

A CRITICAL ANALYSIS OF THE EFFECTS OF ABOLISHING DEATH TAXES IN SOUTH AFRICA

by

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ABSTRACT

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Death taxes are payable by individuals upon their death. It is therefore ironic that the living has devoted so much of their time and energy to arguing about the future of this tax. One can only presume that a person will not find any peace in the after-world if they felt that they were treated unfairly by the tax authorities upon their death.

The arguments surrounding death taxes have been carrying on since the first country abolished the tax in 1978. Very few countries that have implemented the tax have not had in-depth research and discussion surrounding the tax and South Africa is no exception. Until now there have been no measures put in place to abolish the tax in South Africa, however the Minister of Finance has indicated that the future of the tax is currently being reviewed by the tax authority.

Both the proponents and opponents believe that their views are correct regarding the future of the tax. Although their views might differ about the matter, both sides do agree that a decision about the tax needs to be made so that the government and academia can focus on other important matters.

Both sides make use of case studies and research performed in other countries to support their views. However, South Africa has a very unique political, economic and social environment and therefore the findings and views applicable in other countries cannot simply be applied locally.

The primary purpose of this study was to evaluate the advantages and disadvantages noted by international experts and academia against the unique South African climate. This is done to enable the researcher to determine what the possible political, economic and sociological effect might be on the country should death taxes either be abolished or kept for the foreseeable future.

The conclusion is that due to the global recession and the abundance of poverty and unemployment in South Africa, the benefits of keeping death taxes outweigh the drawbacks thereof. Until such a time that the climate in the country has changed dramatically, death taxes should form part of the country's tax regime.

Keywords:

Death tax

Advantages

Disadvantages

South Africa

Climate

Effects

OPSOMMING

'N KRITIESE ANALISE VAN DIE GEVOLGE VAN DIE AFSKAFFINGVAN BOEDELBELASTING IN SUID-AFRIKA

deur

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Boedelbelasting is betaalbaar deur 'n individu by sy dood. Dit is dus ironies dat mense so baie van hul tyd en energie gebruik terwyl hulle lewe om te argumenteer oor die toekoms van hierdie belasting. Dit blyk dat 'n mens geen vrede in die volgende wêreld sal kan ervaar as jy voel dat jy met jou dood onregverdig deur die belastingowerhede behandel is nie.

Die argumente rondom boedelbelasting gaan al voort vanaf die eerste land die belasting in 1978 afgeskaf het. Meeste van die lande wat boedelbelasting geïmplementeer het, het in-diepte navorsing en besprekings rondom die toekoms van die belasting en Suid-Afrika is geen uitsondering nie. Tot nou toe was daar geen amptelike maatreëls in plek gestel om die belasting af te skaf in Suid-Afrika nie, maar die Minister van Finansies het aangedui dat die toekoms van die belasting tans deur die belastingowerhede oorweeg word.

Beide die voorstanders en teenstanders van die belasting glo dat hulle menings met betrekking tot die toekoms van die belasting korrek is. Alhoewel hul menings verskil oor die toekoms van die belasting stem beide kante saam dat 'n besluit oor die belasting gemaak moet word sodat die regering en die akademici op ander belangriker sake kan fokus.

Beide kante maak gebruik van gevallestudies en navorsing uitgevoer in ander lande om hul opinies te ondersteun. Suid-Afrika het egter 'n baie unieke politieke, ekonomiese en maatskaplike omgewing en daarom kan die bevindinge en menings wat van toepassing is in ander lande nie eenvoudig plaaslik toegepas word nie.

Die primêre doel van hierdie studie was om die voordele en nadele van boedelbelasting soos bepaal deur internasionale kundiges en akademici teen die unieke Suid-Afrikaanse klimaat te evalueer. Dus moet die moontlike politieke, ekonomiese en sosiologiese effekte op Suid Afrika bepaal word sodat 'n besluit geneem kan word of die belasting óf afgeskaf word óf vir die afsienbare toekoms gehou moet word.

Die gevolgtrekking is dat as gevolg van die wêreldwye resessie en die oorfloed van armoede en werkloosheid in Suid-Afrika, die voordele van die behoud van die boedelbelasting meer as die nadele daarvan is. Tot so 'n tyd dat die klimaat in die land dramaties verander, moet boedelbelasting deel van die land se belastingwetgewing uitmaak.

Sleutelwoorde:

Boedelbelasting

Voordele

Nadele

Suid-Afrika

Klimaat

Effekte

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A CRITICAL ANALYSIS OF THE EFFECTS OF ABOLISHING DEATH TAXES IN SOUTH AFRICA

CHAPTER 1

INTRODUCTION

1.1 BACKGROUND

Former Arizona Senator Jon Kyl stated “the death tax is unfair, inefficient, economically unsound and frankly immoral” (Brainyquote.com, Not dated). Australia became the first wealthy country in the world to abolish death taxes in 1978. At the time it was seen as an anomaly; however other countries have subsequently followed suite. The debates around death taxes have recently reached a high point in South Africa due to the statement of the Finance Minister in 2010 that National Treasury is re-evaluating the existence and role of the tax (Department of the National Treasury, 2010).

The reintroduction of death taxes in the United States of America (“USA”) has sparked international interest in the subject, including South Africa. Death taxes were reintroduced in the fiscal system of the USA as part of the Obama administration’s objective to increase governmental taxes in an effort to fight the effects of the economic downturn of the country (Donmoyer, 2010).

Capital gains tax is already payable in South Africa by the deceased upon death and therefore opponents of death taxes argue that there is no need for further death taxes that cause a double taxation on the estate. They insist that the abolishment of the tax will help grow business investments and create job opportunities (Pattern, 2010) and that it will encourage long-term capital investment rather than short-term consumption (Dubay, 2010).

On the other hand, proponents of death taxes, such as Bill Creighton, argue that it reduces the concentration of wealth and therefore encourages shared prosperity (Business Week, Not dated). They are of the opinion that those that are able to pay should be taxed the

most (Blackburn, 2007:63). The proponents struggle to comprehend the hostility towards the tax as it only affects a small part of the population (Reed, 2006:1).

Various other papers and articles, as noted further in this study, have been published internationally by academics that have highlighted the views of opponents and proponents of death taxes as well as certain alternatives to death taxes. Historically South Africa has always had a very unique economic, sociological and political environment. The generic arguments for and against death taxes might therefore be rendered invalid in a South African context.

1.2 PROBLEM STATEMENT

Academics, politicians and the general public find themselves in opposite corners when the subject of whether or not death taxes should be abolished in totality is raised. Some have concluded that although death taxes have certain shortcomings they still form part of an effective tax regime, and therefore an acceptable alternative needs to be found before abolishing the tax.

In the USA the income collected from the tax was initially used to fund their war efforts. Inheritance taxes were introduced in the USA in 1862 to help fund the Civil War and in 1898 to finance the Spanish-American War, and were repealed shortly after the wars ended (Gale & Slemrod, 2003:1–2). The trend to implement and keep death taxes even during peaceful times has subsequently been implemented worldwide by various other countries.

In current times governments are faced with large financial challenges and burdens due to the economic recession that is experienced worldwide. A government's tax base is therefore of vital importance to stimulate the country's economy. The abolishment of death taxes will therefore decrease the tax base of the country, albeit by a small portion. It is conceivable that the original purpose behind the tax might not be relevant anymore; however the contribution from the tax, however small, can be applied by governments to decrease their current budget deficits.

There is uncertainty as to whether death taxes are still relevant in a South African context. Therefore the arguments for and against the tax need to be evaluated against the South African economic, social and political backdrop to evaluate the relevance thereof.

1.3 PURPOSE STATEMENT

The purpose of this study is to evaluate the applicability of numerous statements and opinions made by international experts around the abolishment of death taxes against the unique South African political, social and economic climate. The various shortcomings and advantages of the tax will be evaluated for reasonableness in a South African context. This study will aim to identify the possible effects of abolishing death taxes so that an informed decision can be made about the future of death taxes in South Africa.

1.4 RESEARCH OBJECTIVES

The study will be guided by the following research objectives:

- To evaluate whether the arguments made by the opponents and proponents of death taxes are applicable to the unique South African environment.
- To evaluate the possible effects of abolishing death taxes in South Africa against the current economic and political environment.

1.5 IMPORTANCE AND BENEFITS OF THE PROPOSED STUDY

The Minister of Finance noted in the 2013 budget (Department of the National Treasury, 2013) that the National Development Plan will form the basis of the government's plan for job creation and increased infrastructure spend. Housing and basic services to the poor communities are still a high priority for the government (Department of the National Treasury, 2013). All of these projects will need to be funded by taxes that are collected by the tax authorities from the various sources available and abolishing any form of tax will impact the government's ability to meet these goals.

By evaluating the possible advantages and disadvantages of abolishing death taxes in South Africa the study will address a number of the consequences of such a decision and therefore remove a substantial amount of uncertainty about the matter.

The timing of the study is of vital importance due to the comments made by the Finance Minister, as well as the fact that the increase in the inclusion rate for Capital Gains Tax for individuals in 2012 might also be seen as a prelude to the abolishment of death taxes.

1.6 DELIMITATIONS

The purposed study has several delimitations related to the environment, associations and theoretical perspectives of the study. The articles and workings that were selected for use in the study were selected on a relevance basis as assessed by the researcher after a detailed search on various platforms.

This study will neither investigate all arguments made by proponents and opponents of death taxes, nor all the alternatives. The study will focus on the validity of the arguments made by experts with regard to the possible abolishment of death taxes based on a South African context.

The emphasis of this study is on death taxes, and non-taxation-related alternatives for death taxes will not be considered. No other taxes that were implemented as anti-avoidance measures for death taxes will be considered.

The principles used to select the comparative countries are thoroughly detailed in a later chapter and will not be discussed in this chapter.

1.7 ASSUMPTIONS

The following assumptions are applicable to the study:

- The study assumes the effective and efficient functioning of the market.
- The study assumes that all other factors regarding the economic, political and sociological environment will stay constant.

- The study assumes that no reasonable alternatives will be implemented to address the possible disadvantages or detrimental effects of abolishing death taxes.

1.8 DESCRIPTION OF INQUIRY STRATEGY AND BROAD RESEARCH DESIGN

The primary purpose of this study is to evaluate the possible effects of abolishing death taxes on South Africa. A qualitative research study will be performed in order to achieve this purpose. Qualitative research is defined as research that is aimed at gaining a deep understanding of a specific organisation or event, rather than a surface description of a large sample of a population (California State University, Not dated).

