

**IS IT TIME TO ABOLISH ESTATE DUTY IN SOUTH AFRICA?
A COMPARATIVE LOOK AT GLOBAL TRENDS IN LEVYING DEATH
TAXES AND THE FEASIBILITY OF SUGGESTED CHANGES TO SOUTH
AFRICA'S CURRENT REGIME**

By

LINDSEY LEE THORPE

Student Number:

THRLIN002

Research dissertation presented for the approval of Senate in fulfilment of part of the requirements for the LLM in Commercial Law in approved courses and a minor dissertation. The other part of the requirement for this qualification was the completion of a programme of courses.

at the

UNIVERSITY OF CAPE TOWN

Prepared under the supervision of Prof Trevor S. Emslie

Word Count: 24 278

The copyright of this thesis vests in the author. No quotation from it or information derived from it is to be published without full acknowledgement of the source. The thesis is to be used for private study or non-commercial research purposes only.

Published by the University of Cape Town (UCT) in terms of the non-exclusive license granted to UCT by the author.

February 2015

DISCLAIMER

I hereby declare that I have read and understood the regulations governing the submission of LLM in Commercial Law dissertations, including those relating to length and plagiarism, as contained in the rules of this University, and that this dissertation conforms to those regulations.

Lindsey Lee Thorpe

2015

TABLE OF CONTENTS

ABSTRACT.....	9
LIST OF TABLES.....	10
INTRODUCTION.....	11
CHAPTER 1 : THE CONCEPT OF TAXATION.....	13
1.1 A Brief Global History of Tax.....	13
1.2 What is Taxation.....	13
1.2.1 Wealth Transfer Taxes.....	14
1.2.1.1 Inheritance or Estate Tax.....	14
1.2.1.2 Net Wealth Taxation.....	15
1.2.1.3 Capital Gains Tax.....	15
1.2.1.4 Donations or Gift Tax.....	17
CHAPTER 2 : THE OBJECTIVES OF TAXATION.....	19
2.1 Revenue.....	19
2.2 Socio-Economic Objectives.....	20
2.2.1 Redistribution of Resources.....	20
2.2.2 Economic Growth.....	21
2.2.3 Sin Taxes.....	22

CHAPTER 3 : ESTATE DUTY IN SOUTH AFRICA	23
3.1 Introduction	23
3.2 Application	23
3.3 What is Property.....	24
3.4 Excluded Property.....	25
3.5 Property Deemed to be Property.....	26
3.5.1 Domestic Policies on the Life of the Deceased	26
3.5.2 Payments from Pension and other Funds on Death.....	27
3.5.3 Donated Property.....	27
3.5.4 Claim under the Matrimonial Property Act.....	28
3.5.5 Property which the Deceased was Competent to Dispose of for his or her own Benefit or for the Benefit of his or her Estate.....	28
3.6 Allowable Deductions.....	29
3.6.1 Deductible Expenses.....	29
3.7 Exemptions.....	30
3.8 The Section 4A Primary Rebate.....	33
CHAPTER 4 : CAPITAL GAINS TAX IN SOUTH AFRICA.....	34
4.1 Introduction.....	34

4.2	Determining Capital Gains Tax.....	34
4.3	Application of Capital Gains Tax.....	35
4.4	The Capital Gains Tax Event.....	36
4.5	An Asset for Capital Gains Tax Purposes.....	36
4.6	Capital Gains Tax on Death.....	37

CHAPTER 5 : DEATH TAXES & PROBLEMS FROM A SOUTH

AFRICAN PERSPECTIVE.....	39
5.1 Double Taxation.....	39
5.1.1 An Example of Double Taxation.....	40
5.1.2 Concessions Provided by the Legislature.....	40
5.2 Other Problems.....	41
5.2.1 Estate Duty and Capital Gains Tax Avoidance.....	41
5.2.2 Revenue Versus Cost.....	42

CHAPTER 6 : ARGUMENTS FOR AND AGAINST DEATH TAXES.....

6.1 The Case Against Death Taxes.....	44
6.2 The Case For Death Taxes.....	46
6.3 Going Forward.....	48

CHAPTER 7 : DEATH TAXES IN THE UNITED KINGDOM.....

7.1 Introduction.....	50
-----------------------	----

7.2	What is Inheritance Tax (Estate Tax) and How is it Calculated....	51
7.2.1	Exempt Transfers.....	51
7.2.1.1	Potentially Exempt Transfers.....	51
7.2.1.2	The Annual Exemption.....	52
7.2.1.3	The Small Gift Exemption.....	52
7.2.1.4	Wedding and Civil Partnership Gifts.....	52
7.2.2	Potentially Exempt Transfers	52
7.2.3	Chargeable Transfers: Lifetime and Death.....	52
7.2.4	Nil Rate Band.....	53
7.3	Capital Gains Tax.....	53
CHAPTER 8 : DEATH TAXES IN THE UNITED STATES.....		58
8.1	Introduction.....	58
8.2	The Estate Tax.....	59
8.2.1	The Calculation of Federal Estate Tax.....	62
8.2.1.1	Retained Interests.....	62
8.2.2	State Estate Tax.....	63
8.3	Gift Tax.....	63
8.4	Generation-Skipping Transfer Tax.....	63
8.5	Capital Gains Tax.....	64

CHAPTER 9 : DEATH TAXES IN CANADA.....	67
9.1 History of Wealth Transfer Tax.....	67
9.2 Current Situation	69
CHAPTER 10 : DEATH TAXES IN AUSTRALIA.....	70
10.1 History of Wealth Transfer Tax.....	70
10.2 Current Situation.....	71
CHAPTER 11 : DEATH TAXES IN INDIA.....	73
11.1 History of Wealth Transfer Tax.....	73
11.2 Current Situation.....	75
CHAPTER 12 : DEATH TAXES IN BOTSWANA.....	77
CHAPTER 13 : DEATH TAXES IN THE NETHERLANDS.....	79
CHAPTER 14 : SUGGESTIVE ALTERNATIVES TO THE CURRENT REGIME.....	81
14.1 Retaining Estate Duty and Forgoing Capital Gains Tax on Death.....	81
14.2 Abolishing Estate Duty and Relying only on Capital Gains Tax.....	83
14.2.1 The Advantages of Relying Solely on Capital Gains Tax.....	84

14.2.2	The Disadvantages of Relying Solely on Capital Gains Tax.....	87
14.3	Replacing Estate Duty with an Inheritance Tax	88
14.4	Conclusion	89
	CHAPTER 15 : CONCLUSION.....	92
	BIBLIOGRAPHY.....	94

ABSTRACT

This dissertation examines the current system of taxation that is imposed in South Africa on the death of a taxpayer. The main focus of the research, among others, is on the issues associated with a taxpayer having to pay both estate duty and capital gains tax upon his or her death, resulting in a form of 'double taxation', and whether a different system of taxation should be implemented in South Africa. The two main taxes imposed on death in South Africa are studied and arguments for and against the imposition of death taxes are considered. In order to determine what the most fair and reasonable tax system for South Africa would be, various taxation models of other jurisdictions are examined, namely those followed by the United States, the United Kingdom, Canada, Australia, India, Botswana and the Netherlands. Suggested alternatives and their suitability are identified, such as the possibilities of retaining estate duty and 'forgiving' capital gains tax on death (as is done in the United States, United Kingdom, Australia, India and Botswana); abolishing estate duty and imposing only capital gains tax on death (a system followed by Canada); replacing estate duty with an inheritance tax (like in the Netherlands) or retaining the current system in place. Ultimately, it is decided that South Africa should not abolish estate duty or rely solely on capital gains tax or implement a system of inheritance tax. Instead, we should retain the current system as there are already concessions provided by the legislature which aid the majority of South Africans and guard against unfair results occurring in the winding up of their estates. A suitable alternative would be to rely only on capital gains tax, but any amendments would result in major changes to current legislation. Furthermore, it is important to first ascertain whether relevant stakeholders, such as the South African Revenue Service or the Master of the High Court, would have the necessary resources, capacity and time to train staff, educate taxpayers and update their current systems in order to successfully implement these changes and efficiently process deceased estates.

List of Tables

Table 1	19
Table 2	20
Table 3	42
Table 4	43
Table 5	43
Table 6	60

INTRODUCTION

According to the age old saying, first coined by Christopher Bullock in 1716, there are two certainties in life: death and taxes. While death still remains a certainty, paying taxes upon death might not have to be. Since 2001 it has been seriously debated in South Africa whether, with the introduction of capital gains tax, estate duty would be continuously reduced and eventually abolished. It has been argued that the current system creates a form of double taxation upon death, among other problems.

As a result of capital gains tax coming into operation, Finance Minister Pravin Gordhan, in his 2010 budget speech, first mentioned that the levying of estate duty would be reviewed as it constituted a comparatively small amount of revenue, not to mention the administration thereof being cumbersome. Moreover, its efficacy was debatable as many wealthy individuals were able to escape estate duty liability through trust-creation and other means.

Since 2010 the subsequent budget speeches have not made mention of any reviews to this section of the law, and in the most recent 2014 budget speech, Minister Gordhan stated once again that estate duty would be reviewed during the course of 2014.

However, in the most recent development, Minister Gordhan announced earlier this year that Judge Dennis Davis of the High Court would chair a commission of enquiry into the tax structure of South Africa. In June 2014 the Davis Tax Committee made calls for submissions by the end of July 2014 on the review of the tax system and estate duty's role and continued relevance in supporting a more equitable and progressive tax system. During the inquiry, the committee stated that the interaction between capital gains tax and estate duty would be reviewed. It is yet to be announced what outcomes, if any, have been reached in light of the review carried out and it is expected that the above issues will only be fully addressed in 2015.

The aim of this dissertation is to examine why it has been proposed that estate

duty should be repealed, in addition to whether it should be abolished and capital gains tax solely relied upon and extended. In doing so, a brief history of tax on a worldwide basis will be examined, including a discussion on the concept of 'taxation' as well as an overview of the specific wealth transfer taxes of inheritance or estate tax, net wealth tax, capital gains tax and donations or gift tax.

The dissertation shall then look at the various objectives of taxation, and take a closer look at the nature of estate duty and capital gains tax, accompanied by a historical overview of these wealth transfer taxes in South Africa. Problems encountered from a South African perspective will be considered as well as contrasting arguments for and against death taxes in general.

Thereafter, an analysis of selected countries' wealth transfer systems shall be conducted. In particular, this study shall examine countries that have either retained estate duty and in most circumstances 'forgiven' capital gains tax on death, including the United States, the United Kingdom, Australia, India and Botswana; abolished estate duty and relied solely on capital gains tax, such as the Canadian example; or replaced estate duty with a system of inheritance tax, such as in the Netherlands.

Alternatives based on the above examples will then be considered within the context of South Africa's current death tax landscape. A submission shall then be made as to whether estate duty should either be retained and capital gains tax 'forgiven' on death; or whether estate duty should be abolished and capital gains tax solely relied upon; or whether estate duty should be replaced with an inheritance tax; or lastly whether the current system should be retained.

