Financialisation and taxation: undermining democratic cohesion in South Africa

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Abstract

There is an emergent literature on the adverse impact financialisation has on democratic processes. This paper focuses on the consequences of financialisation for democratic cohesion through taxation and public finances. We bring together literature on the political economy of tax and state financialisation, arguing that financialisation exacerbates trends in modern capitalism, undermining democratic cohesion by delegitimizing taxation and tax collection. In doing so, the phenomenon weakens the vertical and horizontal contract underlying taxation in democratic societies, that is the implicit contract between citizens and state institutions, on the one hand, and solidarity among citizens, the very fabric of democratic societies, on the other. South Africa serves as an illustrative case study. The country is one of the most severely financialised societies in the global South. In line with broader neoliberal trends, company tax has declined severely as a source of tax revenue for the state which increasingly has to rely on personal income tax for revenue generation. Driven by financialisation, the labour market has transformed fundamentally over the past 20 years in the country. Today, the vast majority of jobs is created in the tertiary sector, while many manufacturing jobs have been lost. This results in income polarization which means that the bulk of the personal income tax take is raised through taxing finance professionals and government employees. These professional groups often opt out of social provision, relying on private health care and pay-for infrastructure, more broadly. As a consequence, there is a growing resentment amongst these groups towards taxation, which undermines the ability of the state to provide inclusive social provision, while eroding solidarity among South African citizens.

1. Introduction

The collection and redistribution of domestic resources by democratically elected governments is one of the principal roles of the state. Whilst providing revenue to supply security and public goods, it conceptually enmeshes ‘state’ and ‘society’ in a social contract that simultaneously legitimises the state and provides democratic cohesion between both sets of actors. But it is a fragile relationship with numerous factors influencing the quality of the relationship including how much tax is collected, from whom, where it is redistributed and what services are provided. Whilst the tax take and tax spend in democracies are above all political choices, the bargaining process is emblematic of a democratic process through the accountability that is built into this social contract. However, building the social contract is complex and fraught with challenges. Therefore, not all states have been able to build a strong contract with their citizens because of structural, political and socio-economic factors that impede the mobilisation of domestic resources which include the neoliberalisation of tax reforms that have, since the late-twentieth century, favoured lower taxes over corporations and businesses more generally with a higher burden collected through higher income taxes and/or value added taxes.

Nowhere have the challenges to both mobilise domestic resources and build strong fiscal contracts been more acute than across the global South, where the mobilisation of domestic resources has historically been side-lined in favour of a reliance on volatile primary commodity export revenues. But the boom-and-bust nature of export-led development pathways has created barriers for developing nations, which, when coupled with low levels of tax collection has led to governments pursuing other forms of finance pathways to fund state obligations: debt-led development, aid and more recently, private and blended development finance (see Gabor 2021, Karwowski 2022) which tend to usher in processes of finacialisation, referring to the growing size, importance and power of the financial sector.

These processes have allowed governments to bypass the politically difficult task of raising the tax burden domestically. Whom to tax and how much are questions that policymakers have pondered for decades; without any meaningful breakthroughs of note because of how politically challenging and contentious they have been. Moreover, how to mobilise domestic resources in low- and middle-income countries where informality is the predominant pathway through which citizens engage with economic activity presents further challenges to policy-makers in their attempts to raise tax. Attempts to permeate into the informal sector to try and mobilise domestic

resources have centred around government programmes to strengthen the social contract. It is a delicate relationship where the state requires revenue to carry out its obligations and provides public services, infrastructure provision – healthcare and in some cases welfare – to taxpayers in return. Tax collection therefore forms the foundation of this relationship because it is where the infrastructural power of the state intersects with society. So, what taxpayers expect from their taxes is deeply embedded within this contract which forms a central plank of democratic cohesion where citizens elect leaders on promises of a tax design that supports a vision of public service provision. And therefore, by circumventing these processes in favour of other funding pathways it undermines the construction of social cohesion.

Moreover, it is already more difficult to build consensus around taxation in the global South because of problems with legitimacy: the public services and goods that the taxes purchase are deemed to be less value, the burden falls on a more concentrated – specialised – sector of society where there is wealth to be captured and tax reforms are often not subject to the same procedural legalities as in OECD countries. Whilst the process of building the social contract is more complex in developing countries and is less diffused throughout society it has been the cornerstone of democratic cohesion for those citizens enmeshed in this relationship with the state. But in the context of governments choosing politically easier questions and other pathways to finance state obligations and development, what effect this has on the social contract and democratic cohesion is a question that we ask in this paper. We illustrate how financialisation has detrimentally impacted upon democratic cohesion, using South Africa as our case study. Financialisation has significantly shaped South Africa's society and economy especially since the country's transition to democracy in the mid-1990s.

To explore how finacialisation affects democratic cohesion we bring together a number of literatures: fiscal sociology, political economy of taxation and state financialisation. And by taking this novel approach we make a significant contribution to these literatures and to the political economy of development studies more widely by arguing that through bypassing tax collection in favour of financialisation, it delegitimises the social contract and damages accountability. We show that the process of financialisation has had a significant, and multifaceted, negative impact to democratic cohesion in South Africa. Finacialisation processes in South Africa have resulted in wealth concentration in a limited number of sectors, meaning tax revenue is collected from fewer

taxpayers, with workers in financial sectors and government employees being some of those who shoulder the heaviest tax burden, raising questions of legitimacy. Moreover, because these taxpayers are relatively well paid, they are the least likely to draw from social provision, preferring instead to access private healthcare and pay-for infrastructure, more generally. As a result, the process of financialisation has meant that governments are less accountable to their citizens, while solidarity among citizens, that is the shared feeling of 'being in this together', has been eroded.

Methodologically our paper draws from administrative secondary data sources which capture long-term trends in tax collection. Their qualitative interpretation is supported by the analysis of representative opinion pieces across the South African media landscape, reflecting high earners' attitude on taxation.

Our article proceeds as follows: first we discuss the conceptual debates in both the political economy of taxation and political economy of financialisation literatures. Interacting these two bodies of research, we present our argument: that financialisation undermines social cohesion on two accounts, namely between citizens and the state but also among citizens, through its impact on tax collection. We illustrate this process for the case of South Africa in our discussion.