Michaela Mora (2010) noted that qualitative research is by definition exploratory and it is used when the researcher does not know what the outcome of the study might be or to help develop an approach to the problem. A lot of theories have been developed by experts about the possible advantages and disadvantages of death taxes. Yet none of the experts can guarantee that their theories can be proven accurate in all possible scenarios. None of the theories have ever been tested on a unique South African environment. The process of evaluating the possible effects of abolishing death taxes is an exploratory process and therefore analysing specific numerical data would not take into account the possible political and sociological effects. Therefore qualitative research is considered the best approach to solve the problem statement.

A literature review will be used as the primary strategy in performing the qualitative research. These types of reviews are used by researchers who simply seek to discover and understand a phenomenon or a process. Data is collected through various means and is then analysed by the researcher for the purpose of meeting the research objectives (Merriam, 1998:11). This strategy is appropriate for the study due to the fact that research on the subject is still in the initial phase.

The main method used for data collection will be document review and analysis (Merriam, 1998:11). This is primarily due to the time constraints for the completion of the study. The second reason for the method is due to the fact that the general public do not have the knowledge to be able to complete detailed surveys that will be of use for the study. The

response rate associated to surveys is also never good and therefore the researcher chose to make use of document reviews for data collection. A selection of both primary and secondary literature will be used for data collection. Primary research is defined as original research results that were published for the first time and secondary research is derived from primary research (University of New Hampshire Library, Not dated).

Literature reviews have certain limitations. Literature reviews can only summarise and organise information, and even an in-depth analysis of the studies cannot produce new information. It may lead to theoretical insights; however it will still be necessary to conduct an empirical study to test the insights (Mouton, 2001:180).

1.9 DEFINITION OF KEY TERMS

The following definitions relate to the key terms used in this study:

Capital gains: A capital gain is the amount by which proceeds from the sale of an asset exceeds the base cost of the asset (Paragraph 3(a) of the Eighth Schedule to the Income Tax Act (58/1962)).

Capital gains tax: The capital gains tax is the tax levied on a capital gain.

Death taxes: Death tax is defined as a tax that is raised upon the death of a person (Investorwords.com, Not dated). Death tax is used as a collective phrase for the various taxes that are raised upon someone's death in the various countries of the world. In England, for example, it refers to inheritance tax and in the USA and South Africa it refers to estate taxes.

Estate taxes: About.com (Not dated) defines estate tax as a charge upon the right of the deceased person to transfer assets to his or her heirs after death. The definition specifically states that the tax has no bearing on who inherits the estate, but is driven by the value of the deceased's estate.

Table 1: Abbreviations used in this document

| Abbreviation | Meaning |
|---------------------|---|
| GDP | Gross Domestic Product |
| NHI | National Health Insurance |
| OCED | Organisation for Economic Cooperation and Development |
| SARS | South African Revenue Services |
| UK | United Kingdom |
| USA | United States of America |
| VAT | Value-added Tax |

CHAPTER 2

OVERVIEW OF DEATH TAXES

2.1 HISTORY OF DEATH TAXES

The international development of estate taxes was researched by Muller (2010). It was noted that the origins of inheritance taxes can be attributed to Emperor Augustus of the Roman Empire. In later years the recipient-based relief formed the basis of inheritance taxes that were introduced in France in 1553.

In 2003 eleven OECD countries had some form of net wealth tax, although the tax burden between the countries varies considerably (Treasury of the Australian Government, Not dated). In 2006 Finland successfully abolished death tax. On the other end of the spectrum, countries like Germany are experiencing various lobbying initiatives to reinstate the tax.

The proponents of death taxes still believe that a constitutionally acceptable law can be phrased even though the tax was suspended by the German constitutional court in 1997. It appears that the trend of recent years is that more countries are choosing to abolish the tax rather than reinstating it (Schnellenbach, 2007:2).

The history of wealth transfer taxes in South Africa was researched by Muller (2010) and it was noted that it was introduced in the Cape of Good Hope in 1864 by way of recipient-based succession duty. The initial justification of the tax was that it was the taxpayer's social obligation to pay. It was also believed that this was in line with the benefit and privilege theory. This theory notes that the state provides the protection and the environment for individuals to accumulate wealth. The individual then has the freedom to bequest his wealth to the person of his choosing. Due to the fact that the state provides the environment as well as the right for the individual to bequest his property, there is a justification for it to levy a tax on the estate (Kahn, 1946:87).

Similar taxes were later introduced in Natal and the Free State. All previous forms of the tax were repealed in 1922 when the Death Duty Act 29 of 1922 was nationally promulgated as the first national transfer tax. This was then later replaced by the Estate Duty Act 45 of 1955.

According to the SARS *Quick Guide to Estate Duty*, the dutiable amount of a person's estate includes all property and deemed property of the deceased at the date of death, less all allowable deductions. The property of the deceased includes all movable and immovable assets as well as any rights to property. Deemed property includes the amount due under an insurance policy, lump sum payments from any retirement funds and any property that the deceased was competent to dispose of just before his death.

The deductions allowed are set out in section 4 of the Estate Duty Act and include all funeral expenditure, the debts of the deceased and all administration costs incurred with the winding up of the estate. All bequests made to public benefit organisations can also be deducted from the estate as well as all the property included in the estate that accrues to the surviving spouse.

Death taxes were initially levied by making use of a progressive rate; however this changed in 1988 when the tax was set at a flat rate of 15%. In subsequent years there have been numerous changes to the rate as it increased to 25% in 1996 and decreased again to 20% in 2001. Currently an exemption of R3.5 million is available on any estate. If the deceased bequests all their assets to their remaining spouse then the surviving spouse can utilise double the exemption per individual.

The history of death taxes was summarised above and in the next part of the chapter the arguments surrounding the existence of the tax will be highlighted.

2.2 ARGUMENTS REGARDING THE EXISTENCE OF DEATH TAXES

For every argument that calls for the abolishment of death taxes another could be found that lists the advantages and the need for death taxes in a sound tax system of a country. The future of death taxes has come under scrutiny in the recent past in South Africa.

The reasons given by SARS for the review of death taxes are noted below (Budget 2010/2011 Tax Proposals, Not dated):

- Efficiency of estate duty versus estate duty avoidance through trust arrangements.
- Estate duty which raises limited revenue versus burdensome administration.
- Perceived double taxation when estate duty and CGT is levied upon death.

The death tax debate primarily revolves around the possible economic, political and sociological effects of abolishing or retaining the tax. In this chapter the possible advantages of abolishing death taxes will be evaluated with regard to these three key areas.

To be able to understand the possible effect of the abolishment, a brief summary of the current South African climate will be given in the next part of the chapter to indicate the current needs and requirements of the South African public and government.

2.3 CURRENT SOUTH AFRICAN CLIMATE

Rudnick and Gordon (1996:6) noted the possible social, political and moral effects of wealth inequalities in a country. They noted governments could be influenced by small groups of people with large amounts of wealth to protect their interest above those of the rest of the population. They believed that a wide disparity of wealth found in developing countries may exacerbate political and social problems.

Due to the history of apartheid in South Africa the country's poverty and wealth profile is highly skewed to favour certain ethnic groups. Recent research has indicated that 40% of the households in the country earn less than 6% of the total income (Encyclopaedia of the Nations, Not dated).

Due to the policies implemented and promises made by the current South African government, the general population has a high expectation of improvement in the quality of their lives, particularly concerning housing, education, healthcare and employment (Encyclopaedia of the Nations, Not dated).

As noted from the arguments made in the previous chapters, the abolishment of death taxes will have economic, political and social consequences for a country. It is therefore vital that the possible effects of the abolishment be considered before a final decision is made by government about the future of the tax. The poorer population of the country have held numerous protests and illegal strikes in the recent past all due to the fact that the government and the public sector are not doing enough to improve their quality of life. It is therefore imperative to evaluate how they will see the abolishment of a tax that exists in part to encourage wealth distribution. The effects on the middle and higher class must also be evaluated as these individuals are the ones that stimulate the economy through investment in new and established businesses.

The government has committed themselves to the development of the country over the next 20 years through policies like the National Development Plan (Department of the National Treasury, Not dated). It aims to eliminate and reduce inequality by 2030. The challenges that the National Development Plan is addressing are as follows:

- Too few people work.
- The quality of school education for black people is poor.
- Infrastructure is poorly located, inadequate and under-maintained.
- The economy is unsustainably resource intensive.
- The public health system cannot meet demand or sustain quality.
- Public services are uneven and often of poor quality.
- Corruption levels are high.
- South Africa remains a divided society.

The National Health Insurance is also being implemented by government. Grant Thornton noted that the plan will most likely double the burden on existing taxpayers and it will threaten the country's already over-stretched tax base (Grant Thornton, Not dated:1). It is most likely that NHI will be funded from increased income and value-added taxes. It therefore needs to be evaluated whether it makes sense to abolish one tax when there is already a need for increases of other taxes due to a shortfall in the exchequer.

Both the proponents and opponents of death taxes believe that should their views be adopted, it will aid a country in the current economic climate. The repeal of death taxes will

arguably lead to an increase in the budget deficit and will therefore increase a country's debt (Coshocton Tribune, 2011:1). The opponents of death taxes believe that abolishing the tax will help to grow small business that will stimulate a country's economy. The challenge with regards to the abolishment of death taxes is for government to evaluate which of the possible advantages or disadvantages of death taxes are applicable to South Africa and which carry the most weight in the country's unique economic climate.

Estate taxes are combined with other taxes in a category called taxes on property by Treasury for their reporting purposes. As per Figure 1 noted below, the contribution that is made by property taxes has been steadily declining over the years and is currently 1.1% of the total revenue generated through taxes. This is equal to R7 817 million. Only taxes on property and stamp duties show a decline in revenue on a year-to-year basis. The increases in the other taxes are due to inflationary increases as well as the drive by SARS to increase their tax base.

