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Dear Davis Committee members

RE: SUBMISSION ON THE DTC FIRST INTERIM REPORT ON ESTATE DUTY

We appreciate the Committee's openness in affording us with the opportunity to engage in terms of this report. We begin with a brief listing of the proposals followed by comments. We seek to provide input that is hopefully constructive but concede that the issue of wealth taxes has become very political.

Sincerely

Keith E Engel

Deputy CEO

I would also like to thank the following members for their substantial contributions in compiling this report:

- Professor Jackie Arendse - Rhodes University Department of Accounting
- Mr Gert van den Berg – Delpont van den Berg
- Mr Tenk Loubser – TLA Wealth and Advisory Services

SAIT COMMENTARY

1. Brief summary of Davis Tax Committee suggestions

As part of its analysis, the report of the Davis Tax Committee (DTC) makes a series of recommendations. These recommendations are as follows:

- The Estate Duty should be retained (with some modifications) rather than introducing a Capital Transfer Tax (CTT) or Net wealth Tax (NWT).
- General anti-avoidance rules (GAAR) should not be introduced into the Estate duty Act, but the enforcement of existing legislation should be improved.
- The deeming provisions of sections 7 and 25B of the Income Tax Act should be repealed in the case of resident trusts.
- The deeming provisions of sections 7 and 25B should remain in respect of non-resident trusts.
- The flat tax rate for trusts (apart from special trusts) should be retained.
- Trusts should remain as separate taxpayers.
- The definition of “special trust” should be reviewed.
- Transfer pricing adjustments for financial assistance or interest-free loans advanced to domestic trusts should not be added
- A further offshore amnesty should not be considered given that the voluntary disclosure programme already exists to serve this purpose.
- Distributions from foreign trusts to residents should be taxed as income.
- The criminal offence provisions of the Tax Administration Act should reviewed to further penalise those who fail to make full disclosure of their direct or indirect interests in offshore trusts.
- The Estate Duty deduction for spousal bequests should be limited or withdrawn.

- The Donations Tax exemptions for inter-spouse donations in terms of sections 56(1)(a) and (b) of the Income Tax Act should be retained, but the section 56(1)(b) exemption should no longer apply to any donations of interests in any fixed property or company.
- The Donations Tax exemption for donations in contemplation of death (“*donatio mortis causa*”) as provided for in terms of sections 56(1)(c) of the Income Tax Act should be removed.
- The Donations Tax exemption for donations of property acquired prior to becoming a resident or acquired by donation or inheritance from a non-resident as provided for in terms of section 56(1)(g) of the Income Tax Act should be reviewed.
- The Donations Tax exemption for *bona fide* contributions towards the maintenance of any person as provided for in terms of section 56(2)(c) of the Income Tax Act should be limited.
- The double tax on death that arises as a result of the deemed disposal for CGT purposes in terms of paragraph 40 of the Eighth Schedule to the Income Tax Act and the inclusion of the same assets in the dutiable estate for Estate duty purposes should be fully retained.
- The exclusion of retirement benefits from the dutiable estate in terms of section 3(2)(i) of the Estate Duty Act should be retained but limited to contributions that have been allowed as deductions under sections 11(k) or (n) of the Income Tax Act.
- The Estate Duty abatement should be updated for inflation.
- The manner in which spousal abatements are taken onto account must be changed.
- No distinction should be made between asset classes, apart from the primary residence, in the determination of Estate Duty.
- The Estate Duty rate of 20% should be retained.

2. General underpinnings

A. *Wealth Tax as a tool to address inequality*

It cannot be disputed that South Africa has one of the highest levels of inequality both in terms of income and wealth. While the various ratios and statistics that are quoted in the report could be contextualised more clearly, we holistically agree that the level of inequality that exists must be more fully addressed in order for the country to be more sustainable in the long-term. We also agree that tax policy should be (and has been)

used as an effective redistribution tool to address inequality, mainly through progressive tax rates income as well as spending on social grants, education and housing.¹

However, the mere existence of inequality does not automatically lead to the conclusion that wealth taxes (i.e. the Estate Duty in particular) is a viable answer to further alleviate the problem. There is very little literature that supports wealth taxes as being an effective tool to address inequality, mainly because of the notoriously low tax yields.² Adjustments to other taxes may be more effective at a lower compliance/enforcement cost. For example, a simple increase in the top marginal rate for the super-rich may achieve quicker results at a lesser administrative cost. Therefore, the issue of Estate Duty needs to be compared vis-à-vis other options.

