4

Revenue trends and tax proposals

Buoyant corporate activity, a strong housing market, rising levels of imports, employment gains, real wage increases, robust consumption spending and continued improvements in tax collection capacity have contributed to across-the-board revenue increases over the past two years, over and above what was projected in 2004 and 2005. It is estimated that main budget revenue for the current fiscal year will rise to R411,1 billion.

The 2006 tax proposals reduce the tax burden on individuals and businesses, expand the tax base and simplify tax administration. A range of initiatives aims to stimulate investment, innovation, employment and skills development, thereby contributing to economic growth.

Government continues its efforts to open the way for entrepreneurs and the development of small firms with a series of proposals that include tax relief and a tax amnesty for small businesses. To promote skills development and employment creation, particularly among youth, an extension of the learnership allowance is proposed. In keeping with efforts to accelerate economic growth and international competitiveness, incentives are proposed to foster research and development by South African companies.

Government is able to offer gross personal income tax relief of R13,5 billion. Raising the tax threshold to R40 000 effectively exempts many low-income earners from income tax. Similarly, the substantial transfer duty relief reduces the cost of property transactions at all levels, and eases the financial burden on first-time and low-income home buyers. To help South Africans accumulate adequate savings for retirement, a reduction in the retirement fund tax from 18 per cent to 9 per cent is proposed.

Overview

Buoyant revenue collection shows success of tax reform

Over the past decade South Africa has implemented major reforms to broaden the tax base, reduce marginal tax rates and improve the administration of tax collection. These reforms have been broadly in step with international tax reform trends and have bolstered government's revenue-raising capacity. The buoyant revenue collections and tax relief measures implemented over the past few years are evidence of the success of the tax reform agenda.

In the medium term, the tax policy framework supports the goals of accelerated and shared economic growth by promoting long-term retirement savings, reducing the costs of tax compliance and the tax burden on all businesses, fostering small business development, boosting investment in research and development (R&D), supporting skills development and encouraging home ownership. The monetary thresholds of the two top personal income tax brackets are increased substantially – by 30 and 33 per cent respectively. The top marginal tax rate will now start at R400 000 a year, providing substantial relief for middle-income earners.

A lower tax burden for businesses

Proposed adjustments reinforce the long-term growth path by reducing the costs of tax compliance, broadening the tax base and lowering the tax burden on key economic activities. The 2006 Budget takes into account the elimination of RSC levies, which will be abolished on 30 June 2006. This decision effectively grants substantial tax relief for business, reduces their administrative burden and directly reduces the cost of employment. A consultative process has been initiated with a discussion paper exploring possible options for replacing the levies.

SARS implementing reduced compliance costs and enhanced service

The South African Revenue Service (SARS) is also implementing a package of reduced compliance costs, enhanced service, and improved tax and customs administration. To encourage small businesses to become tax compliant, a tax amnesty is proposed. During 2006, legislation will be submitted to Parliament providing tax concessions for the international football association's operations during the 2010 Soccer World Cup.

This chapter explains the main tax proposals included in the 2006 Budget and reviews revenue collections and estimates for 2005/06. Annexure C elaborates on these and other technical proposals.

Main tax proposals

Net tax relief of R19,1 billion

The 2006 Budget tax proposals amount to net tax relief of R19,1 billion, in addition to reduced tax liabilities arising from abolition of the RSC levies. The proposals include:

Tax relief

- Income tax rate reduction of R13,5 billion for individuals
- Tax relief of R7 billion for business resulting from abolition of the RSC levies
- Tax amnesty for small businesses
- Tax on retirement funds reduced from 18 per cent to 9 per cent
- Transfer duty thresholds raised to R500 000 and R1 million
- Monetary thresholds for qualifying small businesses increased
- Monetary thresholds for capital gains and estate duty increased
- Extension of the learnership allowance until 2011 and incentives to encourage the intake of learners with disabilities
- Incentives to boost expenditure on R&D
- *Ad valorem* excise duties abolished on certain products

- Increase in the biodiesel fuel tax concession to 40 per cent of the general fuel levy.

Tax increases

- Increase in the Road Accident Fund levy by 5 cents a litre
- Increase in excise duty on tobacco products by between 4,7 and 10,2 per cent
- Increase in excise duty on alcohol products by between 9 and 20 per cent.

Consolidated national revenue estimates

Consolidated national revenue expected to increase at average rate of 9,9 per cent

Table 4.1 sets out the consolidated national revenue for 2004/05 to 2008/09, consisting of main budget revenue, the receipts of social security funds and foreign technical assistance. Consolidated national revenue amounted to R363,8 billion in 2004/05, which is 6,6 per cent higher than the 2004 Budget estimate. Between 2005/06 and 2008/09, taking into account the tax proposals, consolidated national revenue is expected to increase at an annual average rate of 9,9 per cent.

While the main budget revenue-to-GDP ratio is estimated to increase to 26,4 per cent in 2005/06 due to higher-than-anticipated collection, the ratio declines to 26 per cent in 2006/07 after taking into account the effects of the tax proposals.

Table 4.1 Consolidated national revenue, 2004/05 – 2008/09

	2004/05	2005/06		2006/07	2007/08	2008/09
R million	Outcome	Budget estimate	Revised estimate	Medium-term estimates		
Total tax revenue	354 980	372 774	417 050	456 786	501 670	558 106
Less: SACU payments	-13 328	-12 053	-14 145	-19 744	-20 344	-22 451
Non-tax revenue[1]	6 202	9 148	8 180	9 320	10 677	11 436
Main budget revenue[2]	**347 854**	**369 869**	**411 085**	**446 362**	**492 003**	**547 091**
Percentage of GDP	*24,5%*	*23,7%*	*26,4%*	*26,0%*	*26,1%*	*26,1%*
Social security funds						
Tax revenue	12 969	14 580	14 888	16 645	17 583	18 578
Non-tax revenue[3]	1 377	1 850	4 924	2 630	2 978	3 345
Total social security revenue	**14 346**	**16 430**	**19 812**	**19 274**	**20 561**	**21 923**
RDP fund receipts and technical co-operation	1 634	1 500	1 624	1 550	1 550	1 550
Consolidated national revenue[4]	**363 830**	**387 783**	**429 817**	**467 182**	**514 110**	**570 559**

1. Includes departmental revenue, transactions in assets and liabilities, and foreign grants received. The Budget estimate for 2005/06 includes an amount for the proceeds of the foreign exchange amnesty
2. Included over the medium term is the on-budget financing as replacement of the RSC levies.
3. Includes own revenue, sale of capital assets and grants received.
4. Transfers between funds have been netted out.