Figure 1: Tax statistics 2012. Table A1.3.1: Tax revenue by main category, 2007/08–2011/12

| | Taxes on income and profits | Taxes on payroll and workforce | Taxes on property ¹ | Domestic taxes on goods and services | Taxes on international trade and transactions | Stamp duties and fees & state miscellaneous | Total tax revenue |
|---------------------------------------|-----------------------------|--------------------------------|--------------------------------|--------------------------------------|---|---|-------------------|
| R million | | | | | | | |
| 2007/08 | 332 058 | 6 331 | 11 884 | 194 690 | 27 082 | 769 | 572 815 |
| 2008/09 | 383 483 | 7 327 | 9 477 | 201 416 | 22 852 | 545 | 625 100 |
| 2009/10 | 359 045 | 7 805 | 8 826 | 203 667 | 19 319 | 44 | 598 705 |
| 2010/11 | 379 941 | 8 652 | 9 102 | 249 490 | 26 977 | 20 | 674 183 |
| 2011/12 | 426 584 | 10 173 | 7 817 | 263 950 | 34 121 | 5 | 742 650 |
| Percentage of total | | | | | | | |
| 2007/08 | 58.0% | 1.1% | 2.1% | 34.0% | 4.7% | 0.1% | 100.0% |
| 2008/09 | 61.3% | 1.2% | 1.5% | 32.2% | 3.7% | 0.1% | 100.0% |
| 2009/10 | 60.0% | 1.3% | 1.5% | 34.0% | 3.2% | 0.0% | 100.0% |
| 2010/11 | 56.4% | 1.3% | 1.4% | 37.0% | 4.0% | 0.0% | 100.0% |
| 2011/12 | 57.4% | 1.4% | 1.1% | 35.5% | 4.6% | 0.0% | 100.0% |
| Percentage change year-on-year | | | | | | | |
| 2007/08 | 18.6% | 13.1% | 15.0% | 11.5% | 12.8% | -19.4% | 15.6% |
| 2008/09 | 15.5% | 15.7% | -20.3% | 3.5% | -15.6% | -29.2% | 9.1% |
| 2009/10 | -6.4% | 6.5% | -6.9% | 1.1% | -15.5% | -92.0% | -4.2% |
| 2010/11 | 5.8% | 10.9% | 3.1% | 22.5% | 39.6% | -54.8% | 12.6% |
| 2011/12 | 12.3% | 17.6% | -14.1% | 5.8% | 26.5% | -77.2% | 10.2% |

1. Includes transfer duties, securities transfer tax, donations tax and estate duty.

2. Stamp duty was abolished with effect from 1 April 2009. State miscellaneous revenue received by SARS which could not be allocated to specific revenue types.

The taxes on properties are further broken down into the various taxes that make up the category as per Figure 2 noted below. Although property taxes as a whole have been

steadily declining in recent years, the amount of revenue generated from estate duty has steadily been increasing. All the other taxes that are included in the category have shown steep declines in recent history.

In 2012 estate duties showed a year-on-year growth of 33.6% equalling R1 045 million worth of revenue. In the last five years estate duty revenues have increased by over 50%. According to the statements made earlier in the study, the increases in estate duty revenues are not in line with the current international trends.

Figure 2: Tax statistics 2012. Table A1.5.1: Taxes on property, 2007/08–2011/12

| R million | Donations tax | Estate duty | Securities transfer tax ¹ | Transfer duties | Total |
|---------------------------------------|---------------|-------------|--------------------------------------|-----------------|--------|
| 2007/08 | 28 | 691 | 3 757 | 7 408 | 11 884 |
| 2008/09 | 125 | 757 | 3 664 | 4 931 | 9 477 |
| 2009/10 | 60 | 759 | 3 324 | 4 683 | 8 826 |
| 2010/11 | 65 | 782 | 2 933 | 5 322 | 9 102 |
| 2011/12 | 53 | 1 045 | 2 886 | 3 834 | 7 817 |
| Percentage of total | | | | | |
| 2007/08 | 0.2% | 5.8% | 31.6% | 62.3% | 100.0% |
| 2008/09 | 1.3% | 8.0% | 38.7% | 52.0% | 100.0% |
| 2009/10 | 0.7% | 8.6% | 37.7% | 53.1% | 100.0% |
| 2010/11 | 0.7% | 8.6% | 32.2% | 58.5% | 100.0% |
| 2011/12 | 0.7% | 13.4% | 36.9% | 49.0% | 100.0% |
| Percentage year-on-year growth | | | | | |
| 2007/08 | -41.4% | -7.5% | 35.9% | 9.4% | 15.0% |
| 2008/09 | 353.7% | 9.5% | -2.5% | -33.4% | -20.3% |
| 2009/10 | -51.9% | 0.3% | -9.3% | -5.0% | -6.9% |
| 2010/11 | 7.5% | 3.0% | -11.8% | 13.7% | 3.1% |
| 2011/12 | -18.5% | 33.6% | -1.6% | -28.0% | -14.1% |

1. Uncertificated securities tax (UST) prior to 1 July 2008.

It is clear from the figures noted above that the total contribution of estate tax to the exchequer is not material. However, due to the current economic environment and the deficit in the budget one cannot conclude that it is unnecessary. By abolishing death taxes the deficit will be further enlarged by a possible R1 045 million. The loss in revenue could have a dramatic effect on social grants and various projects aimed at uplifting the poorer communities in South Africa.

The main arguments made by the opponents of death taxes will be summarised and evaluated in chapters 3 to 5. To ensure a balanced view of death taxes, the possible advantages of retaining the tax will be evaluated as well.

CHAPTER 3

ECONOMIC EFFECTS

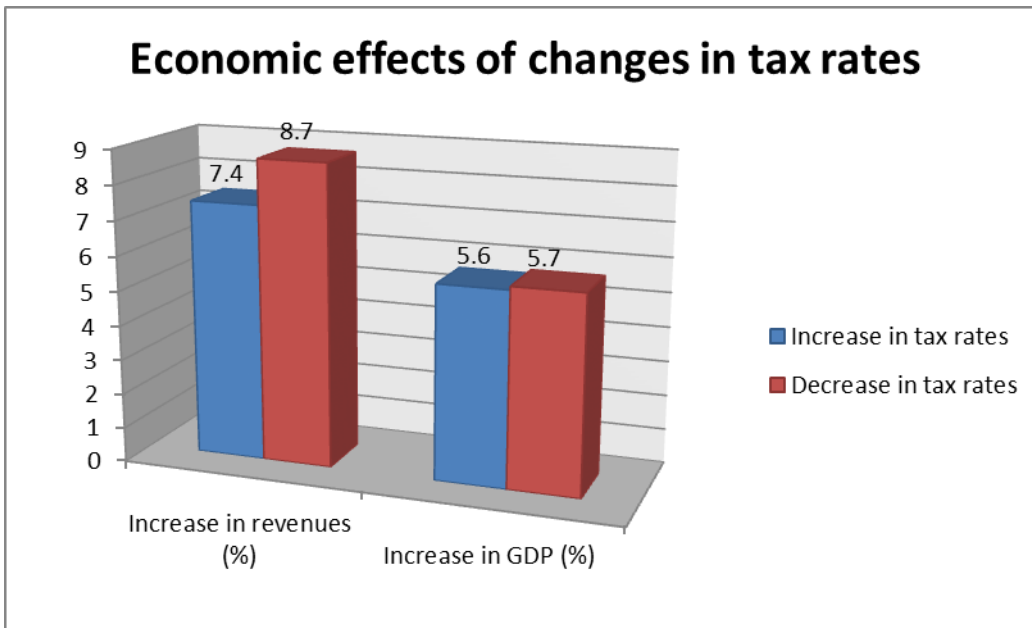
3.1 OVERVIEW

Taxes are instituted by governments to generate income to fund their economic policies and to supply the citizens of the country with basic services. The effects of increasing or decreasing tax rates on a country's economy have been analysed by numerous experts and none can say with absolute certainty what the effect of these changes will be on a country's economy.

In the USA, the Clinton administration implemented both tax increases and decreases during the president's term. In 1993 the Omnibus Budget Reconciliation Act was passed, which brought about a series of tax increases such as the hike in the top income tax rate to 36% for individuals and 35% for companies. The result of these increases was that the revenues of the country rose 7.4% per year and the GDP rose 5.6% per year (Investopedia.com, 2011).

During the president's second term, the Republicans took control of the House of Representatives and implemented various tax-reduction policies. As a result, the capital gains tax rate decreased from 28% to 20%. The policies also included numerous increases to the exemptions available to individuals and companies. The result of these tax decreases was that revenues rose 8.7% per year and the GDP of the country rose by 5.7% per year (Investopedia.com, 2011).

Figure 3: Economic effects of changes in tax rates in the USA



The effect of decreasing tax rates or abolishing certain taxes can therefore not be ascertained with certainty. It is also not possible to conclude on whether or not a decrease in taxes will stimulate a country's economy. Therefore the best objective would be to look at the numerous advantages and disadvantages as identified by various sources.

3.2 BENEFICIAL ECONOMIC EFFECTS OF KEEPING DEATH TAXES

For any government the revenue that is generated from taxes is vital to ensure its proper functioning (Thompson, 2010).

Graetz (2010) believes that the existence of death taxes in a country will encourage entrepreneurship in the economy. According to him, this is due to the fact that the family members of a wealthy parent will need to continue to work to support themselves if the government taxes their inheritances. His view is supported by Rudnick and Gordon (1996:8) who went on to note that individuals that inherit assets or gifts may have less of an incentive to work and this fact will therefore lead to a decrease in economically active individuals in the economy of a country.

Graetz (2010) noted that death taxes are taxes on capital appreciation and not on capital itself. Therefore the tax does not dilute the amount of capital available in the economy and thus will not hamper economic growth.

The Joint Economic Committee Democrats (2003:1) noted that small businesses and farms are not as negatively affected as opponents to death taxes believe. Tax return data from 1998 in the USA indicated that 1.4% of taxable estates included farms that made up half or more of the total estates' value, and only 1.6% of taxable estates included businesses that made up more than half of the estates' value. Therefore the effects of death taxes on these family-owned farms are not as material as it is made out to be. With regards to the arguments made that death taxes are responsible for the closure of small businesses, it was noted by the Joint Economic Committee Democrats (2006:3) that these small businesses will have more than enough cash to settle the tax bill and therefore the arguments are unfounded.

Opponents of death taxes argue that the tax is effectively a double tax due to the fact that the assets that attract the tax were acquired with income that was already taxed in the hands of the individual (Independent Green Voice, Not dated). Graetz (2010) opposes this argument on the basis that all individuals already pay income and payroll taxes on their wages and sales taxes on their spending. Therefore double taxation is a reality that impacts all individuals. He further points out that wealthy individuals primarily earn low tax or tax-free-based income consisting of interest and dividends. Therefore taxing a wealthy individual's estate will not constitute double taxation as stated by the opponents of the tax.

