How should I tax thee? Let me count the ways

By Errol Meyer

24 Feb 2020

If Finance Minister Tito Mboweni announces significant changes to individual taxes during his Budget Speech on 26 February it could have wide-ranging implications for South Africa's heavily burdened tax base.

Image source: Getty/Gallo

There are numerous actions which the minister could take to bolster the state's coffers, including a possible VAT increase, an increase in personal income tax as well as capital gains tax.

Of course, tax increases, while driven by fiscal policy, have weighty economic implications, which I am sure the minister and his team have considered extensively.

For investors, any increases or changes could have an impact on estate and financial planning moving forward. Here is how any one of these increases could impact you.

Value added tax

In 2018, the tax charged on goods and services was increased from 14% to 15%. It's uncertain whether another increase would be implemented but if it is it would mean an almost immediate increase in the cost of living which will impact any household's financial plan.

The point of departure for any financial plan is to determine the living standard of a person and his or her family. The living standard of a household drives a well-prepared budget for the family.

Since VAT is a consumption tax, it will have a direct impact on the budgeting discipline of a household. One should re-visit your priorities, re-arrange, and start making tough decisions between what is necessary to have, and what is nice to have.

Personal income tax

I am sure the minister will have looked at ways to adjust personal income brackets and even weighed up an increase on personal tax across the board. Currently the continuum of income tax ranges from 18% at the lower end to 45% and R532,041 of taxable income at the upper end. It’s difficult to see how government could justify a wholesale income tax increase but it is not impossible to see a rate hike to 46%, or perhaps a once off levy for persons in the top tax bracket.

The marginal rate was much higher in earlier years.

What is more a given, is that the necessary inflationary adjustments will not be made in the income tax brackets. It may also be far too optimistic to hope for an increase in the medical credits, and to a lesser extent age credits.

To neutralise the effect of personal tax increases one must maximise on tax deductions, for instance contributions to retirement funds. These contributions will drastically reduce the effective rate of tax payable.

Currently the taxpayer enjoys generous tax relief for contributions to a retirement fund, and since retirement is a definite goal in our journey through life, the full amount invested in a tax-free growth portfolio, will be of personal benefit one day. It is unlikely that the maximum tax-deductible amount will be increased, given the favourable tax relief we currently enjoy.

Capital gains tax

This is probably the one area where there is room for significant change. Government is under pressure from certain quarters to increase tax on the wealthy and taxing the gains made on the sale of assets could be where they make up some ground.

It has been four years since we saw a significant increase in the capital gains inclusion rate. Initially the inclusion rate was 25%, and gradually increased to 40%. It is ironic that the original rate in 2001 was to allow for relief in inflationary growth of capital assets. Increasing the current 40% inclusion rate will pay lip service to the original intent and will be a serious factor to consider.

Should the effective rate for capital gains be increased the popularity of tax-free investments, where no capital gains are paid upon maturity, will become much more attractive for the long term.

The role of the financial planner and a suitable long-term investment strategy, aligned with a future lifestyle goal, will become important for the investor.

Wealth tax

The idea of a wealth tax has been bandied since 2018 following the conclusion of the Davis Tax Committee. To date very few recommendations were incorporated, save for the curbing of the use of trust for estate duty saving purposes and an increase in the estate duty rate. However, the collections from estate duty was meagre. It will be interesting to see if some of the other recommendations will be considered, for example the estate duty relief for spousal bequest. Spousal bequests currently escape estate duty.

Whatever the minister announces on Wednesday South Africans will be impacted in some shape or form. There are immense pressures on his Department to cut costs and demonstrate responsible fiscal spending. This, however, must be weighed against the growing need for income to aid government in meeting its infrastructure, health, education and social welfare responsibilities. Investors, in fact all South Africans, would do well to tune in to the Minister's speech to gauge the likely impact on themselves and their finances.

ABOUT THE AUTHOR

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