0%
Postgraduate: up to masters	30.0%	22.5%

Source: (Ministry of Higher Education and Training, 2016a)

### 2.5.5.2 The New Funding Framework: Institutional Grants

The total institutional grant allocation, across its various disciplines, constitutes R1 445 538 000 in the 2017/18 tax year (Ministry of Higher Education and Training, 2016b). This represents an increase of 17.9 percent from the previous year with an expected further increase of 6.4 percent in the 2018/19 tax year (Ministry of Higher Education and Training, 2016b).

#### 2.5.5.2.1 Institutional Factor Grants: Disadvantaged Students

The first type of institutional factor grant is determined by the percentage of black, coloured and Indian students enrolled in the institution (Ministry of Higher Education and Training, 2016a). An institution with more than 40 percent of their number of full-time contact enrolled students in this group for the year  $n - 2$  will qualify for a grant in year  $n$  (Ministry of Higher

Education and Training, 2016b). The factor value of the grant, which ranges from 0 to 0.1, is dependent on the following factors (Ministry of Higher Education and Training, 2016:12b):

- 40% or less disadvantaged students receive a factor of 0;
- 80% or more disadvantaged students received a factor of 0.1; and
- [m]ore than 40%, but less than 80% disadvantaged students receive an increasing linear factor of between 0 and 0.1.

The grant awarded per institution, for a specific tax year, is calculated by multiplying the factor value, as a percentage value of total factor values, with the grant amount for that year of assessment (Ministry of Higher Education and Training, 2016b).

#### **2.5.5.2.2 Institutional Factor Grants: Size of the Institution**

The second institutional factor grant is determined by the number of full-time student enrolments (Ministry of Higher Education and Training, 2016b). The value of the grant is a number between the values of 0 and 0.15 and can be calculated as follows (Ministry of Higher Education and Training, 2016b):

- 4 000 or less FTE students receive a factor of 0.15;
- 25 000 or more FTE students receive a factor of 0; and
- [m]ore than 4 000, but less than 25 000 FTE students receive a decreasing linear factor between 0 and 0.15.

The grant, which an institution receives in a specific tax year, is calculated by using the same criteria as the “disadvantaged student” grant as discussed above (Ministry of Higher Education and Training, 2016b).

#### **2.5.5.2.3 Institutional Factor Grants: Multi-Campus Institutions**

The last institutional factor grant is aimed at helping institutions which have teaching duties on more than one official campus. The grant is calculated using a mathematical formula based on the performance and needs of the merged institutional campuses (Ministry of Higher Education and Training, 2016b).

### 2.5.5.3 Earmarked Grants

Earmarked funds are available in order to assist with designated institutional areas. The areas that receive the highest portion of these funds, according to the Ministry of Higher Education and Training (2016b:03), include:

- the National Student Financial Aid Scheme (NSFAS);
- teaching and community development (not linked to development block grants);
- interest on and payment of loans guaranteed by State prior to 1 April 1991;
- restructure of institutions;
- the framework for quality review in tertiary education;
- Research Development Grants;
- Foundation Provision Grant;
- Clinical Training Grant; and
- Gap Funding Grant for the 2017 increase in student fees for poor and missing middle grant.

The total earmarked grant value (R8 701 418 000 in the 2017/18 tax year) is divided according to criteria as set by the department, into the various sub-categories (Ministry of Higher Education and Training, 2016b) This value, which increased by 39.3 percent from the 2016/17 tax year, is expected to increase by a further 5.6 percent in the 2018/19 tax year (Ministry of Higher Education and Training, 2016b).

Since 2001, there has been a significant increase in student enrolments from 638 000 in 2001, to 935 000 in 2013, to approximately 1 087 000 in 2015 with an expected annual average growth rate of 1.9 percent (Ministry of Higher Education and Training, 2012; Department of Higher Education and Training, 2016). As a result, the funding per teaching input unit (or university) has decreased (relative to its size) every year (Department of Higher Education and Training, 2016). Following this, a strategy of “Student Enrolment Planning for Higher Education” commenced in 2006 (Ministry of Higher Education and Training, 2012; Ministry of Higher Education and Training, 2016b). As a result, a predetermined fixed share per institution of the total teaching input units for year  $n - 2$  was calculated (Ministry of Higher Education and Training, 2016b). The first cycle started in the 2010/11 tax year, with the fixing of enrolment planning for a three-year period from 2011 to 2013, after which the next three-year cycle commenced (Ministry of Higher Education and Training, 2012; Ministry of Higher Education and Training, 2016b).

The focus of the research development grant (as indicated above) is to assist universities financially with research output (Ministry of Higher Education and Training, 2012). The unit consists of research publications (through accredited journals, books and conference proceedings), research masters degrees and doctoral degrees awarded (Ministry of Higher Education and Training, 2012). The funds available for this grant were exhausted in the 2013/14 tax year (Ministry of Higher Education and Training, 2012). Since then, a research shortfall for every university (based on the development grant) has been experienced (Ministry of Higher Education and Training, 2012).

#### **2.5.5.3.1 National Student Financial Aid Scheme Grant**

According to the Ministry of Higher Education and Training (2016b), the state budget for the university sector, as it relates to the National Student Financial Aid Scheme (NSFAS) grant, increased from R4.1 billion in the 2015/16 year to R8.8 billion (55.1 percent) in the following year, with an estimated further increase of 55.7 percent and 4.8 percent in the succeeding two years.

The National Student Financial Aid Scheme is an independent juristic organisation set up by the government through the National Student Financial Aid Scheme Act (Act No. 56 of 1999) to manage student financial aid. The National Student Financial Aid Scheme, according to the Ministry of Higher Education and Training (2016b), is considered to be the most significant instrument available to government for opening access to technical and vocational education and training and higher education for the poor and working-class citizens of South Africa. The National Student Financial Aid Scheme's sole responsibility is to provide funding through loans and bursaries to eligible students at all South African universities and Technical and Vocational Education and Training colleges throughout the country (Ministry of Higher Education and Training, 2016b; Qonde, 2015).

In the 2016/2017 tax year, the National Student Financial Aid Scheme implemented a student-centred model with the aim of enabling the organisation to build a direct relationship with students from the initial application phase up until the completion of their studies (Ministry of Higher Education and Training, 2016b). For the 2017/18 tax year, funds meant to go to the Technical and Vocational Education and Training colleges, have been reprioritized to unfunded university students from the 2016-year, totalling R2.4 billion (Ministry of Higher Education and Training, 2016b). Treasury has furthermore made available a carry-through amount of R2.6 billion for the 2018/19 tax year as an additional

provision from what was budgeted to go to the Technical and Vocational Education and Training colleges (Ministry of Higher Education and Training, 2016b). This sudden and continuing reprioritisation of funding is an indication of the instability of the finances within the sector.

### 2.5.5.3.2 Gap Funding Grant

For the 2017/18 tax year, R2 459 800 000 has been set aside (once again through the reprioritisation of funds in the Technical and Vocational Education and Training sector) for a “gap funding grant” to pay the increase in university fees of up to 8 percent for all families with a combined income below R600 000 (Ministry of Higher Education and Training, 2016b). The students who qualify for this subsidy, referred to as the poor and “missing middle”, will experience a zero percent increase on their 2016 fees in 2017 (Ministry of Higher Education and Training, 2016b). Treasury has also made provision for the carry-through of an amount equal to R2 617 988 000 in the 2018/19 tax year for the same purposes (Ministry of Higher Education and Training, 2016b). The grant is managed by the Department of Higher Education and Training and the funds are not transferrable to the National Student Financial Aid Scheme (Ministry of Higher Education and Training, 2016b).

## 2.6 Funding Discrepancies

Since 1994, government support for higher education has increased (Cele and Goodman, 2016). The funding of universities has been on an upward trend, from R11 billion in 2006 to R26 billion in 2013 (Cele and Goodman, 2016). Funding for the 2016/17 tax year is currently at R39.5 billion (Cele and Goodman, 2016). The table below, according to the Department of Higher Education and Training and Training (2016), indicates the budget allocation for universities for the current to medium term:

**Table 1: University Funding Allocation, 2016/17 – 2018/19**

	Medium-Term Expenditure Estimate		
	2016/17	2017/18	2018/19
<b>University funding</b>	39 531 603	41 944 120	44 319 940

Government expenditure on higher education has been declining at an alarming rate both in real (adjusted for purposes of inflation) and student *per capita* terms (Cele and Goodman, 2016). It has been further declining as a percentage of government’s budget and of the gross

domestic product (Cele and Goodman, 2016). The decline in government subsidies has heightened the pressure on the other two main sources of income available to universities, namely: tuition fee income and third-stream income (i.e. external research grants, contract income, donations, etc.) (Cele and Goodman, 2016). While there has been a steady increase in third stream income by universities to some degree, these increases by no means compensate for the decline in government subsidies, leaving universities in an increasingly worse financial position (Cele and Goodman, 2016; Department of Higher Education and Training, 2016).

The following table, according to Sheppard (2016), highlights the disparities in university funding across South African institutions, where the traditionally white universities still benefit financially compared to historically black universities. It shows that the higher education gap is not just growing between those who do or do not have degrees, but among universities themselves (Cele and Goodman, 2016). Where government allocations are failing in providing more funds, historically white universities have private funds/income streams as well as high university fees to assist them (Cele and Goodman, 2016).

**Table 2: “White” Universities’ Income versus Student Body (2012-2013)**

	University of Cape Town		University of the Witwatersrand		Stellenbosch University		Rhodes University	
	2012	2013	2012	2013	2012	2013	2012	2013
<b>Student Numbers</b>	25 805	26 118	30 436	31 134	27 510	27 418	7 395	7 485
<b>Income R’000</b>	3 942 494	4 068 501	4 412 114	4 756 132	3 641 582	4 064 084	910 898	922 105

Source: (Sheppard, 2016).

**Table 3: “Black” Universities Income versus Student Body (2012-2013)**

	University of the Western Cape		Walter Sisulu University		Fort Hare University		Zululand University	
	2012	2013	2012	2013	2012	2013	2012	2013
<b>Student Numbers</b>	19 591	20 383	24 613	24 122	12 044	13 315	16 434	16 591
<b>Income R'000</b>	1 408 265	1 577 477	1 263 468	1 326 520	767 706	779 887	769 891	774 616

Source: (Sheppard, 2016).

In 2013, the University of Cape Town had a slightly higher student body than Walter Sisulu University, 1 996 more students to be exact, but the income difference was not proportional. The University of Cape Town had an income (excluding the state contribution) of R4.068 billion in 2013 as compared to Walter Sisulu University’s R1.326 billion, which is almost three times the amount. Rhodes University had less than half the student body compared to the University of Zululand, but exceeded their income by almost R150 million. Zululand had in excess of 9 000 more students than Rhodes University.

The majority of students enrolled at the “poor” universities are African and Coloured and mostly come from disadvantaged socio-economic backgrounds (Badat, 1999; Cele and Goodman, 2016). Additionally, the majority of these students come from poorly-performing schools, which leaves them poorly prepared for tertiary education and training (Cele and Goodman, 2016). Given the economically disadvantaged nature of the majority of students attending these universities, a low level of fees is maintained in order to allow for greater access and participation, translating into much lower fee income *per capita* for universities (Cele and Goodman, 2016). With this comes the challenge of high student debt (Cele and Goodman, 2016). The combination of low tuition fees and high student debt means that tuition fees are not a viable source of income. Adding to this, being isolated in a rural area, makes the possibility of generating third-stream income extremely difficult, if not impossible, for longevity purposes.

Due to various factors; including slow economic growth, increasing demands on government resources and decades of funding backlogs, free higher education and training for all is highly improbable, for the short to medium term at least (Stellenbosch University, 2016).

Universities are chronically underfunded with an annual increase that is less than the Consumer Price Index (CPI) (Stellenbosch University, 2016). At the start of the century, state contributions to university education (tuition only) were around 49 percent, declining to 40 percent by 2012 (Stellenbosch University, 2016). In the same period, student fees increased from 24 percent to 31 percent (Stellenbosch University, 2016).

The block grant which, as mentioned above, is one of the state's core contributors to higher education, increased by 5.5 percent in 2016/17 and 5 percent in 2017/18, while at the same time, the Consumer Price Index increased by 6.8 percent and 6.42 percent respectively, making higher education and training (in real terms) more expensive for the consumer (Stellenbosch University, 2016). The Higher Education Price Index (HEPI), which is considered a more accurate indicator of the inflation rate applicable to universities than the Consumer Price Index due to the higher costs of the Higher Education Price Index fixed basket of goods and services, is, in 2017, 1.7 percent higher than the Consumer Price Index (Stellenbosch University, 2016). The inflation rate in the higher education and training sector is higher because of the expensive facilities, imported equipment as well as international research publications of universities, for instance (Stellenbosch University, 2016).

The zero percent increase in tuition fees for 2016 and 2017 and its likely continuation into future years, is not as a result of additional available funding through a grant subsidy from the National Treasury, but is a reprioritisation of current funding (Ministry of Higher Education and Training, 2016b). South African universities differ quite substantially in shape, size and composition, which results in varying student fees. A "one size fits all" fee increase is therefore not optimal or sustainable.

The failure to increase state funding is likely to compromise the medium-term financial sustainability of at least two thirds (17) of the universities in the sector (27) (Stellenbosch University, 2016). This is without taking into account Technical Vocational Education and Training colleges. These circumstances prevail amidst pressures from the Department of Higher Education and Training to increase intake and the throughput rate of students (Stellenbosch University, 2016).

Universities are currently in a position where there is no other option but to adjust internal tuition and accommodation fees in a reasonable manner in order to meet the necessary academic and financial demands. Universities, such as Stellenbosch University, have focused on increasing the internally generated funding and bursary support (Stellenbosch University,

2016). Greater internal support for the “missing middle” has been provided (especially the lower income bracket of this missing middle) with an overall increase of bursary support of more than ten percent since 2011 (Stellenbosch University, 2016). However, as long as historically black universities remain under-funded, the problems of equity, transformation and redress will not be addressed.