2. The Social Contract in Financialised Democracies

2.1. Tax and the Social Contract in Democracies

The centrality of tax to the effective operation of the state has long been understood by economic historians and political economists who have argued that the mobilisation of domestic resources is essential if the state is to provide goods and services to its citizens. Such is this centrality that the role of tax collection has been conflated with the very creation and evolution of the modern state. Tilly (1975) in his seminal paper argued that the mobilisation of domestic resources under the threat of war was the principal factor in the very creation of the modern state with the state being created as a consequence of the urgent need to collect revenue for security.[1] Levi (1998: 1) agreed and argued that:

> the history of state revenue production, is the history of the evolution of the state. As specialization and division of labour increase, there is a greater demand on the state to provide collective goods where once there were solely private goods or no goods at all.

But Levi also noted the importance of revenue generation to state capacity; whereby the capacity of the state is increased by enhanced revenue collection but, in a symbiotic relationship, the state first needs to build the capacity to mobilise domestic resources. And in this sense historical sociologists and new fiscal sociologists have pointed to the importance of the relationship between state and society and more explicitly to the social contract that underpins this relationship because it is this relationship that binds rulers and citizens together and one which can curtail the very capacity of governments to govern since 'one major limitation on rule is revenue, the income of the state' (Levi, 1988:?) which in turn impacts upon the provision of public goods to citizens.

And it is the essential role of taxation that underpins the provision of public goods provided by the state on behalf of society which led Bräutigam (2002) to argue that:

> Raising revenue is the most basic task of the state. Before a state can protect its citizens, before it can provide justice or administer a bureaucracy, it needs to raise money. Through its key role as the tie that binds the ruler and the ruled, taxation supports representation, accountability, and state capacity.

How states raise these revenues through this tie that binds the ruler and the ruled has been the focus of literatures in historical and new fiscal sociology which have explored the evolution and characteristics of the distinct institutional arrangements through which tax collection and compliance are implemented, as well as the conflicts and social relations associated with these arrangements, given that 'states tax societies but they do not tax all their citizens equally' (Bräutigam, 2008: 25). How governments legitimise taxation strategies is an important analytical question because it directly impacts upon tax level compliance, tax evasion and ultimately, the fiscal revenues that are available whilst being illustrative of democratic processes.

'No taxation without representation!' was a battle cry synonymous with actors in the American War of Independence in response to British parliamentary attempts to levy taxes over indigenous populations; the attempt was a catalyst for social unrest while highlighting the strong link between raising taxation and democratic processes. Tax collection has thus been a central plank of social

cohesion and is a fundamental factor in the relationship between state and societies in democracies. Scholars exploring the impact of fiscal design on regime type have, on the whole, pointed to a positive correlation between tax collection and the strength of democracies but which are shaped by three causal mechanisms: economic growth, redistribution and legitimacy (Garcia and von Haldenwang, 2016). So whilst the delivery of economic growth and the associated provision of public services strengthens democracies, to first mobilise domestic resources, taxes need to be legitimised through people's consent (Schön, 2018). Compliance with taxes legitimises democratic governments (D'arcy, 2011) and increases the revenue available to be spent by the state apparatus. The two are directly related (Ehrhart, 2011) because if taxpayers both perceive that their interests are properly represented in political institutions and that the governance is good, their willingness to contribute by paying taxes increases (Bird et al., 2008).

Tax can generate links of accountability between taxpayers and rulers that impact on how responsive governments are (Paler, 2013). An increased dependence on the part of governments on taxation generates a *governance dividend* between the state and taxpayers. This dividend describes a state-society relationship that is constructed vis-à-vis negotiation between governments and society that coalesces around what citizens expect to receive for their taxes: what the taxes purchase. In this sense, in democracies, society has a significant influence over higher domestic tax collection and its utilisation by the state, a point Moore (2004:310) highlights is achieved with substantial 'quasi-voluntary compliance'. Levi (1988) also points to the importance of that this quasi-voluntary compliance does not involve coercive tenets of tax compliance but that it only occurs in a situation when taxpayers have confidence that 1) rulers keep their side of the bargain and 2) that other taxpayers keep theirs. Tax becomes embedded within the state-society contract as it concerns politics and power and the manner in which authority is exercised in a nation through its formal and informal institutions. This embedded taxation relationship and state-society contract is fundamental.

In this sense, taxation is central to the relationship that states have with society; a perspective argued by Martin, Mehrotra and Prasad (2009) for whom taxation 'enmeshes us in the web of generalised reciprocity that constitutes modern society' a relationship of necessity, as the state depends on taxes to function which are spent on the behalf of society — who are the recipients of public goods and services. As such, this relationship can generate contention because government

officials and taxpayers are expected to try and 'renegotiate this relationship to their advantage' (Martin, Mehrotra and Prasad 2009: 3-4). Therefore, whilst taxation constitutes a key nexus between states and society, it is a nexus that is far from equal, and because of this, it can be counted upon to generate tensions. Academic studies (Mann, 1984; Mann, 1988; Levi, 1988; Bräutigam and Knack, 2004; Bräutigam, Fjeldstad and Moore, 2008) have explored how different types of states manage these tensions and are able to adopt more legitimate and efficient forms of tax collection, recognising that the same taxes will not be viewed as legitimate and efficient by all groups, so taxes that are legitimate for whom and efficient for whom are important questions in these studies. In general terms, theories of tax compliance can be distinguished between contractual or vertical 'fiscal exchange' models, and horizontal solidarity or 'political community' ones (D'Arcy 2011; Von Haldenwang 2010). Fiscal exchange models argue that taxpayer compliance increases when they expect the state to deliver services and public goods in return for their taxes. A classic argument here is that representative government emerged as part of the democratic legitimation of the fiscal contract, which allowed the state to appear as 'fairer' vis-à-vis its citizens and collect more from more people (Levi, 1988). At the same time, democracies are expected to tax more efficiently because they trade taxation for more inclusive forms of representation (Bräutigam, 2008; Ross, 2004).

