The impact of tax policy changes on the personal income tax burden in South Africa

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The impact of tax policy changes on the personal income tax burden in South Africa

Wynonna Steyn[1] and Yolandé Jordaan[1]

Abstract

A tax micro simulation model populated with the relevant data to simulate tax policy changes is a valuable tool to measure the net impact of various tax policy changes individually or simultaneously. The goals of tax policy changes can be assessed by the tax payable outcome of the model before and after applying the relevant tax policy changes. It should, however, be noted that a tax micro simulation model is constrained by the static nature of these models and the timeliness of comprehensive data.

South Africa is one of the most inequitable societies in the world with a Gini coefficient in 2009 of 63.14 according to the World Bank Development Research Group. This paper illustrates the use of micro simulation methodology to model the shift in the tax burden within the personal income taxpayer population as a result of changes to the personal income tax regime announced by the Minister of Finance in the National Budgets over the past three years. The stated aim of the 2012 Budget proposed tax policy changes was to promote a more equitable, both in vertical and horizontal terms, tax system. The changes introduced since the chosen base year of 2008/09 include an analysis of the inclusion of previously exempt income, as well as the limitations on and/or abolishment of the various tax deductions.

The main findings of the analysis are that the tax burden as result of the announcements in the 2012 Budget across all the income groups increased, but the percentage increases differ for each income group. The R5 million above income group tax liability increases on average by 5.22 percent followed by a 5 percent increase for taxpayers in the R300 000 to R500 000 income group. The average increase for taxpayers up to the R200 000 taxable income group is 3 percent. The total average increase in the tax burden across all income groups is close to 4 percent.

The distribution of tax payable by income group as a percentage of total tax payable before and after the changes in tax policy is a measurement of the impact of the proposed changes in tax policy on the progressiveness of the personal income tax system. The percentage tax payable by taxpayers up to the R150 000 taxable income group is only marginally affected by the changes in tax policy. However, a noticeably decrease in the percentage tax payable in the R150 000 to R300 000 income group is followed by a relatively significant increase in the percentage tax payable for income groups above R300 000.

This is a first in a series of papers and further analysis will focus on the implications for the economy in terms of changes in the income distribution of the after-policy-changes and the subsequent shifts in consumption and savings.

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Keywords: micro-simulation, tax revenue base, personal income tax, tax policy.

[1] Revenue Planning, Analysis and Reporting, SARS, Pretoria.

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1. Introduction

The distribution of income and wealth and the redistribution thereof is core to government policy debates. South Africa has a wide dispersion between the rich and the poor and policies aim to reduce inequality need to be analysed and measured in terms of the stated goals.

The South African Gini coefficient is calculated to be 0.70 when income from work, pensions from previous employment and annuities from own investment is considered. When adding social grants income the Gini coefficient declines to 0.65. Close to 15 percent of budgeted expenditure is allocated to enhance social protection. By further including free water, free sanitation, free electricity and other free services, the Gini coefficient declines further to 0.61. By adjusting incomes for direct personal income tax, the Gini coefficient declines to 0.59 (Bosch and Rossouw 2010).

The Institute for Future Research[2] asserted that South Africa has become one of the most redistributive societies in the world. The rationale for a redistribution programme is compelling:

- structurally high unemployment,
- a 40 percent poverty rate (almost 20 million South Africans have to survive on R388 a month or less in constant 2008 terms), and
- possibly the most uneven income distribution in the world.

The personal income tax system in South Africa is progressive to ensure a more equitable system of taxation whereby persons that earn more income pay a higher average rate of tax to ensure vertical equity. Tax policy changes alter the vertical and horizontal equity of the tax system. Following the dawn of democracy in 1994, the South Africa government embarked on reforms to ensure a more equitable tax system. The 2012 Budget tax proposals are primarily aimed at ensuring a more equitable and efficient tax system with proposals that are geared to firstly, tax the different classes of income at a similar rate, secondly, to minimise the unequal tax impact of tax deductions at different marginal tax rates as opposed to tax credits and lastly to limit the tax that can be deducted of certain important tax deductions.

In the 2012 budget the established trend of providing personal income tax relief was maintained with the announcement of R9.5 billion for thresholds and brackets adjustments. It is estimated that about 54 percent of this relief will accrue to individuals with taxable income less than R260 000 per annum. Moreover, the replacement of the secondary corporate tax by the newly created dividend withholding tax percentage and the increase in capital gains tax will largely increase the tax burden of the more affluent members of society.

The aim of this paper is to quantify and analyse the impact of the various 2012 Budget tax proposals on the tax liability by each income group.

2. Review of personal income tax reform

Nyamongo and Schoeman (2007) identified the first phase of reform to cover the period from 1994 to 1999 which consisted of policy reviews, investigations and reports produced mainly by the Katz Commission (1994). The findings resulted in numerous tax amendments. With regard to personal

[2] Budget Speech 2012: Orthodoxy at all costs

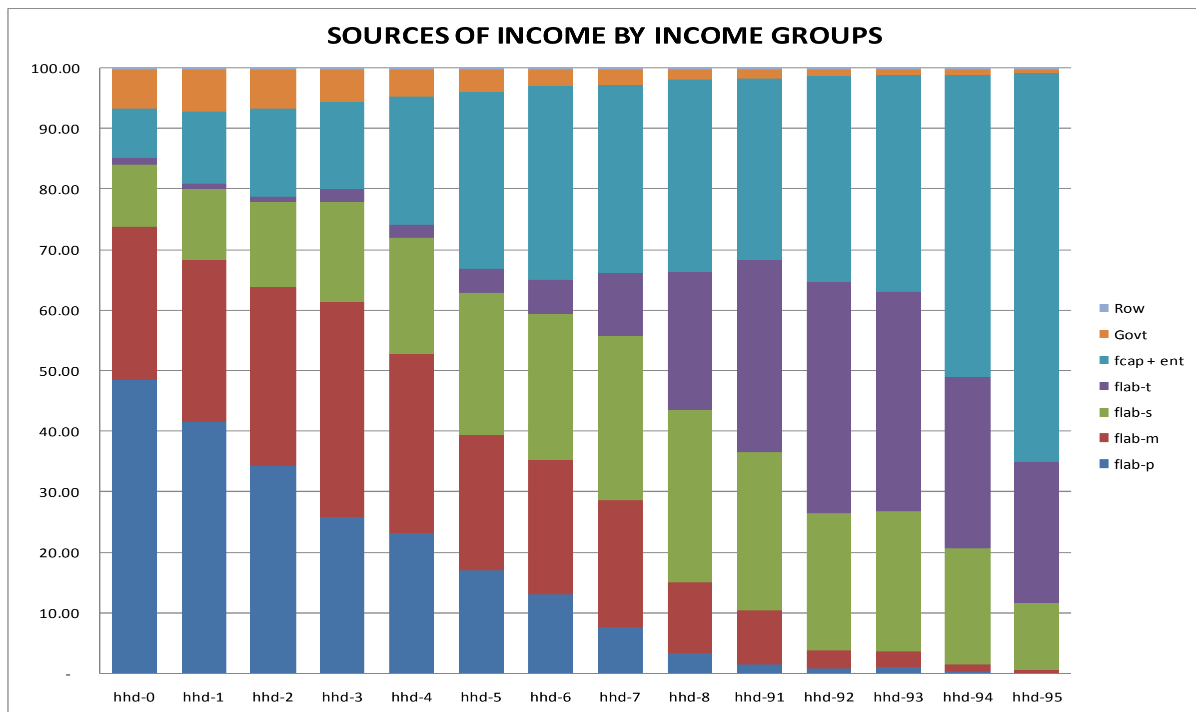
income tax (PIT), the focus was on getting the overall framework in place by considering the appropriateness of individual taxation as opposed to joint taxation and married versus unmarried taxation, tax thresholds, income brackets, tax rates, degrees of progressivity, fiscal drag and income tax exemptions for charitable, religious and educational institutions. The second phase of reform, which covers the period 2000 onwards, focused on broadening the tax base and adapting the tax system to conform to international tax laws. Fundamental changes in phase two culminated in changing from the "source-based" to "residence-based" system in 2001 and the introduction of capital gains taxation to extend the tax base and enhance the equity of the tax system. By 2002 the number of brackets had been reduced to six, the child rebate was removed and the primary rebate and brackets were adjusted annually for inflation.