A second question is how far can the tax system be used to address inequality? In other words, at what point – whatever the tax instrument – does the equalizing effect come at too high a price in terms of economic efficiency and growth? There comes a point when all taxes lumped together have this adverse effect no matter how the tax instruments are divided (even though partially concealed from daily public view).

At the end of the day, it appears that the mere label of the Estate Duty as a wealth tax is driving the analysis (as it seemingly did for the Katz Commission). The concept of repealing the label of a wealth tax in this environment is seemingly the real challenge – if so, all other alternative analyses and options become a waste of time despite their merit.

B. Wealth taxes and offshore wealth

We are concerned that the tone of the report is being perceived as sending another negative message regarding wealth and high net worth individuals (HNWIs). The aggregate effect of these negative messages creates uncertainty for local investors and acts as a deterrent to investment by HNWIs.

Turning to more direct matters at hand, we question the linkage between wealth taxes and offshore wealth. Before addressing this point, we fully recognised that a significant amount of assets have been transferred offshore by individual South African residents over the last few decades. However, the income from these assets earned by South Africans legally does not escape the tax net as the Income Tax Act includes almost all forms of foreign income. Furthermore, details of a resident's foreign income must be declared to SARS. With tougher global rules regarding tax compliance requirements (especially in terms of banking regulations), coupled with the opportunities provided through the various tax amnesties, tax collections on foreign assets

¹ Van der Berg, S. & Moses, E. (2012). *How better targeting of social spending affects social delivery in South Africa*, Development Southern Africa, 29:1, 127-139, DOI: 10.1080/0376835X.2012.645647.

² For example, Schnellenbach, J. (2012). *The economics of taxing net wealth: a survey of the issues*, Public Finance and management, 12(4), pp. 368-400.

should be increasing. Indeed, the 2014 SARS Statistics indicate that foreign income has increased over the last four years as shown in the table below.

Taxable income from foreign investment income

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Type of taxable income	R million	R million	R million	R million
Foreign interest and dividends	445	389	470	578
Foreign capital gains	145	152	214	381

Note: Foreign dividends and foreign interest are no longer eligible for the *de minimis* exemption from the beginning of the 2013 tax year.

If it is assumed that this taxable income is taxed at an average rate of 35 per cent, the estimated tax collections would be as follows:

Estimated tax collected on foreign investment taxable income

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Type of taxable income	R million	R million	R million	R million
Foreign interest and dividends	156	136	164	202
Foreign capital gains	51	53	75	133

It is evident that tax collections on foreign investment income of individuals has increased over the last four years and there is scope for growing these tax collections through more effective enforcement of existing legislation. The increasing sharing of cross-border information will also expose additional foreign income streams that will translate into additional tax revenue. If any legal loopholes remain, they most probably relate to the taxation of offshore trusts and similar vehicles (e.g. foundations).

Turning back to the Estate Duty, we fail to see how this tax instrument will effectively curtail avoidance or evasion in respect of foreign assets. While these offshore assets are admittedly includible within the Estate Duty, the same tools for avoiding income tax can just as easily be used for Estate Duty (and perhaps more so for Estate Duty given the non-recurring nature of the charge). Indeed, the existence of an Estate Duty often becomes a strong reason for emigration of HNWI's given the large lump-sum nature of the charge.

