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Abstract

Historical evidence from state-building processes in Western countries suggests that a substantial governance dividend can be gained from mobilizing domestic financial resources through the tax system. Democratic South Africa is an intriguing case of a fiscal state where the positive tax-governance link that forms the basis of a productive fiscal contract, has not materialized despite the presence of several factors that would normally work in favor of a fiscal contract: there is tax dominance in state revenue; a salient income tax that contributes the largest share of revenue; taxpayers are informed about how revenue is spent, and South Africa is a constitutional democracy where individual rights and freedoms are protected and executive constraint and accountability are part of the institutional architecture. This paper investigates the historical, political, and economic factors that have contributed to this outcome. It also investigates the prospects for a fiscal social contract to emerge in the future, considering the current weakness in governance and accountability, coerced tax collection in a low-trust environment, and non-transactional state-society dynamics.

Key words: Taxation, Governance, Tax Compliance, Fiscal Policies, Social Security, Fiscal Social Contract, Welfare Programs, South Africa

JEL-classification: H2, H26, H3, H53, H55, O23

Introduction

Historical evidence from state-building processes in Western countries suggests that a substantial 'governance dividend' can be gained from mobilizing domestic financial resources through the tax system (Levi, 1988; Tilly, 1992). In Western countries, the tax system contributed to improved governance through three main channels (Moore, 2008, 2015). First, fiscal bargaining and negotiations between the state and citizens over taxes were central to the development of a *fiscal* social contract.[1] From this perspective, taxpayers have a legitimate right to expect something in return for taxes paid and are – unlike non-taxpayers – more likely to hold their government to account if it underperforms. Second, governments have stronger incentives to promote economic growth when they are dependent on taxes and therefore on the prosperity of taxpayers. Third, dependency on taxes requires states to develop a bureaucratic apparatus for tax collection, which can lead to additional improvements in public administration.

Because the pattern of state formation in Western countries was unique to a particular context and time, one should be cautious and not assume similar state-building outcomes in the contemporary developing world. This is why studies of the association between taxation and good governance emphasize its high context dependency (Levi, 1988; Braütigam, Fjeldstad and Moore, 2008). Similarly, although the literature claims that 'no taxation without representation' contributed to democratization, taxation cannot be claimed to have unilaterally led to participatory politics (Bizhan, 2018: 18). Whether taxation produces socially beneficial outcomes depends on how a society is organized and how the state interacts with society. Specifically, the relationship between taxation and the social structure of a society as well as the capacity of social groups to bargain with the state determine whether taxation produces the kind of social benefits seen in Western Europe since the 19th century (Schumpeter, 1918; Levi, 1988). The governance dividend of taxation in the European context emerged from a combination of the coercive power of centralized governments and demands made on the state by influential social classes (Tilly, 1992). Bargaining between states and citizens was instrumental in shaping modern citizenship as defined by mutual rights and obligations. Similarly, negotiation between citizens and governments over taxation is at the foundation of socially beneficial taxation outcomes, balancing coercive political power with the demands of citizens (Prichard, 2015).

But what are the prospects for a fiscal social contract emerging in contexts characterized by histories of oppression, voicelessness and exclusion, which is common for many current lower- and middle-income countries, but is vastly different from the experience of Western countries? Democratic South Africa is an intriguing case for studying this question. Many conditions that would otherwise support the emergence of a social contract characterized the country at the time of its democratic transition in 1994. South Africa has

[1] The concept of the social contract has its origins in the work of a range of influential philosophers, such as Plato (c. 375 BC), Hobbes (1651), Locke (1690), Rousseau (1762), and Kant (1797). They argued that 'civil and political rights constitute a form of exchange where a citizen accepts obligations in return for benevolent government' (Besley, 2020: 1309). If a government fails to deliver such policies, citizens can legitimately withdraw their cooperation and/or actively seek leadership change. Such a contractarian perspective allocates a central role to reciprocal obligations in establishing an effective state in which the power to tax is as fundamental (Levi 1988) as the state's monopoly on violence. The idea of a *fiscal* social contract expresses the notion that fiscal state-society bargaining and exchanges produce socially beneficial outcomes such as political representation, state-building, and responsive and accountable governance (Braütigam, Fjeldstad and Moore, 2008). In this paper we use the phrase 'fiscal social contract' and 'fiscal contract' interchangeably.

for decades been, and remains, a tax-dominant (or fiscal) state, collecting taxes in the region of 25–28% of its gross domestic product (GDP) (National Treasury, 2009 to 2024). In fact, tax revenue constitutes more that 98% of state revenue. The single largest contribution comes from salient and increasingly concentrated personal income tax (PIT), which has been argued to be a main driver for the fiscal social contract in Western countries. Yet, the socially beneficial reciprocity that could have derived from a fiscal social contract has eluded South Africans. Approximately 50% of the population remain economically excluded, subsisting on small tax-funded cash grants.[2] These grants are financed by a small number of income taxpayers who continue to comply with taxes despite the state's failure to deliver basic public goods and services such as a functioning electricity grid and protection against crime. Thus, after thirty years of democracy, taxes have long ceased to contribute to a just and inclusive future. In this paper, we seek to explain why this is the case.

The analysis is based on a variety of sources of data compiled during 2003 and 2004: Official reports and data on tax revenues and public expenditures from the South African Reserve Bank, the National Treasury, South African Revenue Services and South African Social Security Agency; reports from public commissions on state capture, taxation and public expenditures; survey data from Afrobarometer and the World Values Survey; scholarly literature on economic and political development in South Africa during the last three decades; and newspapers articles and media reports.

We find that despite initial favorable conditions South Africa has become a case of a broken tax-governance link. The finding suggests that the unequal fiscal positions in a fractionalized society have set the stage for at least two types of social contract: one among a small number of heavily taxed individuals that could have led to a fiscal social contract, and another among grant recipients who have little fiscal leverage but much vulnerability. However, the small group of taxpaying citizens has no electoral leverage to demand fiscal accountability. The much larger group, which would have electoral muscle to contest pro-elite politics, are captive to a fiscal vulnerability that is leveraged politically to subdue contestation. The specific power dynamics related to the high degree of fractionalization has weakened the bargaining power of different groups where it could have disrupted entrenched politics. These features may explain why the positive tax-governance link reported in current literature has not materialized in democratic South Africa.

Our study contributes to a growing literature exploring the conditions under which a fiscal social contract would (or would not) emerge in the context of diverse and complex developing countries (Prichard, 2015; Meagher, 2018; Moore, Prichard and Fjeldstad, 2018; Bak, 2019; Besley, 2020; Robinson, 2023). This literature suggests that the composition of taxes matters. *Salient* taxes, such as assessed income tax payments or other direct taxes, heighten taxpayers' awareness of their contribution and are more likely to encourage demands for accountability and engagement in the spending of revenue compared to less salient taxes such as the value added tax (Chetty, Looney and Kroft, 2007; Finkelstein, 2009; de la Cuesta et al., 2023). The

[2] For 2024, the monthly grants ranged from ZAR 3010 for the War Veteran's grant, with 15 million beneficiaries, to ZAR 370 for the Social Relief of Distress grant, with between eight and ten million recipients (SASSA, 2024). The weighted (according to number of recipients) average value of the grants is ZAR 773.93 per month (the 2024 Food Poverty Line is ZAR 760). Converted at the prevailing (May 2024) ZAR/USD exchange rate, the average monthly grant translates to USD 42.57.

literature furthermore shows that the salience in public expenditure is important (Alm et al., 1992; Slemrod, 2003; Doerrenberg, 2015). Expenditures that visibly violate reciprocity are more likely to invite taxpayer contestation. Furthermore, existing literature shows that a fiscal contract is unlikely to emerge in an unreceptive or authoritarian institutional environment that favors coercive enforcement and minimal taxpayer rights (Levi, 1988; Tayler, 2006). However, there is not much literature on the contextual dynamics that produce a weak tax-governance link. Our study serves to fill some of this knowledge gap by empirically investigating the case of post-1994 South Africa. Despite initial favorable conditions, democratic South Africa has become a case of a broken tax-governance link. This paper investigates the historical, political, and economic factors that have contributed to this outcome.

Moreover, this study sheds light on the complexities of fiscal sociology in disparate, developing country contexts. Social values are a strong motivator for human behavior, including state-society interactions (Snavely 1990; Ali et al., 2014). Social values largely determine what citizens expect from a government, how forceful they are in their demands, and whether they have a proclivity for contestation, or a high tolerance for exploitation. Social values are therefore likely to influence whether citizens engage in bargaining with the political elite, which has proven to be a crucial counterbalance for coercive politics and instrumental in the emergence of participatory politics and accountable governance (Moore, 2008; Prichard, 2015). Variation in social values across contexts may therefore shape social contracts in fundamentally different ways irrespective of relatively comparable formal institutional arrangements. Power imbalances rooted in unobservable, long-standing social values may, for instance, influence the role and use of taxation in a society more than constitutional arrangements. In such a context, using tax policy narrowly as a revenue tool while relying on formal institutional arrangements for the socially beneficial allocation of tax revenues may prove counter-productive for broad development objectives. In this paper, we argue for a broad view of tax policy as a social rather than a revenue tool in contexts that need to accelerate development. The success of tax policy is then not measured by revenue collection but, because of the significant risk of elite diversion of tax revenues, by its links with social advancement.