Therefore, how to create a tax system that is legitimate and complied with is both essential and complex. And whilst these challenges exist in all democracies, in developing countries in the global South, low tax burdens, high informality, highly concentrated wealth, and poor public services (Barlow and Peña, 2022) mean that legitimizing tax regimes is even more complex. A point which became all the more salient post-1980s when the International Monetary Fund (IMF) and the World Bank turned the dial from previous approaches where capital was taxed instead of labour to advocate more strongly for neoliberal tax reforms, shifting the burden of tax from capital to labour (Casteñeda and Doyle, 2019).

2.2. Raising Tax for Development: A Neoliberal Approach

Tax played an essential 'developmental' role across the global South post-1945, but its function was principally as a fiscal tool to support state-led attempts at managing economic growth and structural change. After the second World War, developing countries' economic development strategies included a 'particular role for tax policy' (Stewart, 2003: 168) which fitted squarely with

the Import Substitution Industrialisation (ISI) programmes that were gathering pace across the global South. The *en vogue* development strategy was a state-managed process to move towards industrialization through structural change and the modernization of developing economies through diversification (Dharam Ghai, 1991). Tax policy was therefore a tool to protect these nascent domestic industries through tariff policies, subsidies and favourable domestic tax design where tax concessions and incentives for industry and lower taxes for workers formed a central plank of tax regimes (Stweart, 2003). But whilst industry and manufacturing workers were enjoying tax breaks, the fiscal burden was heavily concentrated on natural resource exporting elites through a range of mechanisms: state-led price fixing, export taxes and increased taxes on profits. These mechanisms had a double effect: first, it was essential to mobilise domestic resources in support of the structural shift towards industrialisation. Second, they were used as tools to dissuade exporters from exporting and thus accelerating a shift within the economy (Barlow, 2023). But this critically created social tension between interventionist states and exporting elites because of questions of legitimacy and damaged social cohesion as profits were being redistributed to support other sectors.

The utilization of interventionist tax policies that levied a higher burden on traditional capital to support social-redistribution dominated development tax policies into the fifties and sixties but low tax collection and poor development outcomes due to low growth, high levels of poverty, poor public service provision and growing debt burdens, led Hungarian Economist Nicholas Kaldor to ask 'will underdeveloped countries learn to tax?' (Kaldor, 1962). More specifically Kaldor questioned whether 'underdeveloped' countries would be able to implement the orthodox tax policy prescriptions being advocated by the IMF and World Bank targeted at increasing tax take to reduce government borrowing (Gillis, 1989). Central to this framework was the creation of a low- and broad-based tax economy which would create a fiscally friendly environment for business investment by reducing the size and intervention of the state (di John, 2006). Abolishing trade taxes, simplifying sales taxes – through the implementation of a single low rate Value Added Tax (VAT) – and raising the tax burden through low but broad-based income and corporation taxes are all policies within this doctrine that shift the burden from capital to labour.

By the eighties, growing debt levels across the global South meant that the tax policy prescriptions which had, up until this point, been engaged with partially and inconsistently, now became a

condition of the IMF loans that are emblematic of the neoliberal turn. Neoliberal economics and the Washington Consensus which 'encapsulated free-market policies and structural reforms of the Washington based IMF and World Bank' (Panizza, 2005: 717) became the dominant narrative, where reducing the tax burden became part of a wider reform agenda: privatisations, de-regulation of capital markets, abolition of trade barriers – for debt-burdened developing states. So whilst neoliberalism focused on easing the tax burden on capital and financial transactions more broadly, it meant that the social cohesion that came from building the social contract through taxation was less robust. Moreover, through austerity, neoliberalism brought with it reductions in state spending and social redistribution which had further negative impacts on the social contract in cases where the value of what taxpayers received for their tax was diminished, bringing into question the legitimacy of the tax design for those who were purchasing less.

And this is a major development challenge because without sufficiently legitimising tax regimes, historically, states have instead relied on traditional export-led economic production or have sought to bypass domestic resource mobilisation through either debt-led development, aid or more recently blended finance options (Gabor 2021, Karwowski 2022). But this is problematic because these pathways circumvent the process of tax legitimisation and ultimately weaken the social contract between state and society (Barlow and Peña, 2022). Moreover, when the state intervenes into the socio-economic lives of its citizens through taxation, the collection and redistribution of resources impacts societal groups unevenly and therefore, it already has contrasting impacts within society. The fiscal contract is multilayered and complex because vertical exchanges between state and citizens do not affect all citizens equally and some groups share a greater responsibility for the burden which can further exacerbate the challenges. In the context of neoliberalisation, a lower tax burden on business and finance through low corporation tax can negatively impact upon legitimacy and wider democratic cohesion. Whilst the tax burden is lessened for business, it becomes concentrated elsewhere creating tensions, but it also has the ability to paradoxically generate tensions with taxpayers engaged in these financial and business sectors for other reasons because as wealth is concentrated in these sectors, they are less inclined to be consumers of public goods and more likely to engage with private provision, turning away from social and physical infrastructure provided by the state. One of the most emblematic examples of these neoliberal processes in the global South, which, in some cases, has usurped the natural resource export-led model, is the process of financialisation.

2.3. From Neoliberalism to State Financialisation

Neoliberal policies have facilitated and, as some argue, in many areas ushered in financialisation (Fine and Saad Filho 2016). Financialisation is a variegated process broadly referring to the growth in size, importance and power of the financial sector.[1] In this process state agency and power to "impose, drive, underwrite and manage the internationalization of production and finance in each territory" has been central (Fine and Saad Filho 2016: 687). Thus, in democratically organised societies, where neoliberalism in fact emerged first, neoliberal policies implemented by state institutions have paradoxically laid the foundations to undermine social cohesion and those very state entities, weakening their democratic legitimacy.

The fact that capitalism, more broadly, undermines democracy is a long studied phenomenon within critical political economy (Meiksens-Wood 1995, see also Polanyi 2001[1944]) since democratic societies are organised around two conflicting principles: their legislative and legal organisation is based on one-person-one-vote, while their economic resource allocation rather follows the might-makes-right principle. In this context, neoliberal reforms have been criticised for fuelling economic concentration, such as often empirically observed after liberalisation or deregulation drives and the privatisation of public assets. Excessive economic concentration in turn has been identified as a threat to democratic processes as those large individual market players will attempt to shape political and democratic decisions and processes to their advantage (Morck et al. 2005).