3. Estate Duty versus other forms of wealth tax

The decline in Estate Duty collections referred to in the Committee report is depicted on the graph (Figure 3) as having occurred in the period between 1984 and 1990. This decline would be largely attributable to the transfers of wealth offshore that occurred during that period. Following 1990, there is a clear increase in Estate Duty collections in both nominal and real terms. The SARS statistics indicate that Estate Duty collections have

increased from R125 million in 1994/5 to R1.1 billion in 2013/4. Thus, the statement on page 29 that ‘estate duty collections have declined ... in real terms should be contextualised. While Estate Duty collections remain only a small part of the overall revenue mix, these small collections are consistent with international norms (as stated above).

That said, other forms of wealth tax fare no better. For example, Chatalova and Evans³ state that it is unlikely that wealth taxes (including taxes ‘on the holding, transfer or appreciation of wealth’) ‘will ever be more than a minor part’ of the overall tax mix. Therefore, it is unlikely that South African Estate Duty collections will ever increase significantly above the current yield in proportional terms nor will a replacement wealth tax.

Given the fact that wealth taxes fail to generate much revenue as a general matter, we therefore agree that the Estate Duty should not be replaced with another form of wealth tax if wealth taxes are perceived to be a necessary part of the overall revenue mix.

4. Questionable need for a substantial revamp

We are concerned with the unsupported proposals to substantially modify the Estate Duty, which has a long history and many decades of judicial precedence. Unsupported changes to this legislation would create uncertainty with no guarantee of additional tax revenue collections and could have a negative effect in terms of discouraging savings and building wealth. We strongly recommend that any planned modifications be thoroughly researched based on proven South African conditions as opposed to simply adopting unfamiliar foreign concepts.

5. Unwarranted emphasis on inter-spousal transfers

A. Misguided assumptions

In terms of the Interim Report, the following statement on page 29 refers:

‘The South African estate duty system contains generous allowances that permit most estates to be subject to both CGT and estate duty only on the death of all spouses. This defers estate duty collection for many years.’

The statement seems to indicate that there exists a tendency to have ongoing bequests to successive surviving spouses, thus postponing the capital gains tax and Estate Duty liabilities on an ongoing basis. Although spousal relief is indeed permitted, this relief does not necessarily mean that all assets will be bequeathed to successive spouses on an ongoing basis. Indeed, spousal transfers are typically followed by taxable transfers to children (with transfers among successive spouses being extremely rare). While some schemes exist to maximise the dual nature of individual spousal exclusions, schemes to reduce Estate Duty typically require a severe loss of direct control over underlying assets.

³ Chatalova, N. and Evans, C. (2013). Too rich to rein in? The under-utilised wealth tax base. *eJournal of Tax Research*, 11(3), pp. 434 – 452.

The statement on page 30 that ‘South Africa is underperforming in terms of revenue collections on the estate duty and donations tax’ vis-à-vis other countries is not well supported. Furthermore, all of the examples referred to involve developed countries (mainly European), which are not an appropriate basis for comparison for a developing country like South Africa. We also note that the acceptance of tax-free spousal transfers within South Africa is within the global norm and would accordingly not be the reason for any perceived differential. Whilst we agree that there are most probably certain shortcomings in the existing Estate Duty system, we suggest that further local practical knowledge is required.

B. Questionable proposals

The report recommends that the Estate Duty deduction for spousal bequests should either be limited or withdrawn. However, this proposal is contrary to basic international principles – not only in terms of Estate Duty but also Income Tax (including capital gains). In our view, the deduction for spousal bequests exists because married couples typically operate as a single economic unit. Assets are accumulated through mutual effort and sacrifice. Moreover, the fact that an asset may be registered in the name of one spouse does not necessarily mean that only that spouse was the one who contributed to the asset’s acquisition and value. The relief for inter-spousal bequests has existed in the Estate Duty Act since 1955 and has overwhelming international precedent on the basis of this economic unit principle.

One of the motivations for scrapping the spousal bequest deduction is given on page 48 as:

“Today bequests are increasingly being used for the maintenance of the parents and extended family of the deceased and not only the spouses and children of married taxpayers.”

It is a common principle of estate duty or succession taxes that the tax is applied only when assets are transferred from one generation to the next. The inter-spouse bequest is a completely different consideration and should not be blended into the question of needing to support parents and/or children and/or other persons.