National budget revenue – revised estimates

Table 4.2 highlights budget estimates and revenue outcomes of the major tax instruments for 2004/05 and projected revenue outcomes for

2005/06. Tables 2 and 3 in Annexure B set out these numbers in greater detail.

Revenue outcome for 2004/05

Personal income tax, company tax and VAT contributed to higher 2004/05 revenue

Audited results show that main budget revenue for 2004/05 was R347,9 billion, or 6,4 per cent higher than the budget estimate of R327 billion. Significant deviations from the original estimates include:

- Personal income tax up by R5 billion
- Company tax up by R2 billion
- Value-added tax (VAT) up by R8,7 billion
- Trade taxes up by R2,8 billion.

Table 4.2 Main budget estimates and revenue outcome, 2004/05 and 2005/06

R million	2004/05 Budget estimate	2004/05 Outcome	2004/05 Deviation	2005/06 Budget estimate	2005/06 Revised estimate	2005/06 Deviation	2004/05–2005/06 % change
Taxes on income and profits	**189 198**	**195 219**	**6 021**	**200 855**	**228 730**	**27 875**	**17,2%**
Personal income tax	105 938	110 982	5 044	116 890	125 760	8 870	13,3%
Company tax	68 800	70 782	1 982	68 715	84 900	16 185	19,9%
Secondary tax on companies	6 760	7 487	727	8 700	11 850	3 150	58,3%
Tax on retirement funds	6 000	4 406	-1 594	4 900	4 500	-400	2,1%
Other	1 700	1 562	-138	1 650	1 720	70	10,1%
Taxes on payroll and workforce	**4 300**	**4 443**	**143**	**4 908**	**5 000**	**92**	**12,5%**
Taxes on property	**6 870**	**9 013**	**2 143**	**9 820**	**11 120**	**1 300**	**23,4%**
Domestic taxes on goods and services	**121 549**	**131 983**	**10 433**	**143 091**	**152 370**	**9 279**	**15,4%**
Value-added tax	89 500	98 158	8 658	105 975	115 000	9 025	17,2%
Specific excise duties	13 112	13 067	-45	14 509	14 599	90	11,7%
Levies on fuel	17 409	19 190	1 781	20 650	20 700	50	7,9%
Other	1 529	1 568	39	1 957	2 071	114	32,1%
Taxes on international trade and transactions	**10 476**	**13 286**	**2 810**	**13 200**	**18 960**	**5 760**	**42,7%**
Stamp duties and fees	**1 300**	**1 168**	**-132**	**900**	**870**	**-30**	**-25,5%**
State miscellaneous revenue[1]	**–**	**-131**	**-131**	**–**	**–**	**–**	**-100,0%**
Total tax revenue	**333 694**	**354 980**	**21 287**	**372 774**	**417 050**	**44 276**	**17,5%**
Departmental revenue	5 944	5 520	-424	8 502	7 454	-1 048	35,0%
Transactions in assets and liabilities	646	682	35	646	726	80	6,5%
Less: SACU payments	-13 328	-13 328	–	-12 053	-14 145	-2 092	6,1%
Main budget revenue	**326 956**	**347 854**	**20 898**	**369 869**	**411 085**	**41 216**	**18,2%**

1. Revenue received by SARS in respect of taxation which could not be allocated to a specific tax instrument.

Revised estimates for 2005/06

Main budget revenue for 2005/06 is revised upwards by 11,1 per cent

Based on the revised macroeconomic projections outlined in Chapter 2 and the revenue trends, the main budget revenue estimate for 2005/06 is revised upwards by 11,1 per cent to R411,1 billion. In the 2005 Budget, main budget revenue for 2005/06 was anticipated to be R369,9 billion after accounting for tax proposals. The increased revenue estimates stem largely from buoyant consumer spending and increased corporate profits.

Taxes on income and profits are estimated to be 13,9 per cent higher than the original budget estimate. Personal income tax is estimated to reach R125,8 billion, which is R8,9 billion above the original budget estimate, partly as a result of employment growth. Over the past two years the number of personal income tax filers increased by about 700 000.

Taxes on income and profits estimated to be 13,9 per cent

The revised estimate for corporate income tax is R84,9 billion, which is 23,6 per cent higher than originally budgeted. Corporate income tax and the secondary tax on companies are expected to generate R16,2 billion and R3,2 billion respectively more than budgeted as a result of higher-than-expected corporate profits, particularly in the financial and telecommunications sectors.

The skills development levy is expected to raise R5 billion, R92 million higher than the budget estimate.

Skills development levy to raise R5 billion

VAT receipts are expected to total R115 billion, about R9 billion above the 2005 Budget estimate. The revised estimated revenue from specific excise duties of R14,6 billion is R90 million higher than estimated. Fuel levies should raise R20,7 billion, in line with expectations.

Customs duty revenues are revised upwards by R5,6 billion as a result of higher import volumes and the greater value of imports, reflecting strong economic growth and the buying power of the rand.

Revenue trends and tax

Main budget revenue as a percentage of GDP is estimated to increase to approximately 26,4 per cent in 2005/06. Over the past five years the contribution of direct taxes as a percentage of total gross tax revenue declined from 58 per cent to about 56,4 per cent, and that of indirect tax increased from 41,9 per cent to 43,6 per cent.