Financialisation appears to exacerbate these anti-democratic tendencies (Jessop 2013). Thus, Nölke (2021) argues that the large size, networked character and complexity of the financial sector have undermined democratic processes as the financial sector has become more influential. Apart from direct lobbying for which a large networked sector has ample resources, taxation plays a major role. A large finance industry effectively means its tax contribution (directly and through personal income tax on employment) gives the sector considerable leverage over policymakers. These will think twice before enacting policies that might 'hurt' a major domestic industry to avoid

[1] Financialisation is most often defined as "the increasing role of financial motives, financial markets, financial actors and financial institutions in the operations of the domestic and international economies" (Epstein 2003: 5).

its potential relocation. Maybe the most anti-democratic impact of financialisation on taxation emerged in the form of specific financial instruments, so-called tax incremental finance (TIF) arrangements, widely used in the US (see Karwowski 2019 for an in-depth discussion). TIFs are a way for cash-strapped local governments to fill their fiscal coffers now in exchange for handing over the proceeds of tax collection to a financial investor for the foreseeable future, in short the securitisation of tax revenue. This instrument is of course a direct result of the austerity imposed onto municipalities, stripping them of their major source of income for many years as a consequence of short-term financial difficulties. Since local governments are closest to citizens, this type of financial innovation significantly shrinks the ability of citizens to impact policymaking by removing access to future tax income.

Thus, the financialisation of the state has emerged as distinct research and a crucial strand of the financialisation research agenda, dealing with "the changed relationship between the state […] and financial markets and practices in a way potentially detrimental to the state's accountability towards its citizens." (Karwowski: 1001). State institutions across different administrative scales, including urban authorities (Halbert and Attuyer 2016), local governments (Weber 2010, Dagdeviren and Karwowski 2021) and central government institutions (Fastenrath et al. 2017), can be involved in financialisation. Equally, financialisation can be promoted by or pushed onto public entities (financialisation of and by the state, see Schwan et al. 2021).

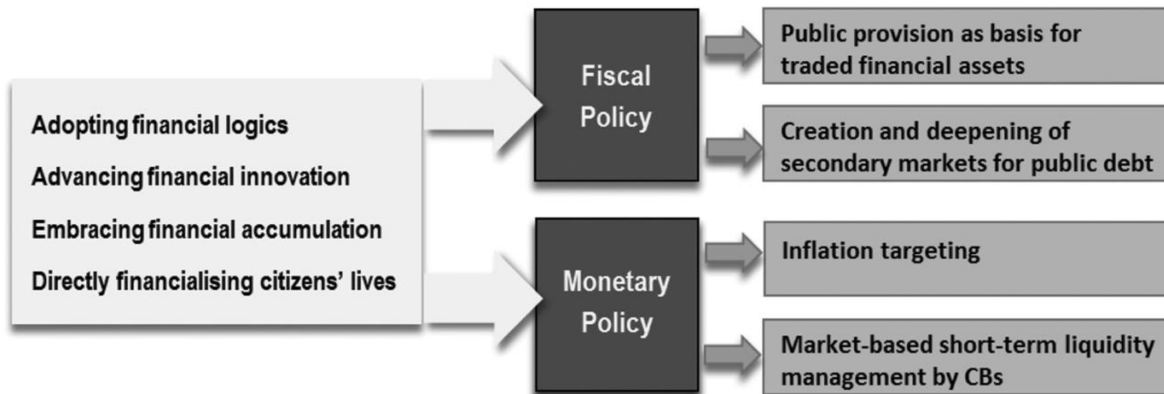
Using a macroeconomic lens which focuses on fiscal and monetary policy, Karwowski identifies four channels through which state financialisation can be at work (see graph 1).[2] State entities can adopt financial logics (see, for instance, Trampusch 2017, Løding 2018). They can advance financial innovation (Cooper et al. 2016, Dowling 2017), embrace financial accumulation (Preunkert 2017, Trampusch 2017, Lagna 2015, 2016), or directly financialise citizens' lives (Adamson 2009, Eaton et al. 2016). In terms of monetary policy, financialisation is closely linked with inflation targeting since that policy regime creates lucrative investment opportunities in financial assets (Epstein and Yeldan 2008, Kaltenbrunner and Painceira 2017). In the US and the Eurozone in particular, Central Banks have promoted market-based banking through their policies

[2] There are other useful analytical frameworks proposed for the study of state financialisation but they focus on the local government level (see Hasenberger 2024, Copley 2022). Since we study the interaction of taxation and democratic legitimacy, the macroeconomic angle is more suitable for our purposes.

and governance practices. Market-base banking effectively refers to the financialisation of banks' liabilities since it describes the shift among large banks towards managing their liquidity in an active and short-term manner through financial markets rather than sticking to deposits or other types of 'patient' capital, meaning long-term borrowing.

State financialisation of fiscal policy in turn can be examined considering the dynamics underlying public income and expenditure flows. The majority of state expenditure is captured by spending on social provision and infrastructure investment. In both areas, policy changes and financialised initiatives have aimed at transforming state expenditure into the basis for financial innovation, creating new financial assets. For instance, public expenditure on and, on a more general and abstract level, the mere public commitment to provide physical infrastructure (O'Brien and Pike 2015, Loftus et al. 2016, O'Neill 2019), healthcare (Mulligan 2016, Vural 2017, Bahia et al. 2016), education (Eaton et al. 2019) and social benefits (Lavinas 2018) have all been pulled into the financial sphere serving as underlying asset for the creation of financial instruments, functioning as financial investment and traded in secondary markets. Considering fiscal policy, financialisation scholars have examined how state entities have fundamentally changed their sovereign debt management over the past three decades or so. Here, financial logics have become deeply entrenched in states' policies and actions. Most notably, in many rich countries so-called debt management offices (DMOs) have been established which explicitly emulate private-sector practices and financial techniques such as mark-to-market or competitive pay levels for their employees (Schwan et al. 2017). DMOs were also at the forefront of embracing financial accumulation, actively managing governments' sovereign debt to reduce cost and ideally generate returns (Schwan et al. 2017, Lagna 2015). However, taxation is by far the largest source of state funds and curiously, with the exception of TIFs (Ashton et al. 2012, Pacewicz 2013, Strickland, 2013) has hardly been analyzed through the lens of state financialisation so far.