CHAPTER 1 : THE CONCEPT OF TAXATION

1.1 A Brief Global History of Taxation

People have been paying taxes for many centuries, but these contributions did not always take the form that they do today. Taxation is generally used by governments to boost productivity and economic prosperity within their country and to assist in limiting the burden placed on the government to support its people. According to Muller, taxation can first be traced back to Ancient Egypt (around 3000 BCE-2800 BCE), where the pharaoh would travel around the kingdom and collect donations from his subjects. In other empires, such as those in Rome and in Greece, taxes were collected by force through wars, harbour tariffs, tolls and customs and through trade.¹ In other European jurisdictions, the collection of taxes was initially voluntary and was collected through excise taxation on commodities such as salt, beer, soap, candles, leather and meat.² It was only during the Middle Ages that the notion developed that taxation should be developed into a compulsory system used by governments to collect revenue from its people.³ This concept became more entrenched what with the development of nation states and an increased need for funds to cover government expenditure. In the modern era, the system of taxation has become far more regulated, and most governments are held accountable to their citizens. Fiscal legislation and constitutional restrictions are put in place when taxing their citizens and governments cannot be seen to have unlimited powers in this regard.⁴

1.2 What is Taxation

¹ E Muller *Framework for Wealth Transfer Taxation in South Africa* PhD (Pretoria) (2010) 12.

² Muller op cit (n1) 13.

³ Ibid.

⁴ Muller op cit (n1) 14.

Taxation is the compulsory payment of contributions by the public or a part thereof to the government according to certain national and sub national guidelines, the purpose of which is to subsidise government expenditure whilst at the same time trying to achieve certain social-economic and political goals for the benefit of the public.⁵

Taxes can be classified into three categories, namely: income, wealth and consumption.⁶ The focus of this study shall be on the taxation of wealth in line with the topic of this dissertation.

1.2.1 Wealth Transfer Taxes

These taxes are charged on inheritances, gifts and estates and are referred to by many different names throughout the world.⁷ They are imposed on the assets of the deceased while at the same time any liabilities or special circumstances of the deceased are taken into account.⁸

1.2.1.1 Inheritance or Estate Tax

In some countries, the beneficiaries of the deceased estate could be taxed as a result of receiving a bequest, at specific rates which usually depend on the relationship between the deceased and the beneficiary him or herself. This type of taxation is sometimes referred to as an 'inheritance tax'.⁹ Other states instead tax the deceased estate itself and this is referred to as an 'estate tax' or 'estate duty'. South Africa currently uses the latter option when it comes to taxing wealth transfers on death.¹⁰

⁵ Muller op cit (n1) 15.

⁶ Ibid.

⁷ Muller cites the following examples: 'death duty', 'probate duty', 'legacy duty', 'succession duty', 'estate duty', 'estate tax', 'capital transfer tax' and 'inheritance tax'.

⁸ Muller op cit (n1) 25.

⁹ Ibid.

¹⁰ Muller op cit (n1) 26.

1.2.1.2 Net Wealth Taxation

Another method which used to be common among certain countries was the concept of net wealth taxation. This type of tax is generally levied annually on the accrual in the value of the taxpayer's assets, usually above a specified exemption limit. This tax used to be very popular in certain European countries however many have recently abolished or amended such taxes. It is still used in only a handful of European countries today¹¹ and is still currently used in India. South Africa does not levy any net wealth tax. The countries that abolished this type of wealth transfer tax did so for various reasons, including cumbersome administration and the high costs involved in collecting the taxes. There has been a rise in countries abolishing this type of tax in favour of one based on taxing a taxpayer on the net increase on his or her capital assets by virtue of a realisation-based capital gains tax.¹²

1.2.1.3 Capital Gains Tax

Capital gains tax was first implemented in the United States in 1913. Prior to 1950 most European countries however, did not make use of this type of tax and instead imposed a net wealth on capital assets tax. It was only introduced in most European countries between 1958 and 2000 in an effort to improve the tax systems in those countries.¹³ It was either implemented through amending existing income tax legislation¹⁴ or it was introduced in a new statute.¹⁵

Capital gains tax is different from net wealth tax as the former is imposed on a realisation basis, whereby only the gains that have accrued to the taxpayer on the disposal (usually by way of a sale or exchange) of his or her capital assets during the year of assessment are taxed. A capital gain is

¹¹ E.g. Norway, Sweden, Switzerland, France and Spain.

¹² Muller op cit (n1) 27.

¹³ Muller op cit (n1) 28.

¹⁴ Such as Australia, Canada, France, Japan, Sweden and Spain.

¹⁵ Such as the UK, Italy and Ireland.

generally assessed as ‘the difference between the (1) original acquisition price (or value) plus value enhancement expenditures and (2) the consideration received for the asset on disposal. It is therefore a tax levied on the ‘profit’ made by the taxpayer on the disposal of his or her capital assets’.¹⁶

When a person passes away, he or she will not be able to realise a capital asset in the future. This does not mean that these unrealised gains are lost, and depending on the circumstances, will be dealt with in either of the following two methods¹⁷: Either the deceased’s assets will be deemed to have been realised on the date of his or her death which means that the deceased will be taxed as if he or she had disposed of the assets falling into his or her deceased estate. Muller refers to this method as the ‘deemed realisation approach’. It is this approach that is followed in South Africa. The other method involves the tax liability on the unrealised gain being placed on the heir(s) of the deceased estate but will be delayed until the heir(s) actually dispose of the asset. Here the heir(s) take over the acquisition cost (referred to as the ‘base cost’) from the deceased and the heir will be liable for capital gains tax on the total gain only upon the eventual disposal of the property. Muller refers to this method as the ‘carry-over’ approach.¹⁸

Muller also describes another approach whereby no capital gains tax is levied on the unrealised gains whatsoever as the heir(s) take over the asset at base cost which is equal to the market value on the date of the deceased’s death. She refers to this as the ‘stepped-up’ approach.¹⁹

In South Africa, capital gains tax was first introduced in 2001 in the Eighth Schedule to the Income Tax Act²⁰. It was argued that implementing this tax in South Africa would be advantageous since there were already mechanisms in place for its administration and collection as a result of the implementation of the Income Tax Act itself.²¹ Section 26A of the Income Tax Act deals with capital gains tax and states that ‘there shall be included in the

¹⁶ Muller op cit (n1) 29.

¹⁷ Ibid.

¹⁸ Muller op cit (n1) 30.

¹⁹ Ibid.

²⁰ Income Tax Act 58 of 1962.

²¹ Muller op cit (n1) 31.

taxable income of a person for a year of assessment the taxable capital gain of that person for that year of assessment, as determined in terms of the Eighth Schedule'.²²

The Eighth Schedule, in turn, sets out how a person's taxable gain is to be determined. It allocates a certain percentage to a person's net capital gain which is determined by multiplying the net capital gain with a specific inclusion rate. The inclusion rate is the portion of the capital gain which is included in a person's taxable income. For a natural person or special trust, the inclusion rate is 33.3 per cent and for a company, close corporation and ordinary trust the inclusion rate is 66.6 per cent.²³

1.2.1.4 Donations or Gift Tax

In many countries around the world, donations or gift tax is levied on any gifts made to individuals during a person's lifetime. It is not a tax on income but a tax on the transfers of assets or wealth. The Act defines donation as 'any gratuitous disposal of property or any gratuitous waiver or renunciation of a right'. In South Africa this tax is governed by sections 54 to 64 of the Income Tax Act which levies tax on donations made by a natural person, corporate entity or a trust.²⁴

A person is responsible for donations tax on any gift that is given or received for no consideration or less than the market value, without obligation or payment in return. It is the responsibility of the donor to pay the donation tax and it must be paid within three months from the date that the donation took place. Should the donor fail to pay the donation tax, then the donor and the donee will become jointly and severally liable for the tax.²⁵

²² Section 26A of the Income Tax Act 58 of 1962.

²³ For the 2014 year of assessment, the maximum rates payable on capital gains are as follows: 33.3 per cent x 40 per cent = 13.3 per cent for natural persons and special trusts; 66.6 per cent x 40 per cent = 26.6 per cent for ordinary trusts and 66.6 per cent x 28 per cent = 18.6 per cent for corporate entities such as companies and close corporations.

²⁴ Section 55 of the Income Tax Act 58 of 1962.

²⁵ Section 59 of the Income Tax Act 58 of 1962.

The Act provides for, among others, an annual exemption in the amount of R100 000 and this is available to natural persons on the total amount of all assets donated during any year of assessment.²⁶ Other exemptions include donations between spouses, bona fide maintenance payments, donations to public benefit organisations, donations where the donee will not benefit until the death of the donor, donations between companies forming part of the same group of companies, property disposed of under and in pursuance of any trust, donations of property or a right in property situated outside South Africa if acquired by the donor before becoming a resident in South Africa for the first time or by inheritance or donation from a non-resident.²⁷

In summary, South Africa imposes estate duty, capital gain tax and donations tax and does not levy any inheritance or net wealth taxation.

The next chapter will focus on what a system of taxation aims to achieve and will take a look at whether these objectives are actually being achieved, with particular reference to South Africa.

²⁶ Section 56 of the Income Tax Act 58 of 1962.

²⁷ Ibid.

CHAPTER 2 : THE OBJECTIVES OF TAXATION

According to Muller taxation has two main objectives: the first being to produce funding for public and government expenditure, whilst the second is to achieve certain socio-economic aims.²⁸

2.1 Revenue

Citizens are taxed in order to increase the amount of funds government has access to for public and government expenditure.²⁹ As can be seen in Table 1 below (from the 2014 Tax Statistics published by the South African Revenue Service) in South Africa, the gross tax revenue collected for the 2013/14 year of assessment was R900 billion and grew by R86.2 billion against the previous year from R813.8 billion. The non-tax revenue collected amounted to R29.78 billion.³⁰

Table 1: Total budget revenue and consolidated revenue, 2009/10 – 2013/14

R million	Tax revenue	% of budget revenue	% of consolidated revenue	Non-tax revenue ¹	Total tax and non-tax revenue	Less: SACU payments	Budget revenue	Other ²	Consolidated revenue ³
2009/10	598,705	103.3%	90.2%	15,323	614,028	-27,915	586,113	84,790	670,903
2010/11	674,183	100.7%	89.0%	16,474	690,657	-17,906	669,738	90,122	759,859
2011/12	742,650	100.3%	88.7%	24,403	767,053	-21,760	740,083	96,971	837,054
2012/13	813,826	103.4%	92.9%	28,087	841,913	-42,151	799,762	109,514	909,276
2013/14	900,015	101.5%	88.9%	29,776	929,791	-43,374	886,416	125,817	1,012,233

Source: National Treasury 2014 Statistics

Table 2 below shows that the tax revenue, as a percentage of gross domestic product, in the 2013/2014 year amounted to 26.1 per cent.³¹

²⁸ Muller op cit (n1) at 37.

²⁹ Ibid.

³⁰ National Treasury (Republic of South Africa) 'Tax Statistics', 21 October 2013, available at <http://www.treasury.gov.za/publications/tax%20statistics/2013/TStats%202013%20WEB.pdf>, accessed on 20 November 2014 at 12.