The paper is structured as follows: Section 2 describes the fiscal system at the inception of democracy in South Africa, and examines events that unfolded after the 1994 political settlement that impact the link between taxation and governance. Section 3 explains how and why, over three decades, these events have culminated in an unsustainable fiscal situation, which may prove unfavorable for the tax-governance link because it paradoxically weakens the bargaining power of heavily-taxed individuals. The prospects for a fiscal contract to emerge in South Africa are addressed in Section 4, followed by a conclusion in Section 5.

2. From political liberation to state capture

2.1 The fiscal system at the inception of democracy

South Africa's historic 1994 election ended apartheid by endorsing a renegotiated, democratic social contract premised on equal citizenship and basic human rights. The transition afforded the country an unusual opportunity to redeliberate its social contract and rewrite its institutional and policy frameworks. At the time, South Africa was by many standards an atypical middle-income country. The democratic social contract was formally codified in a well-designed Constitution that defines the mutual rights and obligations of both state and society. Prominent in the architecture of formalized post-apartheid state-society relations is a powerful set of checking institutions devised to prevent a repetition of the country's exploitative past. Also unusual among middle-income peers are the effective government and high-quality judicial institutions that characterized the young democracy at inception (Levy et al., 2021). The economy was diversified and, at the time, the largest and most industrialized in Africa.

Underpinning the democratic transition was a political settlement that comprised three bargains. The first detailed the explicit terms that would govern the handover of political power from the former to the incoming elite. The terms included the protection of property rights and the rule of law in addition to other elements of constitutionalism that would ensure executive constraint and accountability (Fombad, 2010). The second, more implicit, bargain related to the distribution of power and associated benefits among an ideologically diverse incoming elite. The terms of this bargain were opaque—as was the understanding that the divergent ideologies and aspirations of the new elite would be harnessed and funneled towards broadly shared prosperity. The third bargain contained promises, made to the non-elite, of economic inclusion and accelerated upward mobilization. Constitutional backing for the rights of society and duties of the state lent credence to these promises. In keeping with the shared idea of cooperation towards a transformed society, there was also a society-wide commitment to the comprehensive fiscal restructuring that transformation would require (Levy et al., 2021).

This fiscal undertaking of a progressive tax and transfer system that would contribute to a sizeable 'social wage' and support an agenda of economic inclusion and upward mobilization is important to understand when exploring prospects for a fiscal social contract in South Africa. It hints at the *quid pro quo* that taxpayers accepted in 1994 to satisfy the notion of reciprocity in the tax system. Rather than a conventional, transactional type of expectation of public goods and services provided in exchange for tax payments, taxpayers would contribute to a transformed, fairer, and more inclusive future. Although taxpayers in different contexts are likely to define the quid pro quo that they expect in exchange for taxes differently, there can be no question that reciprocity constitutes the moral justification for taxation (Levi, 1988). In 1927, US Justice Oliver Wendell Holmes Jr. inferred reciprocity by justifying 'taxes as the price that we pay for a civilized society' (*Compania General De Tabacos De Filipinas V. Collector Of Internal*, 275 U.S. 87 (1927), United States Supreme Court, No. 42:100). This is perhaps comparable to the South African context where taxes are considered the price of a just and transformed society. In other words, taxes satisfy reciprocity when they promote social well-being. Frecknall-Hughes (2020:3) confirms that the contemporary rationale for taxation derives from 'the provision by government of public services, redistribution of wealth, and the creation of physical and legislative infrastructure for the benefit of society. The provision of these services is the moral basis for taxation'. The assumption is that taxes translate into government output that is beneficial to society's well-being. It is worth bearing in mind that taxation has no inherent social benefit. As a fundamentally coercive act, it is of social benefit (and therefore morally justifiable) only if tax revenue is used effectively and reciprocatively. This raises the question of what taxpayers can do in instances where taxes do not promote social well-being. If the context and conditions allow taxpayers to bargain for greater engagement and reciprocity, taxes may well forge more responsive governance and greater accountability. If not, a fiscal social contract may prove elusive.

2.2 Patronage and erosion of public institutions

Having campaigned and won the election on the back of the *Reconstruction and Development Programme* (RDP), the government led by the African National Congress (ANC) found delivering on the promises of inclusion and upward mobilization difficult from the outset.[3] Without a macroeconomic framework underpinning the RDP, it proved unworkable by 1996. The economic opportunities necessary to realize the promises did not materialize, in large part due to an ideological gridlock within the ANC leadership that compounded domestic supply-side constraints. The constraints arose and accelerated as a consequence of a pattern that saw critical policy decisions delayed (Hausmann et al., 2022; Hausmann et al., 2023). The ANC-led government favored centralization and state control over private participation in critical areas of service delivery such as electricity supply and railway transport. This had inhibiting effects on economic growth and investment that might have been possible after 1994, but instead became severely constrained since 2009.

Further, policies such as preferential procurement, devised in 1997 to promote 'black economic empowerment' (BEE), imposed far greater costs on complex organizations than leadership acknowledged and in disservice to the objectives of expanding economic opportunity and employment (Hausmann et al., 2023).[4] Public-sector employment was used as an alternative pathway to inclusion, affording the transformation imperative precedence over core functions (Hausmann et al., 2023). Public-sector transformation eventually coincided with an accelerating proclivity for clientelism and patronage, increasing pressure on the fiscus while the quality of services deteriorated (Levy et al., 2021). By 2007, the ANC controlled all levels of government, state agencies and institutions, as well as the state-owned enterprises (Du Toit, 2024). The governing party's cadre-deployment strategy visibly degenerated into a patronage-based politicization of public service during the administration of former president Jacob Zuma (2009-2018), facilitating gatekeeping and rent-seeking (Levy et al., 2021; GoSA, 2022). The fall-out became evident in key institutions, perhaps most disastrously in state-owned enterprises (SOEs) and municipal governments. Over time, core public-management practices disintegrated.[5] Successive bailouts of SOEs also contributed to critically slowing down an economy that struggled to function amidst energy shortages and dysfunctional rail and port services (Hausmann et al., 2023).

[3] The coalition government was known as the Tripartite Alliance. The African National Congress aligned formally with the South African Communist Party (SACP) and the Congress of South African Trade Unions (COSATU) to establish "a broad tent encompassing many ideological proclivities; degrees of public-spiritedness; and regional, ethnic, and economic interests" (Levy et al., 2021: 26). The divergent ideologies and ambitions within the country's new leadership may have been an early predictor of the internecine rivalries and factionalism that would later fracture the intra-elite bargain (Hausmann et al., 2023).

[4] Black Economic Empowerment (BEE) is a policy of the South African government aimed at facilitating broader participation in the economy by black people. It is a form of affirmative action specifically intended to redress the inequalities created by apartheid.

[5] For a detailed discussion of how core public management was eroded, see Levy et al. (2021:16-17). Specifically, the authors report a disregard for the checking systems enacted in the *Public Finance Management Act* and the *Municipal Finance Management Act*.

After 2009, expensive political appointments in the public sector notably came at the expense of much-needed, skilled, frontline employees. Public employee compensation escalated, predominantly benefiting a unionised contingent of public servants in well-remunerated managerial positions (Hausmann et al., 2022). In general, public-sector remuneration invites much controversy given the weight it adds to the country's fiscal burden and its crowding-out ramifications for more productive and pro-poor forms of public expenditure. The politicization of the bureaucracy has also invoked destructive forms of gatekeeping politics within the ranks of the political leadership as the competition for political positions with access to resources intensified drastically from 2010 onwards (Beresford, 2015).

Misuse of black economic empowerment rules opened a further elite pathway to public resources. Preferential public procurement became a tangled web of personal deals and loosely rule-based programmatic reforms concealed behind a façade of transformation. Yet, a mostly legitimate order held until Jacob Zuma assumed power in 2009, following which, elite predation on public resources became pervasive, nearly crippling the fiscus and escalating to a captured state (GoSA, 2022). Towards the end of Zuma's second term as president in 2018, it had become obvious that the democratic social contract premised on inclusion had gone into reverse (Levy et al., 2021).