Main budget revenue as percentage of GDP increases to 26,4 per cent

In the nine years leading up to 1991/92, corporate income tax revenues as a percentage of GDP averaged about 5,1 per cent, decreasing to an average of 2,9 per cent between 1992/93 and 2000/01, and rising to an average of 4,8 per cent in the period 2001/02 to 2005/06. The average shares of personal income tax revenues as a percentage of GDP for the corresponding periods were 7,2, 9,4 and 8 per cent respectively.

The reduction of the personal income tax-to-GDP ratio is a reflection of the R48,5 billion personal income tax relief granted over the past five years. The increase in the tax-to-GDP ratio for company tax revenues indicates increased profitability and improved compliance.

R48,5 billion of personal income tax relief granted over past five years

Table 4.3 sets out actual revenue collections for 2002/03-2004/05 and estimates for 2005/06-2008/09. More detail is provided in Tables 2 and 3 of Annexure B.

Table 4.3 Main budget revenue, 2002/03 – 2008/09

R million	2002/03	2003/04 Actual	2004/05	2005/06 Revised estimate	2006/07	2007/08 Medium-term estimates	2008/09
Taxes on income and profits	164 566	171 963	195 219	228 730	245 816	272 315	306 560
Taxes on payroll and workforce	3 352	3 896	4 443	5 000	5 600	6 150	6 800
Taxes on property	5 085	6 707	9 013	11 120	8 922	12 023	12 845
Domestic taxes on goods and services	97 582	110 174	131 983	152 370	171 885	184 776	203 366
Taxes on international trade and transactions	9 620	8 414	13 286	18 960	23 600	25 420	27 440
Stamp duties and fees	1 572	1 360	1 168	870	964	987	1 095
State miscellaneous revenue[1]	433	-7	-131	–	–	–	–
Total tax revenue	**282 210**	**302 508**	**354 980**	**417 050**	**456 786**	**501 670**	**558 106**
Departmental revenue	4 192	5 931	5 520	7 454	8 585	9 610	10 300
Transactions in assets and liabilities	366	715	682	726	735	1 067	1 136
Less: SACU payments	-8 259	-9 723	-13 328	-14 145	-19 744	-20 344	-22 451
Main budget revenue	**278 508**	**299 431**	**347 854**	**411 085**	**446 362**	**492 003**	**547 091**
Percentage of GDP	*23,2%*	*23,4%*	*24,5%*	*26,4%*	*26,0%*	*26,1%*	*26,1%*
Gross domestic product	*1 198 344*	*1 281 438*	*1 419 991*	*1 559 580*	*1 714 528*	*1 884 866*	*2 095 911*

1. Revenue received by SARS in respect of taxation which could not be allocated to a specific tax instrument.

Completion of exchange control and tax amnesty adjudication process

The amnesty unit has completed the adjudication of all applications received since the announcement of the exchange control and tax amnesty by the Minister of Finance on 26 February 2003.

The amnesty gave South Africans an opportunity to voluntarily declare their offshore assets and to regularise their foreign asset holdings and tax affairs without fear of criminal or civil prosecution. Regularisation entailed the payment of a 10 per cent levy if the foreign assets were kept offshore, or 5 per cent if the assets were repatriated to South Africa. An additional 2 per cent levy was payable for violating certain domestic tax laws. The closing date for applications was extended to 29 February 2004. The Reserve Bank also issued regulations to deal with various challenges and concerns presented by certain complex offshore structures.

The amnesty unit has adjudicated all of the 42 672 applications (after allowing for 456 duplicates) it received since the announcement of the amnesty nearly three years ago. Of this number, 42 184 applications were approved; 924 applications of the total received applications (43 128 including duplicates) were withdrawn, deleted or voided; and 20 applications were declined. The amnesty process has raised R2,9 billion in levies.

When the amnesty process was announced in 2003, it had four objectives: (i) to broaden the tax base and increase future revenue collection through disclosure of assets (both legal and illegal); (ii) to enable South Africans to regularise their affairs without being prosecuted; (iii) to provide the South African Revenue Service (SARS) and the Reserve Bank with details of foreign assets; (iv) and to facilitate repatriation of foreign assets to South Africa, without fear of recrimination.

The amnesty process has successfully achieved all these objectives. A total of R68,6 billion worth of foreign assets have been disclosed under the amnesty process. Approximately 70% of these disclosed assets were illegal, while an approximate 30 per cent were legal or legalised through the Reserve Bank. It is estimated that the income tax base has been increased by an estimated R1,4 billion, which is likely to increase the collection of personal income taxes by an estimated R400 million per annum. SARS and Reserve Bank will also be able to fully update their records on the basis of the information disclosed.

All the approved applications will be sanitised and submitted to SARS and the Reserve Bank with highly restricted access. Unsuccessful applications will be retained at the National Treasury with the necessary security. These procedures will ensure that the objective of having enabled South Africans to regularise their affairs without fear of prosecution or recrimination is fully safeguarded.

Lastly, the R2,9 billion of revenue raised through the levies is a further indication of the success of the amnesty process, and will be used for social development and community infrastructure.

Between 2002/03 and 2005/06, main budget revenue grew at an annual average rate of 13,9 per cent, largely as a result of growth in the collection of taxes on goods and services, which increased at an average annual rate of 16 per cent. Taxes on income and profits increased at an average annual rate of 17,6 per cent. Taking into account revenue trends, policy changes and macroeconomic projections, main budget revenue is expected to grow at an annual average rate of 10 per cent over the medium term.

Revenue estimates and tax proposals – 2006/07

Main budget revenue estimated to be R465,5 billion before tax changes

Table 4.4 sets out the estimates of revenue before tax proposals for 2006/07, based on the macroeconomic assumptions set out in Chapter 2 and the existing tax structure. Annexure C contains additional proposals of a more technical nature.