³¹ National Treasury op cit (n30) 6.

Table 2: Tax revenue as a percentage of GDP, 1994/95 – 2013/14

R million	Tax revenue	Nominal GDP ¹	Tax revenue as % of GDP
1994/95	113,775	497,189	22.9%
1995/96	127,278	564,159	22.6%
1996/97	147,332	635,187	23.2%
1997/98	165,327	699,825	23.6%
1998/99	184,786	757,087	24.4%
1999/00	201,266	837,241	24.0%
2000/01	220,119	951,736	23.1%
2001/02	252,295	1,048,506	24.1%
2002/03	281,939	1,203,145	23.4%
2003/04	302,443	1,303,907	23.2%
2004/05	354,979	1,449,020	24.5%
2005/06	417,196	1,613,812	25.9%
2006/07	495,549	1,832,762	27.0%
2007/08	572,815	2,075,413	27.6%
2008/09	625,100	2,296,571	27.2%
2009/10	598,705	2,456,629	24.4%
2010/11	674,183	2,749,532	24.5%
2011/12	742,650	2,981,828	24.9%
2012/13	813,826	3,198,579	25.4%
2013/14	900,015	3,448,980	26.1%

Source: National Treasury 2014 Statistics

2.2 Socio-Economic Objectives

There are also social and economic objectives which taxation aims to achieve. For instance, it helps aid the government's social policy of redistribution of resources, its policy of economic growth and repriming.³²

2.2.1 Redistribution of Resources

The Legislature considers itself duty bound to create a legal system in South Africa which can achieve political freedom, equality for all and fairness in distribution of resources so that the citizens of South Africa each have the opportunity to try and achieve their economic aspirations. By redistributing resources the government aims to provide more economic, socio-economic and political power to the poor (the majority of South Africans) so as to uplift these communities and remove some of the power possessed by the wealthy (the minority of South Africans). It hopes that by achieving these goals it can also alleviate some of the racial and ethnic tension that has been created by the overwhelming disparity. Hence the reason for the government taxing the

³² Muller op cit (n1) 38.

wealthy and middle class income groups in South Africa on a higher scale than those imposed on the poorer members of society. The government imposes these taxes in various forms, for example through the use of income tax and wealth taxes. Taxation has therefore become the norm of a democratic society.³³

There are however consequences to taxation. It could infringe on rights already entrenched in the Constitution, such as the right to property. It could result in more people trying to avoid or evade taxation or simply emigrating overseas, which would affect the economy. Therefore, the extent to which the government relies on this form of taxation will depend on the current political, social and economic climate.³⁴

2.2.2 Economic Growth

It is believed that taxation can also serve as a tool for economic growth and development of the economy which would in turn prevent high levels of inflation and unemployment while at the same time encouraging investment and saving.

Muller states that while the goals of investment and saving are admirable, some argue that fiscal incentives would not have a large positive effect on personal saving. There has been a move towards an international trend of a broad-based system with lower tax rates.³⁵

Some have suggested manipulating taxes to decrease the high unemployment rates. Muller states that in the short term, this is unlikely to be achieved. The government should focus more of their effort on long term enactments to increase employment figures, as they have recently done with

³³ Ibid.

³⁴ Muller op cit (n1) 39.

³⁵ Muller op cit (n1) 40.

the enactment of the Employment Tax Incentive Act 26 of 2013 (which was implemented with effect in South Africa on 1 January 2014).

2.2.3 Sin Taxes

The government also uses taxation as a way of levying taxes on certain products to discourage citizens from partaking in certain activities, such as on cigarettes to prevent smoking and alcohol to prevent excessive drinking. This is known as reprising and it has been subject to strong criticism as many argue that the government should not be involving itself in people's legal activities. The government however justifies its implementation of these taxes by arguing that they help pay for the social cost associated with the abuse of these products and as a result this discriminatory taxation is justified.³⁶

The aforesaid objectives of taxation also form an essential part of the reason as to why the government imposes death taxes. Death taxes also aim to generate revenue and fulfil certain socio-economic objectives. There are however detractors who suggest otherwise and argue that the imposition of these taxes has a negative effect on these objectives. Chapter 6 shall examine the global arguments for and against death taxes and the reasons therefor, but first it is necessary in the next chapter to discuss the two main death taxes that are imposed on a deceased estate in South Africa, namely estate duty and capital gains tax.

³⁶ Muller op cit (n1) 41.

CHAPTER 3 : ESTATE DUTY IN SOUTH AFRICA

3.1 Introduction

Estate duty is imposed in terms of the Estate Duty Act 45 of 1955 (hereinafter referred to as 'The Act'). It applies to the estate of any person who dies ordinarily resident in South Africa or leaves assets connected by situation or enforcement of rights in South Africa. It is imposed on the dutiable amount of a deceased estate.

The dutiable amount is determined by ascertaining the gross value of the estate (which means the total value of the assets the deceased owned at the time of his or her death). From the gross value there must be deducted all the amounts and values allowed by the Act, the balance being the net value. From this net value a statutory abatement is deducted which is currently set at R3.5 million, the balance being the dutiable amount on which the duty is calculated. From the dutiable amount there may be further deductions made in respect of transfer duty or foreign duties paid on property included in the estate, or amounts deducted for successive deaths within a period or because of double taxation agreements.³⁷

The tax is levied at the rates set out in the First Schedule to the Act.³⁸ The tax was initially levied at progressive rates, but since 1988 it has been levied at a flat rate. The initial flat rate of 15 per cent was increased to 25 per cent in 1996 but decreased to 20 per cent in 2001 where it currently remains.³⁹

3.2 Application

³⁷ D Meyerowitz *The Law and Practice of Administration of Estates and Estate Duty* 2007ed (2007) 27-2.

³⁸ Section 2(2) of the Estate Duty Act 45 of 1955.

³⁹ Meyerowitz op cit (n37) 27-3.

The Estate Duty Act levies a tax on the estate of every person who has died on or after 1 April 1955. A distinction is drawn on the basis of residency – in respect of property of a person who died whilst ordinarily resident in the Republic and the property of a person who was not so resident at the date of his or her death.⁴⁰

3.3 What is Property

Almost all of the property of a person who died ordinarily resident in the Republic is in principle chargeable under the Act, however there are certain exceptions. Although ‘ordinarily resident’ is not specifically defined in the Act, it has been held to mean the country to which a taxpayer would naturally and as a matter of course return from his or her wanderings: as contrasted with other lands it might be called his or her usual or principal residence and it would be described more aptly than other countries as his or her real home.⁴¹

According to s 3(1) of the Act, the estate of any person shall consist of all ‘property of that person’ as at date of death (and includes property mentioned in section 3(2) as well as property deemed to be property, as provided for in section 3(3) of the Act.

Therefore, under s 3(2), property includes: ‘any right in or to property, movable or immovable, corporeal or incorporeal, and includes—

- (a) any fiduciary, usufructuary or other like interest in property (including a right to an annuity charged upon property) held by the deceased immediately prior to his death;
- (b) any right to an annuity (other than a right to an annuity charged upon any property) enjoyed by the deceased immediately prior to his death which accrued to some other person on the death of the deceased’.

⁴⁰ Meyerowitz op cit (n37) 27-2.

⁴¹ Muller op cit (n1) 182.

3.4 Excluded Property

As mentioned above there are certain exceptions whereby some property will not be included in the deceased's gross assets and are allowed as deductions. These include the following:

- (a) in the case of a deceased who was not ordinarily resident in the Republic at the date of his death, any right in immovable property situate outside the Republic;
- (b) any right in movable property physically situate outside the Republic if the deceased was not ordinarily resident in the Republic at the date of his death;
- (c) any debt not recoverable or right of action not enforceable in the Courts of the Republic if the deceased was not ordinarily resident in the Republic at the date of his death;
- (d) any goodwill, licence, patent, design, trade mark, copyright or other similar right not registered or enforceable in the Republic or attaching to any trade, business or profession in the Republic if the deceased was not ordinarily resident in the Republic at the date of his death;
- (e) in the case of a deceased who was not ordinarily resident in the Republic at the date of his death –
 - i) any stocks or shares held by him in a body corporate which is not a company; and
 - ii) any stocks or shares held by him in a company, provided any transfer whereby any change of ownership in such stocks or shares is recorded is not required to be registered in the Republic;
- (f) any rights to any income produced by or proceeds derived from any property referred to in paragraph (e), (f) or (g);
- (g) so much of any benefit which is due and payable by, or in consequence of membership or past membership of, any pension fund, pension preservation fund, provident fund, provident preservation fund or

retirement annuity fund as defined in the Income Tax Act 58 of 1962 on or as a result of the death of the deceased.⁴²

3.5 Property Deemed to be Property

The estate of any person for the purpose of estate duty consists not only of the property of that person as at the date of his death but also of that property which in accordance with the Act is deemed to be property of that person at the date of his death.⁴³ Section 3(3) of the Act specifies what assets are deemed to be property of the deceased:

3.5.1 Domestic Policies on the Life of the Deceased

Although the proceeds of a life insurance policy payable to the deceased estate constitutes property of the deceased, the proceeds payable in terms of that policy to a nominated beneficiary do not fall part of the assets in the estate. In order to prevent a situation where a deceased simply nominates a beneficiary for a policy to avoid having it form within the estate and being taxed, the Act states that the benefit paid out under any policy of insurance, which is a 'domestic policy' upon the life of the deceased should be regarded as deemed property of the deceased.⁴⁴

Third party policies are not the only policies included in the estate. The proceeds of a domestic policy belonging to the estate, although already included as actual property in the estate, is also deemed to be property of the estate. In order to avoid these policies being taxed twice, they are only included once.⁴⁵

⁴² Section 3(2) of the Estate Duty Act 45 of 1955.

⁴³ Section 3(3) of the Estate Duty Act 45 of 1955.

⁴⁴ Section 3(3)(a) of the Estate Duty Act 45 of 1955.

⁴⁵ Muller op cit (n1)191.

An important aspect of these policies is that the deceased must be the life insured under the policy and it is not necessary that the deceased must have taken out the policy or had a financial interest in the policy or even paid the premiums in respect of the policy. If however, a Public Benefit Organisation or a surviving spouse is the beneficiary under the policy, the proceeds of the policy would be deducted under section 4(h) or 4(q) of the Act, respectively.⁴⁶

3.5.2 Payments from Pension and other Funds on Death

Pay-outs from pension funds, (not including annuities) have in the past been included in the deemed property of the estate. However, an amendment was effected in 2009 which resulted in the situation whereby any persons who die on or after 1 January 2009 will be excluded from this provision and their retirement funds will not be regarded as deemed property.⁴⁷

3.5.3 Donated Property

Any property under a *donatio mortis causa* (meaning made deliberately because of death) is property deemed to be property of the deceased. The donation must have, however, been made by the deceased. Here, either the ownership in the property does not pass until death, or if the property is delivered and ownership passes, the property must be returned if the donor does not in fact pass away. Also, the donation is only valid if the donee does not predecease the donor as the donation is only realised upon the death of the donor.⁴⁸

Donations *inter vivos* are with one exception not subject to estate duty. The exception is a donation exempt from donations tax under s56(1)(d) of the

⁴⁶ Ibid.

