#Budget2018: The good news is that the bad news is unlikely to get worse- 21 FEB 2018

Despite growth picking up and a prediction that the medium-term budget policy statement (MTBPS) forecast will be revised downwards by nearly R70bn, the country still faces some serious fiscal issues. Free higher education and National Health Insurance (NHI) will require further tax increases or a redirection of some programmes. So, potentially, some very heavy tax increases could be on the cards for the year ahead.

“There is a sense that things are slowly starting to change. It is unlikely that things will be worse and the R50 billion shortfall might improve,” says Kyle Mandy, tax policy leader for PwC South Africa.

The MTBPS forecast could be revised downwards by nearly R70bn, primarily off the lower 2017/18 base and gross domestic product (GDP) forecast. The good news is that the shortfall is R50/51bn, and not R69.3bn. This is partially set off by lower South African Customs Union (SACU) payments by R17.7bn an expected tax increases of R30bn.

Tax revenue

The expectation is that tax revenue estimates will be increased by a further R15bn for 2018/19.

VAT

The VAT rate could be increased, and even if it’s by as little as one percent, an increase could raise as much as R22bn in additional revenue.Value-added tax is an attractive source of revenue as it can raise a significant amount with a relatively small increase in rates. The VAT rate is relatively low by international standards and there is a growing trend towards indirect taxes as a source of tax revenue globally. “To sell an increase in the VAT rate, the government might need to increase taxes on the wealthy, while giving some relief to the lower income groups and increase on social spending. Social grants would have to increase,” Mandy says.

It is expected, if the VAT rate increases, that the general fuel levy will also increase.

Personal income tax

The personal income tax (PIT) burden is back at levels last seen in the 1999/2000 at 10% of GDP. In addition, a greater portion of the tax burden has been shifted to the higher income earners.

In 2002/03, 78.3% of PIT was paid by 31.8% of taxpayers. In 2015/16, 79% was paid by just 25.7%. The result has been a significant strain placed on the tax base, which is has meant that South Africa has a tax burden that is higher than the average for Organisation for Economic Co-operation and Development countries and far above the average of developing countries.

In light of this, and the fact that Treasury is aware of the strain on the tax base and the significant increase in PIT in recent years, PwC does not expect a relatively large portion of additional tax revenues to be raised from PIT. It also does not foresee changes in the tax rates for 2018/19.

Medical aid tax credits

Speculation is that medical aid tax credits will be removed to provide the initial funding for the NHI fund. However, PwC does not expect the subsidy to be reduced at this stage, but it is possible that no further increases in the tax credits for medical aid scheme contributions will be granted. Such a policy will result in additional tax revenues of approximately R1bn in 2018/19.

Capital gains tax

Capital gains tax (CGT) is perceived to be a tax on the wealthy and the inclusion rate could be increased to 50% and the maximum effective rate to 22.5%. Such an increase would raise in the region of R2bn.

Corporate tax

No change is expected in the general corporate tax rate of 28%. Any increases would negatively impact on the competitiveness of the country's tax rates (the global trend for corporate taxis downwards).

Corporate capital gains tax (CGT) was increased in 2016 from 18.6% to 22.4% and therefore it is unlikely that this rate can be increased any further. An increase in dividends tax is also not expected as its tax rate was increased from 15% to 20% in the 2017 budget.

Corporate tax incentives are being reviewed for their effectiveness with a view to removal where the costs outweigh the benefits. It is possible that the removal of certain tax incentives could be made to broaden the tax base and raise additional revenues.