Table 4.4 Estimates of revenue before tax proposals, 2006/07

R million	2005/06 Revised estimate	2006/07 Before tax proposals	Percentage change
Taxes on income and profits	**228 730**	**260 741**	**14,0%**
Personal income tax	125 760	144 600	15,0%
Company tax	84 900	95 601	12,6%
Secondary tax on companies	11 850	13 850	16,9%
Tax on retirement funds	4 500	4 800	6,7%
Other	1 720	1 890	9,9%
Taxes on payroll and workforce	**5 000**	**5 600**	**12,0%**
Taxes on property	**11 120**	**13 462**	**21,1%**
Domestic taxes on goods and services	**152 370**	**171 537**	**12,6%**
Value-added tax	115 000	132 200	15,0%
Excise duties	15 799	16 608	5,1%
Levies on fuel	20 700	21 800	5,3%
Other	871	929	6,7%
Taxes on international trade and transactions	**18 960**	**23 600**	**24,5%**
Stamp duties and fees	**870**	**974**	**12,0%**
Total tax revenue	**417 050**	**475 914**	**14,1%**
Departmental revenue	7 454	8 585	15,2%
Transactions in assets and liabilities	726	735	1,2%
Less: SACU payments	-14 145	-19 744	39,6%
Main budget revenue	**411 085**	**465 489**	**13,2%**

Main budget revenue in 2006/07 is estimated to be R465,5 billion before any tax changes are proposed. Personal income tax is estimated to increase by 15 per cent to R144,6 billion. Company tax and VAT are projected to raise R95,6 billion and R132,2 billion respectively.

Overview of 2006/07 tax proposals

Proposals aim to stimulate growth

The 2006 tax proposals are designed to stimulate business, investment, innovation, economic growth, home ownership and skills development, while concurrently improving the equity and efficiency of the tax system. Table 4.5 provides the anticipated revenue effects of the tax proposals set out in this budget. The net effect is to reduce total tax revenue by R19,1 billion.

Table 4.5 Summary effects of tax proposals, 2006/07

R million	Effect of tax proposals	
Tax revenue		475 914
Non-tax revenue		9 320
Less: SACU payments		-19 744
Main budget revenue, before tax proposals		**465 489**
Budget 2006/07 proposals:		**-19 127**
Taxes on individuals and companies	**-14 925**	
Personal income tax	-12 125	
Adjust personal income tax rate structure	*-13 500*	
Increase in interest and dividend exemption under 65 years	*-50*	
Increase in interest and dividend exemption 65 years and over	*-45*	
Increase thresholds for learnership allowances	*-80*	
Increase PAYE withholding rate on motor allowances and fringe benefit on company cars	*1 370*	
Capping of medical scheme contributions	*180*	
Corporate income tax	-2 400	
Reduction in retirement fund tax	*-2 400*	
Small business tax relief	-400	
Taxes on property	**-4 540**	
Increase thresholds of donations tax and estate duty	-40	
Adjust table for transfer duties	-4 500	
Stamp duties	**-10**	
Increase threshold exemption for stamp duties on leases	-10	
Taxes on goods and services	**348**	
Increase in duties on alcohol	725	
Increase in duties on tobacco products (52% incidence)	645	
Abolish *ad valorem* excise duties on certain products	-22	
Zero rating of municipal property rates	-1 000	
Main budget revenue (after tax proposals)		**446 362**

Relief for individuals

Personal income tax

Personal income tax relief of R13,5 billion

Under the proposals made in the 2006 Budget, South Africans will benefit from significant personal income tax relief that takes into account the effects of inflation and provides for a real reduction in the individual tax burden. It is proposed to raise the income tax threshold by 14,3 per cent to R40 000, to widen the individual income tax brackets and to increase the upper tax bracket from R300 000 to R400 000, with 73 per cent of the income tax relief benefiting those earning R250 000 or less.

Personal income tax rate relief of R13,5 billion is proposed. The suggested rate schedule is set out in Table 4.6.

The main adjustments are:

- The primary rebate is raised to R7 200 from R6 300, increasing the income tax threshold by 14,3 per cent to R40 000
- The tax threshold for taxpayers age 65 and over is raised to R65 000 from R60 000, an increase of 8,3 per cent.
- Brackets are adjusted to provide relief across the income spectrum.

The distribution of the tax relief is as follows:

- Threshold to R60 000 — 13 per cent
- R60 000 to R150 000 — 36 per cent
- R150 000 to R250 000 — 24 per cent
- R250 000 and above — 27 per cent

Table 4.6 shows the effect of these adjustments and detailed examples are provided in Annexure C.

Table 4.6 Personal income tax rate and bracket adjustments, 2005/06 and 2006/07

2005/06		2006/07	
Taxable income (R)	**Rates of tax**	**Taxable income (R)**	**Rates of tax**
0 – 80 000	18% of each R1	0 – 100 000	18% of each R1
80 001 – 130 000	R14 400 + 25% of the amount above R80 000	100 001 – 160 000	R18 000 + 25% of the amount above R100 000
130 001 – 180 000	R26 900 + 30% of the amount above R130 000	160 001 – 220 000	R33 000 + 30% of the amount above R160 000
180 001 – 230 000	R41 900 + 35% of the amount above R180 000	220 001 – 300 000	R51 000 + 35% of the amount above R220 000
230 001 – 300 000	R59 400 + 38% of the amount above R230 000	300 001 – 400 000	R79 000 + 38% of the amount above R300 000
300 001 and above	R86 000 + 40% of the amount above R300 000	400 001 and above	R117 000 + 40% of the amount above R400 000
Rebates		**Rebates**	
Primary	R6 300	Primary	R7 200
Secondary	R4 500	Secondary	R4 500
Tax threshold		**Tax threshold**	
Below age 65	R35 000	Below age 65	R40 000
Age 65 and over	R60 000	Age 65 and over	R65 000

Interest and dividend income exemption

Interest and dividend exemption threshold increased

The domestic interest and dividend exemption is currently R15 000 for taxpayers under the age of 65, and R22 000 for taxpayers age 65 and over. This exemption encourages a culture of savings and helps retired South Africans to retain interest income. From 1 March 2006, the exemption threshold will increase to R16 500 (10 per cent) for taxpayers younger than 65 years and to R24 500 (11,4 per cent) for taxpayers age 65 and over. It is also proposed to increase the proportion of the exemption applicable to foreign interest income and dividends from R2 000 to R2 500 per year.