## **2.7 Government’s Inability to Fund Free Higher Education and Training for All from the National Fiscus**

In the 2016/17 tax year, budgeted national government revenue stood at approximately R1.21 trillion with national expenditure at R1.41 trillion (National Treasury, 2017). While expenditure increased by 7.8 percent from the previous year, South Africa experienced a national budget deficit of 3.1 percent of gross domestic product (GDP), which was covered by borrowing. This deficit is extremely concerning as the debt continues to increase. According to the National Treasury (2017), as it stands in the 2016/17 tax year, the accumulated national debt is at R2.2 trillion. This amount translates to 50.7 percent of gross domestic product (National Treasury, 2017). As a result, interest payments have become a significant and rising share of expenditure (National Treasury, 2017). What is of further concern is that in the medium-term budget, the deficit is said to increase from R16.7 billion in 2016/17, to R17.1 billion in 2017/18 and to R18.1 billion in 2018/19, even with government’s aim of reducing spending by R26 billion over the medium term (National Treasury, 2017). The rising debt, through increased expenditure, is an indication of government’s inability to further invest in higher education and training, at least over the medium term.

A reprioritisation of the state budget will result in the neglect of other important state funded departments, such as health care and basic education (University of the Witwatersrand, 2016). The estimated cost of free higher education and training (including costs of accommodation, meals etc.) for all is said to cost between R95 billion to R150 billion per year (Cele and Goodman, 2016). According to the Department of Higher Education and Training (2016), an approximate R30.6 billion was allocated to the sector for the 2016/17 year. If such an allocation of the state budget were made towards higher education and training in the pursuit of free education for all, it would be the single highest expenditure item (National Treasury, 2017). It is, however, argued that government would save a great deal on “bailouts” (for example) through the privatization of certain State-Owned Enterprises such as

the South African Airways, as well as through a cut in unnecessary government personnel costs and corruption (University of the Witwatersrand, 2016; Cele and Goodman, 2016). However, such expenditure saving mechanism will not suffice in realizing the hope of free education for all (University of the Witwatersrand, 2016; Cele and Goodman, 2016).

## **2.8 Conclusion**

In this chapter a brief overview of the historical, as well as present challenges as they relate to higher education and training, were discussed. Together with this, a discussion of the past and present funding formulae for higher education was presented. It is clear that the funding of higher education and training in South Africa was previously skewed to entrench the privilege and educational ambitions of a minority, the effect of which can still be seen within the sector today. The funding models adopted were highly regulated, racially biased and did not accommodate the needs of the students, but rather state interests.

Since the advent of democracy, a number of a policy documents that were issued highlight the need for policy coherence and stable funding incentives and formulae to address widening inequality and the unaffordability of education in South Africa. However, implementation of policies to address this has not been evident. The funding formulae, from the 1950s until today, have been ever changing, ultimately lacking stability. This instability is closely associated to, and part of the reason why, a lack of funding management and prioritisation has taken place. Not having the funding available is one problem, being unable to manage what is currently available, is another. The challenges still faced today are deeply rooted in Apartheid and the present lack of transformation and leadership within the sector.

As indicated in the discussion, the higher education and training sector is seriously underfunded, with a decrease in the allocation to the sector by government and the National Treasury in real terms. In addition to this, the funding allocation framework does not fully consider the historical and socio-economic environment of universities and with this, allocate funds accordingly. More should be done to adjust the current and future allocations with the view to ensuring that funding is allocated in accordance with the goals set out in the Higher Education White Paper and National Plan on Higher Education.

In order to ensure that the private sector cost of education decreases, or at least remains stable in the short-term, it is suggested that the government contribution to the sector should (at least) be in line with that of the Higher Education Price Index. South Africa is in debt to the

extent of 50.7 percent of gross domestic product (National Treasury, 2017), indicating its inability, as a government, to increase its contribution to the sector. Together with this, the publication by the University of the Witwatersrand (2016) has shown that the government is unable to re-prioritize the budget from other departmental sources without negatively affecting their functionality.

Lastly, as result of the underfunding, an enormous amount of pressure has been placed on the university and private sector to source funds. The government could work towards providing greater incentives to the private sector so that they contribute towards the success of the sector. One way of providing an incentive for the private sector to invest in the higher education and training sector is through tax incentives. The following chapter will focus on the tax incentives, as they relate to higher education and training, currently available in South Africa.

### **3 CURRENT TAX INCENTIVES, DEDUCTIONS AND EXEMPTIONS AS THEY RELATE TO HIGHER EDUCATION AND TRAINING**

#### **3.1 Introduction**

Although major budgetary and/or fiscal reform would be needed in order to ensure greater access and financial stability within the higher education and training sector, this would be unaffordable for government. A means of encouraging the private sector to assist would be through tax incentives. There are existing tax incentives available for employers and employees in training and developing the skills of the current and potential workforce. These may very well partly address the tertiary education funding problem in South Africa.

This chapter seeks to address the third goal of the research, focusing on the current South African tax incentives available to the taxpayer as they relate to expenditure on education and training.

The Higher Education and Training Department, according to the National Treasury (2016a), has recognised the importance of tax incentives as a measure in aiding the funding shortfall in training and skills development. As a result, many of the current incentives, which this chapter seeks to explore, have been revised upwards in order to provide more support for scarce skills, particularly for artisans. In this chapter, the theoretical, legal and practical factors informing these incentives (and their development) are explored. Together with this, this chapter focuses on the steps taken by the South African government in alleviating the high costs associated with higher education and training for the student (and their donors) and explores the incentives available to the individual and corporate sector in South Africa in advancing this cause.

#### **3.2 General Principles for Deduction of Expenditure**

There are no provisions in the Act that allow specifically for the deduction of expenditure on education and training, other than section 12H, which deals with learnership agreements (Goldswain, 2017). Therefore, the general deduction formula, as set out in the preamble to section 11 and section 11(a), read together with section 23(g), of the Act must be referred to for purposes of claiming a deduction as it relates to training and education expenditure. According to section 11(a) of the Act, for the purposes of determining the taxable income derived by any person from carrying on any trade, “there shall be allowed as a deduction from the income of such a person (a) expenditure and losses actually incurred in the

production of the income, provided such expenditure and losses are not of a capital nature.” While section 11(a) of the Act provides positively for what may be deducted, section 23(g) of the Act provides negatively for what may not be deducted. According to section 23(g) of the Act, “any moneys, claimed as a deduction from income derived from a trade, to the extent to which such moneys were not laid out or expended for the purposes of a trade” shall not be allowed. Thus, the prerequisite for any deduction, in terms of section 11(a) of the Act, is that a trade, to which the expenditure relates, must be undertaken. The term “trade” is defined in section 1 of the Act and includes:

every profession, trade, business, employment, calling, occupation or venture, including the letting of any property and the use of, or the grant of permission to use any patent, or any design or any trade mark, or any copyright, or any other property which is of a similar nature.

In the case of *Burgess v CIR, 1993 AD*, the court ruled that the activities, which constitute a trade, should be “given the widest possible interpretation”. While, as defined, a “trade” covers a wide spectrum of activities, there are certain activities that fall outside of the scope of the definition (Haupt, 2016). Of these, the most common are investments made in dividend and interest-bearing stock (by persons other than share dealers and moneylenders) (Haupt, 2016).

In terms of section 11(a) of the Act, and whether or not education and training meet the requirements as set out in the general deduction formula, the two questions relate, firstly, to whether or not such expenditure is regarded as of a capital or revenue nature. If the expenditure is capital in nature, the enquiry ends there, and the cost may not be deducted. If the expense is regarded as revenue in nature, then the requirement of “in the production of income” must be met. Normally, according to *Port Elizabeth Electric Tramway Company v CIR, 1936 CPD 241 8 SATC 13*, the requirement will be met if the education or training is “closely connected” to the trade. For example, if an audit firm sends a clerk on a gardening course, it is highly improbable that such expenditure has been “incurred in the production of income”. On the other hand, if the audit clerk was sent to an auditing seminar, the expenditure would classify as having been “incurred in the production of income” and thus deductible by the audit firm in terms of section 11(a) of the Act.

There is no specific definition of what is considered capital expenditure. *New State Areas Ltd v CIR, 1946 AD 619 14 SATC 155*, held that the questions to be asked are: has an income earning structure been created? An income earning structure relates to a capital improvement

or addition. Secondly, does the expenditure create an enduring benefit? The issue of the capital nature of expenditure was also considered in *CIR v George Forest Timber Co Ltd, 1934 AD*, in which it was held that an expense in acquiring an ongoing source of profit was a capital expense (at 41):

. . . now money spent in creating or acquiring an income producing concern must be capital expenditure. It is invested to yield a future profit; and while the outlay does not recur, the income does. There is a great difference between money spent in creating or acquiring a source of profit and money spent working it. The one is capital expenditure and the other is not.

Expenditure incurred by an individual in obtaining a formal degree or diploma, for example, may add value to a person's knowledge, which enables him or her to carry out his or her profession and earn money. The expenditure has been incurred in the production of income (or future income), but the expense would be of a capital nature since the professional person is acquiring, creating and/or enhancing his or her ability to earn an income. The cost involved would convey an enduring benefit. Because of the capital nature of the expense, the person could not claim a deduction for tax purposes and therefore no reduction in the cost of education could be achieved. A person undergoing the education may, for example, be doing a "refresher course" and may not be adding to his or her "capital", but merely maintaining the ability to apply this "capital" in his or her income-earning operations, thus a revenue expense. The specific circumstances of each individual case need to be fully examined before any conclusion can be made.

In *Income Tax Case 1066, 1964 27 SATC 114*, a specialist surgeon incurred expenditure on attending a medical congress, which was aimed at improving his knowledge on specific aspects of his work. The expense was disallowed under the (now deleted) section 16 of the Act (postgraduate study courses for dentists, medical practitioners, engineers and scientists) and was not allowed under section 11(a) because the attendance created an "enduring benefit" and the expenditure constituted a capital expense. The expenditure was also held not to be sufficiently "closely connected" to the production of income and could therefore not be regarded as forming part of the cost of performing his income-earning activities.

It is apparent, therefore, that each case must be dealt with on its own facts and a decision must be made as to whether the expenditure is incurred to acquire or create an income-

producing asset or whether the expenditure is incurred in actually working the income-producing asset, i.e., producing the income.

Where a company sends an employee on a training course relevant to the company, whether in the short or long term, the purpose for the company sending the employee on the course is to improve the employee's knowledge, ability to work and to generate income for the company. Thus, from the company's point of view, the expenditure is considered to be "in the production of income" (Goldswain, 2017). Nevertheless, the question remains, is the expense of a capital nature? Has the company obtained an enduring benefit? How long will the employee remain with the company? If there is no obligation for the employee to remain with the company, the employee could resign the day after completing the course and, as a result, no enduring benefit for the company exists. If there is an obligation for the employee to remain with the company, then there could be an enduring benefit. Ultimately, it is not the company that is obtaining the knowledge, but rather the employee. Therefore, it is arguable that, in the instance where the person receiving the education or training is merely an employee, the expenditure may not be of a capital nature (Goldswain, 2017). However, if the employee is a major shareholder of the company, different considerations may apply, as it is assumed that he or she will remain with the company for the near future (Goldswain, 2017). In such circumstances, it is likely that the company has acquired an "enduring benefit" through the knowledge gained by the shareholder and the attendant expenditure will be of a capital nature. The same situation would apply if the taxpayer were a sole proprietor, for example.

In *Income Tax Case No. 1433, 1988 50 SATC 73*, an employee attended an international workshop overseas in order to stay abreast of the latest developments in computer software. He attended the workshop in order to carry out his business duties of giving computer advice. Due to the rapidly changing computer and technological environment, the knowledge was not considered to be of a lasting or enduring benefit, but only of a temporary benefit. Thus, the amount was not considered to be "capital in nature" and was "incurred in the production of income". Therefore, the expenditure was deductible.

Fees payable by practising attorneys, chartered accountants and other professionals, in attending courses as part of their continued education and training in their respective professional associations, are generally considered as deductible (Goldswain 2017). According to Goldswain (2017:06), as cited in Accounting SA (1990:10), the Commissioner

has indicated that the following expenditure would be allowed as a deduction under section 11(a) of the Act:

- fees paid by practising attorneys, chartered accountants and the like (CIS, CIMA etc.) in attending courses conducted by their national professional bodies (e.g. SAICA for chartered accountants) in their programmes of continuing professional education will qualify as a deduction in the determination of the taxable income of their members; and
- expenditure incurred by other professional persons (e.g. doctors, dentists and engineers in attending course or congresses in South Africa as part of a continuing education programme designed to keep such persons abreast of developments and do not lead to any recognised educational qualification will be considered for deduction under section 11(a) of the Act.

According to section 23(m) of the Act, no deduction shall in any case be made in respect of the following (subject to certain exclusions):

. . . subject to paragraph (k) [the deduction of contributions to retirement funds], any expenditure, loss or allowance, contemplated in section 11, which relates to any employment of, or office held by, any person (other than an agent or representative whose remuneration is normally derived mainly in the form of commissions based on his or her sales or the turnover attributed to him or her) in respect of which he or she derives any remuneration, as defined in paragraph 1 of the Fourth Schedule.

A taxpayer, in normal circumstances, would not be able to claim a deduction for any costs in connection with higher education and training if such costs are related to any employment of the person. If an employee who earns remuneration otherwise than mainly in the form of commission bears the cost of his or her personal education or training the amount will not be deductible. However, if the employer bears the costs of the courses, the employer may be entitled to the deduction, if it is not of a capital nature (see above).

Where an employer, therefore, is able to claim as a deduction the cost of education and training of employees, this could provide an incentive that would enable these employees to be trained or educated at no cost to themselves.

### **3.3 Section 12H of the Income Tax Act**

Section 12H of the Income Tax Act (the Act) provides for an allowance to employers in respect of qualifying “registered learnership agreement(s)” entered into between the employer

and employee. According to section 12H of the Act, a learnership agreement must be signed between a learner, an employer and an accredited training provider for a specified nature and duration, which must lead to a qualification that will be registered with the South African Qualifications Authority (SAQA). The allowance is intended to serve as a funding incentive for employers to train employees in a regulated environment in order to encourage skills development and job creation. According to section 12H of the Act, a registered learnership agreement is defined as one that is:

- registered in accordance with the Skills Development Act, 1998; and
- entered into between a learner and an employer before a date specified in the Income Tax Act.

Section 12H of the Act provides that if a learnership agreement has not been registered in accordance with the Skills Development Act from the inception of the agreement, such agreement will be deemed to have been registered on the date it was entered into, as long as actual registration takes place within 12 months after the last day of the employer's year of assessment. This is because of an amendment to section 12H of the Act (effective from 01 January 2013) in which the reality of delays in registration of agreements, through no fault of the employer, is taken into account.

