South African Budget Update

May 2017

Below is a summary of the budget announcements applicable to personal wealth and finance.

With the 2018 tax year having started on 1 March 2017, what follows are some key points for South African expatriates to consider.

The Budget

The Budget Speech was delivered by Pravin Gordhan on 22 February where he presented the 'framework for the next three years'.[1] By the end of March, Gordhan had been replaced as finance minister by Malusi Gigaba. The deputy finance minister was also replaced: Mcebisi Jonas taking up this role. Within days of the re-shuffle there was downward pressure on the rand and credit rating agencies like S&P and Fitch have already downgraded South African government bonds to sub investment grade and even as low as 'junk' status.

Comment

With Finance Minister Malusi saying on 1 April, 'We need to change our approach',[2] expatriates should monitor the situation closely. His observation that, 'the ownership of wealth and assets remains concentrated in the hands of a small part of the population'[3] may mean expatriates will have to re-assess their financial arrangements in light of their wealth planning objectives, especially when set against in the context of the markets.

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[1] http://www.gov.za/SPEECHES/MINISTER-PRAVIN-GORDHAN-2017-BUDGET-SPEECH-22-FEB-2017-0000

[2] http://www.treasury.gov.za/comm_media/speeches/2017/2017040101%20Speech%20by%20Minister%20of%20Finance%20Malusi%20Gigaba%20on%20his%20new%20Portfolio.pdf

[3] http://www.treasury.gov.za/comm_media/speeches/2017/2017040101%20Speech%20by%20Minister%20of%20Finance%20Malusi%20Gigaba%20on%20his%20new%20Portfolio.pdf

Taxation of income and gains

A new top rate of income tax has been introduced of 45% from 1 March 2017, where taxable income exceeds 1.5m rand. Previously the highest rate was 41%. The rate of dividends tax also increased from 15% to 20% for dividends from South African or JSE listed companies paid on or after 22 February 2017. Finally, the 2017 Budget contained a proposal to amend the exemption from income tax for foreign employment income so that it would only apply where the income is taxed in the foreign country.

As a consequence of the new 45% top rate of income tax, the highest effective rate of taxation on capital gains increased from 16.4% to 18% for individuals.

Comment

South African expatriates who benefit from the section 10(1)(o)(ii) exemption on their foreign earnings will need to need to be alert to the potential implementation of these provisions. Further, those building investment portfolios may look to explore with their advisers whether offshore life assurance policies would provide a useful vehicle for deferring taxes on investments and reducing overall income tax bills.

Trusts

Although not a consequence of the recent Budget, 1 March saw the introduction of section 7C of the Income Tax Act 58 of 1962. An effect of this is to create a potential liability to donations tax if an interest free, or low interest (below the official rate, which is currently 8%), loan is made to a trust. Where this happens, an amount equal to the difference between the interest incurred by the trust during the tax year and the amount which would have been charged at the official rate of the interest is subject to donations tax, to the extent that amount exceeds the lender's available annual exemption (currently 100,000 rand). Donations tax is charged at 20%.

The income tax rate for trusts (other than special trusts) rises to 45% and the effective rate of taxation on capital gains for trusts (again, other than special trusts) rises to 36%.

Comment

Trusts are facing increased scrutiny is South Africa. In addition, the increases in trust tax rates and the potential for an immediate charge to donations tax where certain loans are made to trusts mean that expatriates considering trust planning should take professional advice before entering into an arrangement, and review their existing trust arrangements.

A New Wealth Tax?

An output of the Davis Tax Committee (DTC), rather than the recent Budget, there has been a call for written submissions on possible wealth taxes for South Africa. The media statement on 25 April[4] stated that, ‘The distribution of wealth in South Africa is highly unequal […]’. Further it explained that, ‘Currently, South Africa has three forms of wealth taxation, namely estate duty, transfer duty and donations tax which together bring in about 1% of tax revenue.’ The statement said that ‘[…] the DTC has taken the view that CGT [Capital Gains Tax] is a form of income tax’ rather than a form of wealth tax. The DTC has invited people to make written submissions by 31 May 2017 on the ‘desirability and feasibility’ of three forms of wealth tax: 1) A land tax, 2) a national tax on the value of property, and 3) an annual wealth tax.

Comment

Clearly this consultation is only at a very early stage, but it demonstrates that the DTC is willing to look at new ways to raise revenue in order to fund government expenditure. The introduction of a wealth tax would not be without its own issues for the tax authorities. For example, would existing departments deal with collection and enforcements, or would additional staff and a possible a new department be required? Both individuals impacted by any new wealth tax and the tax authorities themselves may also have to consider how to agree the value of the assets within scope, possibly on an annual basis.

[4] http://www.taxcom.org.za/docs/20170425%20Call%20for%20submissions%20on%20wealth%20taxes.pdf