21 February 2018

Budget 2018/19: Summary of tax changes impacting investors

While South African taxpayers have again been presented with an austerity budget, the bulk of the additional tax load announced this year will fall on consumption rather than investment activities. This is as a result of a 1 percentage point increase in the VAT rate to 15%, which is anticipated to garner two-thirds of the additional R28 billion of tax revenue that Government is looking to raise in 2018/9. This can be contrasted with Budget 2017/18 in which 80% of additional taxes were raised through increases in income, capital gains and dividend taxes.

The marginal personal income tax rate, capital gains tax inclusion rate and dividend tax rate were all left unchanged this year. However, limited inflation relief was granted, meaning that nearly all tax payers will pay slightly higher effective tax rates in the new fiscal year.

The proposals made by the Davis Tax Committee relating to estate duty and donations tax were at least partially implemented, with a new two-structure estate duty rate of 20% or 25%, depending on whether the estate is smaller or larger than R30 million. Further information on the technical aspects of this proposal is still outstanding.

Tax allowances for investors

As a reminder, investors qualify for the following investment-related tax breaks:

- Individuals pay a lower marginal tax rate on capital gains (18%) and dividend income (20%) compared to interest, rental and salary income (45%). This means that investors not using tax-advantaged vehicles are, all other things being equal, better off holding equities in their portfolios than other assets.

- The tax-advantaged contribution to a tax-free investment account remains at R33 000 per year. At present, this arguably remains the best tax break available to individual investors with long time horizons. While you use after-tax money to invest in a tax-free investment, all income and growth earned from the underlying funds are tax free, and all proceeds at the time of withdrawal will also be untaxed. Further, there are no investment restrictions within tax-free investments. Just be mindful that any over-contribution (in excess of the annual R33 000 limit) will be taxed very punitively.

- The tax-advantaged contribution to retirement funds also remain attractive. You can contribute the lower of 27.5% of taxable income (excluding retirement benefits) or R350 000 annually to retirement funds, and deduct this amount from your taxable income in the year of contribution (unchanged). Your capital and reinvested income will grow tax free as long as it remains in the retirement fund, and you will only pay tax on the way out when you start to withdraw from your retirement fund (at the then-prevailing tax rate). Your underlying investments must comply with regulation 28, which sets a limit on the level of exposure you can have to equity and offshore assets.

- The general interest exemption of R23 800 for investors under 65, and R34 500 for investors over 65 remains unchanged. At the current yield of around 8% on managed income funds such as Coronation Strategic Income and Coronation Money Market, this means that you can invest R300 000 if you are under 65 or R430 000 if you are over 65 before starting to pay tax on interest earned.

- The Annual capital gains exclusion of the first R40 000 gain remains unchanged. This exclusion makes it more efficient to stagger the realisation of capital gains over different tax years.

- Endowment policies also remain attractive for certain long-term investors. Individual investors in these investment policies currently pay effective tax rates of 30% on rental income, 20% on dividend income and 12% on capital gains.

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