The Joint Economic Committee Democrats (2003) noted that the cost of repealing death taxes would be much greater than just the loss in revenue generated from the tax due to the fact that the taxpayers would increase tax avoidance strategies to reduce income tax collections.

3.3 BENEFICIAL ECONOMIC EFFECTS OF ABOLISHING DEATH TAXES

Death taxes are effectively taxes on capital and savings and therefore have a negative effect on the economy of a country. It is this principle that numerous economists are

against as they believe that capital should not be taxed (Dubay, 2010). This is due to the fact that the taxation of capital encourages short-term consumption and therefore discourages long-term savings (Economist, 2007; Dubay, 2010). This view is supported by Thompson (2010) who believes that any tax on capital stifles the growth of an economy and therefore decreases income to all inhabitants in general.

The Joint Economic Committee United States Congress (2003) argued that it cannot be proven that death taxes have a positive impact on income equality due to the lack of studies and evidence on the matter.

The opponents of death taxes also believe that the tax actually works against the free market principle that is applied in the majority of western cultures and it might even negatively affect the economies of these countries (Independent Green Voice, Not dated).

The opponents of the tax argue that the contribution of the tax is not a substantial amount of money, the argument is made that the net effect of the tax is a loss to the exchequer (Joint Economic United States Congress, 2003). Dubay (2010) noted that the number of people affected by the tax is not important, but the effect of the tax on a country's economy is. Therefore the amount of money that is removed from a country's economy due to the tax is unacceptable.

Small and family-owned businesses are believed to be impacted the most by death taxes due to the possible dissolution of the business to cover the tax bill (Dubay, 2010). Due to the possible high value of the business's assets, the individuals' estates are raised beyond the exemption levels. In order for the remaining family members to settle the tax bill, some of the businesses assets need to be sold. The selling of these assets could eventually lead to the closure and liquidation of the business (Donmoyer, 2010). The effects of the closure of these businesses have a negative effect on the economy in general and the communities in which the businesses operated in (Fagan, 2010:1).

3.4 SUMMARY OF POSSIBLE ECONOMIC EFFECTS

The possible beneficial economic effects of retaining death taxes can be summarised as follows:

- Death taxes generate valuable income for governments to be able to function optimally.
- Death taxes stimulate the economy by ensuring that individuals stay economically active for longer.

The possible beneficial economic effects of abolishing death taxes can be summarised as follows:

- Death taxes are a tax on capital and therefore negatively affect the economy by encouraging short-term consumption.
- Death taxes financially damage small and family-owned businesses.

The possible impact of these abovementioned matters on South Africa will be discussed in detail below.

3.5 ECONOMIC IMPACT ON SOUTH AFRICA

The possible effect on South Africa due to the abolishment or retaining of death taxes will be discussed in detail below.

3.5.1 POSSIBLE BENEFICIAL EFFECTS OF RETAINING DEATH TAXES

The advantageous effects of retaining death taxes will now be applied to South Africa's economic environment.

3.5.1.1 DEATH TAXES GENERATE VALUABLE INCOME FOR GOVERNMENTS TO BE ABLE TO FUNCTION OPTIMALLY

Due to the current economic climate and the enduring recession, unemployment has increased in the last couple of years within the country (Business Day, 2013). South Africa has two basic concepts of social security, namely the insurance concept and the redistribution concept. The insurance concept insures workers against the possible loss of income. This is funded by contributions made by the workers during their employment period. The redistribution concept is a non-contributory benefit that is given by the government to specific groups such as the disabled, elderly and the poor. This is funded by the revenues that the government collect through various taxes (Leibbrandt, Woolard, Finn & Argent, 2010).

The amount of money that the government spends on social grants has increased dramatically in the recent past from R30.1 billion in 2000/01 to R101.4 billion in 2008/09. This resulted in 13.4 million people benefitting from the government's grants. 2.3 million of these people were receiving old age pensions, 1.4 million were receiving grants for disability and 9.1 million children were receiving support grants (Leibbrandt, M. *et al*, 2010).

Increased spending by government is required to ensure that education levels are improved and that basic services are delivered to all South Africans. Rapid growth of the economy is vital to broaden the opportunities for all and increase employment numbers. As noted above, death taxes are a source of revenue for a government which enables them to increase their spend.

A decrease in the government's budget will therefore have a detrimental effect on its ability to perform the specific services needed by the residents of the country to ensure an improved future for all.

3.5.1.2 DEATH TAXES STIMULATE THE ECONOMY BY ENSURING THAT INDIVIDUALS STAY ECONOMICALLY ACTIVE FOR LONGER

The Canadian International Development Agency (Not dated) stated that a skilled workforce is a prerequisite for forming a strong foundation to encourage economic growth in a country. It was noted that many working adults in developing countries lack the literacy and numerical skills required for employment. This also leads to a lack in entrepreneurial, marketing and management skills.

Poverty has a direct impact on the education levels of a child. Research performed by the Children's Institute (Not dated) indicated that the children of wealthy parents have a much higher education level than that of their poorer peers. The study indicated that in 2010 nearly all the learners from financially well-off families had passed Grade 9, whereas only half of the children from the poorer families managed to pass the grade.

It is therefore reasonable to accept that the descendants and family members of a wealthy deceased person will have a higher educational level than that of a person from a poorer background. The fact that these wealthy descendants might be less active in the economy due to a large inheritance will have an unfavourable effect on the sustainable growth of South Africa. Due to the developing status of the country, sustainable economic growth is vital to ensure a brighter future for the country.

3.5.2 POSSIBLE BENEFICIAL EFFECTS OF ABOLISHING DEATH TAXES

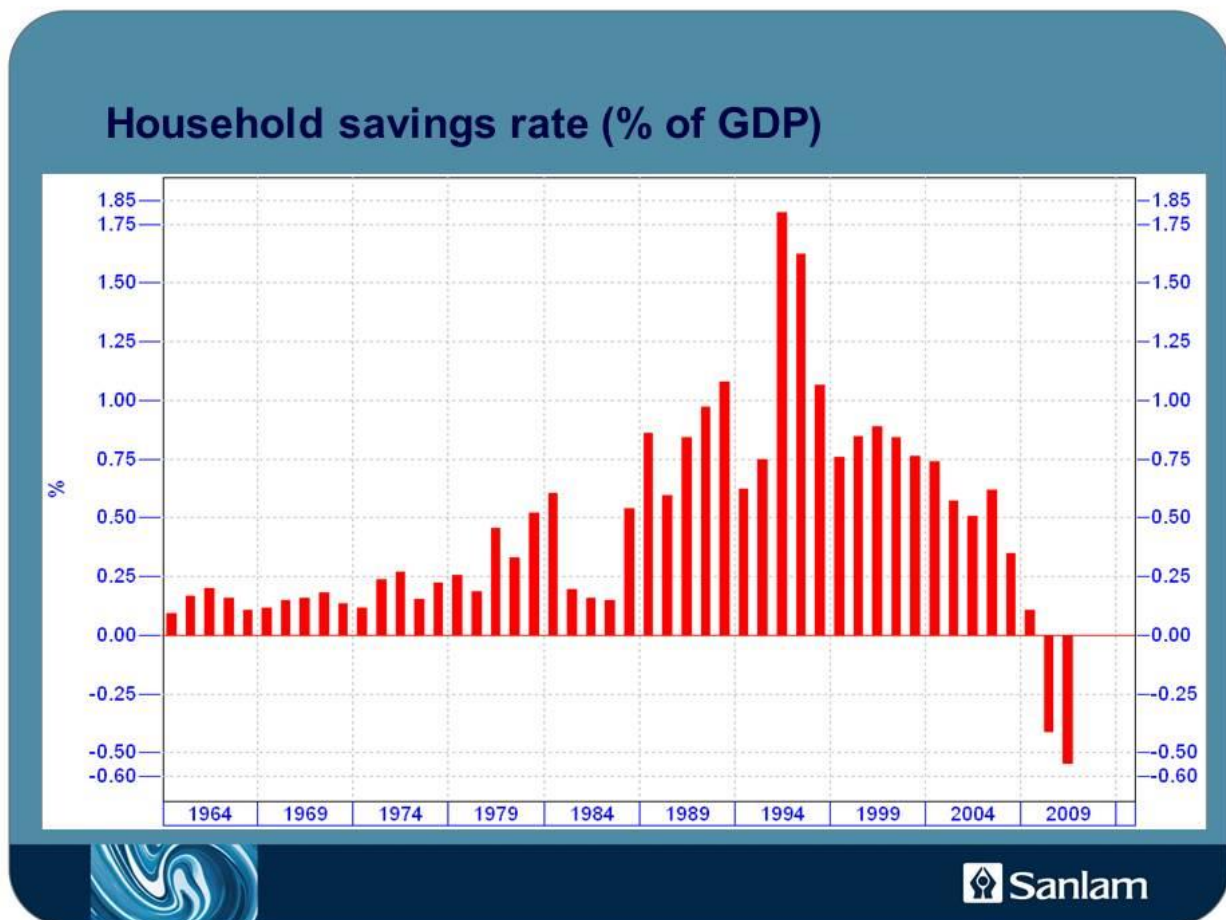
The advantageous effects of abolishing death taxes will now be applied to South Africa's economic environment.

3.5.2.1 DEATH TAXES ARE A TAX ON CAPITAL AND THEREFORE NEGATIVELY AFFECT THE ECONOMY BY ENCOURAGING SHORT-TERM CONSUMPTION

According to the South African Savings Institute (2007) the savings trend for households in South Africa has been decreasing over the recent years.

As can be seen from the graph noted below (South African Savings Institute, 2007), households in South Africa have been spending more than what they have been earning since 2007. This has been credited to a low level of disposable income in the average household due to low economic growth and a rising tax burden (South African Savings Institute, 2007). To combat the trend it is suggested that a culture of saving is created in the country as well as a reduction in income taxes and an increase in consumption taxes.

Figure 4: Household savings rate (% of GDP)



The savings rate of a country has a direct impact on the country’s economic growth. If the savings rate of a country increases then the consumption spend of the residents of the country will also decrease, which will impact on the consumption and economic activity of a country (Atkins & Lund, 2009). It was further noted that the only way that the savings rate of a country can be increased without impacting the consumption amounts is with an increase in the income of households. The South African economy’s growth rate has

drastically decreased to less than 1% per year and therefore a material growth in a household's income is unlikely (Tradingeconomics.com, 2013).