In terms of the actual allowance, the allowance is made up of both:

- an annual allowance, which is available in respect of each year of assessment to which the learner is party to a registered learnership agreement; and
- a completion allowance, which is a once off allowance available in the year of assessment in respect to which the learner successfully completes the registered learnership agreement and is awarded in addition to the annual allowance.

The annual allowance is apportioned if the registered learnership agreement does not cover the full 12 months during any year of assessment. Additionally, different rules apply in determining the completion allowance for registered learnership agreements spanning periods of less than 24 months, and those that cover a longer period. For example, those agreements with a duration of less than 24 months will only be afforded the applicable allowance for the number of full 12-month periods for which the employee was registered.

The availability of the learnership allowance was due to end, with the last allowance being available in respect of any learnership agreements entered into before 01 October 2016. However, after National Treasury (2016b) conducted research into the effectiveness of the learnership allowance as a means of creating more employment, assisting with the funding of employees and thereby growing the economy, a decision was taken to extend the learnership allowance. In light of this, an allowance will now be available in respect of learnership agreements entered into after 30 September 2016, but before 01 April 2022. Allowances in respect of registered learnership agreements entered into before 01 October 2016 will be based on the rules applicable prior to the 2016 amendment.

In addition to the extension of the period for which the allowance is now available, further amendments have been made with respect to the *quantum* of the allowance. The allowances afforded to an employer in terms of section 12H of the Act, are as follows:

<b>Learners with no disabilities:</b>
Annual allowance: <ul style="list-style-type: none"> <li>• NQF level 1 – 6: R 40 000</li> <li>• NQF level 7 – 10: R 20 000</li> </ul> Completion Allowance: <ul style="list-style-type: none"> <li>• NQF level 1 – 6: R 40 000</li> <li>• NQF level 7 – 10: R 20 000</li> </ul>
<b>Learners with disabilities:</b>
Annual allowance: <ul style="list-style-type: none"> <li>• NQF level 1 – 6: R 60 000</li> <li>• NQF level 7 – 10: R 50 000</li> </ul> Completion Allowance: <ul style="list-style-type: none"> <li>• NQF level 1 – 6: R 60 000</li> <li>• NQF level 7 – 10: R 50 000</li> </ul>

Table 7 below illustrates the total value of the learnership tax incentives claimed for completed years under review. As illustrated in Table 7, the finance sector has the largest sectoral share of allowances and/or incentives claimed. Between the years of 2009 and 2014, the total value of claims attributable to the sector was R4.9 billion, accounting for 36.3 percent of total claims (R13.4 billion). Wholesale and retail, and manufacturing are the next

largest claiming sectors, together accounting for 35.5 percent of total claims registered. The total deduction for the tax incentive in the latest year of assessment under review (2014) amounted to R1.9 billion. This equates to approximately 63 333 registered learnership agreements in 2014 (National Treasury, 2016b). Furthermore, the learnership tax incentive cost the fiscus, in total, approximately R13.4 billion for the 2009 – 2014 tax periods (National Treasury, 2016b).

**Table 7: Value of Claims for Learnerships Registered in current Year by Sector**

<b>Sector</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>Total</b>
Manufacturing	59.4	379.4	429.3	630.5	516.8	323.1	2 338.4
Mining and Quarrying	28.2	198.5	113.1	176.8	154.8	40.2	717.7
Transport, storage and communications	6.5	117.9	122.4	184.6	156.4	130.7	718.6
Wholesale and retail trade, catering and accommodation	31.9	434.1	441.9	663.3	543.5	319.5	2 434.3
Financial intermediation, insurance, real-estate and business services	71.9	911.2	1 131.0	1 209.6	959.5	594.0	4 877.1
Electricity, gas and water	8.1	6.2	32.9	269.5	3.3	281.0	600.9
Construction	5.3	54.6	99.4	89.0	79.4	47.4	375.1
Community, social and personal services	31.3	240.1	258.7	218.6	214.9	110.9	1 074.6
Other	4.4	3.3	3.5	1.9	16.2	23.9	53.1
Agriculture	8.2	43.9	57.2	45.8	63.5	29.3	247.9
<b>Total (R mill)</b>	<b>255.0</b>	<b>2 389.1</b>	<b>2 689.4</b>	<b>3 489.8</b>	<b>2 708.3</b>	<b>1 900.1</b>	<b>13 431.6</b>

Source: (National Treasury, 2016b:11)

Another element in the learnership statistics is that, as a proxy for firm size, larger firms in the manufacturing and wholesale and retail sectors (with gross income of R50 million and above) had the most learnership tax incentive claims during tax years under review (National Treasury, 2016b). For the finance sector, however, the claims were distributed much more evenly across various firm sizes (National Treasury, 2016b).

### **3.4 Section 11D of the Act**

In an attempt to encourage research and development in South Africa, section 11D of the Act was introduced to provide a tax incentive that seeks to encourage the private sector to invest in scientific and technological research and development. The purpose of this particular tax incentive is to ensure that, firstly, research and development activities are undertaken more cost-effectively and that, secondly, the economy is stimulated.

Under the provisions of section 11D of the Act, two types of tax deductions are allowable. First, there is a 150 percent deduction on expenditure incurred directly for research and development purposes and secondly, an accelerated depreciation deduction for capital expenditure on any buildings or part thereof, such as, machinery, plant etc. used solely for purposes of research and development. In order to qualify for these tax incentives, a taxpayer must meet various stringent requirements relating to the taxpayer, the particular expenditure and the activities conducted. The particular activity must be in the pursuit of advancing scientific and/or technological knowledge in general.

The requirements of section 11D of the Act state that the taxpayer must operate a trade and must intend to apply the research and development outcomes to generate income. Moreover, the taxpayer must have incurred the expenditure directly for research and development purposes. For example, accommodation costs incurred by a researcher while attending a conference – even though the conference related to the research and development of a qualifying activity – are not tax deductible. Section 11D(5) of the Act further provides that no deduction is allowed for the costs of exploration or prospecting, trademarks, market research, legal and financial activities, sales or marketing.

According to section 11D (7) of the Act, the deduction for research activities funded by a third party, such as commissioned work, is limited to a 100 percent, and not a 150 percent, deduction. If research is funded through a taxable government grant, expenditure equal to twice the grant amount is deductible at 100 percent. Costs incurred in excess of twice the grant are deductible at 150 percent. If the grant is tax exempt, expenditure equal to twice the grant amount is not allowed at a deduction. However, the excess of twice the grant amount will then be allowed as a deductible expense at 150 percent.

The incentives granted in terms of section 11D, however, are restrictive in that they are only granted in respect of expenditure actually incurred in the production of income by persons

carrying on a trade. Furthermore, the research and development must be carried on in the Republic.

### **3.5 Exemption in terms of Section 10(1)(q) of the Act**

Section 10(1)(q) of the Act provides for the exemption from income tax of any *bona fide* scholarship or bursary granted to enable or assist any person to study at a recognised educational or research institution, provided that the scholarship or bursary has been granted by an employer (or an associated institution) to an employee or to a relative of such employee.

A “*bona fide* scholarship or bursary granted” refers to financial or similar assistance granted to enable a person to study at a recognised educational or research institution (South African Revenue Service, 2014). Such financial aid may be awarded with or without taking into account academic merit, and would include a grant that is, in terms of a written agreement, conditional upon the performance, or ultimate completion of, specific requirements (South African Revenue Service, 2014). Furthermore, the grantee may, for example, be required to complete the qualification within a certain time-period, with certain stipulated marks and/or be required to take up employment with the grantor on the completion of the course of study (South African Revenue Service, 2014).

The grant must serve the purpose of allowing the grantee the opportunity to pursue a course of study, the purpose of which is to gain or expand his or her knowledge, aptitude or/and skills (South African Revenue Service, 2014). A reward or reimbursement of study expenses after the completion of studies does not qualify for the exemption, as the grant must be awarded for the sole purpose of providing the student with the necessary funding to study (South African Revenue Service, 2014). A *bona fide* scholarship or bursary, according to South African Revenue Service (2014:02) could include the costs of the following:

- tuition fees;
- registration fees;
- examination fees;
- books;
- equipment (required in that particular field of study, for example, financial or scientific calculators);
- accommodation (other than the person’s home);
- meals and meal voucher/cards; and

- transport (from and to campus).

A “recognised educational or research institution” is one which, according to South African Revenue Service (2014), has been established by or recognised under the laws of South Africa, for example, the Higher Education Act, 1997, the Skills Development Act, 1998, or the National Research Foundation Act, 1998. The exemption would also be allowed if the scholarship or bursary is granted to study at a foreign educational or research institution if the qualification obtained from that institution (upon the completion of such studies) would be recognised by the South African Qualifications Authority under the National Qualifications Framework Act, 2008 (South African Revenue Service, 2014).

According to the South African Revenue Service (2014), the words “to study” refers to the formal process whereby the person to whom the scholarship or bursary has been granted gains or enhances his or her knowledge, aptitude or expertise in the pursuit of learning. It is not a requirement, however, that a formal degree, diploma or certificate or any kind be attained on completion of the course of study (South African Revenue Service, 2014).

The exemption is, however, limited and shall not apply, according to section 10(1)(q):

- (i) in the case of a scholarship or bursary granted to so enable or assist any such employee, unless the employee agrees to reimburse the employer for any scholarship or bursary granted to that employee if that employee fails to complete his or her studies for reasons other than death, ill-health or injury;
- (ii) in the case of a scholarship or bursary granted to enable or assist any such relative of an employee so to study –
  - (aa) if the remuneration proxy derived by the employee in relation to a year of assessment exceeded R400 000; and
  - (bb) to so much of any scholarship or bursary contemplated in this subparagraph as in the case of any such relative, during the year of assessment, exceeds –
    - (A) R15 000 in respect of a qualification to which an NQF level from 1 up to and including 4 has been allocated in accordance with Chapter 2 of the National Qualifications Framework Act, 2008 (Act No. 67 of 2008); and
    - (B) R40 000 in respect of a qualification to which an NQF level from 5 up to and including 10 has been allocated in accordance with Chapter 2 of the National Qualifications Framework Act, 2008 (Act No. 67 of 2008).

With the purpose of supporting skills development and the private sector (employers in particular) in the provision of education and training, government sought to increase (with effect from 1 March 2016) the level of the limit (National Treasury, 2016a). The effective monetary limit increase for bursaries and scholarships granted by employers to employees (or relatives of qualifying employees) increased as follows (National Treasury, 2016a:08):

- i. an increase from R250 000 to R400 000 in respect of the monetary limit of remuneration for qualifying employees; and
- ii. an increase from R10 000 to R15 000 and from R30 000 to R40 000 in respect of the monetary limit of exempt bursaries and scholarships.

While section 10(1)(q) exempts the scholarship or bursary in the hands of the recipient or employee, the deductibility of the scholarship or bursary by the grantor is subject to the general provisions of the preamble to section 11, section 11(a) and section 23(g). *Income Tax Case No. 1129, 1969 31 SATC 144 (R)*, illustrates one situation where bursaries were not a deductible expense. The taxpayer awarded bursaries to three students and deducted these amounts as having been incurred by the taxpayer for the sole purpose of advertising and, as a result, claimed that the amounts were not of a capital nature, but exclusively incurred in the “production of income”. The court, however, ruled that the objective of awarding the bursaries was to increase the taxpayer’s goodwill; it was incurred in order to improve the appellant’s public image. In such a circumstance, the court held that the bursary awards were of a capital nature, as the expenditure was more closely related to the taxpayer’s income-earning structure than to the taxpayer’s income-earning operations.

Any amount which arises as a recoupment in respect of a scholarship or bursary granted by a taxpayer, which amount had previously been allowed as a deduction against the taxpayer’s income, will, in terms of section 8(4)(a) of the Act, be included in the taxpayer’s income in the year of assessment in which such amount is recouped (South African Revenue Service, 2014).

### **3.6 Study Loans**

A loan, whether for purposes of study or other purposes, does not constitute income for normal tax purposes as a loan is of a “capital nature” and is, therefore, not subject to income tax (South African Revenue Service, 2014). Personal loans from a financial institution, or from any other source unrelated to the individual’s employment, are not taken into

consideration for purposes of section 10(1)(q) of the Act, nor are the study expenses incurred by the holder of the loan, together with the interest payable thereon, deductible from the income of the borrower (South African Revenue Service, 2014). Personal loans are, therefore, neither taxable or tax deductible (South African Revenue Service, 2014).

According to paragraph 2 of the Seventh Schedule to the Act, and paragraph (i) of the definition of “gross income” in section 1 of the Act, a taxable benefit is deemed to have been granted by an employer to his employee in respect of the employee’s employment with the employer, if the employee has received (or is to receive) a benefit, advantage or reward, by virtue of his or her employment. While this Schedule specifically deals with benefits to be included in the taxable income of an employee, no value is placed on a benefit that is enjoyed by an employee for furthering his or her studies.

According to paragraph 2(f), read with paragraph 11, of the Seventh Schedule to the Act, where a debt (in the form of a loan) has been incurred by an employee, whether in favour of the employer or in favour of any other person or any associated institution in relation to the employer, and no interest is payable by the employee in respect of such debt, or interest is payable at a rate lower than the official rate of interest, the difference between this amount and the amount which would have been payable on the amount owing in respect of the loan for that year of assessment, is to be included as a benefit in the taxable income of the employee.

In terms of paragraph 11(4)(b) of the Seventh Schedule to the Act, however, no value is placed on a benefit derived by an employee in consequence of a grant granted by any employer to an employee of any low-interest or interest-free loan for the purpose of enabling that employee to further his or her own studies. Any scholarship or bursary, which is granted subject to repayment due to non-fulfilment of conditions as stipulated in the written contract, will be treated as a *bona fide* scholarship until such a time as the non-compliance provisions of the agreement are invoked (South African Revenue Service, 2014). In the year of assessment in which such provisions are in fact invoked, the amount (or amounts) of the scholarship or bursary will be regarded as a loan and, if relevant, any benefit which an employee may have received by way of an interest-free or low-interest loan will constitute a taxable benefit in terms of paragraph 2(f) of the Seventh Schedule to the Act. Thus, the employee will not qualify for the exemption provided for in paragraph 11(4)(b) of the Seventh Schedule to the Act, as the loan was not granted to enable the employee the

opportunity to study. An employee will be subject to a taxable benefit, in terms of paragraph 2(h) of the Seventh Schedule to the Act, if he or she is absolved from repaying a loan received from his or her employer in order to enable him or her to study.