Perold, Greyling and Bonga-Bonga (2009) in a presentation on the history of taxation in South Africa from 1904 to 2008, showed that the South Africa's tax reforms have changed the tax base and progressive rate structure thereby at increasing compliance and promoting simplicity.

3. Income distribution in South Africa

The sources of income by income groups as illustrated in Figure 1 are classified as labour income – primary (flab-p), middle level (flab-m), secondary (flab-s), and tertiary (flab-t), capital and enterprise income (fcap+ent), transfers from government (Govt) and income from the rest of the world (Row) by income group.

Figure 1: Sources of income per decile with last decile disaggregated



Source: 2009 SAM StatsSA

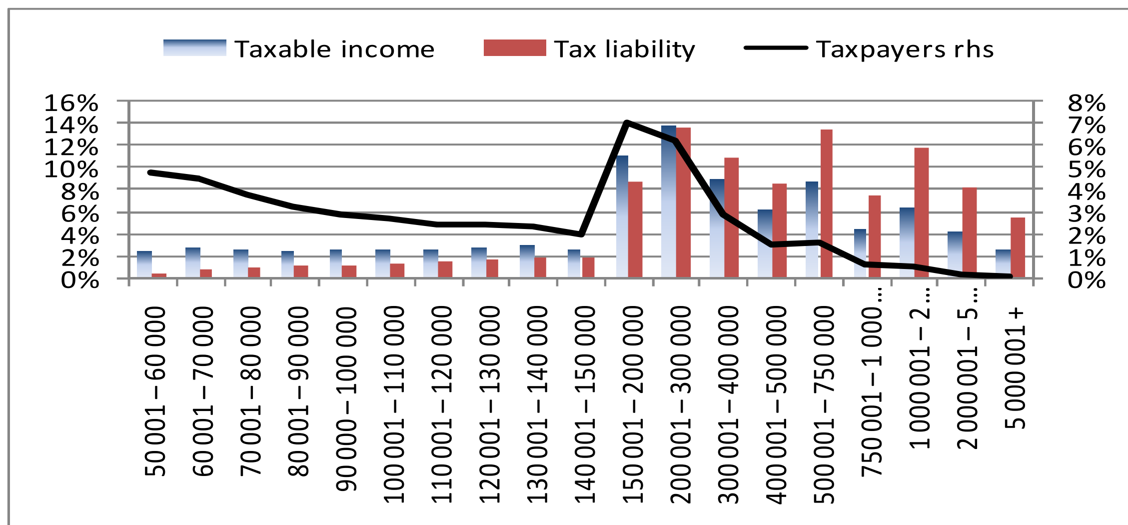
Capital and enterprise income represents a relatively large portion of the income for high-income households as oppose to labour income for the low- to middle-income levels whilst government transfers constitute the major income for lower level income groups.

4. Distribution of taxpayers, taxable income and tax liability

The distributional analysis of the personal income tax system of taxpayers, taxable income and tax liability is shown in Figure 2 and is based on data for the 2008/09 tax year. Taxpayers only become liable for paying personal income tax when their taxable income exceeds the minimum tax threshold. In 2008/09 the minimum tax threshold for persons below the age of 65 years was at R46 000 and for persons aged 65 years and older the threshold was at R74 000. Taxpayers with a taxable income above the minimum tax threshold but below the Standard Income Tax on Employees (SITE) income level of R60 000 do pay tax but is not compelled to register as a filer for personal income tax.

It is estimated that the number of earners under the minimum tax threshold is close to 50 percent of the total personal income tax population. The concentration of taxable income and tax liability is in the R150 000 to R400 000 income group with the concentration of taxpayers mainly between the R150 000 to R300 000 income group.

Figure 2: Distribution of taxpayers, taxable income and tax liability as % of total in 2008/09



Source: SARS PITSIM

The distribution of taxpayers, taxable income and tax liability of assessed taxpayers in 2008/09 is summarised in Table 1. The number of assessed taxpayers with positive taxable income totals 3.96 million, with total taxable income of R799.8 billion. Total tax assessed amount to R168.1 billion which equals an average tax rate of 21 percent.

The unequal distribution of assessed taxpayers, taxable income and tax liability is clear. The number of taxpayers in the above R400 000 income groups totals only 9.1 percent of the total number of assessed taxpayers but contributes 53.5 percent to the total tax assessed in 2008/09.

Table 1: Distribution of assessed taxpayers in 2008/09

Taxable income group	Number of assessed taxpayers	As % of total assessed taxpayers	Taxable income	As % of total assessed taxable income	Tax assessed	As % of total tax assessed
1 – 60 000	579,987	14.6%	20,326	2.6%	244	0.1%
60 001 – 120 000	1,055,363	26.6%	95,881	12.3%	8,140	4.8%
120 001 – 400 000	1,967,299	49.6%	398,174	51.1%	69,718	41.5%
400 001 – 5 000 001 +	361,849	9.1%	285,463	36.6%	89,976	53.5%
Total	**3,964,498**	**100.0%**	**779,947**	**100.0%**	**168,084**	**100.0%**

Source: 2011 Tax Statistics

5. Tax Micro-Simulation Model methodology

The SARS Personal Income Tax Micro-Simulation Model (PITSIM) was used to simulate the changes in the tax burden of the different income groups by calculating the tax liability impact before and after the proposed tax policy changes in tax exempt income and tax deductions.

The model is based on the complete SARS individual taxpayer population. The model estimates the changes in an individual's taxable income and tax liability given an adjustment in the personal income tax system using both individual level survey data as well as data on individuals as pertaining to the systems at SARS. Based on simulated individual responses, the model provides aggregate measures of individual responses across the population. The aggregated effects are then identified for subgroups of the population stratified by income and demographic characteristics, such as age.