Graph 1. Conceptualising state financialisation



Source: Karwowski (2019: 1002).

Using the case of South Africa, a highly financialised democratic society, the next section will illustrate the detrimental effects of financialisation processes on the state's accountability towards its citizens and consequently social cohesion.

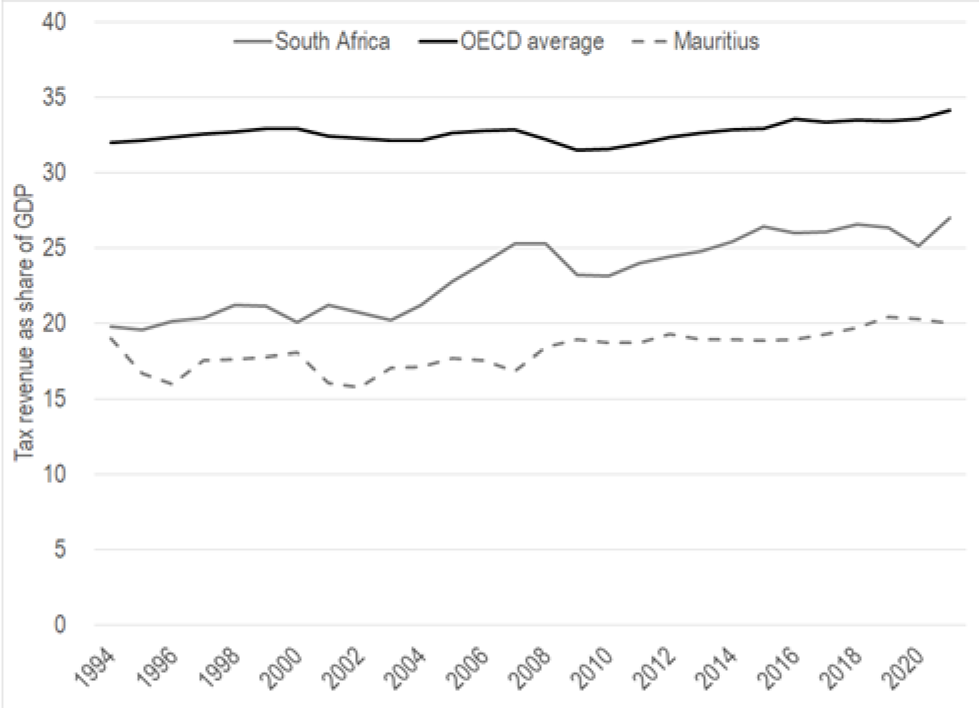
3. The Case of South Africa

South Africa provides an extremely insightful case study into the interaction between taxation, financialisation and democratic legitimacy. Before South Africa transitioned to democracy in 1994, when the first free elections took place, tax collection was extremely weak and tax evasion an expression of resistance against the racist apartheid regime (Hausman and Zikhali 2016) as there was no democratic contract between the apartheid government and most of the population. The New South Africa, now democratically legitimated, inherited the old administrative structures characterized by a relatively large formal sector, but with low tax compliance.

The transformation of the South African Revenue Service (SARS) to a citizen-facing institution, and crucially one that ordinary South Africans respect, under the leadership of Pravin Gordhan is celebrated as a major South African success story. With Gordhan as head, SARS became a highly efficient government entity and a desirable employer (Hausman and Zikhali 2016). The strong increase in the tax-to-GDP ratio, from just below 20% in 1994 to 27% in 2021 (see graph 2), is testament to the administrative body's capabilities. This figure is well above the average tax-to-GDP ratio in sub-Saharan Africa (15.6% in 2021, OECD 2024), while also exceeding the tax take

in Mauritius, a country generally regarded to be one of the few African growth miracles (Subramanian and Roy 2001, Behuria 2023). When compared to other emerging world regions, South Africa's tax take is notably above the average ratio in Latin America (21.7%, OECD 2024).

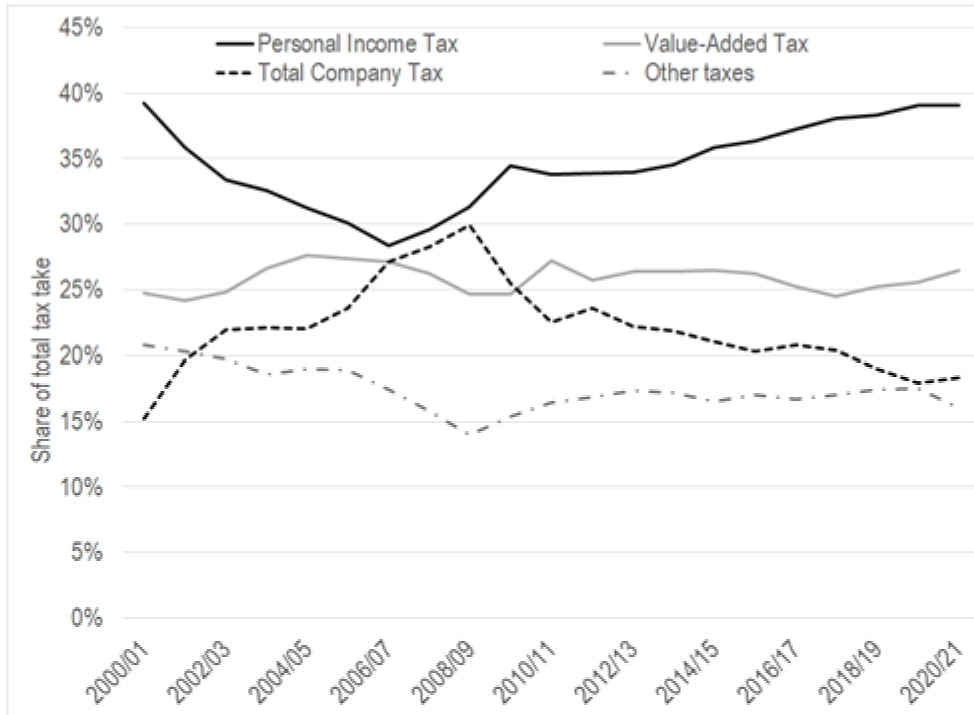
Graph 2. Tax revenue as share of GDP for South Africa, OECD, and Mauritius, 1994-2021



Source: OECD 2024.