⁴⁷ Muller op cit (n1) 197.

⁴⁸ Meyerowitz op cit (n37) 27-29.

Income Tax Act, in other words a donation in terms of which the donee does not obtain any benefit until the donor has passed away.⁴⁹

In the case of property under a *donatio mortis causa* and the exception referred to above, and in respect of the estate of a person dying on or after 8 November 2005, the property concerned forms part of the donor's dutiable estate or is deemed to be included if it does not otherwise form part of the estate.⁵⁰

3.5.4 Claim under the Matrimonial Property Act

Should the deceased estate be entitled to a claim for accrual against the deceased's surviving spouse, provided that the spouses were married out of community of property subject to the accrual system in terms of section 3 of the Matrimonial Property Act⁵¹, then the claim is deemed to be property of the deceased at the date of his or her death.⁵²

3.5.5 Property which the Deceased was Competent to Dispose of for his or her own Benefit or for the Benefit of his or her Estate

A person is deemed to have been competent to dispose of any property if he or she had such power as would have enabled him or her, if they wished to appropriate or dispose of such property as he or she saw fit whether exercisable by will, power of appointment or in any other manner.⁵³

The deceased will also be regarded as having the power to dispose of property if he or she, under a deed of donation, settlement, trust or other

⁴⁹ Ibid.

⁵⁰ Ibid.

⁵¹ The Matrimonial Property Act 88 of 1984.

⁵² Section 3(3)(cA) of the Matrimonial Property Act 88 of 1984.

⁵³ Meyerowitz op cit (n37) 27-30.

disposition retained the power to revoke or vary the provisions thereof, relating to such property.⁵⁴

The power to revoke, appropriate or dispose shall be deemed to exist if the deceased could have obtained such power directly or indirectly by the exercise, either with or without notice, of power exercisable by him or her or with his or her consent.⁵⁵

3.6 Allowable Deductions

Estate duty is calculated on the dutiable amount of the estate, meaning the net value less the abatement. The net value of the estate represents the total amount of all the property of the deceased and of all the property deemed to be property of the deceased less all such amounts as are allowed to be deducted from such total value.⁵⁶

3.6.1 Deductible Expenses

The Act sets out the deductions, some of which are as follows:

3.6.1.1 so much of the funeral, tombstone and death-bed expenses of the deceased, which the Commissioner considers to be fair and reasonable;⁵⁷

3.6.1.2 all debts due by the deceased to persons ordinarily resident in the Republic which it is proved to the satisfaction of the Commissioner to have been discharged from property included in the estate;⁵⁸

⁵⁴ Ibid.

⁵⁵ Ibid.

⁵⁶ Meyerowitz op cit (n37) 28-1.

⁵⁷ Section 4(a) of the Estate Duty Act 45 of 1955.

⁵⁸ Section 4(b) of the Estate Duty Act 45 of 1955.

- 3.6.1.3 all costs which have been allowed by the Master of the High Court in the administration and liquidation of the deceased estate, other than expenses incurred in the management and control of any income accruing to the estate after the date of death;⁵⁹
- 3.6.1.4 all the expenditure incurred in carrying out the requirements of the Master or the Commissioner in pursuance of the provisions of this Act;⁶⁰
- 3.6.1.5 any debts due to persons ordinarily resident outside the Republic discharged from property included in the estate, but only to the extent that such debts exceed the value of any assets of the deceased situated outside the Republic and not included in the deceased estate;⁶¹ and
- 3.6.1.6 the amount of any claim for accrual against the estate acquired by the surviving spouse of the deceased, who was married out of community of property to the deceased, in terms of the Matrimonial Property Act of 1984.⁶²

3.7 Exemptions

- 3.7.1 The Act provides that the value of any property included in the estate which has not been allowed as a deduction under any other provision of this section, may be deducted against the value of the deceased estate, which accrues or accrued by way of bequest to:

⁵⁹ Section 4(c) of the Estate Duty Act 45 of 1955.

⁶⁰ Section 4(d) of the Estate Duty Act 45 of 1955.

⁶¹ Section 4(f) of the Estate Duty Act 45 of 1955.

⁶² Section 4(1A) of the Estate Duty Act 45 of 1955.

- 3.7.1.1 any public benefit organisation which is exempt from tax in terms of section 10(1)(cA) of the Income Tax Act 58 of 1962;⁶³ or
- 3.7.1.2 any institution, board or body which is exempt from tax in terms of section 10(1)(cA)(i) of the Income Tax Act, which has as its sole or principal object the carrying on of any public benefit activity;⁶⁴ or
- 3.7.1.3 the state or any municipality as defined in section 1 of the Income Tax Act 58 of 1962.⁶⁵
- 3.7.2 the value of books, pictures, statuary or other objects of art or so much of the value of any shares in a body corporate as is attributable to such body's ownership of books, pictures, statutory or other objects of art, if such books, pictures, statutory or other objects of art have been lent under a notarial deed to the government of the Republic in the national, provincial or local sphere for a period of not less than thirty years, and the deceased died during such period;⁶⁶
- 3.7.3 so much of the value of any property deemed to be property of the deceased by virtue of the provisions of section 3(3) as has not been deducted under any of the other provisions of this section and as the Commissioner is satisfied has been taken into account under the provisions of section 5(1)(f)*bis* in the determination of the value of any company shares or a member's interest in a close corporation included as property in the estate.⁶⁷

⁶³ Section 4(h)(i) of the Estate Duty Act 45 of 1955.

⁶⁴ Section 4(h)(iA) of the Estate Duty Act 45 of 1955.

⁶⁵ Section 4(h)(iii) of the Estate Duty Act 45 of 1955.

⁶⁶ Section 4(o) of the Estate Duty Act 45 of 1955.

⁶⁷ Section 4(p) of the Estate Duty Act 45 of 1955.

3.7.4 so much of the value of any property included in the estate which has not been allowed as a deduction under the foregoing provisions of this section, as accrues to the surviving spouse of the deceased:

3.7.4.1 provided that the deduction allowable under the provision of this paragraph shall be reduced by so much of any amount as the surviving spouse is required in terms of the will of the deceased to dispose of to any other person or trust;

3.7.4.2 no deduction shall be allowed in respect of any property which accrues to a trust established by the deceased for the benefit of the surviving spouse if the trustee of such trust has a discretion to allocate such property or income there from to any person other than the surviving spouse.⁶⁸

3.7.5 the value of any interest included as property in the deceased estate under the provisions of section 3(2)(a) (such as a fiduciary, usufructuary or other like interest), where such interest was held by the deceased by virtue of a donation to him by the person to whom the right of enjoyment of the property in which the deceased held an interest, accrues or where the interest consists of a right to an annuity charged upon property, by the person who is the owner of that property);⁶⁹

3.7.6 the amount by which the value of any property included in the estate has been enhanced by any improvements made to the property concerned - at the expense of the person to whom the property accrues at the death of the deceased, and during the lifetime of the deceased and with his consent;⁷⁰

3.7.7 The amount by which the value of any fiduciary, usufructuary or other like interest which ceased upon the death of the deceased has been

⁶⁸ Section 4(q) of the Estate Duty Act 45 of 1955.

⁶⁹ Section 4(g) of the Estate Duty Act 45 of 1955.

⁷⁰ Section 4(i) of the Estate Duty Act 45 of 1955.

enhanced by any improvements made to the property concerned – at the expense of the person to whom the benefit arising by reason of the cessation of such interest upon the death of the deceased, accrues, and during the lifetime of the deceased and with his or her consent.⁷¹

3.8 The Section 4A Primary Rebate

The Act allows for a R3.5 million deduction from estate duty. This applies to all estates which means that all estates under R3.5 million are effectively exempt from estate duty.⁷² Where a spouse acquires a benefit from the estate of the deceased spouse, it is exempt from estate duty in terms of section 4(q) of the Act as explained above.

Since 1 January 2011 new legislation in the form of the Taxation Laws Amendment Act⁷³ authorised a roll-over of the unutilised portion of the first dying-spouse's primary rebate to his or her surviving spouse. This means that the second-dying spouse is now entitled to a deduction of R7 million reduced by the portion of the deduction used by a predeceased spouse.⁷⁴

The next chapter shall focus on capital gains tax in South Africa, and how it is calculated and imposed on death.

⁷¹ Section 4(j) of the Estate Duty Act 45 of 1955.

⁷² Section 4A(1) of the Estate Duty Act 45 of 1955.

⁷³ The Taxation Laws Amendment Act 24 of 2011.

⁷⁴ Section 4A as amended by the Taxation Laws Amendment Act 24 of 2011.

CHAPTER 4 : CAPITAL GAINS TAX IN SOUTH AFRICA

4.1 Introduction

Capital gains tax was introduced in South Africa on 1 October 2001. Prior to this date any receipts and accruals of a capital nature were generally not subject to tax. Capital gains tax is governed by the Income Tax Act. Section 26A of the Act states that there shall be included in the taxable income of a person for a year of assessment the taxable gain of that person for the year of assessment determined in terms of the Eighth Schedule to the Act.

The main reason as to why capital gains tax was introduced into the South African tax system was to strengthen the ideals of fairness and impartiality in the taxation of income. Before, a receipt of a capital nature was not taxable whilst a receipt of a revenue nature was taxable, even though the capital receipt benefitted its recipient as much as the revenue receipt. In 2012 the effective rate of capital gains tax was increased for the first time and senior South African Revenue Service officials have indicated that the intention is to increase the effective rate even further.⁷⁵

As previously discussed in Chapter 1, the Eighth Schedule specifies how the gain is to be calculated.⁷⁶

4.2 Determining Capital Gains Tax

Using the Eighth Schedule and section 26A, capital gains tax may be determined by using the following method:

4.2.1 Disposal of asset (or deemed disposal).

4.2.2 Calculation of proceeds of disposal.

⁷⁵ B Victor & K Ronald *Estate Planning & Fiduciary Services Guide* (2013) 117.

⁷⁶ DM Davis, C Beneke & RD Jooste *Estate Planning* Issue 38 (1998) 2A-3.

- 4.2.3 Deduct base cost.
- 4.2.4 Take account of all exclusions from capital gain as well as deferrals and capital losses.
- 4.2.5 Calculate the sum of all capital gains and losses and then take account of annual exclusion, currently R30 000 (R300 000 in year of death). (Only a natural person or a special trust may make use of the annual exclusion.)
- 4.2.6 From this calculation ascertain the aggregate capital gain or aggregate capital loss.
- 4.2.7 Deduct previous assessed capital losses.
- 4.2.8 The set of calculations undertaken from 5.2.2 to 5.2.7 above will determine whether there is a net capital gain or an assessed capital loss.
- 4.2.9 In the event that there is a net capital gain, multiply by the applicable inclusion rate to obtain the amount of taxable capital gain which is added to the taxable income as defined in terms of the Act.⁷⁷

4.3 Application of Capital Gains Tax

Capital gains tax is levied when a resident of South Africa disposes of any asset. Non-residents are however not excluded from having to pay capital gains tax and are liable for gains from the disposal of the following assets:

- 4.3.1 Immovable property situated in South Africa held by a person or any interest or right of whatever nature of that person to or in immovable property, including any equity shares held by a person in a company or ownership or the right to ownership of a non-resident in any other entity or a vested right of a person in any assets of any trust, if:
 - a. 80 per cent or more of the market value of those equity shares, ownership or right to ownership or vested right, at the time of

⁷⁷ Davis op cit (n76) 2A-3.

disposal thereof is attributable directly or indirectly to immovable property held otherwise than as trading stock; and

- b. In the case of a company or other entity, that person (whether alone or together with any connected person in relation to that person), directly or indirectly, holds at least 20 per cent of the equity share capital of that company or ownership or right of ownership of that other entity.