Transfer duty

A lower tax burden on all property transactions

Property prices have increased substantially over the past few years, making it difficult for many people to purchase their first house. To ease the burden on first-time and lower-income home buyers, the exempt threshold for transfer duty will be increased significantly from R190 000 to R500 000, and the second threshold from R330 000 to R1 million.

Table 4.7 Proposed rates of transfer duty, 2006/07

Property value	Rates of tax
R0 – R500 000	0%
R500 001 – R1 000 000	5% on the value above R500 000
R1 000 001 and above	R25 000 plus 8% on the value above R1 000 000

Transfer duty rate for companies and trusts is reduced to 8 per cent

It is also proposed to reduce the flat 10 per cent transfer duty rate for companies and trusts to 8 per cent. These amendments will bring significant relief of R4,5 billion to home buyers, and will come into effect on 1 March 2006. Table 4.8 illustrates the effect of these adjustments.

Table 4.8 Current and proposed transfer duty

Property value	Current duty	Percentage of value	Proposed duty	Percentage of value	Tax reduction
R 500 000	R 20 600	4.1%	R 0	0.0%	R 20 600
R 550 000	R 24 600	4.5%	R 2 500	0.5%	R 22 100
R 600 000	R 28 600	4.8%	R 5 000	0.8%	R 23 600
R 650 000	R 32 600	5.0%	R 7 500	1.2%	R 25 100
R 700 000	R 36 600	5.2%	R 10 000	1.4%	R 26 600
R 800 000	R 44 600	5.6%	R 15 000	1.9%	R 29 600
R 1 000 000	R 60 600	6.1%	R 25 000	2.5%	R 35 600
R 1 500 000	R 100 600	6.7%	R 65 000	4.3%	R 35 600

Stamp duties

Threshold exemption for stamp duties increases to R500

It is proposed to increase the threshold exemption for stamp duties on leases from R200 to R500 per agreement from 1 March 2006, reducing the compliance burden for taxpayers entering into lower-value rental agreements, and the administrative burden on SARS.

Individual monetary thresholds

The tax system contains a number of monetary thresholds that have not been changed for some time. Some of these thresholds are adjusted upwards to take into account the effects of inflation.

It is proposed that the annual donations tax exemption be increased from R30 000 to R50 000 and the estate duty exemption be increased from R1,5 million to R2,5 million, effective from 1 March 2006.

Capital gains

The following proposals are made for tax years commencing on or after 1 March 2006:

- The annual capital gain/loss exclusion will increase from R10 000 to R12 500
- The primary residence exclusion will increase from R1 million to R1,5 million
- The exclusion on death will increase from R50 000 to R60 000.

Motor vehicle allowances

Deemed private kilometres increased to 18 000 per year

As announced in the 2005 Budget, the deemed private kilometres (i.e. the number of kilometres assumed to have been driven for private use) for individuals who receive motor vehicle allowances will be increased to 18 000 per year, and the monthly taxable fringe benefit of a company car will be increased to 2,5 per cent of the determined value of the vehicle, effective from 1 March 2006. To ensure that the correct amount of income tax is collected through the PAYE system during the year, the percentage of the monthly motor vehicle allowances subject to tax will be increased from 50 per cent to 60 per cent from 1 March 2006. A new cost table will be published.

Medical scheme contributions and medical expenses

Revised tax regime for medical scheme contributions takes effect 1 March 2006

A revised tax regime for medical scheme contributions and other medical expenses was announced in the 2005 Budget. The purpose of this new regime is to shift the tax benefits in favour of middle and lower-income earners. This new regime introduces monthly monetary caps for tax-free medical scheme contributions (with the caps to be adjusted annually) and increases the threshold for individual tax-deductible medical expenses from 5 to 7,5 per cent of income. Taxpayers 65 years and older will continue to enjoy a full deduction for all medical expenses. These changes take effect on 1 March 2006.

Promoting retirement savings

Progress with retirement fund regulatory reform

Proposals developed in the course of 2005 represent significant progress in the retirement fund regulatory reform process. To help South Africans accumulate adequate savings for retirement, and taking into account the stabilisation of interest rates at lower levels, the tax on retirement funds will be reduced from 18 per cent to 9 per cent from 1 March 2006 at an estimated cost of R2,4 billion.

This reduction will be accompanied by regulatory reforms in areas such as cost disclosure, commission structure and fund governance. The National Treasury will issue a discussion paper on proposed regulatory and tax reforms. These reforms will aim to ensure that the benefits of the lower tax rate are passed on to retirement fund members in the form of improved returns, and that retirement savings are not depleted by excessive charges and penalties. Further information is provided in a box on developments in the retirement savings industry in Chapter 2.

Relief for business

RSC levy reform

Falling away of RSC levies amounts to substantial corporate tax reduction

By eliminating the RSC levies from 30 June 2006, the 2006 Budget provides significant direct tax relief to business, amounting to R7 billion for 2006/07 and totalling R24 billion over the MTEF period. The administrative burden will be significantly lowered for all businesses, as RSC levies required monthly submissions. Since one of the levies is imposed on payroll, its removal will effectively lower the costs of job creation.

Small business

Thresholds and exemptions increased for small business

Small businesses play a valuable role in stimulating economic activity, job creation, poverty alleviation and broadening development. In addition to the benefits of removing the burden of the RSC levies, government has made considerable efforts to improve the economic environment for small business. Following the tax stimulus measures introduced in the 2005 Budget, the monetary tax thresholds for small business will be adjusted as follows:

- For small business corporations, the following amendments will come into effect for tax years ending on or after 1 April 2006:
  - Firms with an annual turnover of up to R14 million (increased from a level of R6 million) will qualify for the special graduated corporate tax regime
  - The taxable income threshold for the reduced corporate tax rate of 10 per cent will be increased from R250 000 to R300 000
  - The small business income tax exemption threshold will be increased from R35 000 to R40 000.
- The one-time capital gains tax relief for small business will increase from R500 000 to R750 000 with effect from tax years commencing on or after 1 March 2006.
- Immediate 100 per cent depreciation exists for individual small items purchased for business purposes. This threshold will increase from R2 000 to R5 000 for assets purchased on or after 1 March 2006.
- The VAT threshold for both small farmers (Category D) and small business four-monthly filers (Category F) will increase from R1 million to R1,2 million for tax periods commencing on or after 1 July 2006.