An employee, who had previously been granted a bursary, study loan or similar assistance on condition that the employee will render services to that employer for an agreed period (either during or after the assisted period), may be required to refund that employer the full amount (or a portion of the amount) if the employee leaves the employment of that employer before the expiry of the agreed period (South African Revenue Service, 2014). In such a case, no value shall be placed on the benefit (that is, the payment of the employee's debt by the new employer) if the employee has undertaken to work for the new employer for (at least) the unexpired period of the contract with the former employer (South African Revenue Service, 2014). This therefore means that the benefit will not be subject to tax in the hands of the employee (South African Revenue Service, 2014).

### **3.7 Other Forms of Study Assistance**

Expenditure incurred on in-house or on-the-job training provided by an employer to his employees for better performance of their duties, does not represent a taxable benefit in the hands of the employee, if the training is job-related and at the employer's premises (South African Revenue Service, 2014). This is in terms of paragraph 10(2)(c) of the Seventh Schedule to the Act, which provides that no value will be placed on a benefit derived by employees for services rendered by the employer to his or her or its employees at their place of work for the better performance of their duties. The types of training courses that, according to South African Revenue Service (2014:08), could be envisaged under this subsection include:

- computer and word-processing courses;
- management and administration courses;
- bookkeeping courses;
- sales courses;
- courses in operation office and technical equipment
- language courses for employees whose home language is not one of the official languages
- public relations courses;
- in-house courses presented by banks or building societies; and

- soft-skill training, for example, work-life balance or employment equity training.

The in-house or on-the-job training must be distinguished from professional and any other formal education resulting in a qualification of one or another kind (South African Revenue Service, 2014). The employee will, subject to the provisions of section 10(1)(q) of the Act, be regarded as having received a taxable benefit if, for example, the admission to a particular specialised duty is dependent on an appropriate qualification and the employer then subsidises the costs (South African Revenue Service, 2014).

Fees that are payable by an employer in terms of the law, as in the case of the Skills Development Act, 1998, on prescribed workshops or courses attended by his, her or its employees, or fees refundable for these reasons, will not constitute a taxable benefit in the hands of the employee (South African Revenue Service, 2014). These types of courses are not provided to employees as a benefit or advantage of or by virtue of employment, or as a reward for services rendered or to be rendered, but by virtue of an obligation imposed under the law (South African Revenue Service, 2014). The employer will, in most cases, qualify for a deduction for these payments in terms of section 11(a) of the Act.

### **3.8 Deduction of Donations in terms of Section 18A of the Act**

In terms of section 18A of the Act, there shall be allowed as a deduction from the taxable income of any taxpayer so much of the sum of any *bona fide* donation by that taxpayer (in cash or property) which was actually paid or transferred during the given year of assessment. This section has relevance in this research as such a donation may have been made pursuant to the advancement of education and/or training. This may be in the form of cash (i.e. payment of fees) or through the donation of specific property to an institute of higher learning and/or training.

According to section 18A of the Act, a deduction (subject to a limit) is allowed in respect of the sum of any *bona fide* donation in cash or kind made by a taxpayer, during a year of assessment, to any –

- public benefit organisation as defined in para (a)(i) of section 30(1) of the Act; or
- institution, board or body contemplated in section 10(1)(cA)(i); or
- government or any provincial administration or local authority as contemplated in section 10(1)(a) or (b) to be used for purposes of any activity contemplated in Part II of the Ninth Schedule.

Taxpayers, who may or may not be carrying on a trade, could donate, whether in the form of cash or assets, to a public benefit organisation that is involved in higher education and training activities, and obtain some income tax relief. The taxpayer may not necessarily be assisting through providing direct funding, but would be assisting by providing necessary resources useful to the sector, and would be doing so in a tax efficient manner.

Subsection 30(1)(b)(i) of the Act provides that any public benefit organisation (as described) must be carrying on one or more public benefit activity that is conducted in a non-profit manner, or is altruistic or philanthropic in nature. The term “public benefit activity” is defined in section 30(1) of the Act as being any activity listed in Part I of the Ninth Schedule to the Act, or any activity listed by the Minister of Finance in the *Government Gazette* as being of a benevolent nature, having regard to the general needs, interests and well-being of the society. Part I of the Ninth Schedule to the Act, although fairly extensive, includes, as a public benefit activity, that of education and development.

According to section 18A(1)(A) of the Act, the deduction of a donation is limited. Where the taxpayer is a portfolio of a collective investment scheme, an amount determined in accordance with the following formula must be used in calculating such a deduction:

$$A = B * 0.005$$

In the formula, according to section 18A(1)(A)(AA) and (BB) of the Act:

“A” represents the amount to be determined

“B” represents the average value of the aggregate of all of the participatory interests held by investors in the portfolio for the year of assessment, determined by using the aggregate value of all the participatory interests in the portfolio at the end of each day during the year.

Where the taxpayer is not a portfolio of a collective investment scheme, the calculation to be used in determining the amount allowed as a deduction is, according to section 18A(1)(B) of the Act:

ten per cent of the taxable income (excluding any retirement fund lump sum benefit, retirement fund lump sum withdrawal benefit and severance benefit) of the taxpayer as calculated before allowing any deduction under this section: Provided that any amount of a donation made as contemplated in this subsection and which has been disallowed solely by reason of the fact that it exceeds the amount of the deduction allowable in respect of the year

of assessment shall be carried forward and shall, for the purposes of this section, be deemed to be a donation actually paid or transferred in the next succeeding year of assessment.

In summary, section 18A entitles a taxpayer (individual, company or trust) to deduct annually donations to certain public benefit organisations (which includes institutes of higher learning and education) not exceeding a certain percentage of taxable income.

A perceived weakness in the concession granted by the section, however, is that it implies that any income tax benefit would only be available if the taxpayer depletes his or her assets in a benevolent manner, as opposed to granting income tax relief for investing in education and training.

### **3.9 Value-Added Tax Act as it Relates to Education and Training**

According to section 12(h) of the Value-Added Tax Act, Value-Added Tax is exempt on the supply of education and training services, including accommodation fees and state-funded research, provided the institution is registered in terms of the Higher Education and Training Act No. 98 of 1998. Certain contractual research and other membership fees are, however, standard rated for Value-Added Tax purposes (PricewaterhouseCoopers South Africa, 2016). As a result of institutions providing both exempt and taxable supplies, an apportionment calculation needs to be done on an annual basis, making the management of their Value-Added Tax extremely complex.

Students studying at higher education and training institutions are required to acquire textbooks for the purpose of their studies. Nkosi (2014) reports that Lacea Loader, spokesperson of the University of Johannesburg, acknowledged that in 2014 the university management recognised the fact that textbooks were expensive and in most cases, not affordable to students. The cost of textbooks, which is incurred by the student (or sponsors) over and above the costs associated with tuition, accommodation, meals and other costs, are often seen as a luxury in a student's academic journey (Nkosi, 2014).

Kruger (2014) reports that Steve Novel, a qualified South African tax practitioner, suggests that the Value-Added Tax on books, as it currently stands, is too high. Books (for both recreational and study purposes) are subject to Value-Added Tax at 14 percent, an amount much higher than most countries that apply a Value-Added Tax system (Kruger, 2014). Kruger (2014) further reports that it is the belief of Novel that it is this high Value-Added

Tax percentage which has directly contributed to the high retail price of books, putting them out of financial reach for the majority of consumers. As a result, South African consumers are less likely to read books, something that should not be considered a luxury (Kruger, 2014). South Africa currently has an extremely low literacy rate, in comparison to other nations, thus adding to the argument why books (in general) need to be made more affordable to the consumer (Kruger, 2014). Furthermore, the Print Industries Cluster Council supports the argument that the zero-rating of Value-Added Tax on books would boost the efforts to promote literacy and reduce educational costs (Pillary, 2003).

Lobbyists have long advocated for the scrapping of Value-Added Tax on books, including textbooks (Nkosi, 2014). Former Finance Minister, Trevor Manuel had, in 2004, rejected a petition signed by over 100 000 people calling for books to be zero-rated (Nkosi, 2014). According to the then Treasury spokesperson, Phumza Macanda, it was their view that consumers would probably receive a relatively small portion of any benefit arising from a zero-rating (Nkosi, 2014). They considered that the zero-rating would be likely to benefit the supplier more than the consumer, as is the case with a large number of items which are currently zero-rated (Nkosi, 2014). The supplier would benefit through including in the price of the textbooks the 14 percent and thus increase their profit on the sales. This is of course *ceteris paribus* to there being no price ceiling on textbooks and without taking into account the elasticity of market, among other considerations. Also, this was said despite Jeffery Mabelebele, chief executive of Higher Education South Africa at the time, calling on Treasury and South African Revenue Service to add academic books to the list of zero-rated items (Nkosi, 2014). Nkosi (2014) reports that according to Mabelebele, this will not only increase the amount of money available to be spent on academic books, but will also significantly reduce the purchasing costs borne by universities and students alike. The call, as reported by Nkosi (2014), is supported by Mpuka Radinku, executive director of the Publishers Association of South Africa.

The Organisation for Economic Co-operation and Development (OECD) (2008) recommends, as an additional argument that as all Value-Added Tax is ultimately returned to the government the Value-Added Tax charged on school and library books should be ring-fenced and invested into ensuring that all schools are fully provided with textbooks and a basic library of support material. This argument could then be further extended to higher education and training as well.

### **3.10 Employment Tax Incentive**

The Employment Tax Incentive Act No. 26 of 2013 (The Tax Incentive Act), while not directly related to any higher education and training tax relief, does seek to provide an incentive to employers by encouraging employers to employ young work seekers, often those who have just completed their tertiary studies and needing employment in order to assist with high university or college debt. The aim of the incentive is to reduce the employers' costs associated with the hiring of young people through a cost-sharing mechanism with government, by allowing the employer to reduce the amount of employees' tax payable and, at the same time, leaving the salary received by the employee unaffected (National Treasury and South African Revenue Service, 2016b). Furthermore, it aims to incentivise potential students into furthering their education knowing that job opportunities, serving as an initial source of university debt repayment, is guaranteed. The incentive was implemented with effect from 1 January 2014, and was to expire on 31 December 2016 (National Treasury and South African Revenue Service, 2016b). However, according to National Treasury and South African Revenue Service (2016b), the incentive has been extended for an additional two years until 28 February 2019.

According to National Treasury and South African Revenue Service (2016b), many young South Africans are excluded from economic activity within society and, as a result of this, suffer disproportionately from unemployment, personal discouragement and economic marginalisation. High youth unemployment means that young people are not gaining access to the relevant skills, experience, training and education needed to drive the economy forward, resulting in long-term adverse effects on the individual and the South African economy (National Treasury and South African Revenue Service, 2016b).

Employers who are tax compliant and registered with the South African Revenue Service for employees' tax purposes are eligible to claim the Employment Tax Incentive (National Treasury and South African Revenue Service, 2016b). According to National Treasury and South African Revenue Service (2016b:01), the following do not qualify for the incentive:

- national, provincial and local spheres of government;
- public entities listed in schedule 2 or 3 of the Public Finance Management Act;
- parastatals, government entities or municipal entities, unless the Minister of Finance designates them by regulation; and

- employers who have been disqualified by the Minister of Finance due to displacement of employees or by not meeting conditions as may be prescribed by the Minister by Regulation.

An employer is able to claim the incentive by decreasing the amount of employees' tax payable to the South African Revenue Service for every qualifying employee that is hired by the employer (National Treasury and South African Revenue Service, 2016b). This can be done by completing the Employment Tax Incentive (ETI) field on an employer's monthly EMP201 submission to the South African Revenue Service (National Treasury and South African Revenue Service, 2016b). Employers, according to National Treasury and South African Revenue Service (2016b:01), are able to claim the incentive when they have employees who:

- have a valid South African ID;
- are from 18 to 29 years old;
- are not a domestic worker;
- are not related or "connected" to the employer;
- earn at least a minimum wage in terms of wage regulating measures. If no measure exists, then the employee must earn R2 000 per month in wages;
- earn less than R6 000 per month in total remuneration (basic salary plus all other benefits); and
- were newly employed on or after 1 October 2013.

In determining the value of the incentive (for a specific month), the employer must firstly identify all the qualifying employees for that month (according to the requirements as stated above), after which the applicable employment period (1<sup>st</sup> 12 months or 2<sup>nd</sup> 12 months) must be determined (National Treasury and South African Revenue Service, 2016b). Following this, each employee's "monthly remuneration" must be used to calculate the incentive available and then aggregated in determining the total incentive for the stipulated month (National Treasury and South African Revenue Service, 2016b).

The incentive, according to National Treasury and South African Revenue Service (2016b:02), should be calculated as follows:

	<b>Year 1</b>	<b>Year 2</b>
<b>Monthly Remuneration</b>	<b>Employment Tax Incentive per month during the first 12 months of employment of the qualifying employee</b>	<b>Employment Tax Incentive per month during the next 12 months of employment of the qualifying employee</b>
R0 – R2 000	50% of Monthly Remuneration	25% of Monthly Remuneration
R2 001 – R4 000	R1 000	R500
R4 001 upwards	Formula: $R1\ 000 - (0.5 \times (\text{Monthly Remuneration} - R4\ 000))$	Formula: $R500 - (0.25 \times (\text{Monthly Remuneration} - R4\ 000))$

Where an employee only works for a portion of a qualifying month, the “monthly remuneration” of such an employee must be adjusted according to the period for which he or she worked for the employer (National Treasury and South African Revenue Service, 2016b)

A penalty will be levied on an employer when, according to National Treasury and South African Revenue Service (2016b), an employer claims an employment tax incentive in respect of an eligible employee earning less than the minimum wage and when an employer is deemed to have dismissed an employee in order to employ an eligible individual.

### **3.11 Conclusion**

This chapter described the higher education and training tax incentive measures currently provided for in the South African Income Tax, Employment Incentive and Value-Added Tax Acts. These Acts contain few broad-based tax incentive measures that would encourage investment in higher education and training. The incentive measures that are available are restricted in their applicability and are, in most cases, only available to particular classes of taxpayers.

There is little in these statutes that would be to the benefit of an individual. The main incentives of section 12H, 11D and 10(1)(q) of the Act, for example, are dependent on an enterprise’s activities and not on an individual’s decision to pursue education and training endeavours for their individual enhancement. The fiscal incentive for an individual to invest in higher education and training is thus not supported by tax incentives in South Africa. More

could possibly be done to encourage investment in higher education and training through personal income tax incentives.