Formal checking institutions proved an inadequate bulwark against the onslaught of personalized dealmaking and gatekeeper politics that characterized the Zuma presidency (Beresford, 2015). This style of politics, described as 'executive aggrandizement' in the literature (Bermeo, 2016), signals an executive-accountability crisis. Threatening the constitutional notion of executive constraint, executive aggrandizement entails the deliberate and systemic dismantling of horizontal checking mechanisms. It is perpetrated by an elected leadership that repurposes independent institutions of accountability by, for instance, packing them with loyalists or cadres (Khaitan, 2018). In South Africa, this state-led dismantling of democracy-sustaining institutions has been, and in some quarters continues to be, justified through a populist rhetoric that vilifies checking institutions as 'anti-people' or 'anti-transformation'. A legacy of the Zuma administration has been the aftermath of targeting crucial SOEs through a private agenda used to consolidate a network of powerful elites and misrepresented as 'radical economic transformation'.

Compliance of checking institutions was accomplished through the strategic deployment of loyal functionaries, targeting the National Treasury,[6] the South African Revenue Service (SARS)[7] and the judicial

[6] See Report IV, Volume 1, of *The Judicial Commission of Inquiry into Allegations of State Capture, Corruption and Fraud in the Public Sector including Organs of State,* titled 'The Attempted Capture of the National Treasury'.

[7] See the *Final Report of the Commission of Inquiry into Tax Administration And Governance by* SARS (the 'Nugent Commission') (2018: 4) where it is reported that 'what occurred at SARS was inevitable the moment Mr Moyane [i.e., the Zuma-appointed Commissioner General of SARS] set foot in SARS. He … dismantled the elements of governance one by one. This was more than mere mismanagement. It was seizing control of SARS … [S]enior management was driven out or marginalised at SARS, and … senior management appointed by Mr Moyane was anything but compliant … [T]he development of its sophisticated information technology, which has inbuilt checks, was summarily stopped, and the organisational structure of SARS, that provided oversight, was pulled apart. Dissent was stamped out by instilling distrust and fear. Accountability to other state authorities was defied. Capacity for investigating corruption was disabled'. Also (2018: 4), 'there has been a massive failure of integrity and governance at SARS … What SARS has become is sufficient proof that integrity and governance failed on a massive scale'.

system.[8] In 2022, the *Judicial Commission of Inquiry into State Capture,* popularly referred to as the 'Zondo Commission', condemned this agenda as grand-scale state capture.

South Africa's SOEs have a strong, earlier record of infrastructural development that was instrumental in economic growth and development. State-capture affected all SOEs, but targeted the largest two, Transnet and Eskom. Transnet is the country's state-owned rail, port, and pipeline company and is essential for mining and export logistics. Eskom is the state-monopoly electricity supplier. The Zondo Commission reports that tax-funded procurement spending tainted by state capture amounted to an estimated ZAR 57 billion at the time—at least 97% of which came from Transnet and Eskom. Running up massive debts, the collapse of crucial SOEs could only be forestalled through state bailouts. The direct financial loss, however, pales in comparison to the economic-multiplier effects as the country's core infrastructure became eroded and service delivery from Eskom and Transnet was severely compromised.[9] The impact on South Africans has been profound. Starting in 2008, the failing power utility introduced daily, rationed blackouts to avert a collapse of the national grid. The energy crisis is estimated to have shaved two percentage points off the growth of a stagnant, high-unemployment economy in 2023 (South African Reserve Bank, 2023). In the mining sector, traditionally the mainstay of the South African economy, the confluent energy and logistics failures continue to subdue exports, growth, and employment.

After three decades of democracy, unemployment and inequality have risen instead of receded and are at levels unmatched elsewhere in the world. South Africa has suffered low and slowing growth for most of the past thirty years, underperforming both its sub-Saharan African and upper-middle-income peers. Economic stagnation has become particularly stifling over the past fifteen years. From 1994 until the onset of the Global Financial Crisis in 2008, real growth per capita averaged 2% annually (IMF, 2023; World Bank, 2023). Contracting more sharply than its peers during 2008 and 2009 and off a lower base, South Africa's real growth remained flat, eventually contracting to 0.5% in per capita terms in the five years preceding the COVID-19 pandemic (i.e., 2014–19). In March 2020, an extraordinarily restrictive COVID-19 lockdown was announced, because the country's epidemic-related contraction again overshot that of its peers, with growth remaining subdued ever since.

2.3 A fractionalized society: grant recipients vs. taxpayers

According to the Census 2022 population count, there are 62 million South Africans, up from 43 million in 1994. In the third quarter of 2023, *Quarterly Labour Force Survey* (StatsSA, 2023)[10] reported that 16.7 million South Africans were employed in the non-agricultural formal sector, with an official unemployment rate of 33%, up from 20% in 1994. This would increase to 42% if discouraged work seekers were included.

[8] See the 2019 report of *The Enquiry in Terms of Section 12(6) of the National Prosecuting Authority Act 32 of 1998*.

[9] *GAIN Group* has quantified the economic cost associated with the collapse of the rail and port utility. A daily loss of ZAR 1 billion in economic output amounts to an annual loss of ZAR 353 billion for 2023, a loss equivalent to 4.9% of annual output. See the press release by GAIN Group, *Transnet Freight Rail effect on the economy – estimate for 2023.* https://www.gaingroup.co.za/images/Documents/Transnet-Freight-Rail-effect-on-the-economyestimate-for-2023-PR-1-September-2023.pdf.

Unemployment among 18- to 24-year-olds is at 61% (71%, if young people who have given up on finding a job are included). Measured by the upper-middle-income poverty standard (living on less than USD 6.85 per day), 62% of South Africans qualify as poor (World Bank, 2023). Figure 1 illustrates the degree of fractionalization in South Africa that has, by the end of 2023, culminated in nearly twice as many grant recipients as employed individuals, and almost five times as many grant recipients as assessed income taxpayers.

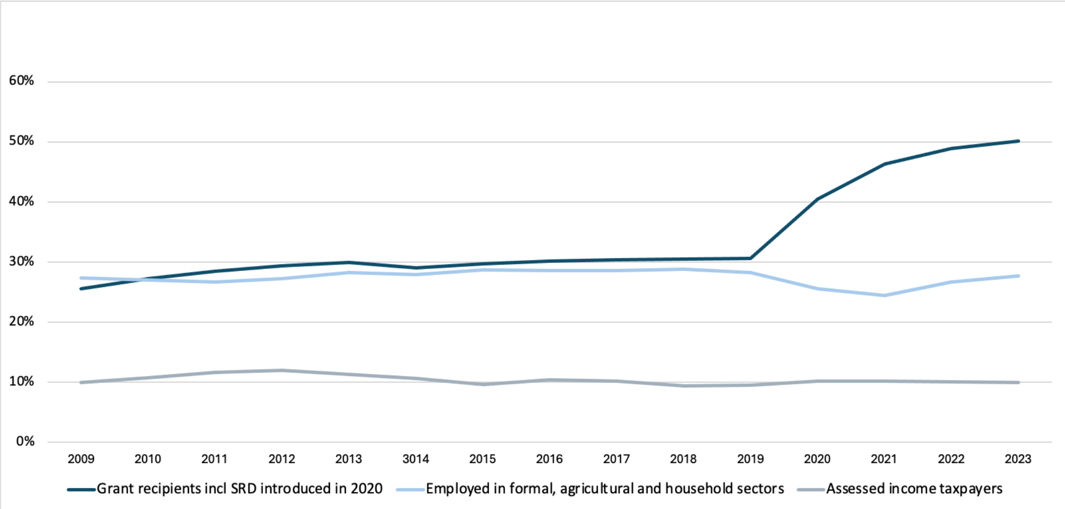

Figure 1: A fractionalized society: Grant recipients, employed individuals and assessed taxpayers as share of population, 2009–2023
Sources: The South African Reserve Bank (2024), National Treasury (2009–2024), and the South African Social Security Agency (2024).

Inequality remains high, too, as is reflected in a Gini score of 0.63 (World Bank, 2023). The 2022 *World Inequality Report* reports that the income share of the highest-earning 10% of South Africans declined during apartheid, reaching a bottom inflection point between 1976 and the mid-1980s. From 1994 to 2022, the income shares of both the top 10% and top 1% have risen markedly while the share of the bottom 50% has steadily trended downwards (Chancel et al., 2022). In 2022, the top-earning 3500 individuals earned more than the poorest 32 million people. The widening rich-poor divide after 1994 has cemented a legacy of non-inclusion and confirms that costly transformation programs have been unsuccessful. The racial profile of income inequality has, however, changed. Black South Africans now outnumber whites in the richest 10% of the population, evidencing grand-scale elite transformation.

Thirty years after political liberation, the prospects for South Africa's development have dimmed significantly and much economic potential remains unfulfilled. Increasing unemployment, poverty, and inequality manifest the effects of escalating state dysfunction. The 1994 promise of inclusion has been undermined as public resources have been diverted towards elite benefits and institutions of accountability dismantled. The country's political leadership has become untethered from the main idea of constitutionalism, of an executive that is limited in its actions and accountable to its citizens.