It is estimated that these changes will cost R400 million.

In addition, the “small business corporation” and “deemed employee” definitions that affect some small businesses will be amended.

Tax amnesty for small business

Greater willingness to enter the tax system

Although small businesses play a valuable economic and developmental role, many were historically marginalised. They were excluded from the economic mainstream, operated informally and remained outside the tax system. A growing understanding of the economic benefits of a more formal approach to doing business, of why it is necessary to pay tax, of the tax system's requirements, and of the risks of non-compliance have now led to greater willingness to enter the tax system.

An obstacle to becoming tax compliant faced by these small businesses is the fear of the consequences of past non-compliance, which include possible liability for additional tax, interest and prosecution. This fear makes the decision to enter the tax system a difficult one. Government is therefore proposing a tax amnesty to ensure that small businesses can overcome this obstacle.

Proposed amnesty allows for SARS to waive taxes due for certain period

The proposed amnesty will allow SARS to waive taxes due by small businesses for years of assessment ending on or before 31 March 2004, where the turnover for the 2005 year of assessment does not exceed R5 million. This waiver will require submission of an income tax return for 2005 as well as a non-disclosure penalty of 10 per cent based on taxable income for 2005. It will not be available to taxpayers who have already disclosed the amounts concerned, or who have been formally notified that they are under investigation before applying for amnesty. It is also proposed to waive penalties, additional taxes and interest on the underlying taxes due.

A two-phase approach is proposed, with the first phase of the amnesty focused on the taxi industry, since access to the taxi recapitalisation programme is dependent on tax compliance. The first phase of the amnesty will take effect on 1 August 2006 and will be open until 31 May 2007. The second phase of the amnesty for other small businesses will take effect later in the year. Small businesses that do not take advantage of this opportunity to enter the tax system voluntarily will be the subject of SARS enforcement activities and subject to additional tax, interest and prosecution.

Revised cooperative taxation

In view of the Cooperatives Act (2005), the tax dispensation will be adjusted. Amendments will also provide cooperatives that operate like small business corporations with the same level of benefits enjoyed by those companies.

Stimulating investment and economic growth

Incentives for oil and gas

Incentives to support oil and gas exploration

South Africa has a long history of special oil and gas contracts known as OP 26 leases with private companies. These leases include tax and other incentives to facilitate oil and gas exploration. With the OP 26 leases about to expire, certain tax incentives need to be renewed. These incentives will be renewed in legislation, which is a more transparent method of granting exemptions. Proposed amendments will include the removal of the 40 per cent discretionary surcharge on oil and gas profits, and accelerated depreciation for drilling.

Review of revenue versus capital distinction

Working towards improving criteria for distinguishing revenue from capital gains

The disposal of assets (including shares) at a gain generally triggers a tax, either as ordinary revenue or capital gains, depending on whether the asset is purchased with the intent to resell. This question of intent is largely governed by judicial decision. However, an exception in the Income Tax Act (1962) allows taxpayers to elect capital treatment for the sale of listed shares held for at least five years. Evidence suggests that the current test creates uneven results, especially for the ownership of shares. A review of the revenue versus capital distinction will begin in 2006.

Incentives for intellectual capital and training

Extension and increase of the learnership allowance

Learnership tax allowance extended to 2011

In 2002, government introduced the learnership tax allowance to encourage on-the-job training and to enhance skills development. This allowance, set to expire in October 2006, has boosted the number of learnerships. In support of the extension of the National Skills Development Strategy, it is proposed that this allowance be extended to October 2011. The maximum initial allowances will increase from R17 500 to R20 000 per year for existing employees and from R25 000 to R30 000 for new employees. Similarly, the maximum allowance upon the completion of the learnership will increase from R25 000 to R30 000 for agreements entered into from 1 March 2006, at an estimated cost of R80 million. Consideration will be given to increasing the allowance for business process outsourcing.

More favourable allowance to promote enrolment of disabled learners

Given the additional expenses associated with employing disabled persons as learners, a more favourable allowance will be introduced effective 1 July 2006. An employer will be allowed to deduct an initial allowance of 150 per cent of the annual salary of an existing learner with a disability, up to a maximum of R40 000; and 175 per cent for an unemployed learner with a disability, up to a maximum of R50 000. The tax allowance for disabled persons completing a learnership will be 175 per cent of the employee's annual salary, up to a maximum of R50 000.

Enhancement of scholarships and bursaries

All employee bursaries and scholarships to become tax-exempt

Employee scholarships and bursaries are tax-exempt, unless viewed as being in lieu of salary compensation. The need to draw such a distinction creates unnecessary difficulties in application. To simplify matters, bursaries and scholarships for current and future employees will be tax-exempt as long as the employer's funds go directly to tuition and tuition-related expenses, and the employee agrees to repay the employer if the employee fails to fulfil their scholarship or bursary obligations. This proposal will take effect from 1 March 2007.

Enhancement of research and development

Deduction for R&D expenses increased

To encourage businesses to increase investment in R&D, the deduction for current R&D expenditure will be increased from 100 per cent to 150 per cent. In addition, the depreciation allowance for capital expenditure will be increased from the current 40:20:20:20 to 50:30:20. Some modification of the R&D definition may be required as part of these amendments.

Intergovernmental coordination

Strengthening the financial position of municipalities

Zero-rating of municipal property rates

VAT zero-rating for municipal property rates

It is proposed to zero-rate municipal property rates for VAT purposes for tax periods commencing on or after 1 July 2006. This will result in a loss of revenue to the fiscus and additional revenue of approximately R1 billion for category A and B municipalities for the municipal fiscal year 2006/07. This proposal will also help to simplify municipalities' accounting and tax records.