Furthermore, very little literature on the actual cost of these incentives, other than section 12H of the Act, is available. The effectiveness of the various incentives is dependent on the extent to which enterprises are in fact making use of them and their contribution to funding the sector. An analysis of the actual financial implications of these incentives, such as their effect on the fiscus and their contribution towards free education for all, would give a much clearer understanding of their effectiveness.

The following chapter explores international taxation and funding measures as they relate to higher education and training. The aim of this investigation is to make recommendations based on international best practice to apply in a uniquely South African content.

## **4 HIGHER EDUCATION AND TRAINING TAX AND OTHER INCENTIVES IN SELECTED INTERNATIONAL JURISDICTIONS**

### **4.1 Introduction**

Issues pertaining to higher education vary from country-to-country as well as from one group of countries (or region) to another (Altbach and Peterson, 2007). The various challenges include, for example, unmet demand and access, weak institutional independence, together with intolerance for academic freedom, and difficulties in maintaining the necessary standard of quality and efficiency, together with the marginal available resources (Altbach and Peterson, 2007). The major contentious concern, however, which in most cases crosses borders from the high income to low income countries, is the issue of financing higher education and the role of the state in doing so (Altbach and Peterson, 2007).

In addressing the fourth goal of the research, this chapter will focus on higher education fiscal policies in selected international jurisdictions across varied economic and social standings in order to highlight the various higher education tax incentives and dedicated higher education taxes available in these jurisdictions. While it will be evident from the literature review that the majority of the selected international jurisdictions favour market-based instruments in the form of higher education grants, bursaries, funds and loans, certain higher education *stimuli*, mostly in the form of higher education tax incentives, are available to taxpayers. Several countries have developed diverse tax incentives in their Personal Income Tax, Company Income Tax and Value-Added Tax legislation, to promote both expenditure in education and training activities and the provision of education and training services. In all the jurisdictions reviewed, however, the effectiveness of such higher education policies are largely compromised by political and other economic pressures.

The chapter will conclude with a brief overview on the appropriateness of adopting such incentives and/or a dedicated tax in South Africa.

### **4.2 Finland**

Two main laws regulate the Finnish taxation system: the Finnish Income Tax Act (which covers both Personal and Corporate Income Taxation) and the Value-Added Tax Act (Value-Added Tax provisions) (Tuononen, 2005). In Finland, the basic right to education and culture is guaranteed by the “National Constitution” (The Organisation for Economic Cooperation and Development, 2005). Public authorities are tasked with ensuring equal access for every

Finnish resident to education; not only at pre-primary, basic and secondary level, but at postsecondary (or tertiary) level as well (Tuononen, 2005). Postsecondary education is, just like basic education, free to all residents (The Organisation for Economic Cooperation and Development, 2005). There are no tuition fees at universities, but students pay for their textbooks, travel costs and meals (The Organisation for Economic Cooperation and Development, 2005). Private schools and colleges are rare, have to be administrated by a non-profit organisation, and cannot collect term fees, so financing comes mainly from state grants (The Organisation for Economic Cooperation and Development, 2005).

In Finland, educational services provided by private or publicly funded institutions are exempt from Value-Added Tax (KPMG, 2002). This applies also to higher education and training; including specialized university courses or tailored vocational training programmes (KPMG, 2002). This exemption applies only to education, however, and not research activities. A university, therefore, does not charge Value-Added Tax on educational service income, but is obliged to adhere to Value-Added Tax regulations on the supply of research activities (KPMG, 2002). Education or training providers not organized by virtue of law are not granted any exemption and are obliged to charge a standard Value-Added Tax rate of 22 percent on services (KPMG, 2002). A reduced Value-Added Tax rate of 8 percent is applied *inter alia* on books and admission fees, with a zero rate on subscription newspapers (*Opetusministerio*, 2006). The *Opetusministerio* (2006) suggests that the Value-Added Tax reduction amount can be seen as a tool to encourage people to gain social capital, although not regarded as a “special tax” in the promotion of education and training as such.

In Finland, costs involved in the provision of education and training are not favoured, as there is no special tax treatment for education and training funders in “Personal Income Tax” legislation (*Opetusministerio*, 2006). Nor is there special treatment for private and non-profit education providers in “Corporate Income Tax” legislation (*Opetusministerio*, 2006). The only exemptions available are linked to state funded grants to public organisations, such as universities and universities of technology.

The fact that education at all levels is free and funded by the State, means that there is no need for tax incentives or a dedicated tax.

### 4.3 France

French education and training is defined and governed at a national level (Ministry of Higher Education, Research and Innovation, 2016). On average, the state, together with the consultation and involvement of local authorities, account for 87 percent of total education expenses (administration, catering, transport and manuals excluded), whereas households account for eight percent and enterprises for five percent (European Centre for the Development of Vocational Training, 2009; Ministry of Higher Education, Research and Innovation, 2016).

French enterprises are obligated by law to contribute to training development *via* a compulsory levy on their total payroll, the amount being dependent on the size of the enterprise (Leibfritz and O'Brien, 2005). Firms with 20 employees or more must contribute 1.6 percent of their total gross wage bill paid during the previous year to vocational training; for enterprises of between 10 to 19 employees, and for those with fewer than 10, the rates are set at 1.05 percent and 0.55 percent respectively (Leibfritz and O'Brien, 2005). Furthermore, all enterprises with at least one employee must pay an "Apprenticeship Tax" which is equal to 0.5 percent of the total gross wage bill paid during the previous financial year (Leibfritz and O'Brien, 2005). Enterprises are also able to deduct the education and training expenses incurred during a financial year from profits only if such expenditure is carried out for the purposes of the trade (Leibfritz and O'Brien, 2005).

Over and above this, the French government has developed several tax incentives aimed at promoting education and training, usually referred to as tax expenses (*depenses fiscales*) as they constitute a loss of income for the state (*Cour des Comptes*, 2008). The three "Corporate Income Tax" incentives according to the Organisation for Economic Cooperation and Development (2005) which support education and training expenses, include:

- (a) [t]ax credits (or deductions) for training expenses incurred by entrepreneurs. This tax credit has been in existence since 2005 and favours the training of entrepreneurs who are not wage earners and, therefore, are not included in the French system of compulsory financing of vocational training as discussed above. The training includes the continuous development of the entrepreneurs' competencies (through vocational studies) and the access of the entrepreneur to the different levels of professional qualifications.

(b) [t]ax credits in favour of apprenticeships. All enterprises (including public establishments and not-for-profit organisations if subject to corporate tax) can benefit from this credit through the deduction of training and wages as they relate to apprenticeships, as long as they employ the apprentice for at least one month during a financial year.

(c) [t]ax credits for training expenses of employees. This tax credit is reserved for small and micro enterprises (SMEs) carrying out training activities for their employees in enterprise economy (understanding the functionality of general financing, accounting and the like). Furthermore, the training has to be provided by a training organisation registered with the relevant officials of the state in that specific region and does not need to be related to the trade conducted.

Furthermore, there are four main French tax incentives in national “Personal Income Tax” legislation aimed at supporting education and training expenses. These, according to The Organisation for Economic Cooperation and Development (2005), include:

(a) [i]ncome tax credits for education expenses in higher education aimed at parents with dependent children. This incentive benefits taxpayers who have dependent children pursuing studies in an institute of higher education. Dependent children are defined as children up to 18 years old and children up to 25 years old if they attend higher education institutions.

(b) [t]ax credits on the interest burden of loans incurred by students in higher education to finance their studies. In order to be deemed a recipient of this tax credit, borrowers must first fulfil three conditions, namely:

(i) [t]hey must be taxpayers in France in the year they request to benefit from the tax credit. This allows students studying abroad to benefit from the tax credit when coming back to France;

(ii) [t]hey must be younger than 26 years old at most on 1 January of the year of the loan; and

(iii) [t]hey must be students in higher education on this same date.

The tax credit can only benefit borrowers themselves; if the borrower is a dependent child, the parent cannot benefit from the credit. The benefit will be delayed, and considered as a tax deferral, until borrowers become independent taxpayers (it will also include the interest paid during the years they were dependent).

(c) [i]ncome tax exemption on wages earned by apprentices. Wages earned by apprentices in connection with their apprenticeship contract are exempted from income tax to the limit of the annual minimum wage for that particular year. The taxpayer (either apprentices themselves or the parents if they are dependent children) are obliged to declare only the wage element that is above the ceiling amount.

(d) [i]ncome tax exemption on wages earned by pupils and students working during school or university holidays. Students in secondary or higher education, who are under the age of 26 years and who have a job, are exempted from income tax on their wage up to a limit of three monthly minimum wages.

It is not clear whether all tax incentives in France for education and training purposes have, as a final goal, the promotion of education and training. For instance, the tax credit for training expenses of employees is aimed at favouring the financial position of employees in small and medium enterprise's and the tax credit for education is often regarded as a tool for improving French household purchasing power (*Cour des Comptes*, 2008; National Centre for Learning Alternatives, 2002). Also, the income tax exemption for wages earned by pupils and students (excluding apprentices) is considered to be a tool for both the promotion of education and training activities and for the improvement of the purchasing power of the French youth (National Centre for Learning Alternatives, 2002).

Furthermore, some tax incentives fail to provide a real financial incentive at all. Given the real costs of the training, as compared to the incentive cost of, for example, the entrepreneurial incentive, it is questionable whether it in fact constitutes an incentive in real terms (*Assemblée Nationale*, 2008; Kaiser, 2007). Certain tax incentives also fail to fulfil their objectives due to added difficulties. Such difficulties include, for example in the case of the tax credit on the interest burden of loans incurred by students in higher education to finance their studies, their ability to find a bank that will lend them the money as students are often not able to offer appropriate guarantees (*Assemblée Nationale*, 2008). To resolve this,

the French government has recently launched a new measure of providing guarantees for students (*Assemblée Nationale*, 2008; Kaiser, 2007).

Tax incentives serve as an important instrument in the stimulation of public policies as it relates to business research and development (*Assemblée Nationale*, 2008; *Cour des Comptes*, 2008). An increasing number of countries have been implementing fiscal schemes relating to research and development, as part of their innovation policy mix (*Cour des Comptes*, 2008). In France, the “French Research Tax Credit” exists as an incentive to any industrial, commercial or agricultural organisation subject to corporate tax in France (*Assemblée Nationale*, 2008; *Cour des Comptes*, 2008). In order to be eligible, the creation or improvement of a product, process, programme or equipment must demonstrate “originality or substantial improvement” (*Assemblée Nationale*, 2008; *Cour des Comptes*, 2008). In other words, only operations aimed at removing scientific and/or technological uncertainties are taken into account. The issue to be resolved needs to be new and have no known solutions, all of which is guided by certain regulations. The tax credit is based on the claimed volume of research and development expenditure. The deduction is equal to 30 percent of the research and development expenditure per year, up to a maximum of EUR 100 million, beyond which the rate is decreased to 5 percent (*Cour des Comptes*, 2008). For companies entering the scheme for the first time, the applicable rate is 50 percent for the first year, and 40 percent for the second year (*Cour des Comptes*, 2008).

#### **4.4 Germany**

Germany is a federal country with sixteen autonomous states, each responsible for their individual higher education affairs (Bohm and Lippert, 2015). The higher education system, which consists of 379 higher education institutions, catering for approximately 2.4 million students from across the world, is a public system that is publicly funded (Bohm and Lippert, 2015). While there are a number of small private institutions, combined they enrol less than five percent of the total student body (Bohm and Lippert, 2015).

According to Gotter, Schleweit and Partner (2007), the provision of education and training in Germany, including all accommodation costs, are exempted from Value-Added Tax. In the granting of the exemption, the courses are not required to be certified, but the education and/or training provider has to be acknowledged and confirmed as registered accordingly with the state (Gotter, Schleweit and Partner, 2007).

In Germany, income from trade or business activities is generally calculated through an operating assets comparison or as surplus of revenue over operating expenses (Gotter, Schleweit and Partner, 2007). Operating expenses are incurred by the enterprises or the self-employed. In general, training expenses incurred by employers for their employees are regarded as operating expenses (including other expenses such as travel, subsistence, etc.) and, as a result, reduce the taxable income of the firm (Gotter, Schleweit and Partner, 2007). This includes enterprises without legal personality and enterprises that are statutory corporations. It is essential, however, that the training relates to the business interest of the employer (Gotter, Schleweit and Partner, 2007). Also, it is recommended that the employer register the employee in the training course and not the employees themselves; otherwise, the expenses are regarded as a “payment in kind” for the employees and as a result cannot be deducted (Gotter, Schleweit and Partner, 2007). Generally, expenses for an employee’s initial education do not constitute operating expenses unless the initial education can be directly linked to the employment, such as an apprenticeship or internship (Gotter, Schleweit and Partner, 2007). Expenses for further and/or continuing education and training, including second courses of studies and retraining measures, can be deducted as work- or income-related expenses to the full extent (Winfoline Bildungsnetzwerk, 2005). To be fully deductible, the education and/or training has to be related to either the occupation/job carried out by the individual or classified as retraining in preparation for a future occupational change (anticipated income-related expenses) (Winfoline Bildungsnetzwerk, 2005).

This tax incentive becomes effective only if the total expenses exceed the automatic lump-sum deduction of EUR 4 000 per year (Winfoline Bildungsnetzwerk, 2005; Schonhoft, 2007). This lump-sum deduction applies to employees only – for the self-employed there is no such lump sum. The lump-sum furthermore applies to any education and training costs; they do not need to relate to the trade (Winfoline Bildungsnetzwerk, 2005). After the expense exceeds the EUR 4 000 consideration, the abovementioned “trade” related clause comes into effect. Eligible costs include course fees, travel costs, registration costs, associated external accommodation, relevant literature, etc. (Winfoline Bildungsnetzwerk, 2005). The deductibility of education costs as work-related expenses has been extended significantly since 2000, triggered by various recent judicial proceedings and decisions (Winfoline Bildungsnetzwerk, 2005; Schonhoft, 2007).

## 4.5 Ireland

The government of Ireland has always placed the development of human capital as a key national priority and sought to keep the cost of the provision of education and training as low as possible to potential recipients (European Centre for the Development of Vocational Training, 2009). The state contribution towards funding of higher education and training is at approximately 80 percent of the total cost for all students (European Centre for the Development of Vocational Training, 2009). This amount has, however, since the early part of the twentieth century, decreased slightly (European Centre for the Development of Vocational Training, 2009).