These developments have also violated the pro-poor fiscal undertaking of the 1994 political settlement in the sense that the tax system now serves the common well-being of society only minimally, being largely diverted towards elite interests. South Africans have, paradoxically, been unable to halt the disintegration of a state that is dependent on taxpayers in a democratic and constitutionally checked setting where both taxes and the scale of misuse of tax revenues are salient. The next section takes a closer look at fiscal developments over thirty years of democracy.

3. The fiscal system

Already during the early years of democracy, it became obvious that the economic opportunity needed to fulfil the 1994 promises would not emerge under the conditions created by an ANC-led government. As a result, the government increasingly resorted to offsetting fiscal, demand-side measures. Growing expenditure requirements cannot be reconciled with a shrinking tax base, forcing either greater concentration and progressivity of taxation, imposed on a small number of taxpayers, or broader-based regressive forms of taxation levied on the same poor citizens that the fiscal machinery aims to support. The revenue-expenditure divide accumulates public debt that a stagnant economy can ill afford and generates debt service payments that steer towards a fiscal cliff where crucial social spending on, for instance, social grants, is at risk (Montalto, 2023). It seems that a pro-elite fiscal system has emerged, crowding out pro-growth and pro-poor management of public finances.

3.1 National taxes

South Africa is a tax-dominant state that relies on taxpayers for 98% of state revenue. The country consistently collects taxes at rates of around 27% and 28% percent of total domestic production, which is much closer to the 34% average of developed OECD countries than to the approximately 15% average collected by other sub-Saharan African countries (OECD, 2023).

The bulk of the country's tax revenue is contributed by quite a steeply progressive tax on individual income. PIT accounts for 35– 39% of the total tax take. The number of assessed taxpayers remains low, at less than 10% of the population—which is to be expected given the high inequality. It does, however, translate into a concentrated PIT on a narrow base and, therefore, a high average tax burden on a relatively small number of individuals, as illustrated in Figure 2.

Figure 2 graphs taxpayers' contribution to PIT revenues by income category in 2024. It shows that fewer than 200 000 taxpayers contribute nearly one-third of all PIT. It also shows that 3.1 million individuals pay 90% of all PIT, and that the contributions of fewer than 300 000 taxpayers cover the cost of all 30 million social grants. Thus, the Tax Administration Act 28 of 2011 (TAA) serves enforcement by the South African Revenue Service (SARS) well: taxes are collected effectively. Some may argue too effectively when interpreted in reference to section 36 of the Bill of Rights in the Constitution.[11] This situation, although predictable in conditions of large income dispersion and stagnant growth, is likely to have a bearing on endeavors to develop a fiscal social contract. To assist small businesses, corporate income tax (CIT) is graduated at low levels of company income. From 1 April 2022, a flat rate of 27% on taxable income exceeding ZAR 550 000 is levied (reduced from 28%). The contribution of CIT to tax revenue is dampened by the subdued economic environment and hovers around 20%. Direct taxation on a relatively small number of individuals and companies therefore accounts for well over 50% of total tax revenues, approaching 60% in some years, which compares to many OECD countries.

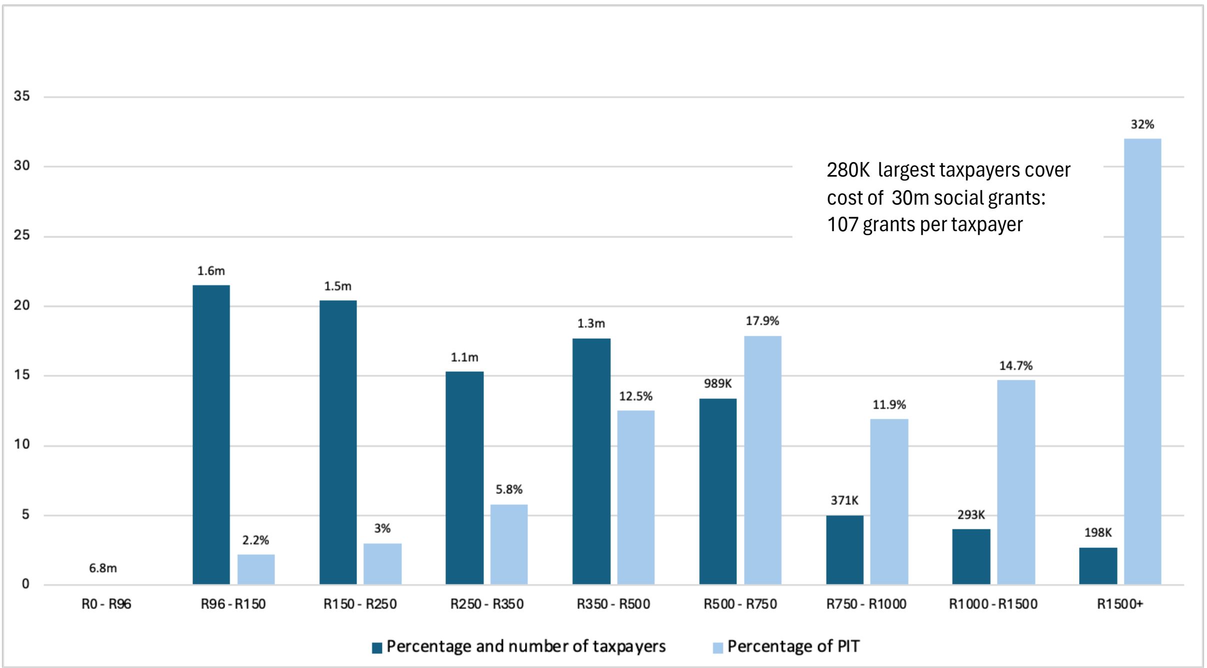

Figure 2: Concentration of PIT: Taxpayers' contribution (%) to PIT across income categories, 2024
Source: National Treasury (2024).

Figure 3 shows the shifts in the relative contributions of PIT and CIT to tax revenue since 2009, together with debt service cost. CIT is declining in response to the base-narrowing economic environment, except for occasional windfall gains from the mining sector on the back of high commodity prices (for instance in

[11] For instance, sections 45(1), (2), 63(1) and (4) of the TAA authorize SARS to conduct warrantless inspections and searches, limiting taxpayers' rights to privacy. Sections 45(1) and (2) may in fact be unconstitutional (Fritz, 2017; Moosa, 2017). In December 2024, the High Court delivered a landmark ruling with regard to SARS's interpretation and use of the TAA. Ruling against SARS with a punitive cost order in *ASPASA NPC and other v C:SARS,* the court noted that statements by SARS were "intemperate, disproportionate, and reflective of an inappropriate hostility toward taxpayers". The court further noted that SARS "adopted a hostile and contradictory stance" in opposing the applicants' reasonable and lawful application and acted in a manner "not befitting of a public authority tasked with administering the tax law fairly and respectfully".

2022 and 2023). Notably, debt service cost is expected to exceed total CIT collections by a substantial margin from 2024 onwards.

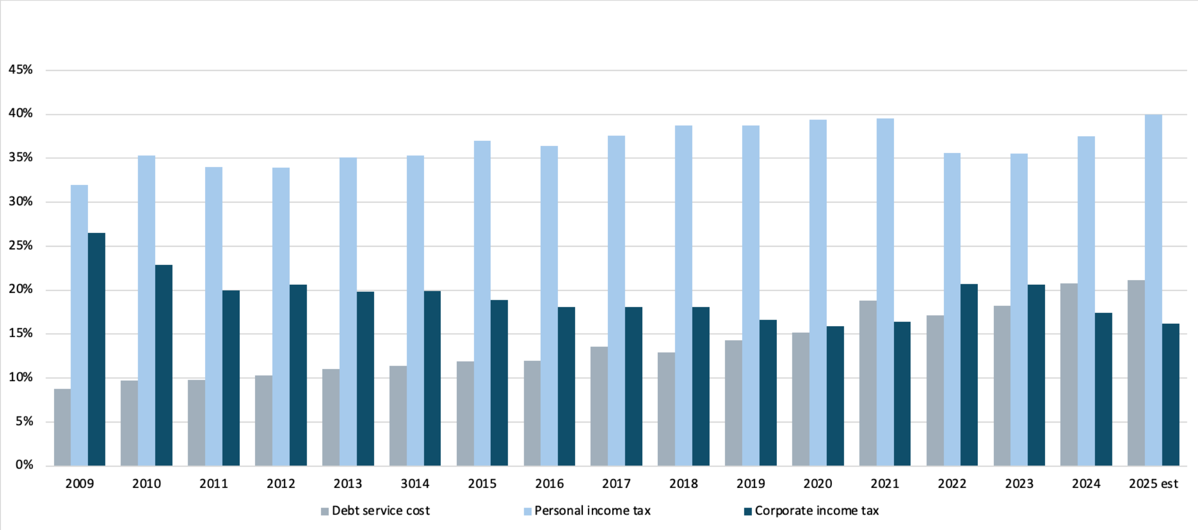

Figure 3: PIT, CIT and debt service cost as % of tax revenue, 2009–2025
Source: National Treasury (2009–2024).