Income tax treatment of parastatals and municipalities

Realignment of tax framework for parastatals

The tax system lacks a uniform framework for parastatals, municipalities and municipal entities. Taxable versus tax-exempt status is often dealt with on a case-by-case basis. In view of these shortcomings, the income tax status of these entities will be realigned in 2006 or 2007. An immediate issue to be considered is the income tax status of industrial development zone management companies and regional electricity distributors, both of which are central to key government initiatives.

VAT treatment of appropriations and grants

Government is completing its three-year effort to clarify the VAT treatment of appropriations and grants at the national level. The next step in this process is to provide greater clarity at the municipal level. Attention will focus on grants by national and provincial governments to municipalities, and on grants by municipalities to municipal entities. As a general rule, grants to municipalities should be zero-rated, with some exceptions (e.g. public bus transportation). Some of these changes may be retroactive to eliminate VAT assessments already raised.

Diamond export levy

A measure to support domestic beneficiation

A proposed diamond export levy aims to reinforce regulatory measures to ensure an adequate supply of rough diamonds for the local market, thereby promoting domestic beneficiation. The levy will be designed to provide credits for local sales that would act as an offset in the determination of the export levy.

Synthetic fuels

The synthetic fuel industry accounts for about 35 per cent of domestic liquid petroleum sales. This industry developed with extensive government support. From 1979 to 1995, the Equalisation Fund, created under the Central Energy Fund Act (1977), gave tariff protection to the industry (Sasol and Mossgas, which is now PetroSA). Funds were collected from motorists using the fuel levy to compensate the industry in times of low oil prices. According to an agreement with the previous government, when the oil price rose above US$28,50 a barrel, Sasol paid 25 per cent of revenues over that level into the Equalisation Fund. This was effective until 1995.

Investigate a windfall tax on additional income by the synthetic fuel industry

Given the price determination process (import parity pricing and partial regulation), the industry is in a position to reap substantial economic rents when crude oil prices are high. Such windfall gains should be shared with the public. A task force will accordingly be appointed to examine this issue for possible legislative resolution.

Mining and other environmental rehabilitation funds

Rehabilitation funds address long-term environmental concerns and aim to ensure that adequate environmental protection is maintained when a business closes. Tax relief is granted to mining enterprises that make financial provision for rehabilitation in the form of trust funds. This relief entails a deduction for reserves as well as the tax-free build-up of those reserves. Government has received requests from the industry to consider the use of insurance products to facilitate rehabilitation of defunct mines. To provide the industry with greater flexibility, the current income tax exemption for mining rehabilitation trusts will be extended to insurance products and other instruments dedicated solely to rehabilitation funding.

Legal changes are expected that will extend environmental rehabilitation requirements to sectors other than mining. The current tax incentive for rehabilitation will be extended as required.

Consumption taxes

Excise duties: alcoholic beverages

Excise duty on wine, beer and other alcoholic beverages increases

Excise duties on sparkling wine, unfortified wine, fortified wine, malt beer, alcoholic fruit beverages and spirits increase by 20 per cent, 12,5 per cent, 9,4 per cent, 9 per cent, 9 per cent and 9,5 per cent respectively with immediate effect. These adjustments are expected to raise about R725 million in additional revenue, and are in accordance with the policy decision to maintain a total tax burden (excise duties plus VAT) of 23, 33 and 43 per cent on wine products, malt beer and spirits respectively. No increase in the excise duty on traditional beer is proposed.

Table 4.9 Changes in specific excise duties, 2006/07

Product	Current excise duty rate	Proposed excise duty rate	Change in excise duties Nominal	Real
Malt beer	R33,65 / litre of absolute alcohol (57,20c / average 340ml can)	R36,68 / litre of absolute alcohol (62,35c / average 340ml can)	9,0%	4,8%
Traditional African beer	7,82c / litre	7,82c / litre	0,0%	-4,2%
Traditional African beer powder	34,70c / kg	34,70c / kg	0,0%	-4,2%
Unfortified wine	140,52c / litre	158,09c / litre	12,5%	8,3%
Fortified wine	263,14c/ litre	287,88c/ litre	9,4%	5,2%
Sparkling wine	387,99c/ litre	465,58c/ litre	20,0%	15,8%
Ciders and alcoholic fruit beverages	168,24c / litre (57,20c / average 340 ml can)	183.38c / litre (62,35c / average 340 ml can)	9,0%	4,8%
Spirits	R50,42 / litre of absolute alcohol (R16,26 / 750 ml bottle)	R55,21 / litre of absolute alcohol (R17,80 / 750 ml bottle)	9,5%	5,3%
Cigarettes	504,44c / 20 cigarettes	556,08c / 20 cigarettes	10,2%	6,0%
Cigarette tobacco	747,30c / 50g	782,47c / 50g	4,7%	0,5%
Pipe tobacco	190,60c / 25g	206,55c / 25g	8,3%	4,1%
Cigars	R32,59/ 23g	R34,16/ 23g	4,8%	0,6%

Excise duties: tobacco products

Excise duty on tobacco products increased

The excise duties on cigarettes, cigarette tobacco, pipe tobacco and cigars will increase by 10,2 per cent, 4,7 per cent, 8,3 per cent and 4,8 per cent respectively with immediate effect and are expected to raise about R645 million in additional revenue. These increases are in line with the policy decision to maintain a total tax burden (excise duties plus VAT) of 52 per cent on all categories of tobacco products.

Given that cigars are significantly more expensive than other categories of tobacco products, the total tax burden on cigars as a percentage of the retail-selling price will be reviewed. The method of calculating the total tax burden on cigarette tobacco will also be reviewed.

Ad valorem excise duties

A number of products on the list of items subject to *ad valorem* excise duties no longer exist or generate very little revenue. In the case of some items, such as fax machines, the tax is no longer appropriate. It is proposed to abolish duties on these products effective from 1 April 2006 as indicated in Annexure C.

Fuel taxes

General fuel levy

No increase in the general fuel levy for 2006/07

Over the past several years government has limited increases in the general fuel levy to a level at or below the expected annual inflation rate. Considering the revenue overrun in 2005/06 and the impact of higher world oil prices on the local prices of petrol and diesel, no increase in the general fuel levy is proposed for 2006/07.