The motivation on page 49 that “the definition of ‘spouse’ is open to widespread manipulation, interpretation and abuse” is a matter that should be dealt with through the normal application of the law. We view this issue as a fringe consideration in relation to most South African family settings (most South Africans do not have multiple wives despite the prominent few to the contrary).

The taxation of joint income has been removed from the Income Tax Act. However, there remain many other married relief provisions, such as: (i) the CGT roll-over provisions in paragraph 67 of the Eighth Schedule of the Income Tax Act, (ii) the donations tax exemption in section 56(1)(a) and (b) of the Income Tax Act, (iii) the spousal bequest deduction in section 4(q) of the Estate Duty Act, and (iv) section 9(1)(i) of the Transfer Duty Act. These provisions correctly recognise that spouses form an economic unit and transfers between spouses should be permitted without tax effect unless the transfer is driven by a tax avoidance motive.

A review of European Union tax systems indicates that “11 out of 18 countries fully exempt the surviving spouse” (page 49) and the table on page 50 confirms that of the 18 countries listed, all of the developing countries (Bulgaria, Croatia, Lithuania, Poland and Slovenia) provide a full exemption for transfers to a spouse. Taxing inter-spousal transfers would most certainly be viewed as an anomalous international outlier.

6. Domestic trusts

A. General repeal of the flow-through principal

We generally support the overall restraint shown in respect of domestic trusts as a legitimate tool for family planning and wealth protection. However, we question the excessive emphasis on tax rate arbitrage, which seemingly leads the Committee to the conclusion that the flow-through principal must be abandoned completely.

Section 25B was introduced into the Income Tax Act in 1991 to codify long-standing judicial precedent and practise. As stated in the Explanatory Memorandum to the Taxation Laws Amendment Bill, 2004 –

‘Section 25B of the Income Tax Act, 1962, regulates the taxation of income received by or accrued to a trust and provides for the flow through principle in the case where the income is received by or accrued to or in favour of a vested beneficiary.’

The flow through principle, or conduit principle, was first confirmed in *Armstrong v CIR* (1938 (AD)). In the Armstrong case, the court held that income received by a beneficiary from a trust retains its nature. The trust is viewed as a conduit pipe through which the income flows. In *CIR v Polonsky* (1942 (TPD)), the court found that the trustees were no more than a “conduit pipe”. In *SIR v Rosen* (1971 (A)) the conduit pipe principal was extended to trust income vesting in a beneficiary in the form of an annuity. The conduit pipe principle was again confirmed in *Estate Dempers v SIR* (1977 (A)), where the court held that income accumulated by the trustee retained its identity despite a specific provision in the trust deed that the income would in such a case form part of the trust capital.

The conduit principle has therefore been a well-established principle of tax law for almost a century and is well-accepted amongst countries with a common law background (such as South Africa). There are a myriad reasons for forming trusts. Whilst we recognise that some founders have been motivated by their quest to save estate duty, much of the same savings could be achieved by simply transferring the assets to the beneficiaries. In a family setting, trusts allow for gifts to be controlled so that beneficiaries do not squander or otherwise misuse funds initially provided for good purpose. Gifts can be made that are controlled with a truly altruistic purpose for family members, It should also be noted that trusts are used to pool funds for investment vehicles, such as rank-and-file/BEE share schemes, private equity funds, infrastructure funds and debt-pooled financing.

The point is that genuine vesting of assets and income does exist, thereby validating the flow-through principle. Children can be given assets for their sole benefit but controlled for specified use (e.g. education, maintenance of the family business). The income arising from these controlled gifts truly belongs to the beneficiary despite the strings attached.

B. More selective approach

We would alternatively suggest a more selective approach toward reducing the potential misuse of the flow-through problem:

Section 7: We agree that section 7 is an anti-avoidance provision designed at a time when trust rates were potentially lower than individual tax rates. Given the change of rate comparisons, section 7 should not become a means for taxpayers to use income-shifting to their benefit. The proposal to exclude domestic trusts from section is accordingly supported.