The largest sources of indirect taxation are value-added tax (VAT) and the levy on fuel, which consists of the General Fuel Levy and Road Accident Fund Levy. Broad-based VAT (levied at a standard rate of 15%) raises in the region of 25% of total revenue, with the fuel levy contributing a further 5%. Combined, the largest indirect sources of revenue contribute about half of the joint contribution of PIT and CIT.

The tax structure reflects the history of inequality as well as developments over the three decades since 1994. Persistent inequality would explain the progressive nature of direct taxation as well as the reliance on these forms of taxation rather than broad-based indirect taxation that may be viewed as regressive (although staples are zero-rated).[12] The underlying trend of a narrowing of the tax base and increasing concentration of the direct tax burden is the result of economic stagnation caused by state dysfunction, although shocks like the COVID-19 pandemic also disrupted revenue collection.

3.2 National expenditure

The expenditure side of the fiscal system reflects large allocations to education, health, and social security, which includes social grant payments. This aligns with the commitment to invest in a sizable and transformative social wage. However, the amounts spent on these allocations have not translated into mass inclusion because of the quality- and service-delivery constraints related to the politicization of the bureaucracy described in Section 2. Rather, politicization itself is evidenced by the expenditure trends. Compensation for 1.3 million employees in the public sector is the largest expenditure item, accounting for

[12] Contrary to the consensus, Bachas *et al.* (2023) find that consumption taxes such as VAT are progressive in developing countries when accounting for informal consumption by poorer segments of the population. Thus, they argue that he widespread policy of exempting food from taxation is hard to justify on equity grounds in low-income countries.

a third of total expenditure. Above-inflation pay rises under union pressure have produced a public-wage premium over private remuneration. In addition to this, the rise in wage expenditure exceeds the rise in employment and has coincided with a decline in service delivery. A constrained economy unable to provide the opportunities needed for transformation has increased the pressure on the fiscus for social assistance while the number of cash grant recipients has steadily increased.

South Africa is widely acclaimed for its extensive rollout of a means-conditional cash grant system, which is the main component of the country's social protection programme. On a scale unmatched for a developing country, the social-grant system has made well-recorded inroads into poverty. Nearly a third of the population subsist on these modest grants every month, yet only 11% of expenditure is allocated towards this item. In November 2024, just over 19.3 million grant beneficiaries were recorded (South African Social Security Agency 2024). A special Social Relief of Distress (SRD) grant was implemented initially temporarily during the Covid-19 pandemic to mitigate the effects of the severe lockdown on low-income South Africans. Sustained economic hardship, however, resulted in a series of extensions of SRD payments and, so far, unheeded calls to transform grant payments into a permanent basic income grant. Adding the SRD grants disbursed monthly to the social grants raises the percentage of grant recipients to 45% of the population of 62 million in 2024 (South African Social Security Agency 2024). National Treasury projects a sustained upward trend in the number of grant recipients. These numbers and trajectories are damning to the 1994 promises of upward mobility and inclusion. Hausmann et al. (2023) argue that the steadily expanding grant system is being (mis)used by a political elite that has laid self-beneficial siege to public resources, largely to the exclusion of poor South Africans and as compensation for the sustained breach of the promise of inclusion.

The widening gap between revenue and expenditure is loan financed (National Treasury, 2023). By 2024, public indebtedness had risen to 75.5% of GDP, with the debt service requirement increasing accordingly. Debt service absorbs 20% of revenue, more than the entire CIT take, and is rising faster than any other expenditure item (National Treasury, 2024). Debt servicing encroaches on government's expenditure on crucial pro-poor items like health and social protection as well as pro-growth economic development. This edges the country's public finances closer to a fiscal cliff. Eventually, additional borrowing may be necessary to afford loan interest payments. Downgrades by rating agencies S&P Global and Fitch and Moody's to sub-investment grade on account of the energy crisis and high level of public debt have raised the cost of South Africa's debt. So has the 2023 grey listing by the Financial Action Task Force (FATF) for non-compliance with international standards to prevent money laundering as well as terrorist and proliferation financing. Over the last 15 years, government spending and public debt have consistently grown faster than the GDP and revenue, driven by employee compensation and rising debt-service costs, which in 2023, jointly amounted to more than 50% of government expenditure. Notably, these expansions have not been accompanied by gains in efficiency. The changed composition of expenditure due to crowding-out pressures in the fiscal system has also reduced the share of infrastructure investment that would support economic growth.

Figure 4 illustrates some of the crowding-out pressures that are evident in the 2024 Budget Review. Most notably, the compensation of 1.3 million public employees exceeds total PIT collection and crucial pro-poor and pro-growth items, for instance the social-grant expenditure for 28 million South Africans. The cost of servicing public debt, driven by above-inflation rises in employee compensation, exceeds the revenue collected from CIT. Employee compensation and debt service together, at ZAR 1136 billion, exceed both total income-tax collection and the sum of pro-poor and pro-growth expenditure shown in Figure 4.

This pro-elite fiscal prioritization, accomplished through politicizing the bureaucracy and a targeted cadre-appointment strategy, significantly weakens the impact that taxation may otherwise have had as a social tool to accelerate post-apartheid progress and transformation.

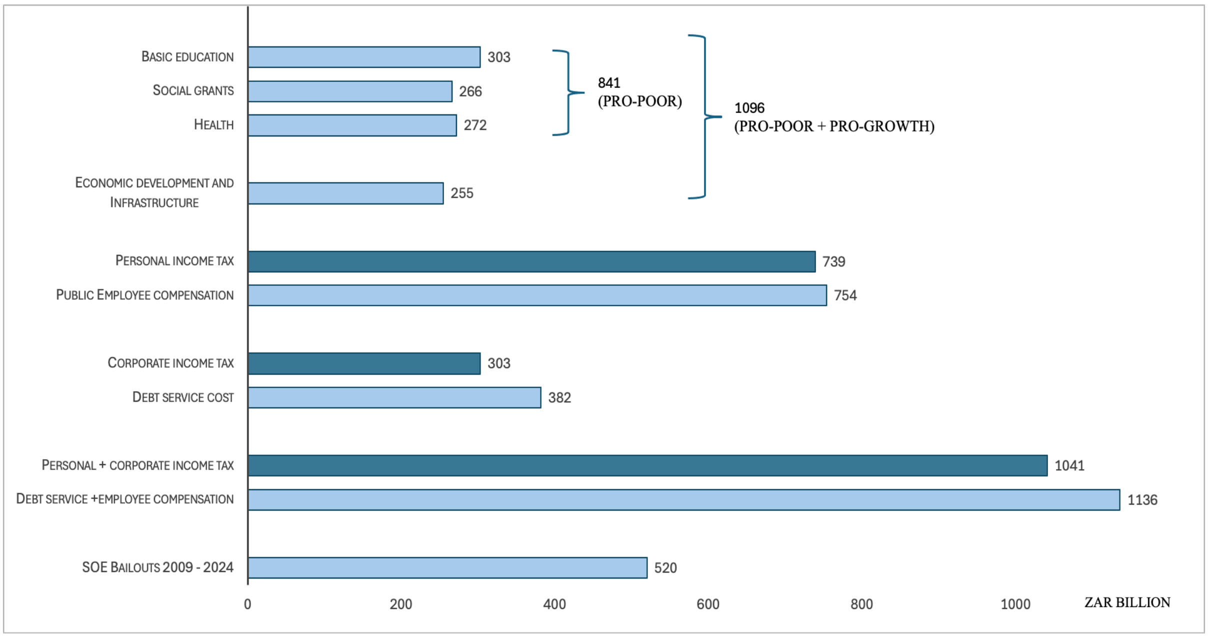

Figure 4: Fiscal prioritization in 2024: crowding out of pro-poor or pro-growth expenditure
Source: National Treasury (Budget Review 2024)

A controversial and sizable share of revenue is used annually to bail out SOEs that no longer function. Unable to effect a turnaround, these organisations are a grave risk to South Africa's economic prospects; prospects that depend on energy as well as road, rail, and port services that are often not available (Gumede, 2022). Their implosion has only been staved off by bailouts that have cost taxpayers an estimated ZAR 520 billion since 2009 (see Figure 4), the bulk of which has gone to the electricity utility Eskom. Despite regular tax-funded lifelines, Eskom remains unable to reform, financially and operationally. The energy crisis is escalating amidst steep hikes in the average energy tariff, which has increased by 749% between 2006 and 2023, from 17.79 cents per kWh to over ZAR 1.51 per kWh (Moolman, 2022; Labuschagne, 2023; National Energy Regulator of South Africa, 2023). In a radical reversal, SOEs that used to be significant corporate taxpayers are now a major drain on society's resources—an outcome directly related to elite capture, political appointments, and the misuse of preferential procurement rules.