The supply of education and training services in Ireland is exempted from Value-Added Tax; this exemption status has been in existence for a number of decades from the 1960s (European Centre for the Development of Vocational Training, 2009). As most primary, secondary and tertiary education; as well as initial and continuing training service providers are not registered for Value-Added Tax they cannot, as a result, deduct the Value-Added Tax on purchases of goods and services (European Centre for the Development of Vocational Training, 2009). This can create particular difficulties for tertiary institutes that often need to purchase expensive, highly evolved equipment for research and teaching purposes (European Centre for the Development of Vocational Training, 2009). In order to assist, the Irish government has made some concessions within the Value-Added Tax system to allow such institutions the opportunity to reclaim the Value-Added Tax input element on the purchase of medical equipment for research and teaching purposes even if they are not registered Value-Added Tax vendors (European Centre for the Development of Vocational Training, 2009). The “Donated Research Equipment Value-Added Tax Refund Order” provides for the repayment of Value-Added Tax incurred in the purchase or importation of any new instrument or appliance by a research institution, a university or similar educational body engaged in either medical and/or laboratory work (European Centre for the Development of Vocational Training, 2009). The primary condition relating to this concession is that the instrument or appliance purchased must cost GBP 25 390 or more (exclusive of Value-Added Tax), be designed and manufactured for use solely in medical research, not have been funded, in part or in full, by the State, and be accompanied by a recommendation by the “Health Research Board” that, having regard to the requirements of medical research in the State, a

refund of tax would be appropriate (European Centre for the Development of Vocational Training, 2009).

In Irish corporation tax, a company is entitled to deductions in respect of expenditure wholly and exclusively incurred for the purposes of its trade, against the profits of the enterprise (European Centre for the Development of Vocational Training, 2009). Thus, where employee training is wholly or exclusively incurred for the purposes of trade, an employer may claim a deduction against the enterprise income (European Centre for the Development of Vocational Training, 2009). If training is provided for the employee's own personal development, the employer cannot claim the cost of the training provision against the company's profits, as the cost is not incurred in connection with the trade (European Centre for the Development of Vocational Training, 2009).

The Irish Business and Employers Confederation, the largest employers' representative organisation in Ireland, has called on the government to introduce an employee's tax credit (not only a corporate tax incentive) on the costs of education and training (European Centre for the Development of Vocational Training, 2009). The Irish Business and Employers Confederation suggests that the credit should be weighted in favour of employees at national framework qualification level three or lower, targeting primarily the low-skilled employees (European Centre for the Development of Vocational Training, 2009). Whether this credit would be applicable if the employee or the employer (or both) bear the cost of the education and/or training is unknown. However, to date, there has been no published response from government on this proposal, although public authorities have confirmed that they are analysing the possibility of introducing a tax credit that encourages companies to increase their training provision, rather than introducing an employee's individual tax credit (European Centre for the Development of Vocational Training, 2009).

In addition to a free-fee higher education initiative, which was introduced in 1995, the Irish government has introduced an "interim" tax relief system for tuition fees paid for several tertiary courses not yet covered by this initiative of free-fee higher education (European Centre for the Development of Vocational Training, 2009). The tax relief system is designed to reduce the taxable income of the individual taxpayer by 20 percent of the fee payable, subject to the maximum level of tuition fees allowable (EUR 5 000) (European Centre for the Development of Vocational Training, 2009). Thus, if an individual pays tuition fees of EUR 6 500 in a tax year, the maximum tax relief by which the taxable income can be reduced is

EUR 1 000 (EUR5 000\*20 percent). If individuals have no taxable income in the tax year in which the relief is being claimed, they will gain no advantage because the tax relief cannot be transferred to a future tax year (European Centre for the Development of Vocational Training, 2009). The tax relief at the standard rate of income tax (20 percent) is available in respect of tuition fees paid in private or publicly funded tertiary level institutions, institutions abroad and by repeat students and part-time students (European Centre for the Development of Vocational Training, 2009).

The tax relief can be claimed either on an individual's tax returns at the end of the tax year or during the tax year when the fees have been paid (European Centre for the Development of Vocational Training, 2009). The tax relief is permissible on tuition fees paid by individuals for their own courses and/or for courses paid for a dependant (that is, a spouse or child of the individual or a person in respect of whom the individual is a legal guardian). The tax relief is per course, per academic year with a taxpayer able to claim for more than one child or dependent at a time (European Centre for the Development of Vocational Training, 2009). The tax relief is not available in respect of, firstly, any part of the tuition fees that are subsidized directly or indirectly by grants, scholarships, or by an employer or otherwise, and, secondly, administration or examination fees (European Centre for the Development of Vocational Training, 2009).

#### **4.6 The Netherlands**

Government funding in the Netherlands differs from one university to the next, dependant largely on the relevant needs and circumstances of the University (European Centre for the Development of Vocational Training, 2009).

The supply of education and training in the Netherlands is, in most circumstances, exempt from the 19 percent Value-Added Tax (*Staatssecretaris van Financien*, 2006). This special tax treatment is intended to reduce the cost of education and training for individuals and to increase participation in lifelong learning activities. There are certain types of activities and courses exempted from Value-Added Tax that, despite not being directly of a vocational nature, are intended to improve the individuals' current or future job position (*Staatssecretaris van Financien*, 2006). Examples of exempt courses include courses in text processing and visits to congresses, seminars etc. In contrast, some training courses not related to the individual's current or future professions are not exempted from Value-Added

Tax, which includes hobby courses such as cooking and photography (*Staatssecretaris van Financien*, 2006).

Education and training expenses incurred by an enterprise for the benefit of employees can be deducted from the income of the enterprise in the calculation of their profits (Thunnisses, 2006; Chevaillier and Paul, 2006). To be deductible, these education and training activities must be intended to assist the individual in obtaining income from work, either in their current job position or in a new position within the same company or group of companies (Thunnisses, 2006). Courses paid for by the firm, but not for purposes of acquiring income from work, cannot be deducted from the earnings (Thunnisses, 2006). Furthermore, one-man businesses can also benefit from this education and training expense deduction (Thunnisses, 2006). The purpose of the education and training must also be to obtain income from work, but in terms of a one-man business, it must be for the current job position only (Thunnisses, 2006).

The Netherlands have introduced a “Payment Reduction Incentive” (European Centre for the Development of Vocational Training, 2009). Businesses are able to benefit from a reduction in taxes if they financially support employees in their participation in education or training activities so that they are able to acquire a stronger position within the enterprise (European Centre for the Development of Vocational Training, 2009). This incentive tries to achieve its goal by lowering the salary costs of employees for firms through deductions in salary and social security contributions paid by firms carrying out educational and training expenses for their employees (European Centre for the Development of Vocational Training, 2009). The following employee groups, according to the European Centre for the Development of Vocational Training (2009), are able to benefit from this incentive:

- (a) a student or a recent graduate undergoing supervised practical training in Technical and Vocational Education and Training colleges within the enterprise;
- (b) employees who are part-time students in higher professional education and secondary vocational education (not for part-time students in university education);
- (c) employees who follow PhD programmes at universities;

(d) employees (including those recently unemployed) who follow educational programmes to acquire starter level qualifications; these are individuals who did not finish secondary education; and

(e) employees who follow assessment programmes to determine current skills and their further educational needs.

There are no specific types of education and training activities, courses or training-related costs defined in this initiative; the only condition is that the employee follows a registered employee-student programme (*Staatssecretaris van Financien*, 2006). This deduction may apply to various types of education: financed education, appointed education (such as compulsory primary and secondary) and education and training for state purposes (*Staatssecretaris van Financien*, 2006). The costs that individuals incur in engaging in education and training that can benefit from the incentive, according to *Staatssecretaris van Financien* (2006), are:

(a) tuition fees, books and literature;

(b) excursions and trips, including travel and accommodation expenses;

(c) visits to congresses, seminars and symposia; and

(d) the depreciation of durable goods, like computers.

#### **4.7 The United States of America**

The state and federal government (equivalent to the South African provincial and national government), have always each provided substantial amounts of funding towards higher education and training in the United States of America (Mitchell, Leachman and Masterson, 2015). Historically, state contributions to higher education institutions and students have been far greater than federal assistance – 65 percent higher than the federal government on average from 1987 to 2012 (The Pew Charitable Trusts, 2015). This difference has, however, narrowed substantially in recent years, as state spending has declined, and federal investment grown sharply, driven mainly by the Pell Grant program, a need-based financial aid program that is the biggest component of federal higher education spending (Mitchell *et al*, 2015).

According to the Pew Charitable Trust (2015), the United State of America provided approximately \$31 billion in tax credits in the 2013 year as it relates to higher education and

training, resulting in a substantial reduction of federal and state revenue. This amount represents an increase from \$29 billion in 2009 (The Pew Charitable Trust; 2015 Woodhouse, 2015). Furthermore, revenue from federal, state and local government sources accounted for 41 percent of total revenue at public colleges and universities in 2013 (The Pew Charitable Trust, 2015). The success of these tax incentives is evident in the fact that the expenditure has grown by \$29 billion, from \$2 billion to \$31 billion, in a matter of 13 years (The Pew Charitable Trusts, 2015; Mitchell *et al*, 2015; Woodhouse, 2015).

The federal government provides a number of different tax reductions (including credits, deductions and exemptions) to assist individuals and families in paying for higher education. Generally, federal tax benefits are targeted at middle and upper-income individuals and families (Mitchell *et al*, 2015). The two main higher education tax benefits available to individuals are the “Lifetime Learning Credit” and the “American Opportunity Credit” (The Pew Charitable Trust, 2015; Mitchell *et al*, 2015).

#### **4.7.1 American Opportunity Tax Credit**

The “American Opportunity Tax Credit” (formerly known as the Hope Tax Credit) was set up by the United States of America government in its attempt to offset the costs of higher education to students (The Pew Charitable Trusts, 2015; Mitchell *et al*, 2015). The tax credit is available for qualified education expenses paid for an eligible student for the first four years of post-secondary, degree-seeking education. A maximum annual credit of \$2 500 per eligible student is available, but if the credit brings the amount payable down to zero, the taxpayer may have 40 percent of any remaining amount of the credit refunded additionally in the following year (Mitchell *et al*, 2015). In order to be eligible for the “American Opportunity Tax Credit”, according to the Internal Revenue Service (2017:05), the student must:

- be pursuing a degree or other recognized education credential;
- be enrolled for at least a semester in one tax year;
- not have finished the first four years of higher education at the beginning of the tax year;
- not have claimed the tax credit (or former Hope credit) for more than four tax years; and
- not have a felony drug conviction at the end of the tax year.

Furthermore, in order to claim the credit, the individual responsible for the fees must have a gross income of \$80 000 or less (\$160 000 or less for married couples filing jointly) (Internal Revenue Service, 2017). If the gross income is over the limit, but less than \$90 000, a reduced amount of the credit can be claimed (Internal Revenue Service, 2017). The credit can be claimed for each qualifying individual, as opposed to the per-family Lifetime Credit (discussed below), making the America Opportunity Credit more valuable to families with multiple students enrolled (The Pew Charitable Trust, 2015; Internal Revenue Service, 2017).

#### 4.7.2 Lifetime Learning Tax Credit

The Lifetime Learning Credit, as stipulated in the Taxpayer Relief Act of 1997, is available for up to \$2 000 annually for an unlimited number of years per individual taxpayer and not per student, like the American Opportunity Tax Credit. In order to be eligible for the “Lifetime Learning Tax Credit”, according to the Internal Revenue Service (2017:06), the student(s) must:

- be enrolled or taking courses at an eligible educational institution; and
- be enrolled for at least one academic period (semester).

Educational expenses that qualify for both the “American Opportunity Tax Credit” and the “Lifetime Learning Tax Credit” include tuition and related fees, such as administration and registration costs (The Pew Charitable Trust, 2015; Internal Revenue Service, 2017). Other related expenses, such as transportation, meals and insurance and medical expenses cannot be claimed for the purposes of these credits (The Pew Charitable Trust, 2015; Internal Revenue Service, 2017). Lastly, it is possible for a taxpayer to claim both the “American Opportunity Tax Credit” and the “Lifetime Learning Tax Credit” in the same tax year if they qualify (The Pew Charitable Trust, 2015).

#### 4.8 Comparative Analysis of Tax Incentives

Country	State Contribution	Tax Incentive
Finland	<ul style="list-style-type: none"> <li>• Free tuition fees, but accommodation, meals, etc. are at the expense of the student.</li> </ul>	<ul style="list-style-type: none"> <li>• The provision of education <u>by virtue of the law</u> is exempt from Value-Added Tax (own emphasis). This excludes research and development expenditure.</li> </ul>
France	<ul style="list-style-type: none"> <li>• State funds approximately 87 percent of all costs involved.</li> </ul>	<ul style="list-style-type: none"> <li>• Education activities are exempted from Value-Added Tax, regardless of their legal status.</li> </ul>

		<ul style="list-style-type: none"> <li>• Compulsory levy on payroll which is used as a contribution to training and development expenditure (levy is dependent on the number of employees).</li> <li>• An “Apprenticeship Tax” is levied at 0.5 percent of the gross wage bill of the previous year.</li> <li>• Education and training expenditure as it relates to the trade is tax deductible.</li> <li>• Corporate tax incentives: <ul style="list-style-type: none"> <li>I. Deduction of training expenses of entrepreneurs</li> <li>II. Deduction of wages as they relate to apprenticeships</li> <li>III. Deduction of training expenses as it relates to employees in small and medium enterprises, regardless of if it is trade related or not.</li> </ul> </li> <li>• Personal Income Tax Incentives: <ul style="list-style-type: none"> <li>I. Deduction of education expenses on dependants</li> <li>II. Deduction of interest on loans in financing education</li> <li>III. Exemption from Income Tax on wages of apprentices</li> <li>IV. Exemption from Income Tax on wages of pupils and students working during vacation</li> </ul> </li> <li>• A “Research Tax Credit” on the expenses incurred in the creation or improvement of a product, process, programme or equipment.</li> </ul>
Germany	<ul style="list-style-type: none"> <li>• Free education for all at public universities and colleges</li> </ul>	<ul style="list-style-type: none"> <li>• Education activities are exempted from Value-Added Tax, if registered with the necessary authorities.</li> <li>• Training offered by the employer for the employee is deductible as it relates to the business activities. An amount of EUR 4 000 is available as an automatic deduction.</li> </ul>
Ireland	<ul style="list-style-type: none"> <li>• Government funds approximately 80 percent of all costs</li> </ul>	<ul style="list-style-type: none"> <li>• Education activities are exempted from Value-Added Tax, regardless of their legal status.</li> <li>• If the taxpayer is not registered for Value-Added Tax – then cannot claim on expenses, such as, expensive research equipment.</li> <li>• The “Donald Research Equipment Value-</li> </ul>