Section 25B: The Committee proposal should recognise that there is a significant difference between *bewind* trusts / vested trusts and a discretionary trust. The real issue in terms of section 25B involves discretionary trusts – not the others. We agree that trusts should not be used as a means of shifting income (or income types) amongst beneficiaries for tax reasons. Hence, if the income generated by an asset can be freely shifted amongst beneficiaries at the discretion of the trustees, one could reasonably argue that the income is income of the trust subsequently to be allocated to beneficiaries tax-free. Discretionary trust profits could arguably be viewed as loosely akin to corporate income (with the income taxable at the entity level) because the managers of the entity determine how the ultimate owners will share the benefits. Under this approach, a discretionary trust should perhaps be taxed exactly on the same basis as a company (28 per cent plus a deemed dividend of 15 per cent).

Of course, the tricky part of this proposal is to separate discretionary versus vesting income. To protect the interests of Government, the definition of vested income should be narrowly defined with the excess being viewed as discretionary. In order for this proposal to work, basic family non-tax planning alternatives need to be understood with the excess treated as tainted.

C. Estate Duty/Income Tax Mismatches

Another common planning tool properly identified involve schemes that exploit the mismatch between Estate Duty and Income Tax. In these schemes, the underlying property falls outside the estate of the taxpayer while the underlying income remains part of the taxpayer's taxable income. In this instance, the Estate Duty should probably contain an anti-avoidance rule to extend the underlying assets so as to be deemed included within the Estate.

7. Foreign trusts

A. Continued application of sections 7 and 25B

We fully concur that sections 7 and 25B should be retained in respect of foreign trusts. However, we are uncertain whether taxing of foreign trust distributions will really have the effect desired. South Africa

specifically exempts foreign dividends under the section 10B participation exemption in order not to discourage the repatriation of earnings. Tainted foreign income should be taxed as that income arises – not upon its return. Presumably, offshore trusts should be treated the same.

We question the proposal not to rethink a new amnesty for foreign assets held in foreign trusts (or otherwise). Many HNWI's now realise that they missed a key opportunity for coming clean. In the new world order of banking and financial institutions, illegal foreign assets are becoming harder to invest without demonstration of legality. The South African amnesty process has also proven to be reliable. A numerical analysis should at least be performed as to the ongoing existence of offshore assets. An amnesty could be a viable revenue raiser during this period of subdued economic activity.

While the voluntary disclosure programme does admittedly exist, the programme has limited benefit as it only applies to defaults that have arisen since the implementation of the Tax Administration Act No. 28 of 2011 (the implementation date being 1 October 2012). The disclosure programme also fails to provide clemency in respect of interest charges. These interest charges could be substantial in the case of assets shifted offshore many years ago with the interest owing effectively wiping out the existing offshore corpus. Better relief in terms of these interest charges could be a viable possibility.

B. Foreign assets given prior amnesty

As a side note, the Committee's proposals do not indicate what is envisaged for foreign trusts that have been the subject of the amnesty that was granted under the Exchange Control Amnesty and Amendment of Taxation Laws Act, No 12 of 2003. South Africans who applied received amnesty had to make an election under section 4 of the 2003 Act that any income derived by a foreign trust to which the resident had donated funds would remain attributable to that resident so long as they are alive. Thus, as and when foreign investment income accrues to the foreign trust, that income must be disclosed and taxed in the hands of the amnesty recipient. Similarly, any capital gains realised by the foreign trust on the disposal of assets will be taxed in the same year of assessment in the hands of the amnesty recipient. When the person who funded the foreign trust passes away, s/he will be deemed to have disposed of the assets held by the foreign trust at market value on the date of death, giving rise to capital gains tax that will be taxed in the hands of that deceased person. Subsequent distributions by the foreign trust after the death of the funder, to South African resident beneficiaries are not liable to tax in the hands of the beneficiaries as they would already have been taxed. Income derived by the foreign trust after the death of the funder will, on distribution to a South African resident, be taxed in their hands, in terms of section 25B(2A) of the Income Tax Act, No 58 of 1962.