Although well adrift from the trajectory envisaged in 1994, there may be potential to catalyse South Africa's fiscal status in order to forge engagement with taxpayers and greater accountability in the spending of revenue. If done successfully, South Africa may yet develop a fiscal contract characterized by a positive tax-governance link - a symbiosis that currently does not exist. The next section explores the prospects for a fiscal contract to develop in the complex context of South Africa—complex because of its apartheid legacy, compounded by state capture that, although exposed in detailed specificity (GoSA, 2022), appears to continue.

4. Prospects for a fiscal social contract in South Africa

In the previous sections we argued that democratic South Africa is a fiscal state where the positive tax-governance link that forms the basis of a productive fiscal contract, has not materialized, despite the presence of several factors that would normally work in favor of a fiscal contract. In Section 2, we described how executive accountability has been eroded in a targeted, systemic manner, with lasting society-wide consequences. In the process, institutional checking mechanisms were dismantled, making horizontal enforcement of accountability all but impossible. Vertical, electoral channels did not punish unaccountable governance adequately to effect change during the first five national elections after 1994.[13] This, for reasons related to historical and ethnic loyalties[14] (Gethin, 2020), but also because state dependence was leveraged for electoral benefit. In Section 3 we summarized how these developments affected the fiscal system.

In this section, we explore whether the prospects for accountable governance and an economic recovery are as dim as these developments would suggest, or whether tax bargaining may present a non-electoral handle on vertical accountability. A key question is whether it is possible for taxpayers to collectively leverage tax reciprocity to establish a positive tax-governance link. We examine possible reasons why South African taxpayers, who spectated state capture as it unfolded, did not, or could not, demand engagement and greater oversight over public resources, seemingly accepting an exploitative social contract. In particular, we investigate the confluence of the effects of social norms, an internalized commitment to the 'new' South Africa, coercive rules of tax enforcement, and possibly the absence of exit strategies. Given the many forms

[13] The seventh national election held on 29 May 2024 produced a result that may appear to signal voters' willingness to mete out electoral sanction for poor governance, with support for the ruling ANC dipping sharply to 40% (down from 57.5% in 2019 and 62% in 2014). In an unexpected development, a populist far-left party, uMkhonto weSizwe (named after the paramilitary arm of the ANC under apartheid), was founded five months before the election with ousted former president Jacob Zuma's face on its campaign posters. The party received 15% of the national vote to become the third largest party nationally, performing especially well in the KwaZulu Natal province where Zuma hails from. The party advocates for deconstitutionalization and the empowerment of traditional leaders.

[14] Questions regarding the impact of South Africa's high degree of ethnofractionalization on state-society relations often arise. It is possible that civic behavior centers on ethnic associations and group interests rather than national identity and overarching national interest. Gethin (2020) reports evidence of this behavior in the electoral context. The 2021 Afrobarometer survey, however, reports that more than two-thirds of South African respondents experience their identity as *equally* South African and ethnic, or *more* South African than ethnic, or *only* South African. These responses support the usefulness of a macro or national perspective on social-contract analyses despite the inevitable impact of ethnofractionlization on aspects of civic behavior.

of fractionalization in the South African population, it is possible that more than one type of social contract represents citizens' interaction with the state.

4.1 Reciprocity and tax morality

The moral justification for taxes derives from the norm that citizens contribute to the cost of maintaining the well-being of society on the assumption that government uses revenue to achieve that (Fjeldstad and Sjursen, 2024; Prichard, 2022). In other words, reciprocity justifies taxes, and tax morality rests on both flows: from taxpayers to the state, and from the state to society's well-being. Tax morality is violated by interrupting either one, that is, by the non-compliance of taxpayers or by the state misspending revenue. There are, however, substantial asymmetries in the instruments available to correct these respective violations. For instance, enforcement and coercion are readily available instruments to speedily correct taxpayer violations. For the second type of breach, that is, when states do not use revenue to the benefit of society, correction channels are weaker and indirect, and power imbalances unfavorable. Apart from resorting to electoral and horizontal mechanisms in the second type of breaches, tax bargaining relies on the leverage that reciprocity offers taxpayers to forge a positive association between taxes and accountability.

The notion of leveraging tax reciprocity to forge a fiscal social contract raises a further asymmetry, one between positive and negative reciprocity. By offering more public goods and services in exchange for increased taxes, positive reciprocity may, at least in theory, be relied upon by states in its efforts to raise revenue. Or, citizens asking for goods and services may offer tax payments in return. This constitutes a collaborative state-society interaction motivated by mutual benefit. Negative reciprocity on the other hand is adversarial. It arises in scenarios where services are suspended because taxes are withheld, or, the contentious scenario, where taxpayers threaten tax withholding in response to the state's breach of reciprocity. The latter spills over into categories of tax behavior that are associated with tax revolts and is usually characterized as morally reprehensible. Building a fiscal contract from this position is therefore difficult, as the South African experience attests. It creates dilemmas for taxpayers who perceive tax compliance as moral behavior but who may also feel the need to resist being coerced into complicity with a state whose behavior they no longer consider to be morally justifiable. Therefore, rather than participating in a tax revolt or deploying strategies of tax evasion, they may opt for exit strategies such as emigration.[15]

This may be the case specifically in societies that subscribe to norms-based state-society interactions rather than a transactional social contract. While both entail reciprocity, in the first mutual responsibilities are based on social values about what each ought to do. Tax compliance is likely to be unconditional in nature and contestation is unlikely to be rooted in demands for tax reciprocity. Tax bargaining, and therefore also a

[15] According to the South African Revenue Service's annual tax statistics for 2024, 37 584 citizens have ended their tax residency in South Africa during 2023 resulting in a loss of ZAR 3 billion in collectable taxes for the 2023/24 tax year. Over the ten years from 2014 to 2023, a total of 432 848 taxpayers have terminated their South African tax residency either through emigration or changing their tax status. The consequence in both cases is that the country loses tax revenue. The trend is generally more prevalent among high-income taxpayers; in 2023 for instance 2 380 taxpayers earning more than ZAR 1 million per year ended their tax residency. There is however a dramatic rise of 575.9% (from 1 814 individuals in 2014 to 12 260 in 2023) in the number of taxpayers with taxable income of zero or less terminating their South African tax residency.

fiscal social contract, are unlikely to materialize in a predominantly value-based environment. A transactional social contract, on the other hand, is characterized by societal expectations premised on tax reciprocity. In other words, tax compliance is conditional on these expectations being met. Society's proclivity for contestation will likely be higher, meaning that transactional state-society interactions may be more conducive to tax bargaining.

4.2 Social norms, reciprocity and contestation in state-society engagements

Whether South Africans' social norms lean towards the conditionality associated with a transactional social contract or towards the unconditional compliance associated with a norms-based social contract is an empirical question. In the absence of a targeted survey of South African taxpayer attitudes, some questions and responses in the World Values Survey and Afrobarometer Survey nonetheless provide an indication of prevailing norms regarding state-society reciprocity. Although they may not directly answer the question whether social values support conditional or unconditional tax morality, they give an indication of whether expectations raised by the social contract contain elements of reciprocity or a proclivity to object, electorally or otherwise, when citizens are dissatisfied with government's performance. One reason why this question is complex relates to the heterogenous composition of the post-1994 citizenry, many of whom historically experienced a state-society relationship that afforded them no voice and no forum to demand minimum rights, let alone reciprocity and accountability. Silent acquiescence or violent protests were the only avenues for civic contestation. Such remnants of the apartheid legacy cannot be summarily erased and often lead to political disengagement, both in terms of participation and contestation.

Evidence from World Values Survey

The South African responses to some questions in Wave 6 (2013)[16] of the World Values Survey (WVS) (Inglehart et al., 2018) suggest a norms-based rather than a transactional social contract. For the majority of respondents, politics is not important, and they are not members of any political party. Just over 50% always vote in elections. Yet, respondents harbor expectations of what the state should provide: the state must tax the rich to subsidize the poor; supply aid to the unemployed and reduce income inequality. Although most respondents have no or little trust in government, they lean towards a norm of compliance, expressing the belief that claiming government benefits to which one is not entitled is never justifiable, nor is cheating on taxes or accepting bribes.

Furthermore, some responses are indicative of a high distance-to-power culture (Hofstede et al., 2010), which may show acceptance of stark power imbalances and a vertical hierarchy of rank and authority. For instance, the majority of respondents (56%) are in favor of a strong leader 'who does not have to bother with parliaments and elections', while 63% consider it a good idea to have non-elected experts rather than government make decisions regarding what is best for the country. They lean towards a belief that citizens must obey their rulers and that greater respect for authority is a 'good thing' (52%). The responses also

[16] A concern about the WVS responses is that the data for Wave 6 was recorded in 2013. South African responses for the more recent Wave 7 have not been reported. The decade since 2013 has seen much change in the country after the full weight and extent of state capture became apparent to citizens.

suggest a low proclivity for collective action and contestation—for instance, the majority would never participate in acts of protest (58%).