Gordhan's reforms were successful as they spoke directly to the need to instill SARS with democratic legitimacy by making sure the staff body is representative, while cutting off nepotistic and corrupt ties which were commonplace at the tax authority during apartheid (Hausman and Zikhali 2016). To achieve this goal, the back and front offices of SARS, meaning tax return filing and tax assessment, were strictly separated. In this process, direct engagement with citizens was also put centre stage. SARS adopted a proactive strategy, meeting citizens at their workplace and in public spaces to explain tax filing processes which were fundamentally overhauled and modernized since the 1990s, including e-filing for instance (Hausman and Zikhali 2016). Despite SARS's generally acknowledged success, voices criticizing the concentration of the tax burden on a relatively small group of individuals in society are becoming louder, threatening to unravel democratic legitimacy of tax collection.

Graph 3. Tax revenue by type, 2002-21



Source: SARS 2024.

Especially after the Global Financial Crisis of 2008/9, South African tax revenue has become extremely dependent on personal income tax (PIT) while the revenue generated through company taxes has fallen dramatically (see graph 3). These two types of taxes - broadly representing a tax on labour and a tax on capital - had almost converged in terms of their contributions to overall revenue at the height of the economic boom between 2006 and 2008, accounting for a similar share of around 30%. In the aftermath of the Global Financial Crisis PIT's share in overall revenue generation grew strongly. This coincided with a 1 percentage point increase in PIT for the second highest tax bracket (from 40% to 41%) in 2016.

Overall, the PIT tax-take is strongly concentrated among top income earners. Table 1 below illustrates this phenomenon at different points over the past ten years, showing figures for 2013, 2017, 2021 and 2024. It captures the tax contribution information that is presented by the National Treasury in its annual budget review (see National Treasury 2024). These figures are widely shared and discussed in South African policy circles, among economic commentators and journalists. As one journalist put it somewhat pointedly: "The National Treasury is obliged to publish the

statistics, but I'm sure it would rather keep them away from the public eye and from prying journalists" (Hesse, 2024).

Table 1. Tax contributions form PIT by tax bracket, selected years

axable bracket	2013		2017		2021		2024	
thousand	% of taxpayers	% of PIT	% of taxpayers	⁄ of PIT	% of taxpayers	⁄ of PIT	% of taxpayers	⁄ of PIT
0 - R750	94.5	54.4	93.5	49.9	92.3	49.3	89.3	43.3
750 - R1 000	3.2	14.7	3.1	11.6	3.8	12.4	5.0	12.8
1 000 - R1 500	2.3	30.9	2.1	12.2	2.3	11.8	3.4	14.1
1 500 +	Tax bracket not available		1.4	26.3	1.6	26.5	2.3	29.8
Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**

Source: SARS 2024.

It is notable that the top two tax brackets shown here contribute around 40% of total PIT revenue, while only making up between 3.5 and 5.7% of PIT payers. This has been widely commented upon over the past decade. For instance, in 2015 BusinessTech, South Africa's largest business website, highlighted the tax contribution figures published by National Treasury in a piece titled 'Do we pay too much income tax in South Africa?', it read: "According to a quarterly Labour Market Report by Solidarity, published earlier this week, only 3.3 million out of a total 33 million eligible tax payers in the country pay 93% of all personal income tax. Worse still, only 3.7% – or 1.1 million people – pay just short of 70% of the total income tax received" (BusinessTech 2015).

Solidarity is a South African trade union, which was established in 1902 and supported the racist apartheid regime. Until today, it mainly caters to the (white) Afrikaans speaking community and has been extremely vocal on taxation issues, criticising the concentration of tax contributions in South Africa (Joubert 2014), and generally vehemently opposing potential tax increases, for instance for the introduction of national health insurance (NHI) (Hermann 2023)[2]. Until today, wealth and income inequalities closely map onto racial backgrounds in South African society, Hence, Solidarity is likely to mostly represent skilled workers. Another long-established organisation that has been strongly criticising PIT concentration is the Institute of Race Relations (IRR), originally established in 1929. The organisation understood itself as reporting and improving on race relations in the country, effectively being a representation of (mostly white)

liberal elites during apartheid. Its current CEO, John Endres, has recently commented on the concentration of PIT contributions, stating that "some 860 000 [South Africans] earned above R750 000 per year. This small group of people was paying almost 60% of all personal income tax (PIT). They were also the people with the skills and the means to leave South Africa" (Endres 2024).

The common narrative here is that government spending must be reined in to reduce taxes for the top income earners in society, otherwise those taxpayers will leave the country or refuse to pay their taxes. Deborah Tickle, member of the South African Institute of Chartered Accountants, academic at University of Cape Town (UCT) and a well-known tax commentator, running a column called 'Tickle on Tax' (SAICA 2020), summarised this view: "So we've got this tiny tax base, and the only way to grow the tax base is to have growth, more employment and more people paying tax, and then you can start funding more" (Tickle as quoted by Hesse 2024). "Unfortunately, in an environment where public trust in government is very low due to unfulfilled promises to address irregular and wasteful expenditure, they are becoming tired of bearing this burden… Consequently, many are engaging in a form of 'tax revolt' by deciding to do easier or less work that results in less tax, leaving the country, or engaging in tax evasion" (Tickle as quoted by SAICA 2020).

Much of government spending goes towards the most vulnerable in society and therefore constitutes redistribution from the top income earners to the poor. South Africa has one of the most extensive social benefits systems in the global South, paying over 13% of GDP to households as benefits in 2022 (OECD 2024). Just before the Covid-19 pandemic in 2020, there were over 11 million beneficiaries of social grants in the country, accounting for almost a fifth of South Africans. At the height of the pandemic, when the benefits system was expanded to unemployed households not in receipt of major grants, 40% of the population was reached by social protection (Patel 2021). Persistence of high levels of poverty, unemployment, inequality and low levels of economic growth make such large spending on social protection necessary.