4.3.2 Any asset of a permanent establishment of that person through which trade is carried out in South Africa during the relevant year of assessment.⁷⁸

4.4 The Capital Gains Tax Event

When an asset is disposed of or is deemed to be disposed of, during the year of assessment, this act triggers the application of capital gains tax and is known as the capital gains tax event. According to paragraph 11(1) of the Eighth Schedule, a disposal is 'any event, act, forbearance, or operation of law which results in the creation, variation, transfer or extinction of an asset'⁷⁹ and includes a sale, donation, expropriation, conversion, grant, cession, exchange or other alienation or transfer of ownership of an asset.⁸⁰

4.5 An Asset for Capital Gains Tax Purposes

A capital gains tax event can only be triggered if an asset is disposed of. An asset includes the following:

⁷⁸ Davis op cit (n76) 2A-4.

⁷⁹ Para 11(1) of the Eighth Schedule to the Income Tax Act 58 of 1962.

⁸⁰ Para 11(1)(a) of the Eighth Schedule to the Income Tax Act 58 of 1962.

4.5.1 Property of whatever nature, movable or immovable, corporeal or incorporeal, excluding any currency but including any coin made mainly from gold or platinum; and

4.5.2 A right or interest in whatever nature to or in such property.⁸¹

Davis et al. state that currency (bank notes and coins) or cash is not classified as an asset for capital gains tax purposes meaning that the disposal of such currency or cash will not trigger the payment of capital gains tax.⁸²

4.6 Capital Gains Tax on Death

When a person passes away, he or she is seen as having disposed of all of his or her assets to the deceased estate which acquires the proceeds of the disposal which equal the market value of the assets at the time of his or her death. At the same time, the deceased estate itself is regarded as having obtained those assets at market value. This could potentially create serious cash flow issues as certain assets, which the beneficiaries do not wish to sell, might incur large capital gains tax costs due to unrealised capital gains in the asset.⁸³

There are exceptions to this rule however, one being that any assets which are transferred to the deceased's surviving spouse are not included in this disposal.⁸⁴ All assets that pass to a surviving spouse in terms of the deceased's will or in terms of intestate succession laws are subject to roll-over relief. Therefore, capital gains tax is postponed until the surviving spouse subsequently disposes of these assets during his or her lifetime or at death.⁸⁵

Another exception is where the deceased left any assets to a public benefit organisation. Similarly, any lump sum payments from pension,

⁸¹ Davis op cit (n76) 2A-5.

⁸² Ibid.

⁸³ Victor op cit (n75) 149.

⁸⁴ Davis op cit (n76) 2A-5.

⁸⁵ Victor op cit (n75) 150.

provident and retirement annuity funds are excluded⁸⁶ as is the first R2 million in respect of a primary residence⁸⁷, the first R1.8 million in respect of small business assets, currency (excluding gold and platinum coins) and the annual exclusion which at death is R300 000.⁸⁸

Also, when an heir or legatee or trustee of a trust receives an asset which has been transferred by a deceased estate, the estate is deemed to have disposed of it at the deceased estate's base cost which means that no capital gain or loss has resulted therefrom. The heir or legatee is deemed to have the same base cost of the asset as the deceased estate.⁸⁹

Capital gains tax is regarded as a liability in the estate, and reduces the dutiable estate for the purposes of estate duty. The estate can, however, claim the capital gains tax from the heir receiving the asset who can in certain circumstances choose to pay the capital gains tax over a period of three years.⁹⁰

The next chapter shall examine the effect the application of estate duty and capital gains tax has had in South Africa and shall address some of the specific problems which have said to have been created by the imposition of these taxes.

⁸⁶ Davis op cit (n76) 2A-5.

⁸⁷ Victor op cit (n75) 149.

⁸⁸ Victor op cit (n75) 150.

⁸⁹ Davis op cit (n76) 2A-8(5).

⁹⁰ Victor op cit (n75) 151.

CHAPTER 5 : DEATH TAXES & PROBLEMS FROM A SOUTH AFRICAN PERSPECTIVE

5.1 Double Taxation

One of the most highlighted problems which has been raised during the debate on whether to abolish estate duty and only impose capital gains tax is that of double taxation. On death, capital gains tax is triggered as well as estate duty (provided the estate is over the prescribed section 4A rebate). Regardless of the fact that these taxes are imposed in different ways - with capital gains tax being imposed on any gain from a disposal, and estate duty being imposed on the transfer of wealth - and even though the capital gains tax liability as a debt owing by the deceased would decrease the dutiable amount of the estate, Ger argues that there is still double taxation on some portion of the same assets in the estate.⁹¹

Other than the dual imposition of estate duty and capital gains tax, double taxation also arises in the following ways: According to Ger, where a deceased from a foreign jurisdiction owns assets, he or she may have to pay estate duty locally as well as death taxes in their home country as estate duty is not recognised by all the international treaties which South Africa has ratified. These treaties are usually limited to income taxes.⁹² Currently, South Africa has only entered into treaties in respect of estate duties with the United Kingdom, the United States, Swaziland, Zimbabwe and Lesotho, which prevent the levying of double death taxes in both South Africa and those particular jurisdictions.

Double taxation is also imposed where the assets in the deceased estate are made up of income or assets which have already been subjected to income tax during the deceased's lifetime and shall be taxed again in terms of estate duty. Ger states that 'while one could quibble and note that these taxes

⁹¹ B Ger 'Time for Estate Duty to Go?' (2012) *De Rebus* 59 at 60.

⁹² Ger op cit (n91) 59.

are different, the levy of estate duty does not mean that the government gets two bites from the same tax cherry'.⁹³

5.1.1 An Example of Double Taxation

An individual has an asset with a market value of R1 million on the date of her death that she bought for R500 000. Assuming that the abatement for estate duty and annual exclusion from capital gains tax has been used and the individual is taxed at the maximum marginal income tax rate, the taxes that will be paid on death in respect of this asset would be:

Capital gains tax at an effective rate of 13.33 per cent on a capital gain of R500 000 = R66 650.

Estate duty at 20 per cent on the dutiable amount of R1 million = R200 000.

The total tax on the asset is thus R266 650.

The individual is taxed twice on the increase in the asset's value of R500 000.

The amount of R66 650 will however be deductible for estate duty purposes.

5.1.2 Concessions Provided by the Legislature

The legislature was well aware of this double imposition of tax upon death and has made an allowance in that where capital gains tax exceeds 50 per cent of the net value of the estate for estate duty purposes and there are not enough funds in the estate to pay capital gains tax - meaning the executor is forced to dispose of an asset in order to cover the tax implications herein - the Act permits the heirs or legatees to acquire the asset which the executor would have had to sell to pay the tax, within three years after the executor has been

⁹³ Ger op cit (n91) 60.

given permission by the Master to distribute the assets. Further concessions include:

- 5.1.2.1 that any capital gains tax liability as a result of death of a person constitutes an allowable deduction in the hands of the estate.
- 5.1.2.2 the annual exclusion being increased from R30 000 to R300 000.⁹⁴

5.2 Other Problems

Taking the above double taxation problem into account, the South African Revenue Service, in the 2010/2011 budget indicated for the first time that death taxes were to be reviewed for this very reason. The Minister has also highlighted the fact that estate duty does not collect a substantial amount of revenue and is burdensome to administer. The Minister also stated that the effectiveness of estate duty has been doubted as people are able to use clever estate planning tools, such as the creation of trusts, which assist them in avoiding the tax altogether.⁹⁵

5.2.1 Estate Duty and Capital Gains Tax Avoidance

Many wealthy individuals have access to lawyers and accountants who are able to advise them about which estate planning techniques they should implement in order to minimise or avoid having to pay estate duty or capital gains tax. For example, an inter vivos trust can be created by a donor during her lifetime and into which she transfers all of her assets, thereby making sure that the growth of the assets remains in the trust and not in the estate. This

⁹⁴ Davis op cit (n76) 2A-8(5).

⁹⁵ J Jacobs 'Is the Capital Gains System about to Replace Estate Duties?', 24 February 2012, available at <http://www.moneyweb.co.za/moneyweb-tax/estate-planning-and-deceased-estates>, accessed on 3 December 2014.

type of estate planning is not as readily available to those individuals who cannot afford this type of advice.

5.2.2 Revenue Versus Cost

Taking a look at Tables 3 and 4 below, it is clear that neither capital gains tax nor estate duty (taxes on property) contribute as much revenue as that received from the other taxes collected.

For example (as illustrated in Table 3 below) between 2001 and 2009 capital gains tax collected only R16 billion. In the 2013/14 year of assessment capital gains tax collected R11 billion.

Table 3: Capital Gains Tax (CGT) raised, 2009/10 – 2013/14

R million	CGT raised		
	Individuals	Companies	Total
Prior to 2009/10	6,824	9,871	16,694
2009/10	4,357	6,023	10,380
2010/11	2,012	7,049	9,061
2011/12	1,550	5,263	6,813
2012/13	2,166	5,008	7,174
2013/14	6,970	4,633	11,603
Cumulative	23,879	37,847	61,726

As illustrated in Table 4 below, taxes on property in the 2013/14 year of assessment only contributed 1.2 per cent of the total tax revenue received by government, amounting to R10 billion. This is almost insignificant when compared to tax on income and profits contributing 56.4 per cent and amounting to R507 billion in the 2013/14 year of assessment.

Table 4: Tax revenue by main category, 2009/10 – 2013/14

R million	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 revenue ²	Total tax revenue
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
2012/13	457,314	11,378	8,645	296,921	39,549	18	813,826
2013/14	507,759	12,476	10,487	324,548	44,732	13	900,015
Percentage of total							
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%
2012/13	56.2%	1.4%	1.1%	36.5%	4.9%	0.0%	100.0%
2013/14	56.4%	1.4%	1.2%	36.1%	5.0%	0.0%	100.0%
Percentage change year-on-year							
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%
2011/12	7.2%	11.8%	10.6%	12.5%	15.9%	292.5%	9.6%
2013/14	11.0%	9.6%	21.3%	9.3%	13.1%	-29.0%	10.6%

It is also clearly illustrated in Table 5 below that estate duty does not contribute significantly to revenue collected, as it only contributed 10.5 per cent amounting to R1 billion in the 2013/2014 year of assessment. Over the past five years, the highest percentage estate duty attributed to this category was 13.4 per cent, being a 33.6 per cent growth increase from the 2011/12 year of assessment.

