Presentation to the Parliamentary Standing and Select Committees on Finance at Public Hearings

2018 Fiscal Framework and Revenue Proposals (2018 Budget)

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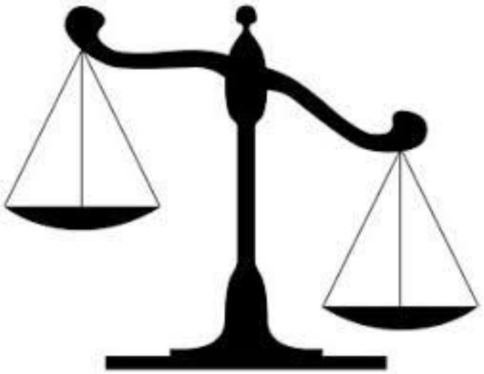
Discussion points



- Compromises in challenging times
- Which taxes have to give and by how much?
- Will these taxes be collected?
  - What will happen in 2018/2019?
  - What happened in 2017/2018?
- Balancing SARS tax collections and taxpayer rights
- Taxpayer Bill of Rights
- Strengthening tax morality
- Balance between tax instruments - VAT increase unavoidable
- VAT rate increase from 14% to 15% - least detrimental effect
- VAT increase – impact on poor and rich
- VAT increase – mitigating the effect on the poor
- Targeted tax incentives for growth and jobs
- Technical proposals and administrative adjustments

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Compromises in challenging times

- Reasonable balance struck between:
  - Tax increases
  - Public expenditure cuts
  - Budget deficit / Government borrowing
  - Funding fee-free higher education and training for poor and working-class students

- Nonetheless, taxes are too high and not sustainable – very high as a % of GDP and compared to other countries; the current trajectory effectively squeezes out the private sector

- Steps should be taken to shrink the government in line with the President's State of the Nation Address in order to get public spending and government borrowing under control

- Corruption and fruitless and wasteful expenditure must be curtailed

- We need growth

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Which taxes have to give and by how much?

Additional tax needed in 2018/2019	R36 bn
VAT rate increase	R22,9 bn
Partial relief to individuals for inflation	R6,8 bn
Excise duty increases	R4,3 bn

Gross tax revenue budget	R1,345 tn	100%
Personal income tax	R505,8 bn	37.6%
Value-added tax	R348,1 bn	25,9%
Corporate income tax	R231,2 bn	17,2%
Customs & excise duties	R97,4 bn	7,2%
Fuel levies	R77,5 bn	5,8%
Other	R84,8 bn	6,3%

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Will these taxes be collected? What will happen in 2018/2019?

Gross tax revenue	Amount	Buoyancy
2017/2018 revised	R1,217 tn	0,96%
2017/2018 shortfall	R48 bn	
2017/2018 budget	R1,265 tn	1,41%
2018/2019 budget increase	R80 bn	
2018/2019 budget	R1,345 tn	1,51%
2018/2019 budget > 2017/2018 revised (10,5% increase)	R128 bn	

- Is a tax buoyancy of 1.51 realistic given the recent years' record?
- Will the gross tax revenue budget be achieved in 2018/2019?
- Or will we have another tax shortfall?

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Will these taxes be collected? What happened in 2017/2018?

- Budgeted gross tax revenue – R1,265 tn
- Expected shortfall in gross tax revenue – R48 bn
- Revised revenue target – R1,217 tn
- SARS collected R1 tn by 22 February 2018:
  - R1 trillion: 1 March 2017 - 21 February 2018 = R3,1 bn/day
  - R217 bn: 22 February - 31 March 2018 = R5,7 bn/day
- SARS Media Statement of 26 February 2018:

"We are focused on closing all revenue leakages through non-compliance and our staff will spare no effort in reaching the revenue target by 29 March, even though the economy is not performing to our expectations," Mr Moyane said.

"We believe that our efforts will provide government with the requisite fiscal space to free up resources for its developmental objectives while allowing it to better manage the levels of debt we are facing," said the Commissioner.

Balancing SARS tax collections and taxpayer rights

- Increasing pressure on SARS to collect tax
- Many competent SARS officials are very successful
- But some SARS officials substitute aggression for skills
- Many taxpayers feel that they do not have rights
- There is a need for a Taxpayer Bill of Rights as recommended by the Davis Tax Committee:
  - To guarantee taxpayers rights in their interaction with SARS
  - To make SARS responsible in its dealings with taxpayers
  - To regulate the interactions and expectations of the relationship between SARS and taxpayers
- The DTC recommended that the Taxpayer Bill of Rights should be enforceable and have legal effect
- Who should be responsible for drafting it?