The resentment of top earners towards the taxman is further confounded by their opting out from public provision, foremost healthcare. South Africa is the country with the highest private voluntary health insurance (PVHI) contribution as a share of total health spending in the world.

This figure stood at 43% in 2021 (WHO 2024). Thus, private spending on healthcare in the country almost equals public healthcare expenditure. However, the beneficiaries of private health insurance are similarly concentrated like PIT contributions, accounting for ca. 15% of the total population (OECD 2015). These South Africans do not use government but private health provision, resulting in what the current South African president calls "apartheid that remains in health care, where you have the best healthcare for the rich and poor healthcare for the poor" (BBC 2024). Therefore, the ANC government has proposed a NHI scheme which would be compulsory for all citizens and, in an unprecedented way, would bar private insurance cover for healthcare available under NHI. The aim is to channel at least part of South Africans PVHI into such a public scheme through progressive taxation.

This has led to a powerful backlash from high-income earners. The Democratic Alliance, a party traditionally representing white voters and, more recently, professional classes more generally, has campaigned in the 2024 elections on a platform opposing NHI. Discovery Limited, the South Africa-headquartered financial services provider, has been a very vocal opponent, stating in its latest annual report that "[f]unding the additional healthcare spend required for NHI through tax increases on a small base is not sustainable" (Discovery 2024, 28), hence also referring to PIT contribution concentration.

Discovery is a major provider of private health insurance in South Africa where it was founded shortly before the end of apartheid, in 1992. The company was listed on the Johannesburg Stock Exchange in 1999 and has since become one of the leading JSE corporations by market capitalisation, being part of the top 40 listed companies, the so-called JSE 40 (ShareData 2024). From its South African base, the company has managed to extend its financial services into 39 markets globally with Vitality UK and Vitality Global, constituting its two other major business divisions next to Discovery which concentrates on South Africa. Although Discovery does not run its private healthcare facilities like some other large private providers in the global South (see Karwowski 2019 for a discussion) it nevertheless is a major proponent and beneficiary of state financialisation in the area of social provisions.

Structurally, the unevenness of the tax burden is a result of income inequality exacerbated by financialisation. South Africa is one of the most financialised economies of the global South and

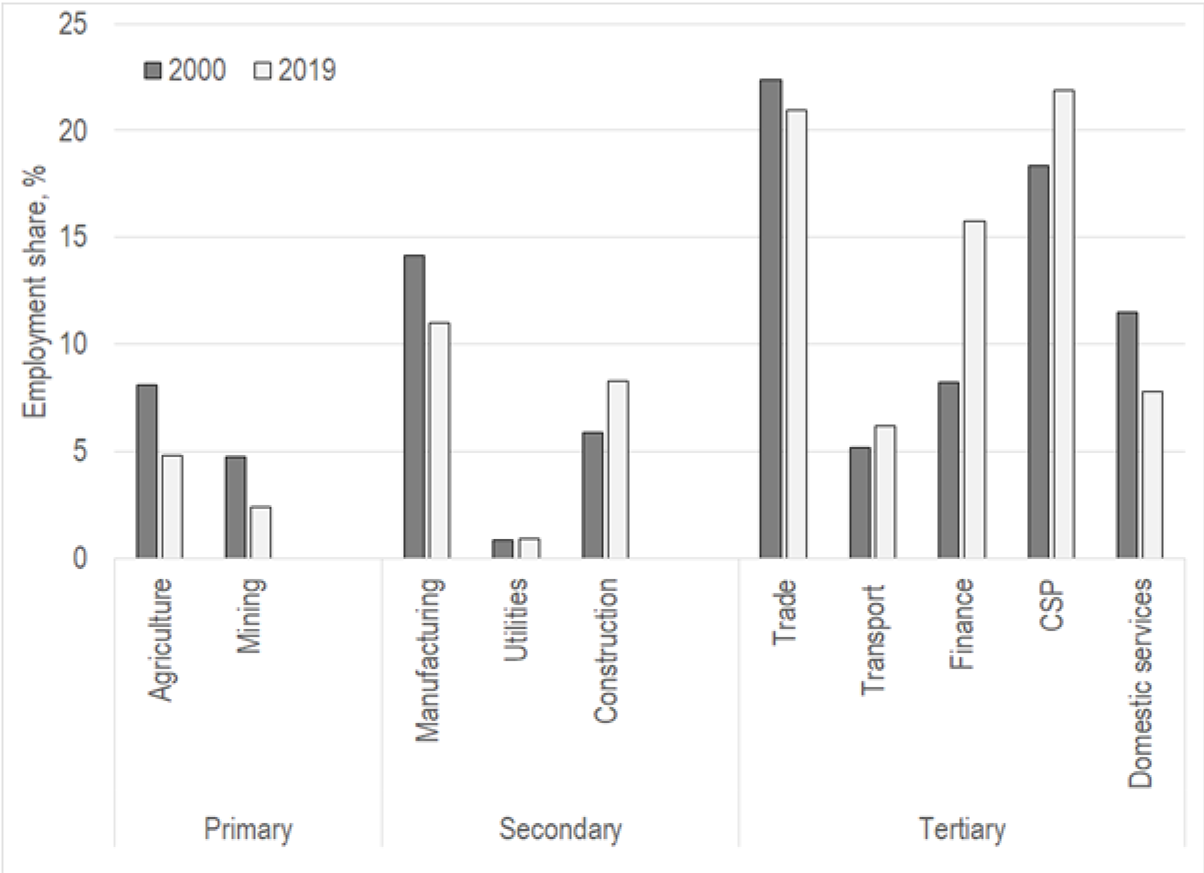
also among middle-income countries. High levels of household debt (Karwowski 2021, Newman 2015), a volatile exchange rate and a relatively strong exposure to foreign investors in domestic government debt (Isaacs and Kaltenbrunner 2018) are some of the symptoms of this situation (see Karwowski 2022, for a comparison among emerging economies).