Micro simulation models have certain limitations such as the over-simplification of assumptions that it might require, for instance tax micro simulation models that need to calculate the tax liability on taxable income might not be able to capture all the detail complex calculations of the tax code based on the information available. Secondly, problems with micro-simulation models pertain not to the quality of the models themselves, but rather to data inadequacies. Micro data is cumbersome and there are generally long lags between data collection and the release of said data. As a result of scheduling of provisional tax submissions, there is a trade–off between the completeness of data or the most current available data. The most complete PIT dataset is for 2008/09 fiscal year.

Tax changes and the proposed tax changes are therefore based on the 2008/09 tax year. It is the most complete data set in terms of assessed taxpayers. In the 2011 Tax Statistics it is shown that the assessment rate for individuals for the 2008/09 tax year was 93.4 percent at the time of the publication. The data for this year corresponds with the base year data of the SARS PITSIM. After analysing the average shift in taxable income, the changes were incorporated into the SARS PITSIM to calculate the total change in the tax burden by income group.

6. 2012 Budget: Personal income tax equity enhancement proposals

"The 2012/13 Budget may well be known as the 'Robin Hood' of budgets"
Marteen Michau, Head: Fiduciary and Tax, Sanlam Private Investments

Tax policy changes to broaden the tax base and improve the perceived fairness or equity of the tax system intensified over the last couple of years. The main tax policy changes that are costed and announced and or proposed in the 2012 Budget are listed below together with the micro simulation model outcome of the change in the tax burden by income group.

6.1 Exempt income

The average effective personal income tax rate is calculated to be about 20 percent of taxable income. High income groups tend to receive a higher percentage of their income from capital income that is taxed at a lower rate than labour income. The impact of changes to capital income, namely, dividends, capital and interest income on exempt income is analysed using micro simulation model techniques. Below is a summary of the policy changes proposed in the 2012 Budget.

6.1.1 Increase in the effective capital gains tax rates

Capital gains tax was introduced in 2001 and with this reform the integrity and progressive nature of the tax system was improved. To further enhance equity, the effective capital gains rates were increased as with effect from 1 March 2012. The inclusion rate for individuals and special trusts increased from 25 percent to 33.3 percent, thereby increasing the maximum effective capital gains tax rate from 10 percent to 13.3 percent. To limit the impact of capital gains taxation on middle-income households, the exemption thresholds for individual capital gains and for primary residences were adjusted for inflation. The following exemptions for individual capital gains are increased from 1 March 2012:

- The annual exclusion from R20 000 to R30 000
- The exclusion amount on death from R200 000 to R300 000
- The primary residence exclusion from R1.5 million to R2 million
- The exclusion amount on the disposal of a small business when a person is over the age of 55 years from R900 000 to R1.5 million
- The maximum market value of assets allowed for a small business disposal for business owners over 55 years increases from R5 million to R10 million.

Table 2 shows the capital gains and the tax thereon for taxpayers per taxable income group. In the 2008/09 tax year 60 312 taxpayers declared taxable capital gains totalling R8.1 billion and the tax thereon was calculated to be R2.9 billion. The distribution of capital gains is concentrated in the taxable income group above R400 000 per annum; close to 82 percent of the tax on capital gains is collected from this group.

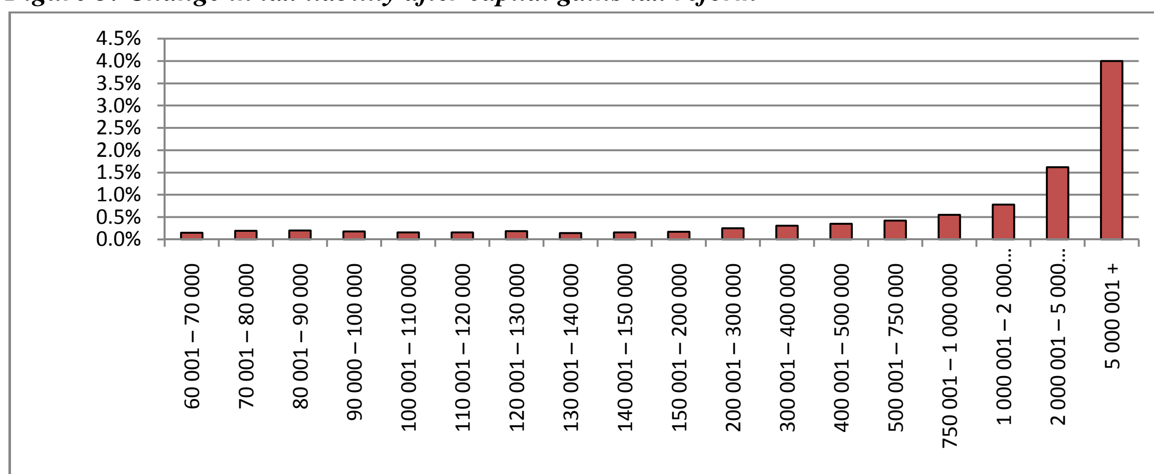
Table 2: Taxable capital gains

Taxable income group	Number of taxpayers	Capital gains (R million)	As % of total	Total tax payable	As % of total
<0	3,830	427	5.3%	76,844,501	2.7%
1 – 60 000	8,611	169	2.1%	30,364,203	1.0%
60 001 – 120 000	9,108	279	3.4%	50,194,373	1.7%
120 001 – 400 000	21,008	1,249	15.5%	364,528,427	12.6%
400 001 – 5 000 001 +	17,755	5,960	73.7%	2,377,341,585	82.0%
Total	**60,312**	**8,083**	**100%**	**2,899,273,088**	**100%**

Source: 2011 Tax Statistics

Figure 3 illustrates taxpayers with taxable income above R2 million are to experience the highest increase in their tax burden after the tax policy changes due to receiving a higher percentage of their income from capital.

Figure 3: Change in tax liability after capital gains tax reform



Source: 2009 PITSIM

6.1.2 Exempt interest income - Encouraging household savings

The current tax-free interest income thresholds are R22 800 for individuals below 65 years and R33 000 for taxpayers 65 years and older. As stated in the 2012 Budget, to provide more visible and effective incentives as alternatives to the current tax-free interest-income caps, tax-preferred savings and investment accounts are proposed. It is proposed that returns generated within these savings and investment vehicles and withdrawals be tax exempt. Aggregated annual contributions could be limited to R30 000 per year per taxpayer, with a lifetime limit of R500 000, to ensure, as stated, that high net worth individuals do not benefit disproportionately.

In the 2008/09 tax year, 274 188 taxpayers declared taxable local interest income of R18.9 billion. It is calculated that close to 92 percent of these taxpayers were younger than 65 years.

The distribution of taxable interest is concentrated in the taxable income group above R400 000 per annum as close to 45 percent of local interest was declared by 21.6 percent of taxpayers in this group. However, the greatest percentage of taxpayers earning taxable interest is in the R120 000 to R400 000 taxable income group and those younger than 65 years.