We suggest that the treatment of foreign trusts that are the subject of the Exchange Control Amnesty has already been adequately dealt with in the legislation and further changes are unnecessary. Hence, we assume the Committee's silence on this matter means that the Committee implicitly concurs with this view.

8. Donations Tax

A. *Inter-spouse donations*

The inter-spouse exemption should be fully retained because a married couple is in essence a single economic unit. Nonetheless, the statements indicating that transfers between spouses constitute “abuses” and that the various exemptions in section 56 “are widely used in the course of reducing the taxpayers’ exposure to estate duty” are misplaced. Inter-spouse transfers are made for many different reasons, often completely unrelated to tax charges. For example, a motor car purchased by one spouse may be given to the other, gifts are frequently exchanged and cash is often transferred in the ordinary course of life. We note that the capital gains tax provides rollover relief between spouses for similar reasons.

It remains a reality that the income and property ownership of men is generally much higher than that of women and many women still sacrifice the earning of income to focus their attention on raising families and/or looking after their husbands. Within a marriage, there must be a facility to transfer assets between spouses without tax consequences. That said, section 7(2) should be retained to ensure where such transfers are entered into as a diversionary tactic for tax avoidance reasons so that the related income will continue to be taxed in the hands of the donor spouse.

Again, we do not see excess abuse arising from the inter-spousal space and strongly believe that this focus is misplaced. There are great risks for spousal transfers during life due to the risk of divorce that keep any perceived abuse in check. As couples get older, inter-spousal relief is more of a timing benefit given that most spouses die within a 10-year period of one another. The schemes of concern relate far more to the passage of assets to children free from wealth tax. However, should one be committed to targeting this space (which we again view as unprincipled), a unified Estate Duty and Gift Tax limit could arguably be viable if the limit is set at sufficiently high levels? For example, the relief could be limited to net assets exceeding R20/R50[?] million because the super-rich can presumably afford to pay the tax for inter-spousal flows without cash-flow concerns.

B. *Donations in contemplation of death (“donatio mortis causa”)*

We do not agree with the recommendation to remove the donations tax exemption provided for in terms of section 56(1)(c) of the Income Tax Act as the exemption is balanced by the inclusion of such donations in the property of the deceased. In other words, while these donations may be free from donations tax, these donations are fully subject to Estate Duty (see section 3(3)(b) of the Estate Duty).

C. *Casual gifts by natural persons (R100 000)*

The annual R100 000 exemptions for natural persons is a pragmatic way of dealing with the myriad of transactions involving small gifts and should be retained as they do not present a significant risk to the *fiscus*.

We further note that exemption has not been increased to keep pace with inflation (the R100 000 exemption for natural persons was last increased in 2007). Parents tend to provide small cash amounts to children (age 20+) during times of need and children may do the same for elderly parents. These sums may not be maintenance but too assist for one-time events.

What the Committee appears to be objecting to, is the use of the R100 000 annual amount is its use as a family estate planning tool by advisors. The R100 000 amount in this circumstance effectively becomes an additional exemption on top of the R3.5 million exemption. The most common use of this technique is when inter-family / trust loans undergo annual R100 000 waivers. One could argue that the R100 000 annual exemption should have been taken into account when the R3.5 million exemption was set by Government, meaning that dual use is acceptable. If not, a portion or all R100 000 donations should work against the R3.5 million amount in abusive cases (i.e. a form of unified exemption system). For instance, one could treat 50 per cent of all exempt donations as working against the R3.5 million limit if performed within 5 years before death and if the aggregate donations for that period exceed R100 000). The goal is to eliminate excessive donations before death clearly designed to duplicate the donation and Estate Duty exemptions.

D. Casual gifts by entities (R10 000)

The rules relating to casual gifts by entities are a more complex issue because it is arguable whether a business entity can ever have a pure donative intent. Businesses never have a fully altruistic purpose for donations (with these donations having a business publicity purpose). Therefore, one should argue that these transfers should be viewed as deductible and completely outside the donations system *per se*.