The abolishment of death taxes might therefore increase the savings rate of the South African household and decrease short-term spend. The decrease in spend would therefore negatively impact the consumption numbers, which will adversely affect the economy of the country. It is therefore not clear-cut whether death taxes negatively affect the economy of South Africa.

3.5.2.2 DEATH TAXES FINANCIALLY DAMAGE SMALL AND FAMILY-OWNED BUSINESSES

There is limited information available from SARS with regards to the amount of death taxes that is attributable to small businesses and farms from SARS. To determine the possible effect that death taxes might have on small businesses in South Africa an analysis was performed on a publication by Statistics South Africa on Employers and the Self-employed (2009:8). The survey indicated that 1 076 individuals had started small businesses in 2009 and that the combined revenue generated by these businesses was R1 657 million. This equalled to R1.5 million per individual as an average. It is therefore reasonable to assume that the valuations of these businesses might be more than the exemption rate of R3.5 million and therefore the transfer of the business upon the owners' death could have possible death tax implications.

Due to the lack of available information from SARS, a publication made in the USA was used to determine the possible effect on small businesses and farms. The Centre on Budget and Policy Priorities (2013) in the USA noted that the amount of small businesses and farms in the USA that will be affected by death taxes in 2013 is approximately 20 per year. This is equal to one out of every 130 000 estates in the country. It was further noted that these 20 estates will only owe 4.9% of their value in tax to the revenue authority. The applicability of the study in relation to South Africa is debateable, however one can clearly see that only a very small percentage of business are affected by death taxes.

Due to the limited information available on the death taxes paid in South Africa relating to small businesses and farms it is difficult to come to a conclusion on the possible effect of the tax. From the above information it would appear that it is possible that small businesses may have a minimal exposure to the tax, and it is debateable whether these taxes will have a material effect on the operations of the business.

3.6 CONCLUSION

The facts noted above indicate that there is a direct link between a country's economic health and their tax system. Abolishing death taxes might positively influence the economy of a country; however it remains questionable whether this will be the case for South Africa.

The possible benefits of abolishment are set off by the probable benefits of retaining the tax. Due to the overwhelming demands that are currently placed on the limited funds of the government to stimulate and support the South African economy, the abolishment of death taxes in South Africa seems to be an option that has to be approached with extreme caution.

The remaining political and sociological effects will be discussed and evaluated in the following chapters starting with the political effects.

CHAPTER 4

POLITICAL EFFECTS

4.1 OVERVIEW

Research has indicated that there is a direct link between the political incentives and the tax policies of a country. It was noted that there exists evidence for the effects of both political ideology and pre-electoral opportunism on the income tax rates of OECD countries. Left-wing governments are more prone to tax capital in relation to labour income (Angelopoulos, Economides & Kammass, 2009).

Supporters of left-wing politics are usually progressive in nature and support those who cannot support themselves. They believe in taxation to redistribute wealth and in equality (Idontgetpolitics.co.uk, Not dated). The current South African government is striving for more social equality and therefore can be described as left-wing.

The study performed by Angelopoulos *et al* (2009), indicated that governments reduce income tax rates before elections to increase their support base. The study also indicated some further interesting political effects; firstly, left-wing governments are in favour of reducing income tax rates rather than taxes on capital and self-employment. Secondly, the study concluded that left-wing governments increase the tax burden on capital by broadening the capital tax base and by decreasing the tax exemptions relating to depreciable capital. Thirdly, it was found that even though income tax rates are reduced before elections, consumption taxes are not. This could possibly indicate that the political cost for increasing consumption taxes is smaller than income taxes. This is in line with further studies which found that left-wing governments are associated with increases in consumption taxes.

As noted above, the current South African government is considered to be left-wing orientated. Although death taxes aren't seen as a tax on income, but rather on capital or capital appreciation, the above study indicates that the government might consider the abolishment of death taxes for an increase in consumption taxes.

It is clear that there is a link between the tax policies and the political environment of a country. In the section below the possible advantageous and disadvantageous political effects of abolishing death taxes are evaluated.

4.2 BENEFICIAL POLITICAL EFFECTS OF RETAINING DEATH TAXES

Economic equality has been one of the focus points of the South African government for the last decade. The government has purposefully implemented strategies like black economic empowerment to assist them with their long-term goal. Thompson (2010) believes that the governments' political agenda will be affected positively by death taxes due to the fact that it helps to ensure income equality. It is argued that death taxes help to create more income equality by taxing large inheritances that are passed on from generation to generation in wealthy families.

Rudnick and Gordon (1996:6) noted that even if a tax on wealth did not have a material effect on wealth distribution, a small effect is still better than none. Statistical evidence indicates that death taxes affect only 1% of a country's population due to the numerous exemptions available. The Joint Economic Committee Democrats (2006:1) states that it is this 1% that has the ability to pay the tax.

Donmoyer (2010) stated that due to the exemptions available very few taxpayers have the means to accumulate the amounts of assets required to attract the tax. Graetz (2010) therefore noted that it is not understandable why a tax that affects so few is hated by so many that it needs to be repealed.

The fact that the rich are taxed on their inheritances will result in wealth being distributed from the extremely wealthy to the poor through the government's various incentives. Due to the fact that the majority of South Africa's population lives in poverty, the political support that can be obtained through these incentives is a huge driving factor for any political party that wants to win the general elections. It is therefore reasonable to assume that government will not easily make a decision to decrease their tax base by repealing a tax.

It is also generally accepted that those with the ability to pay more taxes should do so. Graetz (2010) notes that it is basic fairness for children of wealthy parents to be taxed on their inheritance as a means of helping to finance government. This is in line with the current view that is held by the poor in South Africa that the rich need to contribute more to alleviate poverty.

From the information noted above it would appear probable that the abolition of death taxes will have some, possibly far-reaching, negative political effects.

4.3 BENEFICIAL POLITICAL EFFECTS OF ABOLISHING DEATH TAXES

Russel (2008) believes that the economy suffers directly due to the existence of death taxes because it prevents job creation and retention. This is due to the fact that capital is removed from the economy to fund an estates tax bill.

As noted above, it is also believed that small and family-owned enterprises are affected negatively by the tax which affects the job market. Job creation has been labelled as one of the primary focus areas of the current South African government and therefore the existence and requirements of death taxes must be evaluated.

The tax has been labelled a “communist tax” by the Independent Green Voice (Not dated). This is due to the fact that the proponents of the tax believe that the tax helps the spread of wealth, and this principle goes directly against the principles of capitalism. Capitalism is defined by About.com (Not dated) as an economic system built on private ownership and the private control of the economy. Companies and people live according to a profit motive and they exist to make money and to maximise their wealth.

It is also noted that it is a matter of political principle that people should be able to pass on the assets and wealth that they have accumulated in their life to whoever they desire (Independent Green Voice, Not dated).

Communism or socialism is defined as a system where the means of production is owned by the state. Every person or company works for wealth that is in the end distributed to everyone (About.com, Not dated).

The question therefore needs to be asked why countries that apply capitalism institute a tax with such strong communistic principles. Mankiw (2006) stated that in a free market there should be no need to institute a tax to ensure fair wealth distribution. Graetz (2010) believes that the tax is charged by capitalistic countries due to the fact that wealthy people owe the country in which they have earned their wealth for the opportunity to do so. This argument was not well received due to the fact that a country levies numerous other taxes on their citizens for the right to be in that country and therefore it doesn't explain the existence of death taxes.

The Independent Green Voice (Not dated) addressed the question on why the children of wealthy parents should not be taxed on their inheritance by simply stating "Why not?". They further noted that political principles cannot be built on envy. It is generally accepted in many cultures that parents will provide for their children and they are entitled to do so. The inheritance might also serve to supplement children that are struggling financially and therefore it might even relieve the government of the burden of caring for these individuals.

The government would need to evaluate the possible negative effects should death taxes not be abolished as the effects thereof could be imperative.

4.4 SUMMARY OF POSSIBLE POLITICAL EFFECTS

The possible beneficial political effects of retaining death taxes can be summarised as follows:

- Death taxes help the advancement of income equality.
- Death taxes could increase political support due to increased spend on the basic needs of the poor.

The possible beneficial political effects of abolishing death taxes can be summarised as follows:

- Death taxes remove capital from the economy and decrease job creation.
- Death taxes are a communist tax that opposes South Africa's socialist views.

The possible impact of these abovementioned matters on South Africa will be discussed in detail below.

4.5 POLITICAL IMPACT ON SOUTH AFRICA

The possible effect on South Africa due to the abolishment or retaining of death taxes will be discussed in detail below.

4.5.1 POSSIBLE BENEFICIAL EFFECTS OF RETAINING DEATH TAXES

The advantageous effects of retaining death taxes will now be applied to South Africa's political environment.

4.5.1.1 DEATH TAXES HELP THE ADVANCEMENT OF INCOME EQUALITY

As noted in the previous chapters, there is very little information available about the make-up of the current death taxes that are being collected by the revenue service. Many wealthy individuals will make use of a family trust for estate planning purposes and therefore they will avoid paying death taxes upon their death. Many financial entities and institutions advise clients to make use of trusts in this manner (Sanlam, Not dated).

Due to the fact that there are certain financial and regulatory requirements for making use of trusts it is reasonable to assume that trusts are used more by the middle- and upper-class individuals for estate planning. It is therefore possible for these individuals to elude death taxes and to contribute to the distribution of wealth through death taxes.

During the 2013/2014 budget it was noted by the Finance Minister that tax laws surrounding trusts will be amended. It is proposed that all income that is received by a

trust be taxed in the hands of the trust and therefore the flow-through principle will no longer apply. Any distributions made to the beneficiaries of the trust will be treated as a deduction by the trust (Alexanderforbes, 2013:5). The main motivations for the proposed changes are that trusts are utilised mainly as tax-avoidance vehicles. The proposed changes should not currently affect the effect of trusts on death taxes; however it is obvious that the tax laws surrounding trusts are being evaluated in detail by the revenue service.

From the above information it appears that death taxes only assist with wealth distribution to a certain extent. This is due to the fact that certain means are available to the middle and upper class to bypass the tax that is currently being utilised by many individuals.

4.5.1.2 DEATH TAXES COULD INCREASE POLITICAL SUPPORT DUE TO INCREASED SPEND ON THE BASIC NEEDS OF THE POOR

As previously stated, there are massive income inequalities experienced in South Africa. The majority of the country lives below the breadline and poverty is rife. Part of the reason why the ANC has been so successful in securing the majority vote of the people of South Africa since the start of democracy is that they are promising a better life for all. It is understandable that when a person is faced with large-scale poverty and no basic services that they will react positively to a promise of a better life in the future.