		<p>Added Tax Refund” allows for a claim on Value-Added Tax if the cost is EUR 25 390 or more.</p> <ul style="list-style-type: none"> <li>• A deduction is allowable on costs of education as it relates to the trade</li> </ul>
The Netherlands	<ul style="list-style-type: none"> <li>• Government funding differs per university with the average university funding at 60 percent.</li> </ul>	<ul style="list-style-type: none"> <li>• Value-Added Tax exempt on cost of education and training as it relates to the trade.</li> <li>• Payment reduction initiative – reduction in salary costs of employees to the extent of the training and education cost in calculating tax payable.</li> </ul>
The United States of America	<ul style="list-style-type: none"> <li>• Federal, state and local government account for approximately 41 percent of total funding cost.</li> </ul>	<ul style="list-style-type: none"> <li>• An American Opportunity Tax Credit of \$2 500 is available on education and training expenses per year and student for up to 4 years.</li> <li>• Lifetime Learning Tax Credit of \$2 000 is available as an additional credit on education and training expenses per tax year.</li> <li>• Both credits can be claimed simultaneously.</li> </ul>

#### **4.9 Potential Success, Affordability and the Impact of Incentives on the South African Economy**

As illustrated above, most countries either exempt Value-Added Tax on education and training services (including expenses such as textbooks and research and development activities) or charge a reduced percentage. These lower costs can be regarded as a reduced barrier for individuals and companies to take part in education and training. While the provision of education and training is Value-Added Tax exempt in South Africa, according to section 12(h) of the Value-Added Tax Act, the supply of textbooks and certain research activities, is not. In the 2015/16 tax year, according to National Treasury and the South African Revenue Service (2016a), tax revenue in South Africa totalled R1.07 billion with 26.3 percent (or approximately R282 million) as a result of Value-Added Tax. While the extent to which the revenue relates to textbooks (or any other associated education and training expenses) is unknown, Value-Added Tax does contribute substantially to the tax revenue base of South Africa. Any reduction in such revenue can be assumed to have adverse consequences on revenue collection in South Africa (and the growth) as, besides personal income tax which contributes 36.4 percent of total revenue, Value-Added Tax is one of the largest contributors to the national fiscus (National Treasury and South African Revenue

Service, 2016a). While a reduction (or exemption) of Value-Added Tax on the supply of goods and services to universities and colleges in South Africa (especially on textbooks and any other additional learning materials borne by the student) may be costly, ensuring they are affordable to tertiary institutes is a necessity in ensuring a quality-driven education system which produces graduates who are employable and able to contribute effectively towards the development of the economy.

According to Berkhout (2005) businesses generally appreciate the tax incentive deduction of education and training expenses. According to estimates, approximately 80 percent of the firms eligible in the Netherlands made use of it, for example (Berkhout, 2005). The incentive reduces salary costs and provides a *stimulus* for firms to get more involved in the education and training of their employees. It is believed that this incentive is particularly used by firms offering vacancies for student-employees in vocational education (Berkhout, 2005). Enterprises indirectly benefit *via* better qualified personnel, as employees can apply their acquired knowledge and skills in the firm, serving as *stimuli* for economic growth and development.

While there may be tax relief systems in place in South Africa for small and medium enterprise's, no specific tax relief as it relates to furthering one's education and training in such a context, is available. The SME sector plays an important role in the South African economy. According to the Organisation for Economic Co-operation and Development Economic Survey (2016), the sector provides approximately 60 percent of employment and accounts for roughly 34 percent of gross domestic product. The Organisation for Economic Co-operation and Development Economic Survey (2016) suggests that approximately 60 percent of small and medium enterprise's fail within the first five years of their existence due to issues pertaining to a lack of skills, training and guidance. Together with this, South Africa had an unemployment rate of 27.7 percent in the first quarter of 2017, the highest figure since September 2003 (Statistics South Africa, 2016). Therefore, in order to stimulate the sector and to facilitate skills and training development, the tax relief system as adopted in Ireland in which individuals within the small and medium enterprise sector are able to decrease their personal income tax by the cost of education and training expenses for National Qualification Framework levels three and lower, could serve as an incentive in South Africa in this regard.

Cruywagen (2015) notes that, according to the Department of Labour, there remains a critical skills shortage in the artisan and engineering (or apprenticeship) sector. The National

Development Plan – which aims to ensure that all South Africans attain a decent standard of living through the elimination of poverty and reduction of inequality by 2030 – states that South Africa should produce more than 30 000 qualified artisans a year if the labour demand is to be met. Currently, South Africa is producing only approximately 13 000 qualified artisans per year (Cruywagen, 2015). In order to promote entry into the sector, as in France, the wage of an apprentice could be allowed as a deduction from the corporate income tax of an enterprise, conditional upon the enterprise bearing the cost of the training. Furthermore, the introduction of an “Apprenticeship Tax” on the wage bill of an enterprise could serve as an additional incentive in ensuring South Africans are trained as artisans.

Very few incentives exist in South Africa as it relates to personal income tax. In France, for example, the cost of education for parents, the student or sponsor (whoever is responsible for the fees) and wages of students earned as holiday or part-time work are all deductible from personal income tax. In South Africa, the average salary of those employed in 2016 is R224 244 per annum (before deductions) while the cost of higher education (tuition alone) can be as much as 25 percent (or more) of the total salary of an individual (Statistics South Africa, 2016). This amount is exorbitant for many. Allowing the deduction of tuition costs from one’s personal income tax would assist in the affordability of education and training for those individuals responsible for payment. While what the exact cost of this would be is unknown, it could be a large burden on the national fiscus. Thus, the relief could be subject to certain limits, such as in the case of the “American Opportunity Tax Credit” and “Lifetime Learning Tax Credit”.

According to Statistics South Africa (2016), South Africa faces a low growth, middle income trap characterised by a poor skills profile. Together with this, Statistics South Africa (2016) states that approximately 65 percent of college and university students are turned away from a potential job as a result of poor or no work experience. Thus, work during university holidays or vacation does not only serve as a measure for paying for one’s studies, but as a benefit necessary in ultimately finding a permanent job once studies are completed. As a measure to promote such practical skills development and work-place experience, as is done in France, the salary of the individual could be allowed as a deduction in the individual income tax calculation. It may also encourage a greater number of students to find (or take-up) vacation work in order to assist with the payment of their university or college fees.

French companies are further obliged to contribute a certain sum, dependent on the size of their workforce, towards the training and development of their workforce. In South Africa, according to the Commission for Employment Equity (2016), a shortage of skills has long been a feature of South Africa's economic and social landscape. The South African government, in its aim to redistribute wealth more equitably, has noted the need for an increase in skilled labour (Commission for Employment Equity, 2016). However, in 2015, unskilled labour accounted for 28.9 percent of the total labour force (Commission for Employment Equity, 2016). While a section 12H of the Act deduction is available for expenditure on learnership agreements, such expenditure is not compulsory for a firm. If a levy on the payroll of a company for education and training expenditure is introduced, as in France, this will ensure that the company does in fact enter into training and development contracts with their employees. With this, it ensures that employees are provided with the necessary funding needed to enter into training and development.

#### **4.9.1 Increasing Corporate Income Tax**

For the 2015/16 tax year, corporate income tax (which is levied at 28 percent on the taxable income of companies) accounted for 18.1 percent of total tax revenue for the state, making it the third largest contributor overall (National Treasury and the South African Revenue Service, 2016a). Although corporate income tax has maintained its status as the third largest contributor, its relative contribution has declined from the pre-recession peak of 26.7 percent in 2008/9 (National Treasury and the South African Revenue Service, 2016a). This is further demonstrated by the reduction in the ratio of tax to gross domestic product, which has decreased from 7.3 percent to 4.7 percent during the same period (National Treasury and the South African Revenue Service, 2016). The decline can largely be attributed to reduced company profits in the face of weak global demand following the global financial crisis (National Treasury and the South African Revenue Service, 2016a).

Government notes that in a highly unequal society and for a tertiary education funding model that is fair, interventions are required, not only because of the social and economic impact, but because of the requirements as set out in the South African Constitution, which requires higher education and training to be made progressively available to the general population (Department of Education, 1997; National Council of Higher Education, 1996). The concentrated nature of the South African economy is evident as only 325 large companies (0.2 percent of companies with positive taxable income) had taxable income of more than

R200 million and were liable for 57.6 percent of total corporate income tax assessed (National Treasury and the South African Revenue Service, 2016a). It is for this reason that system as adopted in France, in which there are categories of corporate income tax, in which the more profitable companies pay tax at a higher rate, would be appropriate to explore in a South African context in order to increase tax revenue and ultimately fund higher education and training (Davis, 2017). An increase in corporate income tax, however, especially as many countries such as Australia and Poland have decreased their rate, would serve as a disincentive to foreign direct investment and have dire consequences for economic development and growth (Davis, 2017).

#### **4.9.2 Scepticism regarding the Effectiveness of Higher Education and Training Tax Incentives**

There is scepticism in some policy circles over the effectiveness of tax incentives in positively contributing to the affordability and ultimate engagement of the population in higher education and training (European Centre for the Development of Vocational Training, 2009). There is a perception that persuading people to further their education is dependent to a large extent on their personal motivation and circumstances. It is believed that high-income earners, in comparison to low-income earners, are well aware of the economic benefits of increasing their skills and are thus well motivated to acquire additional qualifications that generally result in increases in earnings (European Centre for the Development of Vocational Training, 2009). Consequently, policy-makers are of the opinion that introducing tax incentives that are generally aimed at motivating high-income individuals (as it is high-income earners who generally benefit from tax incentives) could have significant deadweight outcomes (European Centre for the Development of Vocational Training, 2009).

Similarly, using the tax system to encourage people in low-income groups to increase their take-up of education and training is also seen as problematic (European Centre for the Development of Vocational Training, 2009). The issue is that lower income residents either pay income tax at the lowest marginal rate or may pay no tax at all because their income falls below the income tax threshold and a tax incentive would, therefore, have little or no impact (European Centre for the Development of Vocational Training, 2009). If individuals have no taxable income, they, in most cases where such relief is available, cannot carry over tuition fee tax relief to another tax year. Ultimately, tax incentives are meant to serve the purpose of actively encouraging investment in the sector to which the incentive is dedicated. Thus, if

existing tax incentives, as they relate to education and training are achieving this, remains to be seen.

Although there is support among policy-makers for the concept of using tax incentives to promote education and training, there is a perception that they, in most cases, may be a “blunt instrument” (European Centre for the Development of Vocational Training, 2009). Policy-makers often seek to target specific groups and use a tax incentive – in the context of a tax system that is universally applied – to address specific policy challenges. This is seen as problematic in terms of this deadweight potential (European Centre for the Development of Vocational Training, 2009). As a result, policy-makers feel more comfortable with the concept of using grants to encourage skills improvement, rather than tax incentives or a dedicated higher education and training tax *per se* (European Centre for the Development of Vocational Training, 2009).

#### **4.9.3 Impact of a Dedicated Higher Education Tax in South Africa**

While there may not be much existing literature on dedicated international higher education taxing systems, some proposals from tax professionals in a South African context, have advanced the idea of expanding higher education funding through increased taxation, or a graduate tax (University of the Witwatersrand, 2016). It has been suggested that a dedicated graduate tax is not a sustainable idea as there is no guarantee that the tax will be used for higher education purposes. Together with this, it might provide an incentive for people to migrate or hide their educational status in order to avoid the tax (University of the Witwatersrand, 2016). It has been suggested, however, that more “courageous public financing policies”, such as increasing taxes for the very rich through increased personal and corporate taxes, could increase the tax purse of South Africa (University of the Witwatersrand, 2016).

Several submissions have suggested that the South African Revenue Service could be more fruitfully involved in various aspects of the higher education funding system (University of the Witwatersrand, 2016). For example, the South African Revenue Service could implement a system of taxing students who need to repay their student loans once they are earning in excess of a certain amount (University of the Witwatersrand, 2016). An as example, in the United Kingdom, students pay back nine percent over and above their set payment plan if they earn above approximately R300 000 a year (University of the Witwatersrand, 2016).

Such a system – which would be linked and managed by the South African Revenue Service – would have the additional benefit of ensuring compliance in the repayment of loans by those who can afford such repayments (University of the Witwatersrand, 2016).

Sitas (2016), of the University of Cape Town, believes that tertiary education could be funded through a ring-fenced, South African Revenue Service-administrated Graduate Tax of one percent on graduate salaries from the start of permanent employment onwards. For example, a university professor earning X amount will contribute one percent of his or her salary in the same way as an employee such as a cashier, for example, would need to contribute one percent of his or her salary if he or she is a tertiary education graduate. Given the socio-economic climate of South Africa, however, there are disagreements on whether this amount should go towards the higher education system rather than basic education, the health department or towards social grants (University of the Witwatersrand, 2016; Sitas, 2016). It is further suggested that instead of a one percent contribution across the board of employed graduates, graduates should instead make a contribution based on their salary, with the rate of tax rising across bands in much of the same way that income tax already does (Hain, 2016). No graduate tax would, for example, be levied on earnings of up to R180 000 a year. Earnings of between R180 000 and R440 000 would attract a tax rate of two percent, with 2.75 percent applied to earnings between R440 000 and R750 000 and earnings above this amount taxed at 3.5 percent (Hain, 2016). Hain (2016) suggests that it would be perfectly practical for the South African Revenue Service to implement such a system, as a far more sustainable stream of revenue for the Treasury would be ensured. However, economists, according to Hain (2016), have argued against yet another tax on the working population, saying that the tax base is already being overtaxed. Struggling students owe over R6 billion in student fee debt, with over 400 000 defaulting on their loans after graduation (Hain, 2016). As a result, an additional tax could be a heavy burden on a taxpayer and may result in graduates hiding their qualifications in order to avoid the tax.

#### **4.10 Conclusion**

After a review of literature on various international support mechanisms and tax incentives as they relate to higher education and training, there is evidence of similar tax incentive policies, with slight deviations, from one jurisdiction to another.