While high income and wealth inequality is not new to South African society and the financial sector has historically played an important role in economic development[3], only with the re-integration of South Africa into global economic and financial structures during the 1990s has financialisation started unfolding with a significant impact onto the labour market and wage and asset inequality. The phenomenon brought about what Karwowski, Fine and Ashman (2018) call the four-low economy: low investment, low employment, low wages and low productivity. But apart from having a dampening effect on economic growth, financialisation also brought about a profound structural transformation of the South African economy. As the financial sector grew while other areas of growth were subdued, its share in overall employment expanded dramatically from just over 8% of total employment in 2008 to almost twice as much, 15.8% in 2019 (see graph 4). It was the economic sector that gained the most over the past two decades, leading the overall expansion of the tertiary sector which by 2019 employed 73% of all South Africans in work (up from 66% in 2000, Bhorat et al. 2021).

Financialisation has been shown to fuel inequality by inflating financial sector pay, financial asset and real estate prices (Lin and Tomaskovic-Devey 2013, Godechot 2016, Kohl 2021). These trends have also been documented for South Africa (Karwowski 2018). Sectoral changes in employment have in turn contributed to income polarization. The rise of tertiary-sector and especially financial employment has been accompanied by a growth in the share of jobs (up from 10% in 2000 to 15% in 2019) in overall employment. While that itself could be a positive development, it did not induce a substantial move away from low-skill jobs which only declined from 29.5% to 28.8% of total employment. Rather, mid-skill level jobs were lost relatively as high-skill positions increased in number (Bhorat et al. 2021). But most crucially, wage developments over the past two decades or so resulted in a squeezing of the middle-income earners. Thus, Bhorat et al. (2021) show how between 2000 and 2017 wages between the 40th and 65th percentiles of the wage distribution, so exactly the middle section of earners, experienced a decline in average annual real wage growth, while the bottom and the top saw positive growth on average. The consequence of such wage

polarisation is that a relatively small group of finance professionals and high-skill government employees contribute a large share to tax revenue.

Graph 4. Employment shares by sector, comparison 2000 and 2019



Source: based on Bhorat et al. 2021.

This creates resentment, especially as this small group of people often do not partake in social services, opting for private provision instead. As discussed, South African high earners have opted out from public healthcare provision as ca. 15% of the population are willing to spend on their private health insurance as much as the South African state spends on public funding. Equally, wealthy South Africans pay into private pension funds to secure their retirement. Just over one tenth of the population (in 2017/18, 6.8 million people of a population of just below 60 million, National Treasury 2022) contributes to a private pension plan. The total value of pension assets in the country, including private and underwritten funds, was 78% of GDP in 2020 (OECD 2024). This is well above the OECD average of just over 60% (OECD 2024). Hence, there is substantial

wealth in South African pension funds which to a large extent benefits a small share of the population, once again the top earners, who do not have to rely on public provision. Finally, high earners in South Africa also spend substantially on private security amidst high crime levels. Hence, in March 2023 the Private Security Industry Regulatory Authority (PSIRA) had 2.8 million registered private security guards on its books. The latest available figures for official police staff indicate just over 180,000 employees in March 2021 (SAPS 2021). While the comparison to police staff is not straight forward since registered security guards do not have to be active throughout the year, the figures capture the fact that affluent parts of South African society use private security services extensively.

4. Discussion and conclusion

We argue that the structural changes brought about by financialisation, especially the tendency to exacerbate income and wealth inequality, undermines democratic processes by weakening the implicit contract between state institutions and citizens which are seen as crucial to vertical tax legitimacy. Since decisions about taxation are tightly linked to redistribution through public provision they always influence citizens' perception of tax justice. In many respects, these issues are at the core of modern democratic societies, encompassing societal debate and political decisions about whom to tax, how much, to provide which services to whom. But more fundamentally, taxation and government spending, especially on public provision, are built on and continuously reproduce solidarity among citizens in a democratic setting. Financialisation with its logic of self-sufficiency of the individual and drive to transform public provision into the basis of financial assets and a stream of financial profits undermines this very fabric of democratic society.

Thus, financialisation of the state does not only chip away at vertical legitimacy of tax collection, the implicit contract between the state and its citizens, but also at horizontal legitimacy of taxation, the solidarity felt among citizens who finance through their taxes, access, and share the same public services. Therefore, the definition of state financialisation, referring to "the changed relationship between the state […] and financial markets and practices in a way potentially detrimental to the state's accountability towards its citizens" (Karwowski: 1001), requires a revision to account for this aspect.

We propose to update Karwowski's definition of state financialisation referring to: the changed relationship between the state and financial markets and practices in a way potentially detrimental to the state's accountability towards its citizens, citizens' solidarity within society, and social and democratic cohesion. This tendency is inherent to financialisation, and especially financialisation of public provision, since it takes as a starting point the logic of self-sufficiency. This is most prominent in pension provision and the shift from a taxpayer funded pay-as-you-go system to funded pensions across OECD countries. The narrative justifying this shift was one of excessive cost for taxpayers given an aging population together with a promise of more efficient private provision in the light of buoyant financial markets. Similar arguments have been made about the provision of universal health coverage in South Africa, the NHI scheme. For policymakers outsourcing the funding and provision of key social infrastructure (such as pensions and healthcare) is convenient as they can avoid difficult discussions and decisions centring around tax increases and redistribution. Instead of engaging in these debates which require compromise solutions to yield legitimate policies, building democratic consensus, policymaking in democratic societies but also increasingly in the context of development programmes and policies, be they led by the World Bank/IMF or the United Nations, is increasingly trying to sidestep difficult decisions by relying on financial innovation. The belief that financial markets and instruments can somehow generate 'free' funds out of nowhere is at best wishful thinking but in actual fact a dangerous fallacy since it distracts us from the actual important questions in democratic societies of whom and what to tax and where and on whom to spend, together shaping a socio-economically just community we want to be part of.

5. References

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[1] We understand the state here by using Mann's (1986) definition as a territorially bounded and centralized regulation of all important aspects of social life.

[2] https://vorms.solidariteit.co.za/wp-content/uploads/2023/10/SRegsdienst23100509321.pdf

[3] Mainly in the service of gold and diamond mining and its exploration (Kubicek 1979).