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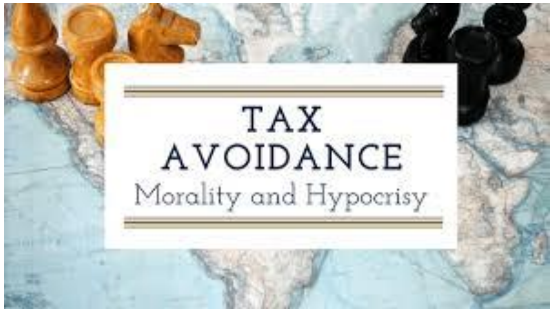
Taxpayer Bill of Rights

- DTC recommends that it should contain these rights:
  - The right to finality
  - The right to privacy and confidentiality
  - The right to complete, accurate, clear and timely information
  - The right to pay no more than the correct amount of tax
  - The right not to pay tax amounts in dispute before you have had an impartial review
  - The right to legal representation
  - The right to quality service
  - The right to fair and just tax system

Strengthening tax morality



- It is acknowledged in the Budget that:
  - Corruption and wasteful expenditure in the public sector have eroded taxpayer morality in recent years
  - The lack of an effective government response to allegations of corruption and poor governance has undermined the social contract between taxpayers and the state
- We welcome the following measures which have been announced to strengthen tax morality:
  - The overall emphasis by the new President to curb corruption and waste
  - The establishment of a commission of inquiry into the functioning and governance of SARS
  - Steps to improve the governance and accountability of SARS & to strengthen the operational independence of the Tax Ombud, following the recommendations of the Davis Tax Committee

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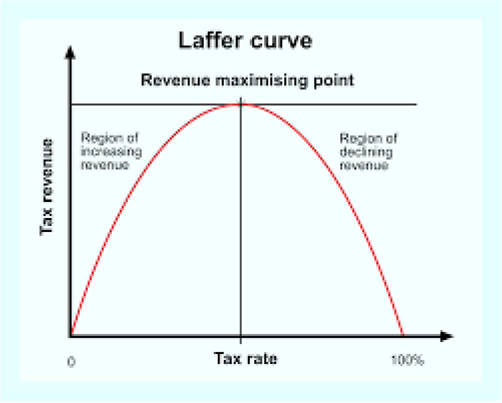
Balance between tax instruments - VAT increase unavoidable

- "The VAT proposal recognises limits on the medium-term revenue-raising potential of other major tax instruments, given recent increases in those categories. An appropriate balance is required."
- Personal income tax collections for 2017/2018 is expected to undershoot the target by R21,1bn – Laffer curve?
- Corporate income tax rate is high in comparison & the global trend is that they decrease – competitiveness?
- VAT rate is relatively low compared to Africa and the world
- "Increasing the VAT rate by one percentage point is estimated to have the least detrimental effects on economic growth and employment over the medium term."



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VAT rate increase from 14% to 15% - Least detrimental effect

- Broad-based and efficient tax – easy for SARS to increase collections immediately (and the projections are likely to match the actual results)
- Should bring in a significant amount of revenue – R22,9bn
- Tax on consumption of most goods and services
- Better than the alternative foreshadowed in 2017 Budget that VAT may be imposed at the standard rate (of 14% then) on fuel
  - This would have meant that the fuel price would have increased by 14% (which would have been a hard blow for the working poor)
  - This could have had a significant inflationary impact
- The increase in VAT from 14% to 15% is an 0.88% increase on standard rated goods and services consumed

VAT increase – impact on poor and rich

- Will affect the poor and the rich roughly proportionally
- A 2015 paper titled 'The distributional impact of fiscal policy in South Africa' found that:
  - VAT is broadly neutral in South Africa
  - Households across the income brackets pay roughly the same proportion of their income on VAT
  - VAT does not make inequality better or worse in South Africa
  - Higher income earners pay a slightly higher proportion of their income on VAT when zero-rated goods are taken into consideration than lower income earners.
- The unfair impact is overstated:
  - Low-Income Example: A person living on R36 000 per annum (i.e. roughly R3 000 a month) will have to pay an additional R360 per annum
  - High-Income Example: A person earning R1.8 million per year with R300 000 retirement savings per annum has R982 026 of spending power, resulting in R9 820.26 additional VAT per annum

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VAT increase – mitigating the effect on the poor

- We have sympathy for the poor because the poor is vulnerable
- List of zero-rated basic food items to be reviewed?
  - Many essential food items are not zero-rated e.g. tea, salt, white bread, margarine, peanut butter & jam
  - Many other essential items are subject to VAT at 15% e.g. soap
  - Many zero-rated food items benefit the rich e.g. exotic fruits (e.g. kiwi and dragon fruit) and frozen vegetables
- Will the higher than inflation increase in social grants be effective in protecting the poor?
  - Many of the poorest of the poor do not qualify for grants
  - Grants only given to pensioners and disabled and for foster care and child support
  - Many poor households have no access to grants even if they are jobless
- Other targeted measures to protect the poor?

Targeted tax incentives for growth and jobs

- Six special economic zones (SEZ's) will be approved
  - Encourage investment in manufacturing
  - Boost employment and growth
  - Corporate tax rate of 15% welcomed
  - Employment tax incentive for all ages welcomed
- Research & Development incentive
  - Changes to remove complexity would be welcomed
- Support programme for industrial innovation (s12I)
  - Need a further allocation of funds while the window is open
- Awaiting outcome of review of all tax incentives and grants

Technical proposals and administrative adjustments

We particularly wish to acknowledge these proposals:

- Amendments resulting from the application of debt relief rules
  - Further amendments to be made to address unintended consequences
- Refining anti-avoidance rules dealing with share buybacks and dividend stripping
  - Interaction with corporate reorganisation rules to be reviewed

Proposed change in “official rate of interest” – creates uncertainty

Looking forward to further engagement on all the tax proposals during the legislative cycle

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THANK YOU

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