Table 3: Taxable local interest

Taxable income	Number of taxpayers	As % of total	Local interest (R million)	As % of total	Taxpayers < 65 years	As % of total	Taxpayers => 65 years	As % of total
<0	11,352	4.1%	917	4.8%	8,859	3.5%	2,493	10.8%
1 – 60 000	50,391	18.4%	1,260	6.7%	42,162	16.8%	8,229	35.7%
60 001 – 120 000	52,387	19.1%	2,131	11.3%	47,370	18.9%	5,017	21.8%
120 001 – 400 000	100,738	36.7%	6,106	32.3%	96,179	38.3%	4,559	19.8%
400 001 – 5 000 001 +	59,320	21.6%	8,507	45.0%	56,561	22.5%	2,759	12.0%
Total	**274,188**	**100%**	**18,920**	**100%**	**251,130**	**100%**	**23,058**	**100%**

Source: 2011 Tax Statistics

The current tax-free interest distribution is shown in Table 4. It is calculated that the value of the total interest exempted is about R6.5 billion. Close to 88 percent of the total interest exempted is claimed by taxpayers younger than 65 years. The majority of taxpayers 65 years and older, namely 35.7 percent, who is claiming tax-free local interest, have a taxable income less than R60 000 per annum.

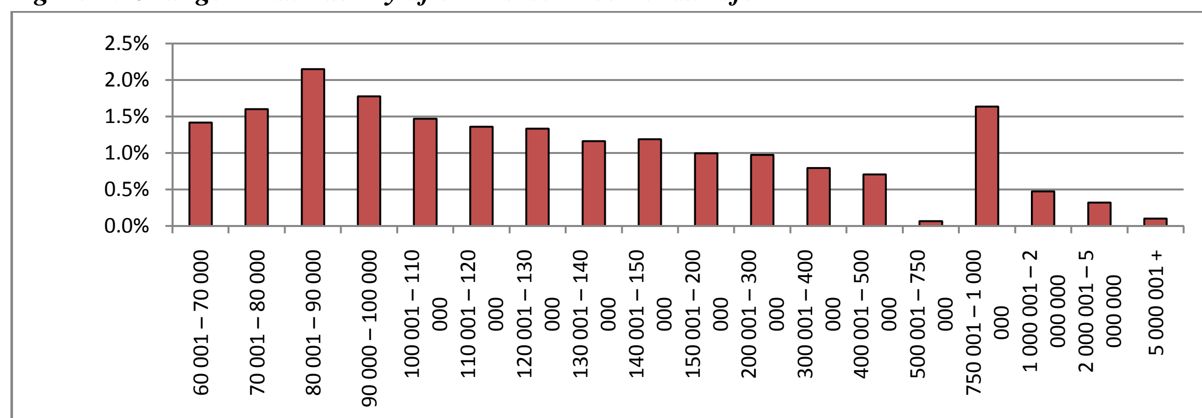
Table 4: Tax free local interest per age group

Taxable income	Tax-free local interest R million< 65 years	As % of total	Tax-free local interest R million=> 65 years	As % of total
<0	202	3.5%	82	10.8%
1 – 60 000	961	16.8%	272	35.7%
60 001 – 120 000	1,080	18.9%	166	21.8%
120 001 – 400 000	2,193	38.3%	150	19.8%
400 001 – 5 000 001 +	1,290	22.5%	91	12.0%
Total	**5,726**	**100%**	**761**	**100%**

Source: 2011 Tax Statistics

Figure 4 illustrates that the elimination of the current tax-free interest income thresholds will increase the tax liability of all taxpayers receiving interest income. The highest percentage increase will be for taxpayers in the R80 000 to R90 000 income group indicating the relatively high reliance on fixed income by this income group as a percentage of their taxable income.

Figure 4: Change in tax liability after interest income tax reform



Source: 2009 PITSIM

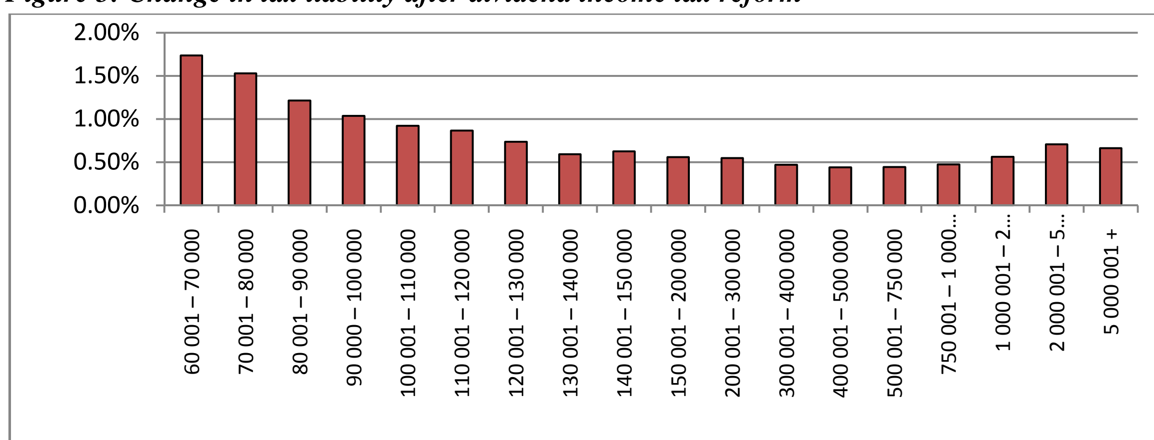
6.1.3 Implementation of a dividend withholding tax

It is stated in the 2012 Budget that high-income individuals tend to receive a larger portion of their income in the form of dividends and capital gains. A new dividend withholding tax regime was due to come in effect on 1 April 2012, replacing the secondary tax on companies. Pension funds and PBO's that are exempt from income tax will benefit as they will receive their dividends tax free and foreigners in countries that have double taxation agreements with South Africa with no or lower maximum rates of tax on dividend income. It was proposed that the dividend withholding tax be increased by 5 percentage points from 10 percent to 15 percent as a measure to equalise the taxation of investment income closer to international benchmarks.

The change in the tax on dividend income on a shareholder level at a higher rate of 15 percent was modelled to be a rate change from 10 percent to 15 percent. Due to the lack of distributional data on dividend income the tax liability impact was calculated based on the assumption that the distribution is equal to that of interest income for illustrative purposes.

The increase in tax liability is shown in Figure 5. The highest increase in tax liability, close to 1.8 percent is to be experienced by low income earners based on the dividend income distribution assumption.

Figure 5: Change in tax liability after dividend income tax reform



Source: 2009 PITSIM

6.2 Personal income tax deductions

6.2.1 Changes to medical expense deductions

In the 2005 Budget it was announced that contributions to medical schemes are to be capped. The purpose was to shift the tax benefits in favour of the middle and lower-income groups. This new regime from 1 March 2006 introduced monthly monetary caps for tax-free medical scheme contributions at R500 for the first two dependants and R300 for each additional dependant. In addition, the threshold for individual tax deductible medical expenses was raised from 5 to 7.5 percent of taxable income.