Evidence from Afrobarometer

More recent survey evidence from Afrobarometer is consistent with the findings from the WVS. In South Africa's Round 9 results of the Survey (2022), only 42.5% of respondents consider democracy as preferable to other forms of government. Politics play a minor role in their lives: 82% never discuss politics with friends or family; the majority (64%) do not think that elections allow voters to remove leaders who disregard the people; they harbor significant distrust in political leaders and institutions, and dissatisfaction with the performance of different levels of government. Using Afrobarometer data from Rounds 5 to 9, Figures 5A and 5B show that distrust in and dissatisfaction with leaders and institutions have risen markedly from 2009 onwards, which is the era associated with state capture and its aftermath. The effect of Jacob Zuma's resignation as president in February 2018 is visible in Figure 5A, sparking a temporary dip in distrust in the president. A further interesting result is that, despite the ANC's electoral dominance until 2024, 53% of respondents reported 'no trust at all' in the ruling party in 2022, exceeding distrust in opposition parties (46%).

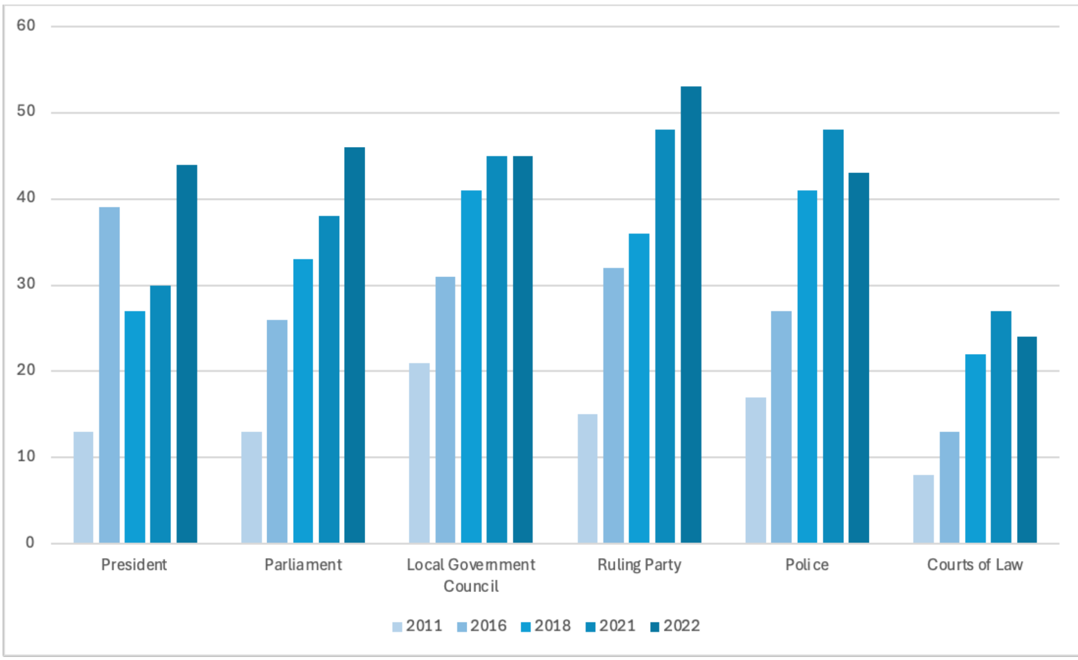

Figure 5A: Percentage of respondents with 'no trust at all' in leadership and institutions
Source: Afrobarometer Rounds 5 (2011) to 9 (2022).

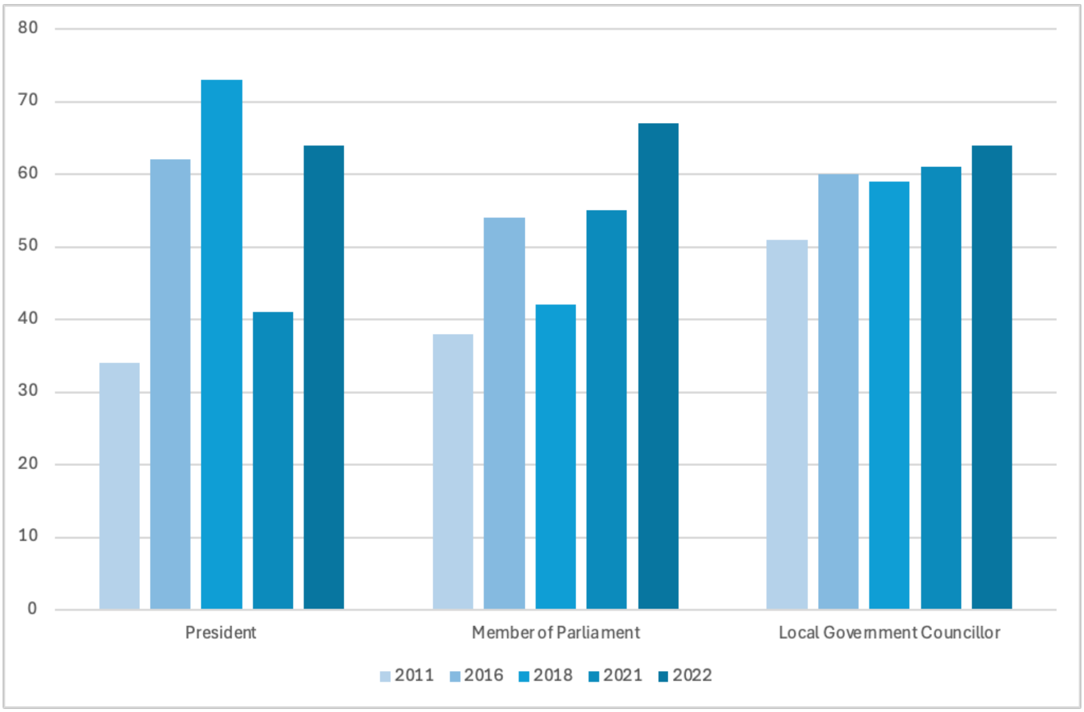

Figure 5B: Percentage of respondents that 'disapprove' and 'strongly disapprove' of performance
Source: Afrobarometer Survey, Rounds 5 (2011) to 9 (2022).

Amidst the high levels of distrust and civic dissatisfaction, the Round 9 results show that the proclivity for civic activism or collective mobilization remains low: responding to a question whether they have or would ever get together with others to raise an issue, 55% replied 'no'; when asked if they have or would ever participate in a march or demonstration, 73% responded 'no'; in response to questions regarding executive accountability, a minority of respondents considered it the responsibility of voters to hold members of parliament (20%) or the president (21%) to account. Instead, voters rely on horizontal accountability mechanisms that they clearly mistrust. Following the 2024 election (see footnote 13), it may be important to understand the underpinnings of the shift in support away from the ruling party to the new Zuma-led *uMkhonto weSizwe* party. While an expression of discontent, it appears not to signal a demand for more accountable governance (given Zuma's prominence in the published state-capture records), but rather a radicalized backsliding towards more populist and personalized politics; away from a programmatically motivated and transactional state-society engagement.

Against the historical background of South Africa's fierce liberation struggle, one country-specific question produced a paradoxical response: 72% of respondents (up from 66% in Round 8, 2021) are 'willing or very willing' to give up elections in exchange for a non-elected government that would deliver law and order, jobs, and houses. This response is in keeping with respondents' dissatisfaction with what they receive from the current democratic government. These responses are overwhelmingly pessimistic about the way the economy and upliftment of the living standards of the poor are being handled. Similar responses were received to questions regarding the government's success in reducing crime, meeting health and educational needs, looking after essential infrastructure like roads, rail and bridges, and in providing electricity and water. To fix this, respondents do not look towards increased political participation or transactional state-society engagement that would improve accountability. They paradoxically lean in the opposite direction, expressing a willingness to relinquish hard-won democratic rights and levers of accountability at their disposal to an authoritarian government if it means that a wide range of also private goods is publicly provided.

The AB Round 9 results offer some insight into respondents' awareness of the misuse of taxpayer money. Most respondents think that corruption got 'a lot' worse over the previous year, while 72% would not dare to report incidents of corruption for fear of retaliation or other negative consequences. Respondents overwhelmingly believe that the president and his office, members of parliament, civil servants, local government councillors, the police, judges and magistrates, the South African Police Service, and the South African Revenue Service are all corrupt and go unpunished. Answers to questions directly related to the fiscal contract suggest a norm of unconditional compliance. Nearly two-thirds of respondents agree that government always has the right to levy taxes. Expectations of reciprocity are also reflected in the responses. Asked whether they would be prepared to pay more tax for better services, the majority say 'yes'. The willingness to pay more taxes rises significantly with the introduction of salience regarding how increased taxes would be spent. One-third of respondents agree that the president does not need to waste time justifying his actions or explaining how taxpayer money is spent.