Table 5: Taxes on property, 2009/10 – 2013/14

R million	Donations tax	Estate duty	Securities Transfer Tax (STT)	Transfer duties	Total
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
2012/13	82	1,013	3,272	4,278	8,645
2013/14	113	1,102	3,784	5,489	10,487
Percentage of total					
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%
2012/13	0.9%	11.7%	37.8%	49.5%	100.0%
2013/14	1.1%	10.5%	36.1%	52.3%	100.0%
Percentage year-on-year growth					
2010/11	7.5%	3.0%	-11.8%	13.7%	3.1%
2011/12	-18.5%	33.6%	-1.6%	-28.0%	-14.1%
2012/13	55.9%	-3.1%	13.4%	11.6%	10.6%
2013/14	37.3%	8.7%	15.7%	28.3%	21.3%

Taking the above mentioned problems into account and the fact that the South African legislature has been debating whether to abolish certain death taxes, it is necessary to examine the arguments made by various proponents and detractors of these death taxes from around the world to determine whether the current system in place should be retained or amended.

CHAPTER 6 : ARGUMENTS FOR AND AGAINST DEATH TAXES

6.1 The Case Against Death Taxes

According to the opponents of death taxes, the payment of these taxes by the public has severe economic consequences. Dubay argues that it encourages people to spend their money immediately rather than save and invest in their future. He argues it does not encourage entrepreneurship or other economic endeavours but instead pressurises people to consume now rather than have to spend their money on paying taxes at a later stage.⁹⁶ Instead of pursuing entrepreneurship, a person is more likely not to create a new business venture when weighing up all the associated costs and taxes that will ultimately be levied on his or her business and on his estate when he or she passes away.

Dubay goes further and argues that the death tax 'raises the costs an entrepreneur will pay because it promises to confiscate a portion of his or her business upon his or her death. The prospect of their children or other family members being forced to pay a hefty tax in order to keep the business they have rightly inherited causes many entrepreneurs to refrain from starting a business'. As a result of stifled entrepreneurship and lack of investment and saving, fewer jobs are created and economic growth is hindered.⁹⁷

Another argument against paying death taxes is that as a result of discouraging saving and investing, they stifle job creation. Instead of people using their money to create new businesses and employ workers to expand their operations, they are spending what they have accumulated now rather than having to pay tax on it after they have passed away.⁹⁸ As a result wages

⁹⁶ C Dubay 'The Economic Case Against the Death Tax', 20 July 2010, available at <http://www.heritage.org/research/reports/2010/07/the-economic-case-against-the-death-tax>, accessed on 24 November 2014.

⁹⁷ Dubay op cit (n96).

⁹⁸ Ibid.

and productivity remain low and businesses are unable to upgrade their resources and equipment.⁹⁹

Other opponents, like McCaffery argue that death taxes do not actually aid governments in raising funds for public and government expenditure, due to the high costs involved in collecting them, the revenue lost to other taxes such as income tax, and general economic problems.¹⁰⁰ McCaffery supports Dubai's theory that death taxes discourage saving and investment. He calls the death tax a 'bad tax' as it falls on savings as opposed to immediate consumption. He states that 'a fair tax system should consistently tax spending, not work or savings, and should use progressive rates to meet whatever liberal or redistributive objectives it has'.¹⁰¹

It has been argued that death taxes do not assist the government in achieving its goal of equality for all citizens, the notion upon which estate duty has been said to be founded. The notion that once a person dies, the wealth is supposed to be spread amongst all members of society is not plausible as the wealthy nowadays are more likely to leave everything to their heirs in terms of a Last Will and Testament.¹⁰²

Block and Drenkard similarly agree with McCaffery and add that costs involved in collecting death taxes are enormous due to the amount of administration work involved. As a result, an entire estate planning industry has been created in response to the existence of a complex estate tax and those wanting to subvert it. Block and Drenkard argue that this industry is able to charge exorbitant and wasteful fees when the resources employed could be utilised elsewhere.¹⁰³ They found that the compliance costs associated with estate planning actually exceed the revenue accumulated by the tax itself.¹⁰⁴

⁹⁹ Ibid.

¹⁰⁰ E McCaffery 'Grave Robbers: The Moral Case Against the Death Tax', 4 October 1999, available at <http://www.cato.org/sites/cato.org/files/pubs/pdf/pa353.pdf>, accessed on 24 November 2014.

¹⁰¹ McCaffery op cit (n100).

¹⁰² Ibid.

¹⁰³ D Block and S Drenkard 'The Estate Tax: Even Worse than Republicans Say', 4 September 2012, available at <http://taxfoundation.org/article/estate-tax-even-worse-republicans-say>, accessed on 24 November 2014.

¹⁰⁴ Block & Drenkard op cit (n103).

This is because of the employment of estate attorneys and accountants who are employed to limit the amount of tax that is payable upon death. By continuing to impose death taxes the government is creating a demand which these industries will continue to meet. Block and Drenkard state that 'all of these compliance costs represent economic waste, as these human and capital resources would be employed elsewhere more productively if the tax were eliminated'.¹⁰⁵

One last argument against death taxes is that they result in double taxation which is unfair and punitive. Double taxation arises as the assets on which the deceased is taxed on upon death have already been subjected to tax during his or her lifetime.¹⁰⁶

The above authors all agree that death taxes instil in people the need to do exactly the opposite of what a sound tax system ought to encourage: entrepreneurship, savings, investment and equality amongst the poorer and wealthier members of society.¹⁰⁷

There are however, proponents of death taxes who argue that without these taxes being imposed, the prospects of ever attaining the ideals of equality and fairness would be lost forever.

6.2 The Case For Death Taxes

Graetz in his article begins by asking the question: is it fair for Paris Hilton to inherit her great-grandfather Conrad's fortune without paying any tax on it? Or Yankee owner George Steinbrenner's 13 grandchildren? This is exactly what

¹⁰⁵ Ibid.

¹⁰⁶ Independent Green Voice 'Abolish the Death Tax' available at <http://www.sovereignty.org.uk/features/articles/manifesto07/iht.html>, accessed on 24 November 2014.

¹⁰⁷ Block & Drenkard op cit (n103).

happens when there is no estate or inheritance tax on the bequests of the very rich'.¹⁰⁸

Graetz argues that estate tax is a fair tax and without it the wealthier members of society would continue to accumulate their masses without having to give back to society in any way. He states that in 2008 in the United States that the estate tax brought in about \$29 billion from only 20 000 deceased estates, an amount which was collected from only 1% of the population who died during that year.¹⁰⁹

Graetz acknowledges that death taxes do in many cases result in double taxation. In South Africa the argument is currently that death taxes result in paying both estate duty and capital gains tax for example. However, regardless of whether this is fair or not, he argues that in most cases the wealthiest minority of the country are able to hold onto their assets without having to pay capital gains tax or they are able to find ways around having to pay the highest of the taxes to which their assets should be subjected. Death taxes are used as a way to prevent this from happening and trying to encourage a more level playing field so as to ensure equality of opportunity for everyone.¹¹⁰

Graetz argues further in contradiction of Block and Drenkard's views, that there is no evidence that the wealthy are simply spending all their money, failing to invest or save their fortunes and dabbling in entrepreneurship to in order to evade the tax upon their deaths. The heirs and beneficiaries to the massive estates, on the other hand, are the ones who are being encouraged not to work after they receive their large inheritances.¹¹¹

Other proponents of death taxes also argue that death taxes are a vital tool in increasing government revenue for public expenditure. It further assists in collecting revenue where the income tax falls short and it is in some cases

¹⁰⁸ M Graetz 'It's Fair, and We Need the Revenue', 20 September 2010, available at <http://online.wsj.com/articles/SB10001424052748704358904575477593075638722> , accessed on 24 November 2014.

¹⁰⁹ Graetz op cit (n108).

¹¹⁰ Ibid.

¹¹¹ Ibid.

able to encourage charitable giving at death.¹¹² Hutton goes further in his support for death taxes and the economic advantages inherent in the tax as he argues that more property would have been sold on death to pay the tax which would give people the chance to buy property which would otherwise not have come on the market.¹¹³ Hutton sums the death tax up as follows: 'it promotes social mobility, creates opportunity, limits entrenched advantage, redistributes wealth and helps keep property cheaper'. Hutton advances that this is unfortunately not how it is known in popular culture.¹¹⁴

6.3 Going Forward

Many authors are aware that imposing death taxes is not ideal. The tax itself can be overly complicated and the costs in collecting it are cumbersome. Graetz suggests that the exemption level be set and rated according to the size of the bequests received. He says that 'such a change would better align tax rates with ability to pay and make it easier to adjust the tax for family circumstances'.¹¹⁵ Even with the disadvantages the tax brings, Graetz is certain in his belief that countries do need death taxes in order to help alleviate the hardships caused by the recent worldwide recession and in an effort to redistribute the wealth and prevent the wealth from being enjoyed by only the top echelons of society.

In order to consider possible alternatives to the current regime in South Africa, it is useful to conduct a brief overview of how deceased persons are taxed in other jurisdictions. Estate duty and capital gains tax are imposed, not only in South Africa, but in many countries around the world. Another tax,

¹¹² Block & Drenkard op cit (n103).

¹¹³ W Hutton 'The Case for Keeping Inheritance Tax' *The Observer*, 7 October 2007, available at <http://www.theguardian.com/commentisfree/2007/oct/07/comment.inheritancetax>, accessed on 24 November 2014.

¹¹⁴ Hutton op cit (n113).

¹¹⁵ Graetz op cit (n108).

namely inheritance tax, is also levied in many countries and shall equally be discussed.

CHAPTER 7 : DEATH TAXES IN THE UNITED KINGDOM

There are some similarities between how the United Kingdom's taxes a deceased upon his or death when compared to that of South Africa. For example, the United Kingdom levies an estate tax (called an inheritance tax) but chooses not to 'forgive' capital gains tax on death.

7.1 Introduction

In and around 1894 estate duty was introduced in the United Kingdom. The tax was levied on assets which passed from a person on his or her death to his or her deceased estate and it was also imposed on gifts or donations made in a certain period one year before death.¹¹⁶

In 1975 estate duty was replaced with capital transfer tax which extended all capital gifts made during a deceased's life and which created specific legislation for discretionary trusts. The extension created by the capital transfer stifled economic growth to an extent as this extension resulted in the situation where individuals refrained from making donations to younger generations.¹¹⁷ Therefore, the approach with regard to gifts under the previous estate duty returned with the introduction of an inheritance tax (meaning an estate duty tax) in 1984 under the Inheritance Tax Act (hereinafter referred to as 'the Act'), as amended by the yearly Finance Acts¹¹⁸ which is still currently in operation, the latest being the Finance Act 2014.¹¹⁹ It has been argued that this tax is unfair and far too complicated resulting in calls for its replacement by a recipient-based wealth transfer tax, which is a tax imposed on the

¹¹⁶ Muller op cit (n1) 267.

¹¹⁷ Ibid.

¹¹⁸ Muller op cit (n1) 268.