In the 2012 Budget it was announced that the monthly deductions to medical schemes and for qualifying out-of-pocket expenses will be converted into tax credits. The reasoning is that a tax credit provides for more equitable tax relief, as the relative value of the relief does not increase as the marginal tax rate of the individual increases.

The monthly tax credits took effect from 1 March 2012 at R230 for the first two dependants and at R154 for each additional dependant. From this date onwards, where medical scheme contributions in excess of four times the total allowable tax credits plus out-of-pocket medical expenses combined exceed 7.5 percent of taxable income, the expenses may be claimed as a deduction against taxable income.

To ensure improved equity of the tax system and to help curb increases in health costs, additional out-of-pocket medical expenses will be converted into tax credits at a rate of 25 percent for taxpayers below 65 years with effect from 1 March 2014.

Taxpayers 65 years and older, and those with disabilities or with disabled dependants, can currently claim all medical contributions and out-of-pocket medical expenses as a deduction against their taxable income. Taxpayers 65 years and older and those with disabilities or disabled dependants will be able to convert all medical scheme contributions in excess of three times the total allowable tax credits plus out-of-pocket medical expenses into a tax credit but at a rate of 33.3 percent.

Table 5 indicates that a total number of 972 608 taxpayers younger than 65 years claimed deductions for medical contributions of R6.9 billion. The highest percentage at 60.3 percent of taxpayers is in the R120 000 to R400 000 taxable income group claiming 54.9 percent of the medical contribution deductions. In terms of total medical expenses allowed as a deduction, the highest percentage at 56.5 percent is again in the R120 000 to R400 000 taxable income group claiming 51.8 percent of the deductions.

Table 5: Medical contributions and medical expense deductions allowed for persons younger than 65 years

	Contributions				Total medical deductions allowed			
Taxable income group	**Number of taxpayers <65 years**	**As % of total**	**Contributions claimed R million**	**As % of total**	**Number of taxpayers < 65 years**	**As % of total**	**Total medical deduction allowed R million**	**As % of total**
<0	1,247	0.1%	12	0.2%	30,153	1.7%	885	5.3%
1 – 60 000	24,846	2.6%	85	1.2%	125,288	6.9%	1,602	9.5%
60 001 – 120 000	189,726	19.5%	902	13.1%	464,163	25.5%	3,786	22.5%
120 001 – 400 000	586,736	60.3%	3,793	54.9%	1,029,464	56.5%	8,707	51.8%
400 001 – 5 000 001 +	170,053	17.5%	2,116	30.6%	173,556	9.5%	1,842	10.9%
Total	**972,608**	**100%**	**6,908**	**100%**	**1,822,624**	**100%**	**16,822**	**100%**

Source: 2011 Tax Statistics

Table 6: Medical contributions and medical expense deductions allowed for persons 65 years and older

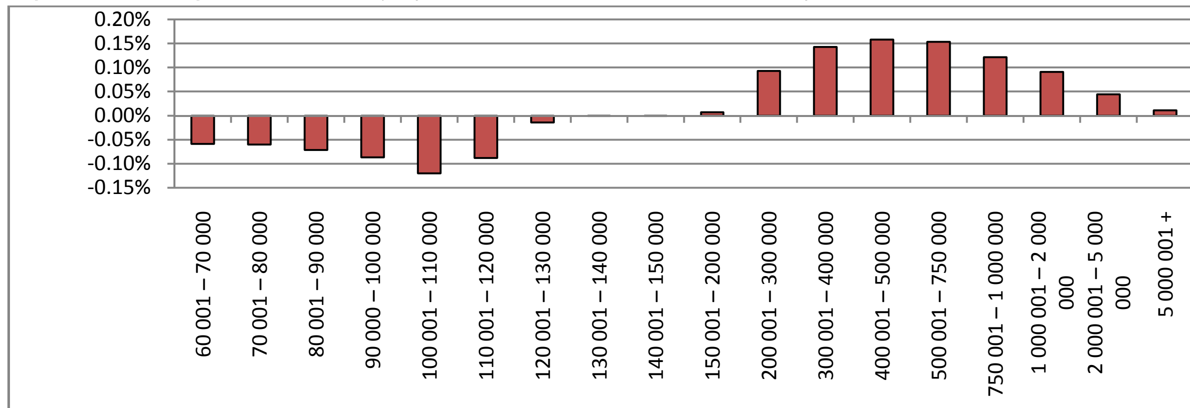
Taxable income group	Contributions				Total medical deductions allowed			
	Number of taxpayers =>65 years	As % of total	Contributions claimed R million	As % of total	Number of taxpayers => 65 years	As % of total	Total medical deduction allowed R million	As % of total
<0	16	0.7%	0.2	0.7%	13,197	6.4%	507	9.5%
1 – 60 000	198	8.5%	1.7	6.2%	44,263	21.5%	1,027	19.3%
60 001 – 120 000	445	19.2%	3.6	13.3%	65,819	31.9%	1,453	27.3%
120 001 – 400 000	1,107	47.7%	12.5	45.8%	69,695	33.8%	1,822	34.3%
400 001 – 5 000 001 +	555	23.9%	9.3	34.0%	13,310	6.5%	505	9.5%
Total	2,321	100%	27.2	100%	206,284	100%	5,314	100%

Source: 2011 Tax Statistics

Table 6 shows that the total number of 2 321 taxpayers who were 65 years and older claimed deductions for medical contributions of R27.2 million. The highest percentage at 47.7 percent of taxpayers claiming deductions is in the R120 000 to R400 000 taxable income group. Total medical deductions for persons 65 years and older of R5.3 billion was claimed by 206 284 taxpayers.

The contributions to medical schemes that were capped in 2006 resulted in a significant shift in the tax burden. Figure 6 shows the percentage increase in the tax burden after the change from a capped deduction system to a capped tax credit system. Taxpayers with a marginal tax rate less than 25 percent will experience a reduction in their tax liability and those taxpayers with marginal tax rates above 25 percent will experience an increase in their tax liability. The highest percentage increase is to be experienced by taxpayers in the R300 000 to R750 000 income groups.