Road Accident Fund levy

RAF fuel levy to increase by 5 cents

The value of claims lodged with the Road Accident Fund (RAF) increased significantly in recent years, mostly as a result of an increase in the number of car accidents. The RAF Amendment Act will limit claims for future loss of income and general damages to reduce the fund's exposure in the future, but the anticipated savings will not be realised until 2007/08.

The RAF fuel levy is to increase by 5 cents per litre effective 5 April 2006 to allow the fund to settle its expected road accident claims for 2006/07, while savings resulting from the legislative amendments will allow it to reduce its claims backlog over time.

Table 4.10 Total combined fuel levy on leaded petrol and diesel, 2004/05 – 2006/07

	2004/05		2005/06		2006/07	
	93 Octane petrol	Diesel	93 Octane petrol	Diesel	93 Octane petrol	Diesel
General fuel levy	111,0	95,0	116,0	100,0	116,0	100,0
Road Accident Fund levy	26,5	26,5	31,5	31,5	36,5	36,5
Customs and Excise levy	4,0	4,0	4,0	4,0	4,0	4,0
Equalization Fund levy	–	–	–	–	–	–
Illuminating Paraffin marker	–	0,2	–	0,2	–	0,2
Total	**141,5**	**125,7**	**151,5**	**135,7**	**156,5**	**140,7**
Pump price: Gauteng (as in February)[1]	408,0	347,5	420,0	384,5	550,0	517,8
Taxes as % of pump price	*34,7%*	*36,2%*	*36,1%*	*35,3%*	*28,5%*	*27,2%*

1. Diesel (0,05% sulphur) wholesale price (retail price not regulated).

Biodiesel fuel tax rebate

Biodiesel fuel tax rebate at 40 per cent of the general fuel levy

As announced in 2002, biodiesel will in future be classified as a fuel levy good, making it zero-rated for VAT and subject to fuel taxes. However, the original proposed rebate of 30 per cent on the general fuel levy was based on the limited information about production costs available in 2002. A review of international practice indicates that to support the industry the rebate should be set at 40 per cent of the general fuel levy. Given the emerging character of the industry, this is expected to have a limited effect on the fiscus.

Extension of diesel refund scheme to peak power generation

In response to capacity constraints in electricity generation, four diesel-powered electricity generation plants are planned. Eskom will build two plants, and two independent power producers will build the others. Diesel power plants with a capacity of more than 200 MW will receive a full refund of the general fuel levy and the RAF levy.

Large diesel power plants to receive a full refund of general fuel levy and RAF levy

Policy coherence: removal of anomalies

Public benefit organisations

Since 2001, government has continued to adjust tax rules for public benefit organisations (PBOs). Further proposed adjustments include:

- Refining the list of tax-exempt PBO activities
- Exempting foreign PBOs operating in South Africa
- Extending deductible donation status for PBOs committed to "Conservation, Environment & Animal Welfare"
- The alignment of the statutory tax rates for the taxable trading activities of all PBOs irrespective of their legal form
- Relaxing the rules for permissible investments
- Streamlining the dual registration process.

South African organisations receiving development assistance

Some South African organisations receive development assistance pursuant to international agreements under which their management is accountable to government. International organisations offering such assistance often seek to ensure that aspects of these assistance packages remain tax-exempt. Although the National Treasury is part of the overall process, the Minister of Finance does not have the legislative authority to grant full or partial income tax exemption in these cases. This legislative weakness will be corrected.

Recreational clubs

Recreational clubs operating for the benefit of their members are tax-exempt and subject to few restrictions. Some clubs appear to be claiming exemption irrespective of whether their amenities are used by the general public or by their members. Furthermore, some clubs are starting to conduct more trading activities to raise funds beyond membership contributions. As a result, the taxation of recreational clubs will be reviewed.

Tax treatment of recreational clubs to be reviewed

VAT place of supply

The VAT treatment of internationally traded services presents challenges to tax authorities worldwide. Government seeks to provide greater clarity in this area, especially for telecommunications. Due consideration will be given to the current work of the OECD concerning VAT treatment of internationally traded services.

Measures to enhance tax administration

Corporate income tax

SARS to modernise corporate income tax administration

SARS plans to modernise the corporate income tax administrative system. A move to a full self-assessment system, which will provide faster turnaround times and greater certainty, is being explored. The system would be reliant on a number of building blocks, including greater reliance on taxpayer integrity, an advance rulings system to resolve cases of doubt, more clearly defined disclosure requirements, a shift from returns to be assessed to returns of tax owing, e-filing, more consistent interest charges, enhanced risk identification, and well-defined penalty systems for non-disclosure and under-declarations of income.

Advance tax ruling system to be brought into operation

The advance tax ruling system will be brought into operation on a phased basis starting in 2006. A managed pilot programme of e-filing for large company income tax returns will also commence. Amendments will be proposed to align the provisional tax system for all taxpayers more closely with current incomes, rather than historical "basic amounts" for years of assessment commencing on or after 1 March 2007.

Provisions relating to interest paid and received will be reviewed to remove discretions and the inconsistent bases of calculation. The current STC dividend cycle system will be reviewed and additional guidance with regard to penalties to be imposed for non-disclosure and under-declaration of income will be issued.

General anti-avoidance rule

Government received various comments in response to the discussion paper on the general anti-avoidance rule released by SARS in November 2005. These comments will be evaluated before legislation is finalised in the latter half of 2006.

Personal income tax

Extension of e-filing to certain individuals

The record 3,7 million individual income tax returns filed in 2005 is evidence of a growing culture of tax compliance. To help individuals file their returns and to speed up processing, some e-filing for individual income tax returns will be introduced by June 2006. SARS will select employers who provide employees' tax information electronically and will make e-filing available to those employers for employees who earn only a basic salary or wage.

The introduction of e-filing for individuals will be accompanied by the matching of information from third parties, such as employers, against information provided in returns.