At issue may be trusts and companies that are passive saving vehicles for family members. In this narrow case, one could argue that any donation made is really a transfer by the entity on behalf of the owner. In these circumstances, the donation is more akin to a transfer to the ultimate owner, flowed by a donation. Under this formulation, the natural person should be able to apply the R100 000 exemption (with a deemed income tax result (e.g. dividend) for the initial deemed transfer to the ultimate owner). This more accurate view (albeit more complex) would require adjustments to section 57 as well as integration with the Income Tax Act.

E. Maintenance

We understand the theoretical concerns that the Davis Tax Committee has with the undefined nature of the “reasonable maintenance” exemption. Indeed, the main intent is to cover typical family support to children, spouses and other close family members (most typically relatives as defined). These would rightly include food, shelter, clothes, schooling, and sundry living expenses (and even a car for teenager/young adults). We would not object to a definition in this regard as long as the definition fully takes actual life examples into account.

However, in narrowing this definition, it should be remembered that it is a reality in South Africa that many people provide financial support for others outside their family circle or beyond the legal requirement for maintenance. Many persons provide support to friends and distant relatives and have not reverted to a narrower “nuclear” family view. This customary tradition should not be targeted. Indeed, donations to persons outside the family circle should be encouraged because the donations tax / estate duty is designed solely to prevent family accumulations of wealth (indeed, one could easily argue as a theoretical matter that the charge should solely be limited to family and controlled entities).

9. Estate Duty and Capital Gains Tax on death

The report supports the dual application of Estate Duty and Capital Gains Tax on death. It is unfortunate that Professor Roeleveld’s paper examining the question of capital gains tax and estate duty both being levied on a person’s death was dismissed in the report out of hand. While the two taxes are technically different, a definite adverse perception issue exists and we reiterate that South Africa is truly falling outside international norms.

We agree with the conclusion in the Professor’s paper that the situation now results in an element of double tax and is matter worthy of full examination in order to provide a balanced view on the impact of taxes arising upon death.

It should also be recognised that the Katz Commission, which preceded the implementation of the capital gains tax, recommended the introduction of a capital transfer tax (a wealth tax) without any capital gains tax charge. Thus, the Katz Commission envisaged that, upon a person’s death, there should be only one type of tax being a wealth tax – not the dual situation that now exists. We expect that the Katz Commission would have fully rejected a dual charge had the issue been raised during their proceedings.

It should be recognised that the dual-tax system generates significant additional tax revenue. It would be useful to consider data from SARS on the tax revenue that has been collected in the form of CGT on deceased estates. The SARS statistics, 2014 provides the following table of CGT collected since 2008. There is no breakdown to indicate how much CGT has been collected from individuals as a result of the deemed disposal on death. The author has added the last 2 columns to the table to provide a comparison of CGT collected as a percentage of total tax collected.

Capital Gains Tax (CGT) raised, 2009/10
2013/14

	CGT raised (R million)			Total income tax assessed	CGT as a % of total income tax assessed
	Individuals	Companies	Total	Individuals	Individuals
Prior to 2008/09	3 017	5 735	8 752		
2008/09	3 807	4 136	7 943	172 641	2,21%
2009/10	4 357	6 023	10 380	178 066	2,45%
2010/11	2 012	7 049	9 061	197 354	1,02%
2011/12	1 550	5 263	6 813	215 915	0,72%
2012/13	2 166	5 008	7 174	226 263	0,96%
2013/14	6 970	4 633	11 603	263 000*	2,65%
Cumulative	23 879	37 847	61 726		

Source: SARS Statistics, 2014 (adapted to include 2009 statistics)

* Estimate based on National Treasury data published with 2015 Budget

It is clear from this table that CGT collections vary considerably from year to year both in real terms and in relation to total income tax collections. It is impossible to estimate what proportion of CGT collections are derived from deceased taxpayers, but this information would be important in the process of evaluating any proposed changes to the existing tax treatment on the death of a taxpayer.

Nonetheless, we fear that the Committee had made its decision in regard to this matter before the proceedings began and is unlikely to change its views regardless of the numbers presented.