Value-Added Tax, for example, is exempt on services provided by institutions of higher learning. In Finland educational services are exempt, but the exemption excludes research and development activities. Together with this, a reduced Value-Added Tax rate of 8 percent, instead of 22 percent, is applied on books and other education accommodating expenses. Such an exemption also exists in Ireland. In order to qualify, however, institutions need to be registered and if they are not, certain provisions allow for the deduction of Value-Added Tax on high priced goods and services purchased for purposes of research and development. The Value-Added Tax exemption in the Netherlands is meant not only to reduce the cost of education and training, but also to increase an individual's participation in lifelong learning activities. While a Value-Added Tax exemption may reduce the financial barrier of access for individuals to higher education and training, the contribution of this towards the overall alleviation of the cost of education is unknown.

The French government has initiated a compulsory levy on companies as it relates to the payroll of employees. The extent of the contribution, or "wage subsidy", is dependent on the number of employees in the firm. Over and above this, corporate tax credits exist for education and training expenses as they relate to the trade, apprenticeship wages and on employee training for small and medium enterprises, regardless of whether the expense is related to the trade or not. Such direct and compulsory incentives, in the promotion of skills training and affordable education for employees provided for by an enterprise, would most likely benefit a highly unskilled South Africa labour force.

Personal tax credits, from a French perspective, also exist on interest on loans, education expenses for parents with dependants, on the wage of an apprentice and on wages of students working during school holidays or vacations. Together with this, a research tax credit exists for specific research and development expenditure. The United States of America adopts a similar approach in their "American Opportunity Credit" in terms of which an individual is able to claim an amount of up to \$2 500 per year per person for expenses as they relate to education and training. The "Lifetime Learning Tax Credit" is available for individual taxpayers pursuing an academic degree. In South Africa, very few incentives exist as they relate to personal income tax. In a nation burdened with high unemployment and low skills development, it may be useful to use personal income tax incentives as a means of directly encouraging individuals to undertake education and training.

Scepticism over the use (and with that the effectiveness) of tax incentives as they relate to higher education and training, to a large extent, is based on the fact that they are seen as a deadweight initiative in their attempt at lowering the cost of education and providing a form of access to institutions for most students. From an individual tax perspective, the rich, who can afford to pay tax, often understand the importance of an education and can thus easily access institutions, while those who are in the lower income tax brackets and often cannot afford education, do not benefit from a tax break as they pay no or very little tax. Given the widely evident social inequality in South Africa, a graduate tax, which aims at taxing employed graduates, levied at a minimal rate of, for example, one percent, could be used as a tool to increase national revenue and address social inequality from an educational perspective. While it has been suggested that such a tax could be administered by the South African Revenue Service and ring-fenced for educational purposes, a full-scale analysis of its success or failure needs to be carried out, as there is the possibility of graduates avoiding the payment of the tax.

The following chapter provide a summary of the research findings.

## **5 CONCLUSION**

### **5.1 Goals of the Research**

The first goal of the research is to provide a brief overview of how higher education and training in South Africa has been, and currently is, funded. The second goal is to briefly discuss the historical socio-political and current challenges of funding the South African higher education and training sector. The third goal is to document the existing higher education and training taxes and tax incentives that have been enacted in the South African taxing statutes. A review of the higher education and training tax policies in selected international jurisdictions comprises the fourth goal. Particularly, the policies of the United States of America, Finland, France, Ireland, Germany and the Netherlands are analysed, with the aim of focusing on the suitability of the higher education and training tax incentive policies adopted in these jurisdictions in ensuring greater access and affordability in South Africa.

These investigations are carried out with a view to determining whether a “stand-alone”, dedicated higher education and training tax is appropriate for South Africa, or whether alternative measures could be adopted, whether in conjunction with, or instead of a higher education and training tax, in the formulation of an appropriate higher education and training policy aimed at access to the sector through appropriate funding.

#### **5.1.1 Findings and General Discussion**

Chapter two illustrates that institutes of higher learning have historically been considered to be “creatures of the state” with a vast number of restrictions on government funding. Universities were classified as white, black, coloured or Indian with white institutions receiving approximately twice the level of funding provided to the others. Together with this, the higher education sector was highly politicised and under-resourced with inferior quality education reaching the majority of black students. As a result of this, avenues of access and funding for white students, and historically white institutions, remain more favourable (National Council of Higher Education, 1995).

Higher education and training policy has undoubtedly become an increasingly important on the national agenda. The widespread recognition that tertiary education is a major driver of economic competitiveness in an increasingly knowledge-driven global economy has made high-quality tertiary education more important than ever in both industrialised and

developing countries. The National Council of Higher Education has recognised that in order to realize this, financial incentives, rather than a commanding measure of control must be enforced. Moja and Hayward (2005) however recognize that, while the challenges have been identified, the National Council of Higher Education have failed to make lasting recommendation of greater access to funding.

A number of higher education and training funding frameworks, from as early as 1950 have been introduced, each with challenges, changes and inefficiencies. In an attempt to rectify this, and in order to provide policy stability and clear objectives in terms of access and affordability, the government has developed a Higher Education White Paper and National Plan on Higher Education. The current funding model adopted is characterised by two streams of funding, namely; block grants, which are awarded mainly based on input and output factors and used for operational expenses and earmarked grants, which are awarded on the basis of a specific need. However, apparent issues, as they relate to the funding shortfall, include:

- decreasing financial subsidy from government in real and per student terms;
- a lack of policy coherence in correcting the injustices, including the uniquely individual university and technikon challenges still seen in institutions today; and
- a lack of leadership and will from those tasked with serving the sector.

There has been a decrease in financial support by the Government to the sector from 3.03 percent of gross domestic product in 1995 to 0.64 percent of gross domestic product in 2015 (De Villiers and Steyn, 2007; Department of Higher Education and Training, 2016). In order to realise free education for all, it will cost approximately R 95 – 150 billion, which for the 2016/17 tax year, is at least a R55.5 billion short-fall (Cele and Goodman, 2016). With a national deficit already at 3.1 percent of gross domestic product for the 2016/17 tax year, an accumulated debt of R2.2 trillion (50.7 percent of gross domestic product in 2016/17) and a budgeted deficit increase over the next three years, government has shown its inability to fund the sector through a reprioritisation of the budget, without negatively affecting other areas of funding (National Treasury, 2017).

Chapter three addresses the third goal of the research and discusses the various incentives that are available in South Africa in terms of the Income Tax, Tax Incentive and Value-Added Tax Acts, and concludes that there are few incentives that *all* persons can avail themselves of.

Those incentives that have been legislated in the Acts reviewed are restricted in their nature for the following reasons:

- they are available only to a particular class of taxpayer carrying on a specified activity, often resulting in high deadweight impact;
- limited information, except for section 12H of the Act, is available in terms of the actual financial cost of the incentives (and the effect thereof) as it relates to higher education and training;
- they are only available in respect of highly specified education and training activities;
- they are only available to persons incurring the expenditure in the production of income, and carrying on a “trade”; and
- with the exception of the concessions afforded in terms of section 18A of the Income Tax Act, there are no incentives that are directed at private individuals to encourage and assist them in investing in higher education and training.

The various tax incentives available in South Africa, as they related to higher education and training, according to the Acts, include:

- deductions that comply with the general deduction formula in terms of section 11(a) of the Act;
- the exemption of Value-Added Tax on the supply of education and training activities;
- section 12H learnership agreements;
- section 11D research and development expenditure;
- section 10(1)(q) exemptions for scholarships and bursaries;
- no value placed on the benefit derived from study loans at low or no interest, in terms of paragraph 2 of the Seventh Schedule to the Act;
- paragraph 10(2)(k) of the Seventh Schedule to the Act benefit, where no value is placed on the benefit derived from on-the-job and in-house training for the better performance of duties;
- section 18A of the Act deduction of donations as they relate to higher education and training; and
- an Employee Tax Incentive aimed at providing tax relief to employers who employ young South African job seekers.

Chapter four addresses the fourth goal of the research and investigates the implementation of higher education and training taxes and tax incentives in the United States of America, Finland, France, the Netherlands and Germany and their suitability within South Africa. There are important differences among the countries analysed in respect of the tax treatment of spending on education and training. Finland, for example, has minimal tax incentives as it relates to higher education and training, but has free education for all. France, on the other hand, has a large number of different tax incentives as they relate to higher education and training, but also provides for approximately 87 percent of the total cost.

Tax incentives are often criticised for their high deadweight effects, especially among large enterprises and highly qualified individuals. Additionally, they can be counter-productive as they end up favouring those groups already with access to education and training. It is argued that public authorities should try to introduce specific targeted incentives for those groups less favoured, such as small enterprises and their employees, those earning a low level of income and the poorly skilled.

The use of tax incentives in the United States and in France is well established. In the United States of America, both the state and federal government provide substantial amounts of funding towards higher education and training. The “American Opportunity Tax Credit” is available to the corporate sector as an incentive to subsidise and ultimately employ young graduates. Together with this, the “Lifetime Learning Tax Credit” is available to individual taxpayers as an incentive to invest in their own personal education and training. In France, enterprises are obligated by law to contribute to the training and development of employees *via* a compulsory levy on their total payroll, the amount being dependent on the size of the business. Together with this, tax credits are available on training expenses incurred by entrepreneurs, apprenticeships and on the training of employees in small and medium enterprises. Personal Income Tax credits also exist for expenses of parents with dependent children pursuing education, on loans undertaken for educational purposes and on wages of students working during school or university holidays. Over and above this, and unlike the other jurisdictions, a mandatory tax incentive of up to EUR 4 000 is awarded to French businesses for expenditure on education and training per year that is not work-related.

In Germany, Ireland and the Netherlands a deduction of education and training expenses as they relate to the trade of the business is allowed. In Ireland, a number of courses are provided free of charge to students. If the course is not covered by this initiative, a “Tax

Relief System” is available to individuals at a maximum amount of 20 percent of the total tuition fees, subject to a maximum level allowable.

Value-Added Tax is exempt on services provided for by institutions of higher learning in each of the international jurisdictions discussed. The extent to which this incentive is available, however, differs from one jurisdiction to another. In Finland for example, educational services are exempt, but the exemption excludes research and development activities. A reduced Value-Added Tax rate of 8 percent, instead of 22 percent, is applied on textbook expenditure, for example.

Taking into account the incentives across the varied jurisdictions, followed by the discussion on the suitability of such incentives in South Africa in chapter four, the following incentives serve as suggestions as to what may be gainfully implemented in South Africa:

- Value-Added Tax exemptions on university textbooks and on research and development needs;
- a regulated contribution by enterprises for training development *via* a compulsory levy on the total payroll;
- tax credits for training expenses reserved for small and medium enterprises, regardless of whether such expenses are linked to the trade or not;
- personal Income Tax credits for education expenses in higher education aimed at parents with dependent children;
- personal Income Tax exemptions on wages earned by apprentices (up to a certain limit);
- tax credits (or deductions) for training expenses incurred by entrepreneurs who are not wage earners;
- personal Income Tax exemptions on wages earned by pupils and students working during school or university holidays; and
- a “Tax Relief System” aimed at reducing the taxable income of those who are taxpayers and pursuing further education and training.

It is acknowledged that a large proportion of the South African population do not pay income tax and therefore the suggested income tax incentives would not be of any benefit to the majority of the population who cannot afford higher education and training. The proposed

Value-Added Tax concession, however, would benefit a far greater percentage of the population.

Various tax professionals have also promoted the idea of expanding higher education funding through increased taxation, or a graduate tax. It is, however, argued that unless such funds are ring-fenced.

It has also been suggested that an increase in tax revenue through increasing personal and corporate taxes for the rich be pursued. The already highly progressive taxing system, the economic recession South Africa is currently facing, as well as the general lack of economic confidence are all factors that make this unsuitable.

An additional recommendation is that the South African Revenue Services be responsible for implementing a system of taxing students who need to repay their student loans once their earnings are in excess of a certain amount. A system such as this is currently in operation in the United Kingdom, where students are obliged to pay back nine percent per year over and above their set payment plan, if they earn above approximately R300 000 a year.

It is further urged that tax incentives should serve as a supplementary measure, rather than the main instrument, in the policy makers' attempt to address the funding issue. The fine-tuning of tax incentives, together with other joint-financing policies is needed in order to achieve the best possible funding outcome.

## **5.2 Problems Encountered in the Research**

The focus of the work in this thesis was directed at particular areas of interest. The body literature on higher education and training tax law and policy is extensive and far greater than what this work might indicate. For the purposes of this study, only a few focus areas could be analysed in detail. There are many areas that are closely connected with the development and implementation of higher education tax policy that are alluded to in this work, but could not be explored without exceeding the limitation of scope of this project. These areas are, nonetheless, still acknowledged to be relevant.

A further area of concern is that the body of literature on the development of issues as they pertain to higher education tax and funding models is expanding on a daily basis. In this respect, the original limitation of scope placed on the research prevented the entire body of literature being investigated fully.

### **5.3 Potential Areas of Further Research**

It has been stated above that the limitation of scope of this research did not permit the entire body of literature to be investigated, nor did it allow for the investigation of the peripheral issues.

Given the rate at which the body of literature is expanding and the current topical nature of higher education tax, policy and funding, it is submitted that there exist many potential avenues for further research in these fields.

The Presidential Commission of Inquiry into Higher Education Funding, which has received many submissions from various institutions and stakeholders, such as universities and Non-Government Organisations, will indeed influence the future of South African higher education funding models and/or taxes (Council on Higher Education, 2015). It is submitted that the decisions, which will follow on from these submissions, will lay the foundation stone for a large body of future research.

Furthermore, the exploration of a “University Graduate Tax”, together with the above-submitted potential tax incentives, could make for a useful body of future research.

In many international jurisdictions, all spheres of government are responsible for financing higher education and training and the adoption of tax measures unique to their jurisdiction. In South Africa, on the other hand, only national government is responsible for the funding and implementation of tax measures specific to the sector. According to the National Treasury (2017), of the national budget for the 2017/18 tax year of R1.4 trillion, approximately 31 percent is allocated to the various provinces, with the provinces able to generate approximately three percent revenue additionally. While it is clear that provinces are heavily dependent on national government support, applying various tax measures, as they relate to higher education and training, in order to uniquely serve the interest of institutions within their jurisdiction, could be beneficial. For example, a graduate tax could be implemented in the various provinces. Research into the potential tax incentives, per individual province, in order to serve the unique interest and well-being of institutions within that province, could be beneficial.

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