The ANC adopted the Freedom Charter in 1955 and this document still forms the basis of the organisations' policy over 50 years later. The document states that the people of South Africa shall share in the wealth of the country, there shall be work and security and that there shall be houses and comfort to all South Africans (ANC, Not dated).

In recent years there has been a surge in uprisings in the country due to dissatisfaction with the delivery of basic services and the non-creation of jobs for the unschooled and middle class. Workers are conducting illegal strike actions to voice their disappointment with the fact that the promises made to them have not been delivered. This culminated in the death of 34 miners at Marikana late in 2012.

Political figures have also found a reasonable following due to promises of wealth distribution from the rich to the poor. A person like Julius Malema has established a new political movement that has identified the following key pillars:

- The expropriation of South African land without compensation.
- The nationalisation of mines, banks and other sectors without compensation.
- Free quality education, healthcare, houses and sanitation (Politicsweb, 2013).

These types of promises find traction with the unschooled labour force in South Africa and due to their large numbers this equates to a strong following for the new party. If a political party therefore abolishes a tax that is perceived to bring about wealth equality it is possible that the large lower class in the country will lose their confidence in the party to deliver a better life for them. Fewer taxes on the wealthy will also mean that less cash is available for the government to spend on its initiatives for the poor. In the current climate of unrest this might have dire effects for the ruling party.

4.5.2 POSSIBLE BENEFICIAL EFFECTS OF ABOLISHING DEATH TAXES

The advantageous effects of abolishing death taxes will now be applied to South Africa's political environment.

4.5.2.1 DEATH TAXES REMOVE CAPITAL FROM THE ECONOMY AND DECREASE JOB CREATION

A report issued by McKinsey South Africa highlighted the top five barriers experienced by business owners in Africa to grow their businesses and to enlarge their workforce (Howwemadeitinafrica.com, 2012):

- Macroeconomic and political stability.
- Access to finance.
- Infrastructure shortcomings.
- The business environment.
- Lack of practical skills and work readiness.

An article published on Fin24.com noted that the failure rate of small businesses in South Africa is as high as 63% in the first two years (Fin24.com, 2010). This is due to the lack of start-up capital, poor management and a lack of proper infrastructure. The high failure rate of these businesses results in a very small increase in sustainable employment numbers for small businesses. This sector was earmarked as one of the major contributors for employment growth in South Africa.

The lack of finance and start-up capital noted above refers to the funds needed by entrepreneurs to properly set-up a business and to fund it through its initial stages. There is no difference between South Africa and any other country with regards to the availability of capital to entrepreneurs and small businesses (Gibs, Not dated).

Taxing small businesses on the death of the owner does remove capital from the economy; however the actual effect of this on the growth of small businesses and the economy's ability to generate new jobs is arguable. As noted above, the main challenges that small businesses face to survive their first two years relate more to a skills shortage and initial start-up capital. Death taxes only become payable over the R3.5 million benchmark and therefore it is debatable whether newly formed businesses will be affected at all.

The political effects of death taxes are therefore minor due to the fact that the capital that is removed from the economy will not materially affect the government's focus on job creation.

4.5.2.2 DEATH TAXES ARE A COMMUNIST TAX THAT OPPOSES SOUTH AFRICA'S SOCIALIST VIEWS

The main difference between communism and socialism is ownership. With communism ownership of entities and assets fall to the state, whereas with socialism ownership falls to the workers and community.

Presently there are numerous calls for the nationalisation of mines and banks in South Africa. These calls have been made under the banner of socialism due to the fact that it is

believed that these valuable assets need to be taken from a select minority and redistributed to the communities for upliftment. However, nationalism will give ownership of these high-value assets to the state, which means that it is a structure of communism.

Contradictory to this is the current BEE legislation that encourages companies to give a certain portion of the shares to their workers and the previously disadvantaged. This principle falls under the definition of socialism.

The ruling party (ANC) officially rejected nationalisation at their fifth yearly conference in Bloemfontein in 2012. However, a resource rental tax was suggested to ensure that the state captures an equitable share of the countries' resources to deploy the money into long-term economic growth. The tax of 50% will be levied once the investors have made a reasonable return on their investment (Mail & Guardian, 2012). The introduction of such a high tax rate has certain communistic principles attached to it due to the fact that the state is taking "ownership" of the profits of certain mines.

There is therefore a fine line between communism and socialism and in reality it is hard to imagine a country that can function purely on the one principle without traces of the other in its economic policies. The fact that death taxes might therefore be seen as a communistic tax that is implemented by a socialistic government would be of no great effect.

4.6 CONCLUSION

The current South African climate is seeing an increase in the calls for the government to deliver on their electoral promises. The numerous strikes over service delivery and salary increases indicate that it is an important time for the ruling party to show leadership and support to the country. For the government to be able to deliver on their promises they require a large amount of funds. It is therefore reasonable to accept that the possible political impact would be larger should the government abolish death taxes in the current atmosphere. It will therefore make more sense to keep the death tax regime for the foreseeable future.

The sociological effects of abolishing death taxes are the last focus area to be addressed and will be done in the following chapter.

CHAPTER 5

SOCIOLOGICAL EFFECTS

5.1 OVERVIEW

Marc Leroy (2008) performed a study on the sociological effects of tax on a country's population. It was noted that a progressive tax rate or the taxation of the richest inhabitants of a country will lead to redistribution of wealth. The main purposes of taxes are to reduce inequalities, to finance the government and to protect the weaker members of society (Leroy, 2008).

Many sectors of society are also reliant on the funds received from tax collections to be able to serve the community. The social responsibilities of governments take up a large portion of all taxes collected. In countries like Canada, France and the USA it represents about 35% of all of the governments' objectives whereas economic objects take the remaining 65% (Leroy, 2008).

A selection of countries make use of tax policies to encourage philanthropy through incentives. Taxes (such as tobacco and alcohol taxes) are also used by countries to limit the intake of harmful substances or habits by its citizens. Countries like the USA implemented gambling taxes because gambling is seen as immoral, whereas the UK socially accepts gambling and therefore did not implement any sort of tax in this regard (Leroy, 2008).

It is clear that any changes to a country's tax system could affect the sociological environment of the country. It is therefore vital to evaluate the possible consequences of abolishing death taxes in a South African context before a decision is made on the future of the tax.

5.2 BENEFICIAL SOCIOLOGICAL EFFECTS OF RETAINING DEATH TAXES

Thompson (2010) noted that death taxes will positively impact a community in a sociological manner due to the fact that it encourages charitable giving. This is due to the fact that tax deductions are available to estates for any donations made to charities. A study performed by Bakija, Gale and Slemrod (2003) noted that the abolishment of death taxes will result in a decrease in charitable bequests. This is mainly due to the fact that the abolishment of the tax will also abolish the possible tax deductions that incentivise the bequest in the first place. A decrease in bequests will adversely affect a number of charities who are reliant on charity to be able to continue to uplift the communities within which they function.

It is well documented that death taxes only contribute a small portion of countries' yearly fiscal revenue. Dubay (2010) noted that in the case of the USA this is as little as 1%. However, 1% of countries yearly fiscal revenue is still a large amount of money that can be used to stimulate and grow a country's economy and to cover vital expenditure of the country. Thompson (2010) noted that the 1% is close to USD 700 billion. This is a large sum of money that can be utilised by a government for social projects to uplift poor communities.

The Joint Economic Committee Democrats (2006:1) stated that the abolishment of death taxes would either decrease the spending capabilities of a nation and therefore decrease its service delivery, or increase the rates of other taxes. Such an increase will affect the lower and middle class of a country more dramatically than the current effect of death taxes. This is due to the fact that death taxes do not affect the poor due to the exemptions that are available to them. An increase in consumption or income taxes will, however, directly decrease the amount of money of the poorer members of the country.

5.3 BENEFICIAL SOCIOLOGICAL EFFECTS OF ABOLISHING DEATH TAXES

Due to the timing and nature of death taxes it has been labelled as outright immoral (Kirchoff, 2002). It is considered to be socially despicable that a government imposes a tax on a person while the family is grieving (Russel, 2008).

Based on the principles that were established by the Joint Economic Committee United States Congress (1998) of vertical and horizontal fairness, death tax is considered to be an unfair tax. The principle of vertical fairness states that a person in a high income bracket should pay more taxes than a person in a lower income bracket. Horizontal fairness is achieved when two taxpayers in the same income bracket pay the same amount of tax. It is regarding this principle that the Joint Economic Committee Democrats (2006:2) argues the unfairness of the tax.

This is due to the fact that wealthy individuals can easily avoid death taxes with good estate planning and therefore the burden is felt more by the middle class and uninformed than the wealthy. The liability of a tax payer is therefore determined more by the craftiness of a tax planner rather than the principles of the law (Dubay, 2010; Thompson, 2010). The proponents of the tax agree with this statement; however they are of the opinion that the loopholes must rather be addressed than the abolishment of the tax (Graetz, 2010).

Mazansky (2013) noted that there is no real need for death taxes in an environment where the state has already introduced capital gains tax. He noted that this is due to the fact that both taxes primarily tax the same assets and therefore death taxes are seen as a double tax. The argument for capital gains tax is improved by the fact that the tax brings in more revenue to the state.

Currently in South Africa the minority of the country funds the operations of the government due to the large unemployment rate and therefore the small tax base of the country. By eliminating a tax that is seen as a double tax it will improve the social environment of the country and its citizens that are already paying large amounts of tax.

Cummings, Martinez-Vazquez, McKee and Torgler (2006) noted that tax compliance levels can be explained by the fairness of tax administration and the overall attitude of the taxpayers towards the government. Their research supported the hypothesis that tax compliance increases with a person's perception that the tax system is fair and that quality services are being provided by government with the collected revenues.

Taxpayers are making use of structures like family trusts and with the assistance of estate practitioners they are decreasing their death tax obligations. These structures and plans are normally very complex and sometimes unlawful. Death taxes are seen to be an unfair tax and therefore the abolishment of the tax will increase the perception of fairness of the country's tax system. This will result in a higher compliance level that will generate additional revenue for the government.