¹¹⁹ The National Archives 'Finance Act 2014' available at <http://www.legislation.gov.uk/ukpga/2014/26/contents/enacted>, accessed on 9 December 2014.

beneficiaries of an estate instead of the estate itself, like in the case of the Netherlands (discussed in Chapter 13).¹²⁰

7.2 What is Inheritance Tax (Estate Tax) and How is it Calculated

Inheritance tax is paid on a deceased estate and in some cases by trusts or on gifts made during a deceased's lifetime. The inheritance tax applies to the value of a person's estate upon his or death (upon death the deceased is deemed to have made a transfer of his or her entire estate immediately before such time) and it also applies to certain transfers or gifts made during the person's lifetime. The inheritance tax applies on the basis of the loss to the donor's estate that arises by reason of the transfer of value.

There are three types of transfers under the Act:

7.2.1 Exempt Transfers

Some transfers are exempt from inheritance tax (whether they during the deceased's lifetime or upon death). Exempt transfers include: those where gifts are made to a charity or a surviving spouse or civil partner for example, and no inheritance tax is payable regardless if the estate's value exceeds the 'nil rate band' (explained below in paragraph 7.2.4). Other examples include:

7.2.1.1 Potentially Exempt Transfers

If the deceased made a gift to a person and lived for seven years after making such a gift, the gift will be exempt from inheritance tax regardless of its value.

¹²⁰ Muller op cit (n1) 268.

7.2.1.2 The Annual Exemption

In terms of the Inheritance Tax Act, a person is allowed to give gifts to any persons to the value of up to £3 000 per year without attracting tax.

7.2.1.3 The Small Gift Exemption

A person is permitted to give away small gifts with a value of up to £250 to as many individuals of their choice on a tax free basis.

7.2.1.4 Wedding and Civil Partnership Gifts

When someone receives a gift as a result of a wedding or civil partnership these gifts will be exempt from tax up to a certain amount.¹²¹

7.2.2 Potentially exempt transfers

As referred to above, when a person makes a gift to someone and survives for seven years after making the gift, no tax is payable. However, should the person making the gift (usually an outright gift) die within those seven years, this lifetime transfer will be taxable.¹²²

7.2.3 Chargeable Transfers: Lifetime and Death

These types of transfers are immediately chargeable and make use of the nil rate band and any available annual allowances, with any excess being liable

¹²¹ HM Revenue & Customs 'Inheritance Tax – the Basics' available at <http://www.hmrc.gov.uk/inheritancetax/intro/basics.htm>, accessed on 24 November 2014.

¹²² Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/IEIT-2013/IEIT-GB.xml>, accessed on 24 November 2014.

at 20 per cent (and could be higher if death occurs in the following seven years). Examples of a lifetime chargeable transfer would include a transfer to a trust or to a company in which the transferor does not have complete ownership thereof.¹²³

Transfers on death are fully chargeable at 40 per cent unless specific reliefs are available or the transfer is exempt or made to an exempt person such as a registered charity.¹²⁴

7.2.4 Nil Rate Band

Similar to South Africa's Section 4A primary rebate, the Act contains a provision whereby a threshold is created (or a 'nil rate band'), which means that any estates with a total value of less than £325 000 (for the 2014/15 year of assessment) will not have to pay this tax. Should an estate be valued over this nil rate band, then the tax is payable at a rate of 40 per cent on the amount over this nil rate band or 36 per cent if the estate qualifies for a reduced rate as a result of a donation to a charity.¹²⁵ The value of the nil rate band is adjusted for inflation on an annual basis.¹²⁶

Just like in South Africa, in the United Kingdom an amendment was passed in 2007 whereby spouses and civil partners could double the nil rate band on their estates upon the death of the second dying to the value of £650 000 (for the 2014/15 year of assessment). The unused portion of the nil rate band is transferred to the second spouse or civil partner upon their death.¹²⁷

7.3 Capital Gains Tax

Capital gains tax was introduced in the United Kingdom under the Finance Act of 1965. Today capital gains tax is governed by the Taxation of Chargeable

¹²³ Ernst & Young op cit (n122).

¹²⁴ Ibid.

¹²⁵ HM Revenue & Customs op cit (n121).

¹²⁶ Muller op cit (n1) 289.

¹²⁷ HM Revenue & Customs op cit (n121).

Gains Act of 1992. There are certain provisions in the Act which apply to the death of a person. For instance, capital gains tax is imposed at a rate of 28 per cent on disposals made by the executor of a deceased state.¹²⁸

However, certain exemptions are provided for the deceased estate which usually result in no capital gains tax being payable on death. For example, the deceased estate qualifies for the annual exempt amount which currently is £10 900 limited to the annual exempt amount in the year that the deceased person passed away plus the annual exempt amount for the following two tax years.¹²⁹

Section 62 of the Act states that:

(1) For the purposes of this Act the assets of which a deceased person was competent to dispose –

(a) Shall be deemed to be acquired on his death by the personal representative or other person on whom they devolve for a consideration equal to their market value at the date of death, but

(b) Shall not be deemed to be disposed of by him on his death (whether or not they were the subject of testamentary disposition).

...

(4) On a person acquiring any asset as legatee (as defined in section 64)-

¹²⁸ J Van Jaarsveld *The Levying of Capital Gains Tax at Death* LLM (Johannesburg) (2013) 43.

¹²⁹ Section 2 of the Capital Gains Tax (Annual Exempt Amount) Order of 2013.

- (a) no chargeable gain shall accrue to the personal representatives; and
- (b) the legatee shall be treated as if the personal representatives' acquisition of the asset had been his acquisition of it.

Van Jaarsveld explains the effect that section 62(1) of the Act has, stating that a taxable asset which a deceased person was competent to dispose of prior to his or her death, will be deemed to have been acquired by the personal representative at his or her death at an amount equal to the market value of the asset as at the date of death. Even though a deemed acquisition has taken place, there is no deemed disposal of a taxable asset which means that no capital gains tax would be payable on death.¹³⁰

Section 62(4) of the Act also results in a similar situation, as no capital gains tax is payable on the transfer of the asset from the personal representative to the legatees of the deceased as the personal representative's acquisition is treated as the legatee's acquisition.¹³¹

The consequences are thus that any heirs or legatees of the deceased, whether nominated in a will or in terms of intestate succession, will receive the asset at the market value on date of death without any capital gains tax liability on the part of the personal representative, even if the asset's value had increased since date of death.¹³²

Van Jaarsveld goes further in his explanation of this Act and states that section 274 contains an advantage for heirs or legatees. In terms of this section, the market value of the asset for inheritance tax purposes is equal to the asset's market value for capital gains tax purposes. However, in order for this section to apply, inheritance tax must have been chargeable on the value of the deceased's estate immediately before his or her death and the value of

¹³⁰ Van Jaarsveld op cit (n128) 45.

¹³¹ Ibid.

¹³² Ibid.

an asset forming part of his or her estate had to be 'ascertained'. The value will not be ascertained when for example a taxable asset is passed to the surviving spouse, as a roll-over relief similar to the roll-over relief between spouses as provided for in South African tax law would apply.¹³³

Van Jaarsveld states that "even though a higher value would result in a higher amount of inheritance tax payable, the personal representative or legatees are at a great advantage as there will be a corresponding step-up in their base cost by virtue of section 62(1) of the Taxation of Chargeable Gains Act of 1992. The personal representative will not receive and the legatees will not inherit the asset at the base cost of the asset to the deceased, but at the higher market value as ascertained on the deceased's date of death, with no capital gains tax liability to the deceased estate".¹³⁴

This means that the base cost of the asset will change to the higher value in respect of either the personal representative or legatees. Should the asset have to be sold during the winding up process for any reason, capital gains tax will only have to be paid if the selling price, minus any capital expenditure and qualifying costs, is greater than the market value of the asset as on the date of the deceased's death, which will be the new base cost of the asset.¹³⁵

The personal representative might have to pay capital gains tax if the disposal of the asset results in a capital gain, but this will only occur in certain circumstances where there is for example, a delay in the winding up of the estate or the value of the asset has greatly increased from the deceased's date of death to the date when the asset was realised.¹³⁶

In summary, the United Kingdom follows a similar system of levying taxes upon death to that implemented by South Africa. For example, as detailed above, the United Kingdom levies an estate tax (but is referred to as an inheritance tax) and provides an exemption of a certain amount referred to

¹³³ Van Jaarsveld op cit (n128) 46.

¹³⁴ Ibid.

¹³⁵ Ibid.

¹³⁶ Ibid.

as the nil rate band whereas South Africa provides an exemption amount referred to as the Section 4A primary rebate.

Where these two countries differ materially is on the imposition of capital gains tax on death. The United Kingdom follows a system, referred to above, which results in the majority of cases 'forgiving' capital gains tax at death whereas South Africa, while providing an exemption for capital gains tax, results in the majority of deceased estates paying capital gains tax, thereby resulting in double taxation.

CHAPTER 8 : DEATH TAXES IN THE UNITED STATES

8.1 Introduction

The tax system in the United States is structured differently to that of the United Kingdom and South Africa, as the United States consists of various sovereign states, each with their own state laws which in many cases differ from state to state as well as a federal tax system.¹³⁷ The United States also imposes an estate tax (similar to South Africa and the United Kingdom) but like the United Kingdom, does not impose capital gains tax on death.

The tax system in the United States has undergone many changes since it was first introduced approximately 150 years ago. During the first years of its inception, direct tax on individuals was restricted by the federal government who relied on indirect taxation through taxes on imports or tariffs and excise taxes. Tariffs were the major source of government revenue up to the early 1900s. Income tax rates were low by modern standards, levied at a maximum rate of 10 per cent along with generous exemptions. This resulted in about only 10 per cent of households being subjected to any income tax.¹³⁸

A new federal income tax was introduced in 1862, with a large exemption of \$4 000, but the Supreme Court ruled it unconstitutional in 1895. Eventually, in 1913 after various proposals and amendments, an updated version of income tax was introduced and in 1916 the estate tax was created.¹³⁹

During the most recent decades, the tax system has undergone many changes, with the creation of The Economic Recovery Tax Act of 1981 (or

¹³⁷ B Roach 'Taxes in the United States' (2010) available at http://www.ase.tufts.edu/gdae/education_materials/modules/Taxes_in_the_United_States.pdf, accessed on 10 December 2014.

¹³⁸ Roach op cit (n137) 11.

¹³⁹ Roach op cit (n137) 12.

'ERTA') by Ronald Reagan. ERTA introduced the largest tax cut in American history and inspired tax cutting by many other nations during the 1980s. The idea behind ERTA was that by providing reductions in tax it would create greater incentives to increase investment and economic activity. The theory was that tax cuts would increase federal revenues while at the same time assisting the growing federal budget deficit.¹⁴⁰ However, this Act ultimately failed to control the growing federal deficit.¹⁴¹

The most recent changes to the tax system in the US came in 2001 in the form of the \$1.35 trillion Bush tax cut. Importantly, this Act included the scheduled repeal of the estate tax in 2010 which was later reinstated in 2011.¹⁴² Another tax cut was passed in 2003 which lowered the maximum tax rate on capital gains among other things.¹⁴³

Today, the United States still functions under a federal legal system and taxes are imposed at federal and state levels. The state law of each state determines the property rights of the taxpayer.¹⁴⁴ Wealth transfers, in particular, are currently taxed in three ways through the federal transfer tax system: through estate tax, gift tax and generation skipping transfer tax.¹⁴⁵

8.2 The Estate Tax

The United States imposes an estate tax on the transfer of a deceased's taxable estate on death.¹⁴⁶ As shown in Table 6 below, in 2010 estate tax was repealed for one year under the Economic Growth and Tax Relief

¹⁴⁰ Roach op cit (n137) 14.