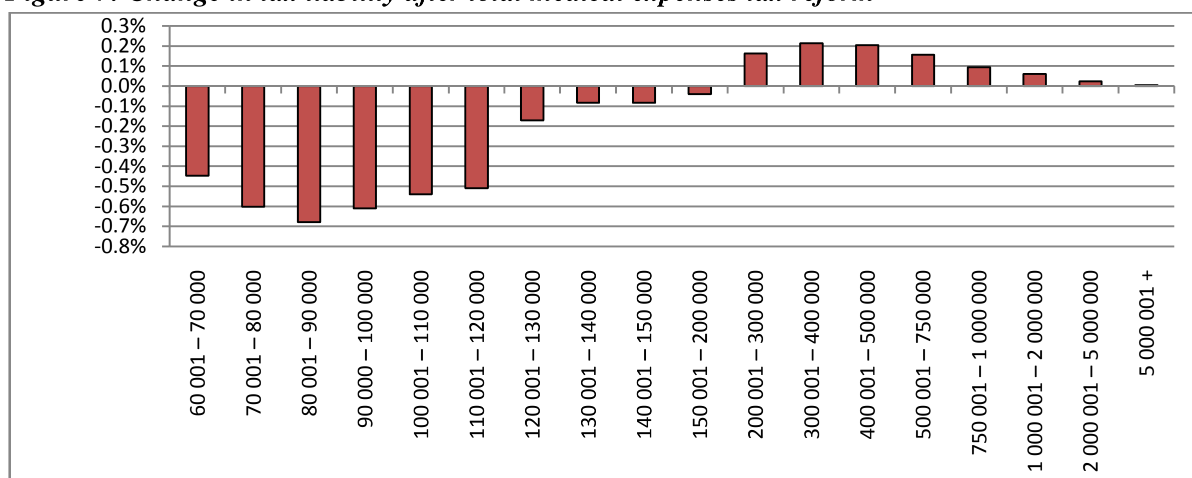
Figure 6: Change in tax liability after medical contributions tax reform



Source: 2009 PITSIM

Similarly, to the conversion of medical contributions from a deduction system to a tax credit system, an increase in tax liability is experienced by taxpayers in terms of total medical expenses when converted to a tax credit. Taxpayers above the R200 000 taxable income will experience an increase in their tax liability with the highest increases to be experienced by taxpayers in the R300 000 to R750 000 income groups as illustrated in Figure 7.

Figure 7: Change in tax liability after total medical expenses tax reform



Source: 2009 PITSIM

6.2.2 Changes to current pension fund and retirement annuity contribution deductions

Currently contributions to a pension fund are allowed as a deduction limited to a maximum of:

- R1 750
- 7.5 percent of remuneration from retirement-funding employment

Currently contributions to a retirement annuity fund are limited to a maximum of the greatest of:

- 15 percent of non retirement funding employment
- R3 500 less any amount allowed in terms of current pension contributions
- R1 750

Contributions by an employer to pension and provident funds that exceed 10 percent of the approved remuneration of an employee may be disallowed by the Commissioner. In practise the Commissioner allows a deduction of up to 20 percent of the approved remuneration of the employee.

As from 1 March 2014, individual taxpayer deductions for pension and retirement annuity contributions will be limited to 22.5 percent and 27.5 percent of taxable income, for those below the age of 45 years and equal or above the age of 45 years respectively, of the higher of employment or taxable income. Annual deductions will be limited to R250 000 and R300 000 for taxpayers below 45 years and equal or above 45 years, respectively. A minimum threshold of R20 000 will apply to allow low-income earners to contribute in excess of the prescribed percentages.

To improve the transparency and information flow of pension and provident fund contributions, employer contributions on behalf of employees will be deemed to be taxable fringe benefits in the hands of employees. All contributions up to the limit will be tax deductable.

Table 7 indicates that a total number of 1 773 554 taxpayers claimed deductions for pension contributions of close to R19.5 billion. The highest percentage at 61.1 percent of taxpayers is in the R120 000 to R400 000 taxable income group receiving 63 percent of the pension deductions allowed.

A total number of 1 228 494 taxpayers received deductions for retirement annuities (RA) of close to R10.2 billion. The highest percentage at 59.8 percent of taxpayers is in the R120 000 to R400 000

taxable income group claiming 45.3 percent of the pension deductions allowed. Persons in the above R400 000 income group that totals only 15.4 percent of taxpayers received 41.5 percent of the RA deductions. Retirement annuity contributions as a means to save for retirement are of high importance to high income individuals.

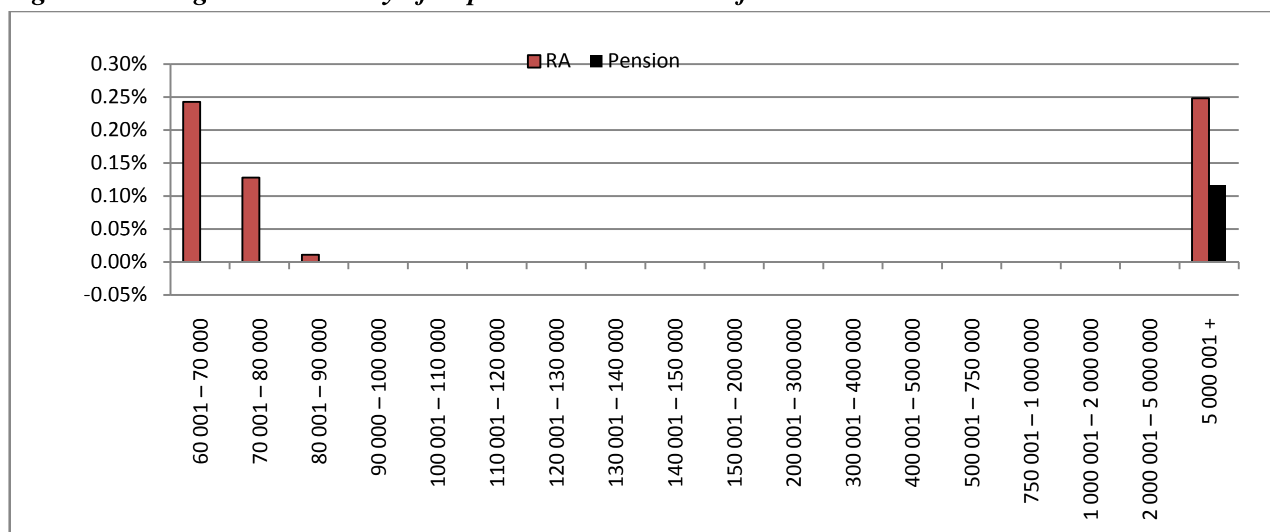
Table 7: Pension and retirement annuity deductions allowed

	Pension				Retirement annuity			
Taxable income group	Number of taxpayers	As % of total	Deduction allowed R million	As % of total	Number of taxpayers	As % of total	Deduction allowed R million	As % of total
<0	1,661	0.1%	16	0.1%	5,990	0.5%	25	0.2%
1 – 60 000	77,058	4.3%	242	1.2%	79,647	6.5%	365	3.6%
60 001 – 120 000	453,596	25.6%	2,663	13.7%	218,675	17.8%	954	9.4%
120 001 – 400 000	1,083,004	61.1%	12,267	63.0%	734,539	59.8%	4,603	45.3%
400 001 – 5 000 001 +	158,235	8.9%	4,275	22.0%	189,643	15.4%	4,219	41.5%
Total	**1,773,554**	**100%**	**19,464**	**100%**	**1,228,494**	**100%**	**10,166**	**100%**

Source: 2011 Tax Statistics

Figure 8 illustrates the change in tax liability after the tax reform to pension and RA contributions. The proposed caps to pension contributions deductions are calculated to only impact on the R5 million plus income group. The new limits will however, increase the tax liabilities for those taxpayers contributing to retirement annuities in the below R80 000 income group and the above R2 million taxable income group. This tax proposal could be a disincentive for individuals saving for retirement and especially individuals without or limited pensionable salary income.

