Davis Tax Committee's second report on estate duty a major improvement

MONEY MATTERS
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After scoring a consensus three out of 10 for the first report, the Davis Tax Committee has delivered what I consider to be a vastly improved second report, which I will touch on very briefly in this article. The key proposal, which is substantial, is a recommendation to increase the primary rebate from the current R3,5 million to R15 million per person. This will effectively set the combined estate duty exemption for a couple at R30 million, thereby eliminating estate duty for the average South African family.

Readers should take note on how they arrived at the R15 m, which may be a wake-up call for risk and retirement planning. The committee calculated that on the death of a breadwinner, the surviving family would require between R500 000 to R600 000 to sustain their lifestyle, which would require life cover and/or savings of R10 m rand. On top of this the committee assumed a family home worth R5 m, thus getting to the figure of R15 million.

This proposal is genius in that estate duty is a wealth tax, which should target the wealthy and not prejudice the average family. By setting the exemption high, the majority have been excluded from this tax and the administrative burden of collecting and policing has been reserved for the very few. Sounds a bit socialistic, but it is likely to go down very well with the voters, but that's another topic entirely.

What's the catch? How can Treasury afford to lose all the taxes they could have collected under the current much lower limits? Unfortunately, there is a big catch. Currently all bequests to the surviving spouse avoid estate duty and capital tax on first dying, only becoming payable on the death of the surviving spouse. The committee proposes repealing these exemptions with both capital gains tax and estate duty liability arising on first dying. The early collection of these taxes is expected to make up for the loss in revenue from the increased abatement. As part of this the current donation exemption between spouses will also be removed, which is important from a planning perspective.

The other key proposal pertaining to trusts is the abolishment of the conduit principle, which allows for trust income and capital gains to be taxed in the hands of beneficiaries at lower rates. The committee wants to force the taxation of trust income and capital gains in hands of the trust at punitive trust taxation rates.

Also zero interest loans, which are generally used to fund trusts are firmly in the cross hairs, with the committee proposing the inclusion of trust assets in the estate of the lender when funded from zero interest loans, which on top of recent proposals in the Tax Law Amendment Bill to eliminate zero interest loans, is probably the death knell for establishing new inter-vivos trusts.

Of course you have to keep in mind all of the above are only proposals at this stage. So don't panic and adjust planning until we have all the facts. The committee actually refers to the fact that sufficient time and forewarning should be given to taxpayers, which is a turnaround on the first paper, which seemed to take a different attitude.

I recommend reading the full report, which can be downloaded at www.taxcom.org.za.