Although nine crucial years apart, responses to both Wave 6 of the World Values Survey (2013) and Round 9 of the Afrobarometer survey (2022) suggest that the majority of South Africa's citizenry are unlikely to use the vertical mechanisms of participatory politics to pursue the high expectations they have about what government should offer. While they display high levels of distrust in institutions and political leadership, and overwhelmingly disapprove of the performance of leaders and institutions, they minimize the role of voters and show a low proclivity for political engagement and collective action. These responses and beliefs likely counter indicate that citizens will engage the state in the bargaining and negotiations necessary to produce beneficial social outcomes. It seems unlikely that a transactional (fiscal) social contract premised on a society that is capable of and willing to making reciprocal demands from government in exchange for tax payments will emerge in such a context.

4.3 A fragmented social contract?

Given the heterogeneity of South African society, the above interpretation of survey results to make inferences regarding a norms-based social contract cannot be generalized. Another approach would be to make some assumptions about the divergent ways in which the fiscal system impacts the lives of South Africans and to extrapolate what state-society interactions might look like from such disparate vantage points.

Individual taxpayers, for instance, may have transactional views regarding the misuse of their contributions to state revenue on a scale that has derailed the country's future trajectory. While these taxpayers—as contributors to the tax and transfer system—receive hardly any public goods and services, they also face the additional cost of infrastructural and economic collapse. Generally, under such conditions, taxpayers wishing to contest the lack of government accountability have limited avenues. Given the small number of income taxpayers, these individuals may be viewed as a source of revenue rather than votes. Taxpayer dissatisfaction may therefore be seen as electorally irrelevant and politically costless. Dissatisfied taxpayers are, however, opting for an exit strategy (see footnote 14) despite 'exit taxes' that are made increasingly punitive. This is consequential, considering how small the number of income taxpayers is. Withholding tax is a risky strategy, if at all possible, given third-party tax collection. SARS is an effective collector and penalties for detected non-compliance are severe. Withholding may also trigger a moral dilemma, requiring individuals to decide whether the most moral course of action would be to fulfil tax obligations to an immoral state, or to resist complicity in a tax system that is no longer morally justifiable. Lasting memories of South Africa's unjust history, continued poverty, and the 1994 commitment to pro-poor fiscal restructuring are also likely to continue motivating compliance among voters who are less transactionally inclined.

An alternative may be to organize collectively and attempt to engage in tax bargaining with relevant authorities. Realistically, however, tax bargaining may face fierce political resistance in an environment where greater public engagement for the purpose of responsive governance and greater accountability is politically not welcomed. Greater transparency may heighten pressure on a state that is underperforming and politically vulnerable. It is unlikely that tax bargaining could be institutionalized in an environment where it will serve to disrupt entrenched networks of rent seeking and patronage (van den Boogaard et al., 2022). Therefore, under the current conditions, some of which would have boded well for productive tax bargaining in a different context, the emergence of a fiscal social contract in South Africa is unlikely.

A particular feature of the South African fiscal system is the monthly cash grants paid to approximately half the population. It creates a tilted state-society dynamic where extreme vulnerability dominates interactions. From the perspective of grant recipients, fiscal reciprocity may mean their tolerance of, and electoral support for, unaccountable politics in exchange for a continuation of the cash grant system, resulting in clientelistic forms of accountability (Persson and Rothstein, 2019). Vulnerable citizens may also have no choice but to be co-opted in order to maintain a system that perpetuates their vulnerability. Of course, these citizens also contribute to less salient indirect taxation, yet their social-contract expectations are dominated by the welfare they need from the state, which weakens their bargaining position to demand accountability.[17] Conditions characterized by an extreme power imbalance are never favorable for the emergence of transactional state-society-type relations that would likely produce a fiscal social contract. In a vicious cycle, the economic vulnerability largely caused by unaccountable politics ends up serving the perpetuation of a pro-elite fiscal system.

[17] A recent study on *Extreme Inequality and the Structure of Political Cleavages in South Africa, 1994-2019* (Gethin, 2020) uses data from the *South African Social Attitudes Surveys (SASAS)* to report that 'the poorer, Black population have kept their support for the government broadly unchanged' (p. 18) and that 'opposition parties from across the political spectrum have been incapable of mobilizing low-income, low-educated citizens' (p. 23).

5. Conclusion

South Africa post-1994 displayed characteristics that invited favorable predictions of a productive fiscal social contract supporting a positive tax-governance link. On average, South Africa raises revenue close to 28% of its GDP. It is a tax-dominant, in fact a PIT-dominant state, in a constitutional-democratic setting where horizontal and vertical checking mechanisms were deliberately crafted to form part of foolproof, accountable governance. But these conditions did not prevent state capture, grand-scale corruption, and dysfunctional state-institutions with ongoing economic and fiscal effects. The fiscal system has ceased to support a depressed economy or to deliver much-needed public services. A pro-elite distribution of public resources has driven expenditure and public debt upwards while base narrowing has increased the concentration of progressive direct taxation. Despite initial favorable conditions, democratic South Africa has become the puzzling case of a broken tax-governance link. In this paper, we have attempted to understand and explain why a conducive fiscal social contract between state and citizens did not, and is unlikely to, emerge.

Unequal fiscal positions in a fractionalized South African society have set the stage for (at least) two types of social contract: one among heavily taxed individuals that, in a more relenting institutional environment, could have led to a fiscal social contract, and another among grant recipients who have little fiscal leverage but much vulnerability. Non-electoral, vertical demands for accountability via fiscal leverage may have come from a small number of individual taxpayers. However, this avenue towards a fiscal social contract seems to have been closed through a combination of coercive enforcement, taxpayers' lasting commitment to undo the unjust legacy of the country, and an institutional environment that does not tolerate tax bargaining. The small group of taxpaying citizens has no electoral leverage to demand fiscal accountability. The much larger group, which would have electoral muscle to contest pro-elite politics, are captive to a fiscal vulnerability that is leveraged politically to subdue contestation. The specific power dynamics related to the high degree of fractionalization has weakened the bargaining power of different groups where it could have disrupted entrenched politics. This is supported by responses in the 2013 World Values Survey and the 2022 Afrobarometer Survey related to attitudes to political participation, engagement and contestation that suggest a low proclivity for any of these forms of political involvement. From these responses we may conclude that social values do not correspond with transactional state-society relations. This may explain the confluence of events that conspired to permit grand-scale elite capture of a democratic, fiscal state with initially strong checking institutions. Coupled with the controversial nature of instrumentalizing negative tax reciprocity, these features would explain why the positive tax-governance link reported in current literature has not materialized in democratic South Africa.

Where these events will lead is difficult to predict, although the incompatibility of a narrowing tax base and dwindling numbers of taxpayers with growing numbers of state dependants flags the sustainability of the current fiscal system. An electoral solution may effect positive change only if it reverses the current weaknesses in governance and accountability. This may not be likely in a context where state-society dynamics are predominantly non-transactional. Following the general election on 29 May 2024, where the ANC fell below the 50% needed to maintain its 30-year-old outright majority in Parliament, ten political parties with seats in Parliament agreed to join an ANC-led government of national unity (GNU). Some observers refer to the establishment of GNU as "the initial step towards South African state recovery" (see, e.g., *Daily Maverick*, 29 August 2024). However, if the GNU does not hold, unstable coalitions with populist-leaning parties that campaign for de-constitutionalization may follow. This is likely to introduce greater coercion rather than greater accountability, with further economic and fiscal slides, placing a fiscal social contract further out of reach of South Africans. One important area for further research would be to explore fiscal contestation at municipal level, given that local governments spearhead the national government's development policy. Building on the work on subnational taxation in Africa (Franzsen and McCluskey, 2017), understanding the factors that may strengthen the tax-governance link in municipal contexts would be valuable.

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Historical evidence from state-building processes in Western countries suggests that a substantial governance dividend can be gained from mobilizing domestic financial resources through the tax system. Democratic South Africa is an intriguing case of a fiscal state where the positive tax-governance link that forms the basis of a productive fiscal contract, has not materialized despite the presence of several factors that would normally work in favor of a fiscal contract: there is tax dominance in state revenue; a salient income tax that contributes the largest share of revenue; taxpayers are informed about how revenue is spent, and South Africa is a constitutional democracy where individual rights and freedoms are protected and executive constraint and accountability are part of the institutional architecture. This paper investigates the historical, political, and economic factors that have contributed to this outcome. It also investigates the prospects for a fiscal social contract to emerge in the future, considering the current weakness in governance and accountability, coerced tax collection in a low-trust environment, and non-transactional state-society dynamics.

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