Figure 8: Change in tax liability after pension and RA tax reform



Source: 2009 PITSIM

6.2.3 Changes to travel allowance deductions

Claiming 'deemed business kilometres' as a travelling expenses was one of the few remaining salary structuring methods used to reduce tax liability. The deemed business kilometre deduction was scrapped from 1 March 2010. It was then stated that excessive deductions that do not match actual business expenses distorted household purchasing decisions and travelling choices. Taxpayers who are required

to use their personal vehicles for business purposes are able to keep a logbook to claim business travelling expenses.

Table 8 indicates that a total number of 518 416 taxpayers received deductions for fixed cost travel allowances of close to R21.6 billion. The highest percentage at 55.7 percent of taxpayers is in the R120 000 to R400 000 taxable income group claiming more than half of the deductions allowed. This was a very generous allowance that was mainly claimed on a deemed annual business kilometre travelled basis.

Table 8: Travel allowances at fixed cost allowed

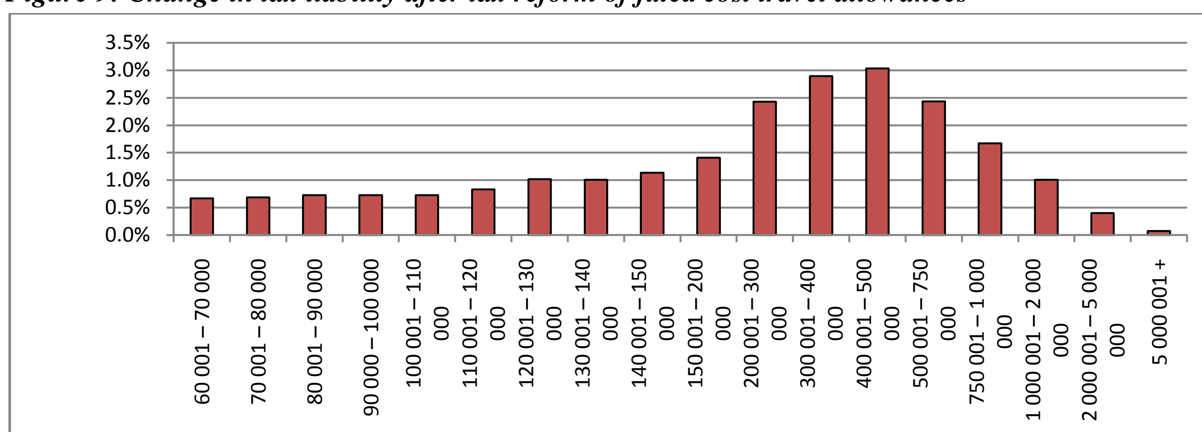
	Motor allowance fixed cost			
Taxable income group	Number of taxpayers	As % of total	Deduction allowed R million	As % of total
<0	914	0.2%	37	0.2%
1 – 60 000	10,902	2.1%	232	1.1%
60 001 – 120 000	43,042	8.3%	1,124	5.2%
120 001 – 400 000	288,660	55.7%	11,090	51.3%
400 001 – 5 000 001 +	174,898	33.7%	9,141	42.3%
Total	**518,416**	**100%**	**21,624**	**100%**

Source: 2011 Tax Statistics

By assuming that half of the deductions claimed in 2008/09 will no longer be claimable with the introduction in 2010/11 of deductions allowed only for actual business kilometres travelled, the impact is most severe on high income earners.

Figure 9 illustrates the change in tax liability after the tax reform of the fixed cost travel allowances. The changes to the motor allowances at fixed cost from the deemed principle to actual business kilometres travelled, increase the tax liability of all taxpayers, but more so for the R200 000 to R750 000 taxable income groups. It was assumed that the motor allowance is reduced by 50 percent across all taxpayers claiming motor allowances at fixed cost or on the deemed business kilometre basis.

Figure 9: Change in tax liability after tax reform of fixed cost travel allowances



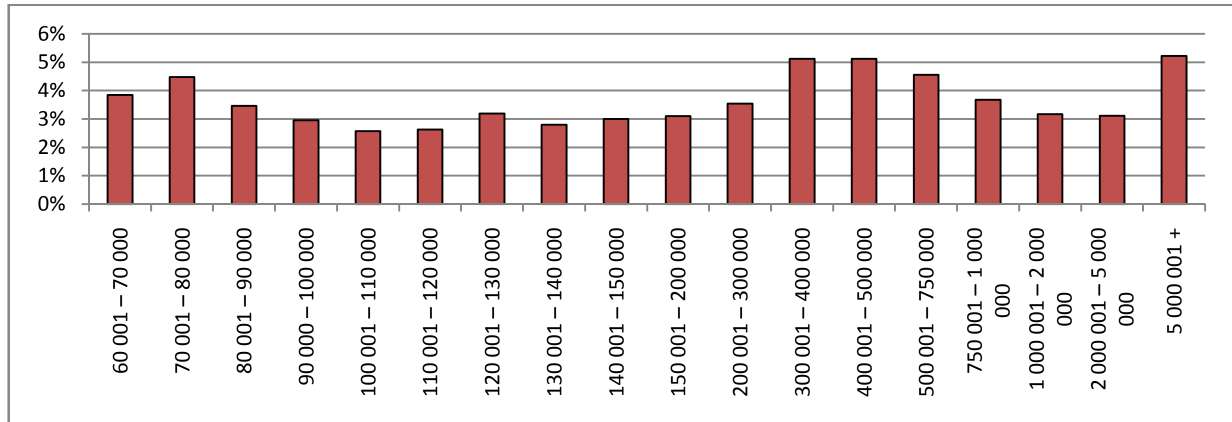
Source: 2009 PITSIM

7. Main findings

The average increase in total tax liability is calculated to be 3.94 percent based on the changes to the tax system as discussed. It is to be noticed that all income groups will pay more tax. It is calculated that close to 53 percent of the increase in the total tax burden will be paid by the R200 000 to R750 000

income groups. The tax liability of taxpayers earning above R5 million will increase the most as their tax burden will increase by 5.22 percent followed by taxpayers in the R400 000 to R500 000 income group with an increase of just more than 5 percent. The percentage change in the total tax burden per income group is illustrated in Figure 10.

