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Analysing the predicted Budget shortfall and possible funding alternatives in 2018

Johannesburg, Tuesday 24 October 2017: Minister of Finance, Malusi Gigaba, will be the center of attention on Wednesday 25 October 2017 when he presents his first Medium Term Budget Policy Statement (MTBPS), since being appointed as the Minister of Finance in March 2017. The MTBPS is sure to set the scene for the forthcoming budget.

"South Africa is in for a bumpy ride, utilising the 2017/18 statistics as at 31 August 2017 per National Treasury's summary table of national revenue and expenditure compared to the 2017 Budget Review announced on 22 February 2017, which indicates an estimated net revenue shortfall of about R53 billion," says Madelein Grobler: SAICA Project Manager – Tax Legislation. "This is the net result if last year's trends continue, whereby actual revenue collections for the 2017/18 fiscal year will fall short by R68 billion, while actual expenditure will decline by almost R15 billion.

The 2017/18 fiscal year is almost at the end of the road. The revenue collections of just over R1 billion during the Special Voluntary Disclosure Programme, released by the South African Revenue Service, would make little to no difference to the estimated revenue shortfall. The Minister may have to resort to extreme measures, such as another tax rate increases in the short fall to shrink the net revenue shortfall. Given the volatile economic and socio-political climate, even such measures may not have the desired funding result as the previous Finance Minister, Pravin Gordhan, had to concede in February 2017.

The question therefore remains how South Africa would fund revenue shortfalls in the 2018/19 fiscal year? So here are some options.

Option 1 - Bracket creep elimination: Individual taxpayers may encounter no adjustment for bracket creep, which will only contribute R2.48 billion to the future revenue shortfall. The R2.48 billion would represent the final depletion of the historic bracket creep availability of R9.5 billion 5 years ago (i.e. 2012/13 fiscal year). High net worth individuals may therefore also encounter a further increase in individual tax rates from 45% to 48% in 2018/19, which would fund any future revenue shortfall by only about R4.9 billion - utilising the average 2017 Budget Review figures.

Option 2 – Medical credits repeal: The 2017 Budget Review provided consideration to possibly reduce the current medical scheme tax credit to subsidise the National

Health Insurance (NHI) framework. If the aforementioned was to be implemented based on the 2016/17 Council for Medical Schemes Annual Report, another R26.7 billion would be available in the 2018/19 fiscal year to further decrease any future revenue shortfall though clearly it would mean no NHI funding. The consequential loss in medical scheme membership is also still unknown of such a proposal and with no funding for NHI would result in a double hit to the already overburdened taxpayers.

Option 3 – VAT increases and base expansion: The prospect of expanding the value added tax (VAT) base in the 2018/19 fiscal year by removing the zero-rating on fuel, while counter-adjusting the fuel levy was already alluded to in the 2017 Budget Review but how exactly this would be done remained unclear. The current fuel levy would generate about R69.8 billion. VAT on fuel would only generate R26.5 billion which means it would not be viable to eliminate the fuel levy for VAT, but rather to impose it in addition. If VAT was added to the basic price of fuel (i.e. not on the tax components) it would increase the current inland price of petrol by R1.09, which would be in addition to the annual increases in the fuel and other levies. Although traditionally an increase of the 14% VAT rate has always been mooted without any adjustment, it should not be ruled out given the tough choices the Minister has to make. The elusive increase of the VAT rate by 1% could contribute about R23 billion to the 2018/19 fiscal year revenue collection.

Should all the above be implemented an addition of approximately R83.5 billion could be added to revenue collections, which could pave the way for the 2018/19 fiscal year net revenue, incorporating a little extra for the growing Budget shortfall," concludes Grobler.

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