Personal Taxes - The fragile state of South Africa’s golden goose

The 2020/21 National Budget will continue to have an underlying dual challenge, namely that we not only need to grow our economy, but very importantly, we also need to grow our economy inclusively – so that more South Africans can participate in it and can benefit from it.

This year the minister will again need to walk a tight rope when delivering the National Budget Speech as he seeks to navigate the fiscal, tax and economic landscape in order to bring about the necessary structural economic changes, while at the same time ensuring that South African citizens are not unduly burdened with further tax hikes.

To address South Africa’s many challenges, we of course need a buoyant revenue base and as always, “tax” is one of our main sources of revenue for the government.

Whilst South African taxpayers continue to feel the “tax” pinch on their disposable incomes, the South African Revenue Service (SARS) 2019 Tax Statistics report (which was published during December 2019) highlights the fragility of the South African revenue collection ecosystem – our country is heavily reliant on a relatively small base of taxpayers to generate the majority of the country’s revenue collections.

In South Africa, personal income taxes, value-added tax (VAT) and corporate income taxes collectively account for approximately 80% of the total tax revenues of the country. Of the R1 287.7 billion revenue collected during the 2018/19 fiscal year, personal income taxes continue to be the main contributor to our country’s tax coffers, contributing a total of 38.3% of the total tax revenues. VAT contributed 25.2% and corporate income tax contributed approximately 16.6% to the total tax revenue. Other taxes (e.g. transfer duty, capital gains tax) account for the balance of the revenue collected in the 2018/19 fiscal year.

The South African taxpayer – the fragility of the golden goose

The SARS report shows that the country’s total tax collections for the 2018/19 fiscal year of R1 287.7 billion, was footed by a very small portion of the population. The tax collections was also R14.5 billion behind the revenue collection target of R1 302.2 billion (though there was a 5.9% increase over the prior fiscal year).

The report indicates that of the 3.2 million companies which were registered for corporate income tax at 31 March 2018, just over 814 000 companies were assessed for tax in the 2018/2019 fiscal year, and only 24.3% of these latter companies had positive taxable income (i.e. paid tax). More concerning, of this 24.3%, only 380 companies had taxable income in excess of R200 million and collectively, these 380 companies contributed 57.2% of the corporate income tax collected in 2018/2019. Similarly, of the 4.9 million individuals assessed for tax in the 2018/2019 fiscal year, just over 40% of these had positive taxable income. More concerning, of this, approximately 8% had income in excess of R1 million and collectively, these 400,000 individuals contributed 50% of the total tax revenues collected during the 2018/19 fiscal year.

Article written by Anthea Scholtz, Director: Regional Leader Western Cape Tax & Legal, Deloitte Africa Tax & Legal

Claudia Gravenorst, Senior Manager, Deloitte Africa Tax & Legal
tax, 1.5 million individuals earned taxable income in excess of R350 000 and these individuals contributed 83% of the total personal income tax collected.

It is clear from these statistics, that a very small percentage of the South African population is financing the tax bill and that further, the "man-on-the-street" is paying a significant amount of tax (both direct taxes such as personal income tax as well as indirect taxes, such as VAT).

Whilst these statistics should be viewed within the context of South Africa’s progressive income tax system (where the wealthy contributes a greater proportion towards supporting the state than the poor and hence the more you earn, the higher tax you should pay), these taxpayers seem to be bearing a disproportionate share of the country’s tax burden.

It is thus unlikely, given the current economic environment, that the maximum marginal tax rate would be further increased {it was increased from 41% to 45% for the 2018 tax year}. That said, it is anticipated that the tax brackets at the higher marginal tax rates will have low or no inflationary adjustments and hence limited tax relief, whilst continued tax relief will still be granted for low income earners.

The question is thus: What alternative measures could be considered to generate additional revenue for the fiscal coffers, other than increasing personal tax rates? We explore some of these below.

**Indirect taxes**

As is the case every year, the “sin taxes” (i.e. tax on alcohol and tobacco) is expected to increase as well as possible increases to “environmental taxes” (e.g. plastic bag levy, electricity levy).

Due to the increase in the use of electronic cigarettes and tobacco heating products, there could potentially be a tax levied on these items as well.

We also anticipate an increase in the fuel levy, a consumption tax that is “hidden” in the price of petrol. Per the SARS 2019 Tax Statistics report, this levy has had a 55% increase from the 2014/2015 fiscal year (generating R75.3 million in 2018/2019) and we anticipate that this may increase further in the next fiscal year.

A gambling tax may also be on the cards as National Treasury’s 2019 Budget review document alluded to fact that government intends issuing draft legislation for comment on this matter.

Whilst we do not anticipate an increase in the “wealth taxes” such as estate duty and donations tax, executive remuneration may come under the spotlight.

**Reforming SARS to its former glory**

SARS was once the crown jewel of revenue authorities on the continent. However, due to the tax administration and governance issues at SARS in recent years, revenue collections were below targets and inefficiencies crept in. SARS is now slowly emerging from this dark cloud...

The recommendations from the findings of the Nugent Commission of Inquiry into Tax Administration and Governance are being implemented. Many positive developments are also starting to take place at SARS, most notably it has re-established its Large Business Centre (LBC) unit.

Increasing capacity and skills in certain specialist tax areas, making it easier for taxpayers to liaise with SARS, targeting specific industries and sectors, as well as increasing the digital capabilities of SARS, will go a long way in assisting SARS to generate additional revenue and meet its revenue collection targets.
Cross-border flows and tax evasion

South Africa continues to look at ways to effectively combat the significant financial leakages in the South African economy through the erosion of the tax base, profit-shifting and illicit money outflows. The use of tax havens by taxpayers whereby profits are shifted to no-tax or low tax jurisdictions where the taxpayer has no or very little economic presence, remains a significant concern to the fiscus. It is however also a significant potential pool of revenue, if South Africa manages to get its fair share of these taxes.

The re-building of the transfer pricing unit at SARS will ensure that targeted audits are conducted and that shifting profits through transfer pricing schemes is clamped down.

It appears that steps are underway at SARS to focus on this matter and attempts to stop this leakage will add significantly to the revenue collection efforts.

Conclusion

A revenue budget that supports South Africa’s future, should go further than just tax increases and alternative avenues should be considered to generate additional revenues. Whilst the main component of our revenue base will as always be tax revenues, tax is certainly not the only solution to raise additional revenues. Key parts of the solution must also include expenditure cuts, curbing the size of the civil service, reducing policy uncertainty, restoring investor confidence, creating jobs and focusing on state-owned entities.

No doubt there are tough times ahead and South Africans will have to continue to tighten their fiscal belts, come 1 March 2020.
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