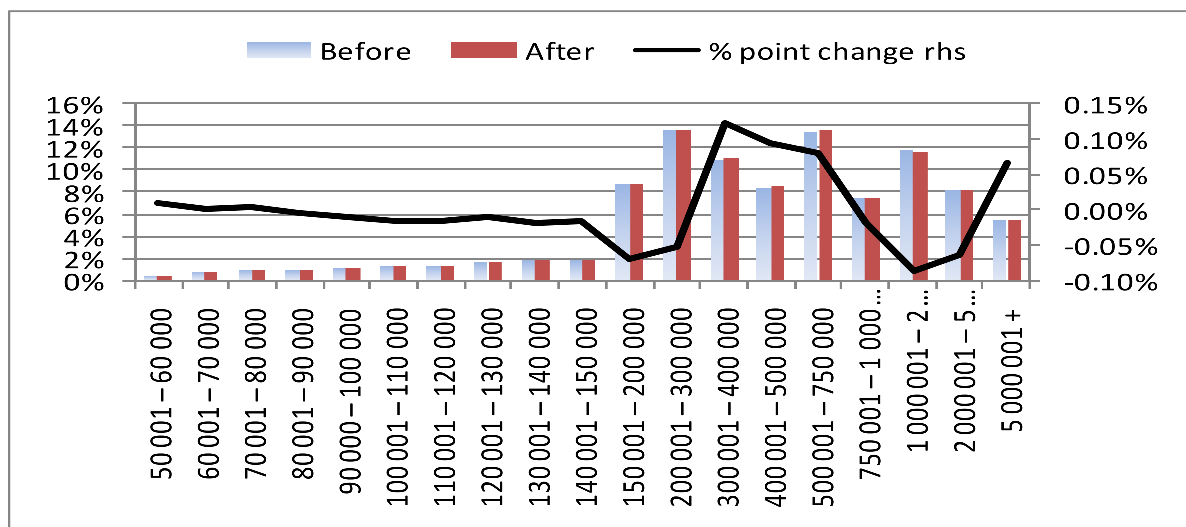
Figure 10: Percentage change in total tax liability



Source: 2009 PITSIM

Figure 11 shows the distribution of tax payable by income group as a percentage of total tax payable before and after the changes in tax policy and is a measurement of the impact of the tax policy changes on the progressiveness of the personal income tax system. The percentage tax payable by taxpayers up to the R150 000 taxable income group is only marginally affected by the changes in tax policy. However, a noticeably decrease in the percentage tax payable in the R150 000 to R300 000 income group is followed by a relatively significant increase in the percentage tax payable for income groups above R300 000.

Figure 11: Percentage point change in the distribution of tax payable by income group



Source: 2009 PITSIM

The Gini coefficient before tax proposals is measured at 0.313 with the after tax proposals Gini coefficient equal to 0.311. The slight decrease in the Gini coefficient indicates that the proposed tax policy changes increase the progressivity of the personal income tax system.

8. Summary and conclusion

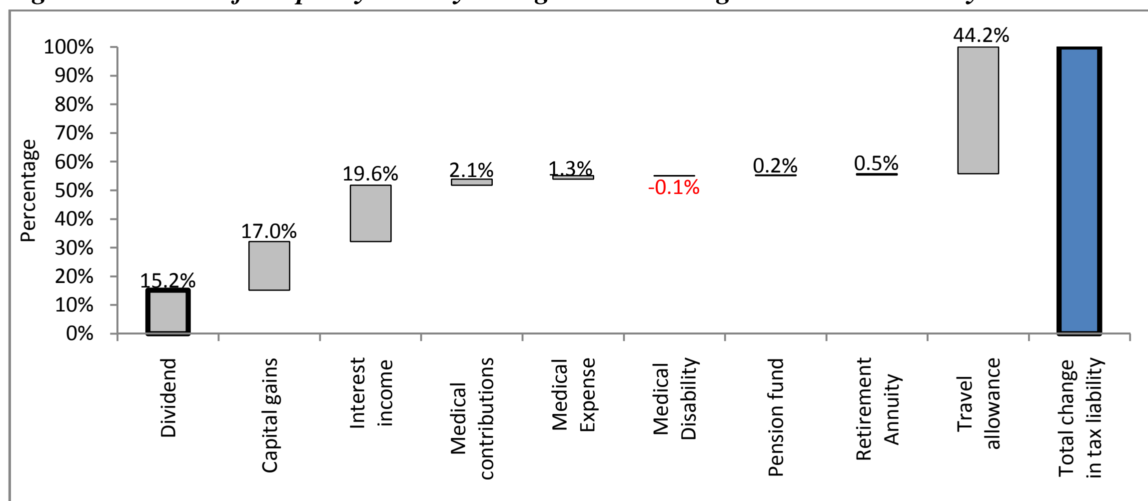
The personal income tax system for South Africa is a broad based system with relatively very few exemptions and deductions. The tax proposals are quantified to measure the impact on the tax liability of personal income taxpayers by income group. The tax proposals that were costed include the tax exempt income for interest and the increases in the tax rates for dividend income and capital gains. The tax deductions costed are the change in medical contributions and expenses from an allowance to a tax credit, the limits to pension and retirement annuity contributions, and the change in the deemed motor allowances.

The reform in the taxation of capital gains is significant for taxpayers in the high income groups. The change in the tax on current capped exempt interest income is more significant for taxpayers in the lower income groups. It is not possible to measure the impact of the new dividend tax on shareholders due to the lack of distributional data. For illustrative purposes it was assumed that the distribution of dividend income is the same as interest income.

The policy reform in medical contributions and expenses increases the tax burden for taxpayers above R150 000 with either no change in the tax burden or tax relief for persons with taxable income below R150 000. The reform to pension contributions only impact on persons with taxable income above R2 million while retirement annuity contributions also affect taxpayers with taxable income below R90 000. The reform in travel allowances increases the tax burden relatively more for taxpayers in the R200 000 to R500 000 taxable income groups.

Figure 12 illustrates the share of the various tax policy changes to the increase in the average total tax liability. The tax liability changes for capital income total 51.8 percent as a share to the total increase in tax liability of which the share of interest income is to be highest at 19.6 percent and then capital gains at 17 percent.

Figure 12: Share of tax policy liability changes to the change in total tax liability



Source: 2009 PITSIM

The tax liability changes for the fixed motor allowances deductions are high with a share of 44 percent to the change in total tax liability. The share of tax liability changes for medical expense deductions are relatively small but this is due to the net effect of the shift in the tax burden whereby taxpayers with

marginal tax rates above 25 percent will pay more and those with marginal tax rates less than 25 percent will pay less. The share of tax liability changes to pension contributions only impact on the above R2 million income group while the share of tax liability changes to retirement annuities are higher as the tax liability changes also impact on the lower income groups.

The increase in tax liability is driven by the changes in the taxation to capital income with more than 51 percent of the increase attributed to the change in the taxation of capital gains, interest and dividend income. The change to the fixed cost travel allowances contributes about 44 percent to the total change in tax liability.

The tax liability of all income groups is to increase. The highest percentage increase in the tax burden, 5.22 percent, is in the above R5 million taxable income group. The total tax liability of taxpayers in the R300 000 to R500 000 income categories increases by close to 5 percent. The average increase for taxpayers up to the R200 000 taxable income level is 3 percent. The slight decrease in the Gini coefficient for income before and after the proposed tax policy changes indicates that the proposed tax policy changes increase the progressivity of the personal income tax system.

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