5.4 SUMMARY OF POSSIBLE SOCIOLOGICAL EFFECTS

The possible beneficial sociological effects of retaining death taxes can be summarised as follows:

- Death taxes encourage charitable giving through incentives to estates.
- Death taxes generate revenue that is used for the upliftment of communities by government.

The possible beneficial sociological effects of abolishing death taxes can be summarised as follows:

- The abolishment of death taxes will increase the perceived fairness of the tax system, which will improve tax compliance.
- The elimination of double taxes will alleviate some of the burden placed on the minority of citizens to fund the government's operations.

5.5 SOCIOLOGICAL IMPACT ON SOUTH AFRICA

The possible effect on South Africa due to the abolishment or retaining of death taxes will be discussed in detail below.

5.5.1 POSSIBLE BENEFICIAL EFFECTS OF RETAINING DEATH TAXES

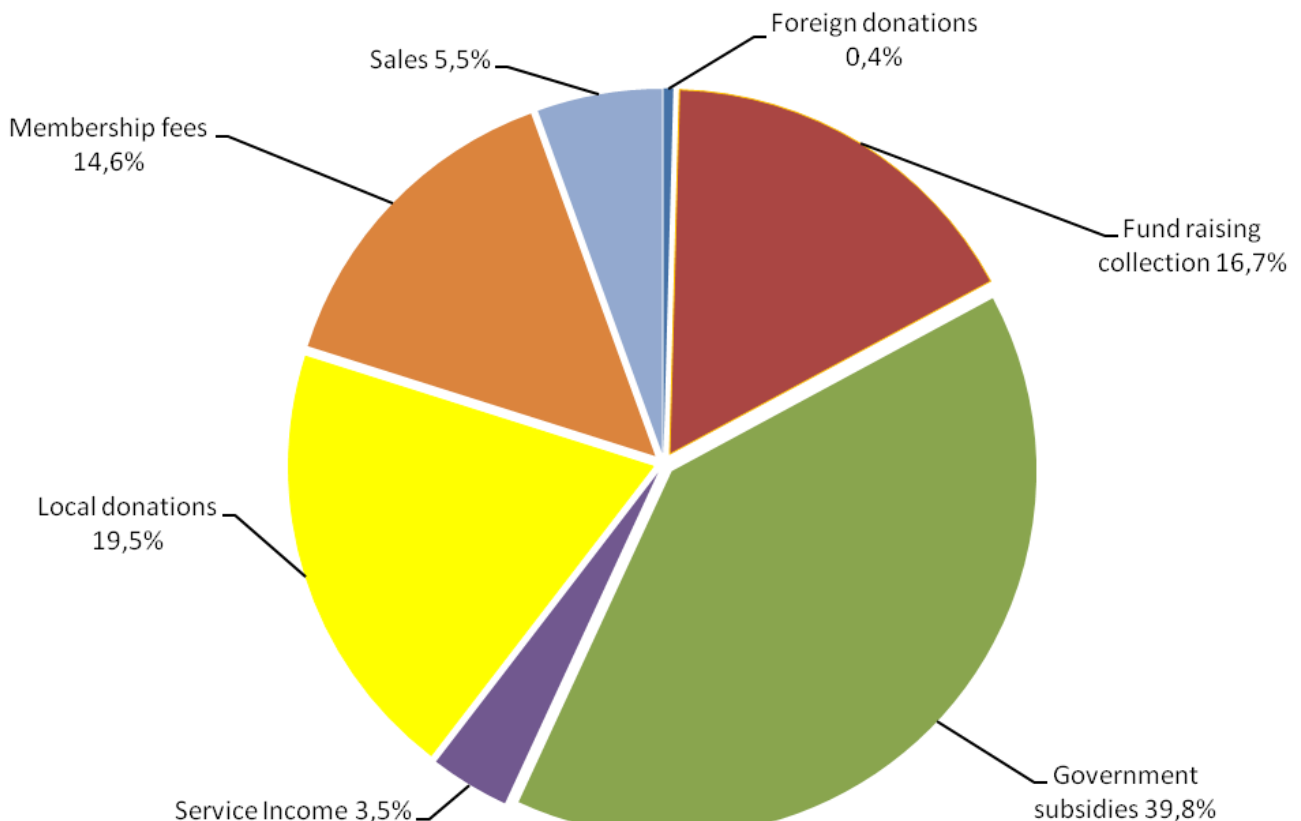
The advantageous effects of retaining death taxes will now be applied to South Africa's sociological environment.

5.5.1.1 DEATH TAXES ENCOURAGE CHARITABLE GIVING THROUGH INCENTIVES TO ESTATES

The current legislation in South Africa notes that the net value of an estate shall be calculated after deducting any bequests made to public benefit organisations. The legislation incentivises people to leave a portion of the estate to a charity to be able to decrease the estate’s tax liability.

There are numerous charities at work in South Africa due to the large portion of the population living on or below the breadline. Statistics released by Statistics South Africa has indicated that up to 19.5% off all the income received by charities come from local donations (Statistics South Africa, 2013:34). Unfortunately no information is currently available to indicate what portion was from bequests of estates directly, however it is clear that a large portion of the income is given by individuals whether it is when they are living or from their estates.

Figure 5: Income sources for South African charities



Should death taxes be abolished, the tax benefit will also be removed and the only other benefit available will be the R100 000 donations tax exemption. This could well affect the functioning of these charities due to a decrease in bequests from an individual's estate.

5.5.1.2 DEATH TAXES GENERATE REVENUE THAT IS USED FOR THE UPLIFTMENT OF COMMUNITIES BY GOVERNMENT

Vote 19 of the 2013 budget relates to social development. The document states the following strategic goals which the government is striving towards (National Treasury, 2013):

- To reduce income poverty.
- To increase household food security.
- To improve service delivery.
- To prevent new HIV infections.
- To improve the quality of early childhood development.
- To reduce the demand for illegal substances in local communities.

The abovementioned goals highlight the current needs and expectations of the South African population. The government needs to invest large sums of money to ensure that the quality of life of the majority of South African residents are improved and brought to an acceptable level. These goals support the basic needs and rights that all individuals should have.

As can be seen from the budget table noted below, these goals bear a massive financial burden on the government. Death taxes do not account for a large amount of revenue for the state, but there is a dire need for all the funds that are generated. It is therefore vital that all available sources of income are kept by the government to ensure that its goals are met.

Figure 6: Total expenditure estimates per Vote 19 of the 2013 budget

Budget summary

| R million | 2013/14 | | | | 2014/15 | 2015/16 |
|--|--------------------------|------------------|-------------------------|-----------------------------|------------------|------------------|
| | Total to be appropriated | Current payments | Transfers and subsidies | Payments for capital assets | Total | Total |
| MTEF allocation | | | | | | |
| Administration | 264.0 | 261.5 | – | 2.5 | 278.8 | 293.3 |
| Social Assistance | 113 006.8 | – | 113 006.8 | – | 121 482.1 | 129 493.3 |
| Social Security Policy and Administration | 6 417.9 | 104.4 | 6 312.3 | 1.2 | 6 682.5 | 6 950.8 |
| Welfare Services Policy Development and Implementation Support | 513.1 | 191.0 | 320.2 | 1.9 | 525.7 | 545.7 |
| Social Policy and Integrated Service Delivery | 289.7 | 81.5 | 207.5 | 0.8 | 310.2 | 327.0 |
| Total expenditure estimates | 120 491.6 | 638.4 | 119 846.8 | 6.4 | 129 279.4 | 137 610.1 |

5.5.2 POSSIBLE BENEFICIAL EFFECTS OF ABOLISHING DEATH TAXES

The advantageous effects of abolishing death taxes will now be applied to South Africa's sociological environment.

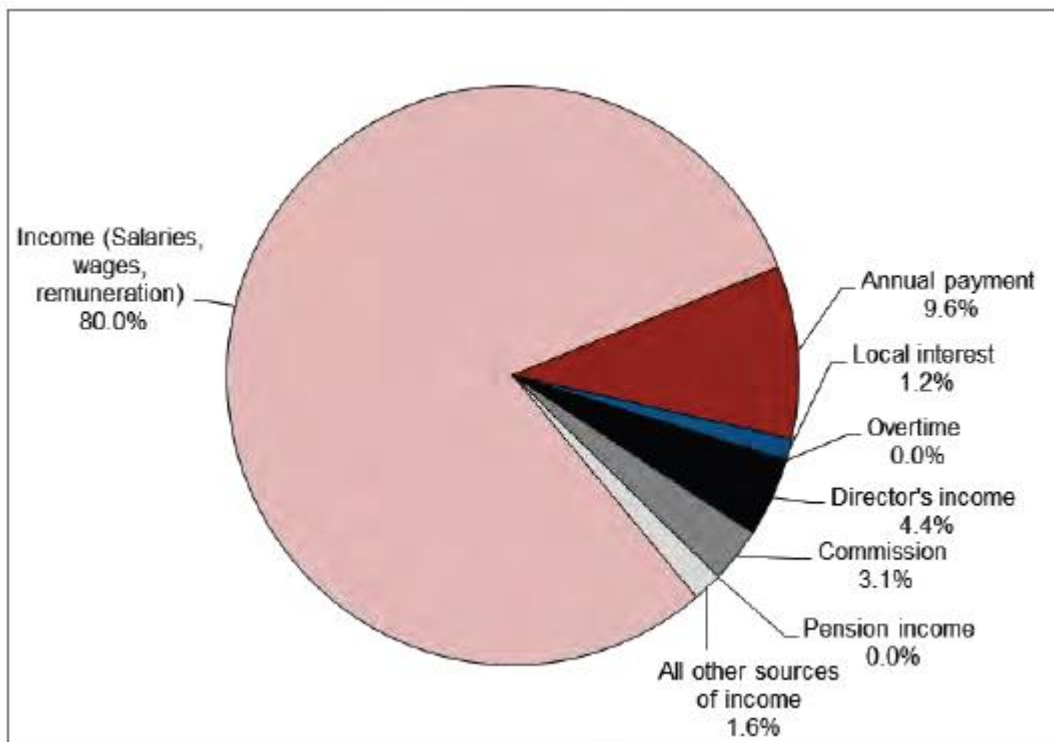
5.5.2.1 THE ABOLISHMENT OF DEATH TAXES WILL INCREASE THE PERCEIVED FAIRNESS OF THE TAX SYSTEM, WHICH WILL IMPROVE TAX COMPLIANCE

An increase in tax compliance by South Africans will ensure that a larger amount of tax revenue is collected by the tax authority. As stated earlier, the country currently funds a large number of individuals and organisations through its tax revenues by way of social grants.

As per the 2012 statistics released by SARS, the amount of personal income tax payers has increased from 5.2 million in 2008 to 10.3 million in 2011 and then to 13.7 million in 2012 (South African Revenue Services, 2012:13). Therefore the amount of people registered for income tax has more than doubled in the last four years. This is due to the recent drives of SARS to ensure that all employees are registered for income tax, whether the employee is required to submit an income tax return or not. SARS has put the onus on the employers to ensure that all the employees have tax registration numbers. According to the statistics noted above it has been a hugely successful campaign.

As noted in the figure below (South African Revenue Services, 2012) the largest portion of personal income tax relates to salaries for services rendered. Due to the abovementioned procedures that have been put in place, there is therefore very little opportunity left for individuals to still receive remuneration without it being declared to SARS.

Figure 7: Breakdown of personal income tax for the 2011 taxation year



The abolishment of death taxes might increase the perceived fairness of the tax system in South Africa and therefore increase the amount of tax compliance, however from the abovementioned data it is very unlikely that this will lead to a material increase in the amount of revenue collected by SARS.

The increased compliance will therefore not lead to a materially larger amount of revenue collection by the government and the effect on the government's social funds will be immaterial.

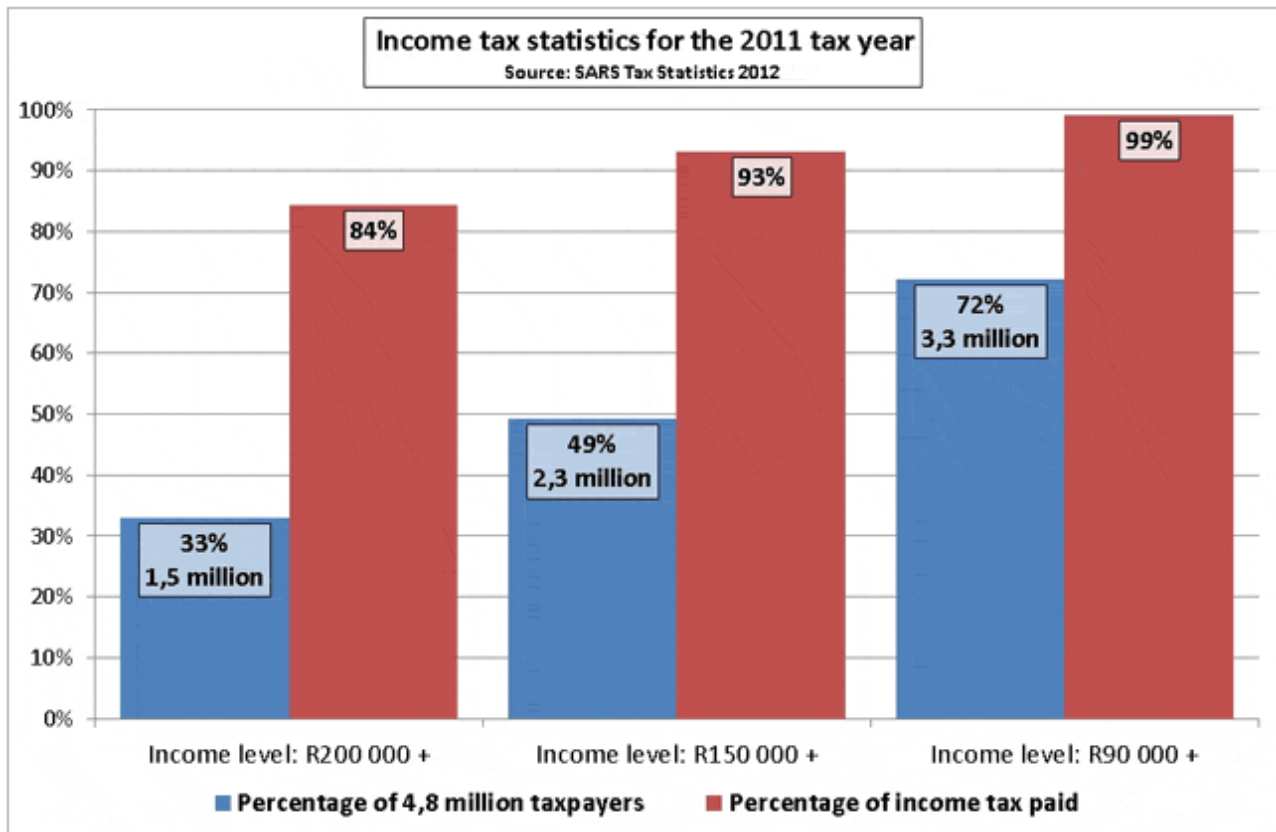
5.5.2.2 THE ELIMINATION OF DOUBLE TAXES WILL ALLEVIATE SOME OF THE BURDEN PLACED ON THE MINORITY OF CITIZENS TO FUND THE GOVERNMENT'S OPERATIONS

As noted above, in 2012 there were 13.7 million tax payers registered for income tax in South Africa. This figure does however not correctly reflect the amount of people that were liable to pay income taxes. This is due to the fact that the number includes people that were registered for income tax that were not liable for tax payments due to the fact that their income was less than the required rate or that the person was unemployed.

The data released by SARS indicates that only 4.8 million individuals were required to submit tax returns. Of the 4.8 million individuals 0.2 million people submitted tax returns for the year with no taxable income. Approximately 1.3 million people that filed tax returns had an income of less than R90 000 for the year. These individuals therefore contributed less than 1% of the income received from individuals. Therefore about 99% of the total revenue collected from individuals came from approximately 3.3 million individuals.

1 million individuals earning between R90 000 and R150 000 contributed 5.9% of the total income tax. If one deducts all individuals earning between R150 000 to R200 000 it will indicate that about 84% of all income taxes are paid by 1.5 million individuals (Moneyweb.co.za, 2013).

Figure 8: Contributions of income tax per income level for the 2011 taxation year



One can therefore clearly see that there is a massive tax burden on a select few individuals in South Africa. The abolishment of death taxes that mainly affect the wealthy will therefore give much needed relief to these individuals.

5.6 CONCLUSION

There are currently huge income disparities in South Africa. A very small portion of the country is living in security estates and has access to great medical care and other basic services. On the other hand, the majority of the country is living below the breadline and is reliant on social grants and free services that are supplied by the government for survival.

Unfortunately this means that there is a massive burden placed on a small portion of the country to ensure that these much-needed services are available to those that need it the most. It might be seen as unfair to the rich that they need to carry this burden, however from a sociological point of view there is currently no other choice available for the government.

CHAPTER 6

CONCLUSION

6.1 INTRODUCTION

The main objective of this study was to evaluate the numerous arguments and statements made by various academia and economists about the possible abolishment of death taxes. These arguments needed to be evaluated against the unique South African climate so as to be able to assess what the possible impact of the abolishment might be on this country.

6.2 PURPOSE STATEMENT AND RESEARCH OBJECTIVES

The purpose of this was to evaluate the reasonableness of numerous arguments made for the abolishment or retention of death taxes against the unique South African climate. The possible advantages and disadvantages of the tax were measured against the current South African climate.

The study was guided by the following research objectives:

- To evaluate whether the arguments made by the opponents and proponents of death taxes are applicable to the unique South African environment.
- To evaluate the possible effects of abolishing death taxes in South Africa against the current economic and political environment.

6.3 SUMMARY OF FINDINGS

There are numerous possible advantages and disadvantages to having death taxes as part of a country's tax regime. It is unlikely that any proponent or opponent of the tax will not admit that the other parties' comments and statements have some form of truth embedded in them.

The challenge, however, is to determine the applicability of the arguments in a South African context. This is due to the fact that no matter how similar countries may be, it is still a reality that the answer for one country will most likely not be the answer for another.

The arguments made by the numerous experts and academia were therefore measured against the current South African climate to determine their applicability. It was found that a number of assumptions were not applicable to South Africa and should not be taken into account when evaluating the future of death taxes. The applicable arguments are summarised as follows:

The possible beneficial economic effects of keeping death taxes:

- Death taxes generate valuable income for governments to be able to function optimally.
- Death taxes stimulate the economy by ensuring that individuals stay economically active for longer.

The possible beneficial economic effects of abolishing death taxes:

- Death taxes financially damage small and family-owned businesses. However, the actual materiality of the impact of the tax on these small and family-owned businesses is unknown.

The possible beneficial political effects of keeping death taxes:

- Death taxes help the advancement of income equality.
- Death taxes could increase political support due to increased spend on the basic needs of the poor.

The possible beneficial political effects of abolishing death taxes:

- There are no material detrimental political effects.

The possible beneficial sociological effects of keeping death taxes:

- Death taxes encourage charitable giving through incentives to estates.
- Death taxes generate revenue that is used for the upliftment of communities by government.

The possible beneficial sociological effects of abolishing death taxes:

- The elimination of double taxes will elevate some of the burden placed on the minority of citizens to fund the government's operations.

6.4 SUMMARY OF CONTRIBUTIONS

The first contribution made by this study was to demonstrate that one cannot simply accept the statements made by experts in their field as the ultimate truth. The circumstances and background that lead to those statements need to be evaluated as well as the possible impact on the current circumstances.

The other contribution of this study was that it highlighted the unique and challenging environment that exists in South Africa. The government needs to evaluate the probable effects of all of their decisions on the environment as a whole to ensure that the country is uplifted and improved.

6.5 SUGGESTIONS FOR FUTURE STUDIES

As was noted throughout this study, there is very little information available with regard to the actual application of the revenues raised by death taxes. Future research needs to investigate the possible effects on the areas that the current death tax revenues are being spent on. Possible alternatives for death taxes can then be measured against the South African climate to evaluate their probability of success and to determine whether they address the shortcomings of death taxes.

6.6 CONCLUSION

Death taxes do have numerous shortcomings and in certain ways they affect the current South African climate negatively. However, the advantages of the tax currently outweighs all of these arguments.

South Africa is still a relatively young country with regard to its democracy and it still has a long way to go to correct the wrongdoings and challenges of the past. It is the duty of the

government to ensure that the lives of its people are improved and that they have access to certain basic services. For them to be able to deliver this duty, they unfortunately need to tax those that are in a position to pay.

The advantageous effects of death taxes therefore outweigh the detrimental effects thereof and therefore for the foreseeable future the death taxes should stay part of the South African tax regime.

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