¹⁴¹ Roach op cit (n137) 15.

¹⁴² Ibid.

¹⁴³ Roach op cit (n137) 16.

¹⁴⁴ C Bornman *Estate Planning: The Impact of Estate Duty and Capital Gains Tax on Offshore Assets* MCom (North West) (2010) 53.

¹⁴⁵ Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/IEIT-2013/IEIT-US.xml>, accessed on 24 November 2014.

¹⁴⁶ Ernst & Young op cit (n145).

Reconciliation Act of 2001 ('EGTRRA'). Under the same Act the estate tax was readjusted in 2011 to the 2002 exemption level with a 2001 top rate. Had no further legislation been passed, the estate of a person who deceased in 2010 would have been completely exempt from this tax while that of a person who died in 2011 or later would have been taxed as heavily as in 2001. However, on 17 December 2010, the government passed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 which reinstated the federal estate tax. This Act provided an exemption for citizens and residents at \$5 million per person,¹⁴⁷ and it provided a top tax rate of 35 per cent for the years 2011 and 2012.¹⁴⁸

Table 6

Year	Exclusion Amount	Max/Top Tax Rate
2001	\$ 675,000	55%
2002	\$ 1 million	50%
2003	\$ 1 million	49%
2004	\$ 1.5 million	48%
2005	\$ 1.5 million	47%
2006	\$ 2 million	46%
2007	\$ 2 million	45%
2008	\$ 2 million	45%
2009	\$ 3.5 million	45%
2010	Repealed	
2011	\$ 5 million	35%
2012	\$ 5.12 million	35%
2013	\$ 5.25 million	40%
2014	\$ 5.34 million	40%

On 1 January 2013, another piece of legislation was introduced in the format of the American Taxpayer Relief Act of 2012 which created a permanent exemption of \$5 million (as 2011 basis with inflation adjustment) per person with a maximum tax rate of 40 per cent for 2013 and onwards.¹⁴⁹ Uncertainty exists however, as to the continued existence of this amendment as the 2014

¹⁴⁷ Internal Revenue Code section 2010(c), as amended by section 302(a)(1) of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010.

¹⁴⁸ Title III of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.

¹⁴⁹ G Ruffenach 'Coming Soon: More Estate Tax Battles', 29 April 2013, available at <http://blogs.marketwatch.com/encore/2013/04/29/coming-soon-more-estate-tax-battles/>, accessed on 25 November 2014.

US budget speech proposed returning the estate tax exemption to what it was in 2009 starting in 2018.¹⁵⁰

Bearing this in mind, currently United States citizens and residents who pass away in the 2014/15 year of assessment will pay an estate tax of 40 per cent and receive a \$5.34 million estate tax exemption, which is adjusted annually for inflation. The estate tax exemption will be \$5.43 million for 2015.¹⁵¹ Non-residents are taxed at a rate of 40 per cent and only receive an exemption amount of up to \$60 000 which is not indexed for inflation.¹⁵²

The estate tax is imposed on all United States citizens and residents.¹⁵³ In addition to the federal estate tax, many states levy their own estate taxes and in some cases, inheritance taxes. Today, 15 states and the District of Columbia have an estate tax, while six states impose an inheritance tax. Only the states of Maryland and New Jersey impose both taxes.¹⁵⁴ Washington imposes the highest maximum estate tax at 20 per cent, while 11 other states impose a maximum rate of 16 per cent. Hawaii and Delaware allow the highest exemption threshold at \$5 340 000 which is currently the same as the federal exemption. New Jersey has the lowest exemption rate of only \$675 000.¹⁵⁵

On the one hand, many states are considering repealing the estate and inheritances taxes altogether, with Indiana retrospectively repealing its inheritance tax to 1 January 2013. Tennessee has indicated that it will repeal its estate tax by 2016. On the other hand, some states are simply increasing their exemption rates. For example, Maryland and New York have agreed to phase in a higher estate tax exemption, and eventually match the federal

¹⁵⁰ Ruffenach op cit (n149).

¹⁵¹ A Ebeling 'IRS announces 2015 estate and gift tax limits', 30 October 2014, available at <http://www.forbes.com/sites/ashleaebeling/2014/10/30/irs-announces-2015-estate-and-gift-tax-limits/>, accessed on 24 November 2014.

¹⁵² W Finestone 'United States: 2014 Estate and Tax Planning', 13 February 2014, available at <http://www.mondaq.com/unitedstates/x/292812/Capital+Gains+Tax/2014+Estate+And+Tax+Planning>, accessed on 24 November 2014.

¹⁵³ Ernst & Young op cit (n145).

¹⁵⁴ L Emanuel, S Drenkard & R Borean 'State Estate and Inheritance Taxes in 2014', 28 May 2014, available at <http://taxfoundation.org/blog/state-estate-and-inheritance-taxes-2014>, accessed on 25 November 2014.

¹⁵⁵ Emanuel op cit (n154).

exemption level by 2019 while Minnesota has promised to double its exemption from \$1 million to \$2 million by 2019.¹⁵⁶

8.2.1 The Calculation of Federal Estate Tax

This tax is calculated by taking the gross estate and deducting applicable deductions. For a United States citizen or resident, the gross estate is the fair market value of a deceased's worldwide assets at date of death.¹⁵⁷

8.2.1.1 Retained Interests

In the United States there are retained interest rules which means that the estate tax is not only imposed on the assets a deceased owned at the date of his death as certain other property may be deemed to be included in the gross estate at death. Such property which would be subject to these retained interest rules are:

- Certain gifts made within three years of death;
- Transfers with a retained life estate;
- Transfers taking effect at death;
- Certain annuities;
- Interests owned jointly;
- Transfers that provide for broad powers of appointment; and
- Revocable transfers.¹⁵⁸

¹⁵⁶ Ibid.

¹⁵⁷ Ernst & Young op cit (n145).

¹⁵⁸ Ibid.

8.2.2 State Estate Tax

Many states impose their own estate tax which is separate to the federal estate tax. The estate taxes themselves are quite significant, and as a result, individuals are granted a reprieve whereby the deceased estate are granted a deduction at the federal level for any state estate taxes paid.¹⁵⁹

8.3 Gift Tax

Gift tax is imposed on all United States citizens and residents on transfers of all property, tangible and intangible, regardless of the location of the property. Gift taxes are applied on the fair market value of the transferred assets as at the date the gift was made.¹⁶⁰

An annual exclusion is permitted per donee (being (\$14 000 in 2014) and is indexed for inflation. Gift taxes are levied at a top rate of 40 per cent and United States citizens and residents are entitled to a \$5 million gift tax exemption which is adjusted annually for inflation (\$5.34 million for 2014). The US gift and estate tax are unified and there is only one exemption for both gift and estate tax. This means that any gifts made during a person's lifetime will reduce his or her estate tax exemption.¹⁶¹

8.4 Generation-Skipping Transfer Tax

Generation-skipping transfer tax was introduced in 1986. This tax was created as a way to prevent the wealthy from transferring property to beneficiaries more than one generation removed from such individuals effectively allowing

¹⁵⁹ Ibid.

¹⁶⁰ Ibid.

¹⁶¹ Ibid.

that property to pass without any estate or gift tax being paid in between the transfers.

Generation-skipping transfer tax is imposed on all direct transfers to 'skip persons' and on taxable distributions and taxable terminations by trusts that have skip persons as beneficiaries. A 'skip person' is defined as a person who is two or more generations below the transferor or a trust for which all beneficiaries are skip persons. Generation-skipping transfer tax is imposed at a rate of 40 per cent and there is an exemption of \$5 million which is adjusted annually for inflation (\$5.34 million for 2014).¹⁶² The generation-skipping transfer tax exemption is in addition to the gift and estate tax exemption.¹⁶³

United States citizens, residents and non-residents are given the same generation-skipping transfer tax exemption amount. A person may irrevocably allocate generation-skipping transfer tax exemption to any property transferred during his or her life or at death.¹⁶⁴

8.5 Capital Gains Tax

The Internal Revenue Code was introduced in 1913 and, among other taxes, governs the imposition of capital gains tax in the United States. In terms of this code, individuals pay federal income tax on the net total of all their capital gains. Long term capital gains are taxed at a preferential rate in comparison to ordinary income. The amount an investor is taxed depends on both his or her tax bracket, and the amount of time the investment was held before being sold.¹⁶⁵

¹⁶² J Garber 'Overview of 2014 Estate Tax, Gift Tax & Generation Skipping Transfer Tax Laws', available at <http://wills.about.com/od/2014-Estate-Tax-Rules/fl/Overview-of-2014-Estate-Tax-Gift-Tax-amp-Generation-Skipping-Transfer-Tax-Laws.htm>, accessed on 25 November 2014.

¹⁶³ Ernst & Young op cit note (n145).

¹⁶⁴ Ibid.

¹⁶⁵ D Roos 'How Capital Gains Tax Works', available at <http://money.howstuffworks.com/personal-finance/personal-income-taxes/capital-gains-tax.htm>, accessed on 25 November 2014.

Short-term capital gains are taxed at an individual's ordinary income tax rate and are defined as investments held for a year or less before being sold. Long-term capital gains are defined as gains on dispositions of assets held for more than one year and are taxed at a lower rate than short-term gains. In 2003, this rate was reduced to 15 per cent and to five per cent for individuals in the lowest two income tax brackets.¹⁶⁶

Capital gains tax is 'forgiven' at death meaning if a taxpayer holds on to an asset until he or she dies, neither the deceased estate nor the beneficiaries will have to pay capital gains tax on any increase in the asset's value prior to the deceased's death.¹⁶⁷ Even though this rule is not embodied in the Internal Revenue Code, the government has consistently treated bequests by a deceased to beneficiaries as non-taxable events and not as a disposal.¹⁶⁸

Section 1014(a) of the Internal Revenue Code states that the basis of property acquired from a deceased estate is either the fair market value of that property on the date of death hereinafter referred to as the 'date-of-death basis'.¹⁶⁹ The date-of-death basis will apply to property acquired by way of bequest or inheritance or by the deceased's estate from the deceased.¹⁷⁰ In the event that a capital asset of the deceased has not been distributed, sold, exchanged or otherwise disposed of by his or her executor within six months of the deceased's death, the executor may, in terms of the code, elect to use the asset's fair market value six months after the deceased's death, which value will then be the basis of the asset.¹⁷¹ This usually means that the basis will be a greater amount. If no election is made the basis of the asset will then automatically be the fair market value of the asset as at the date of the deceased's death. If however, the capital asset is distributed, sold, exchanged or otherwise disposed of within six months of the deceased's death the basis

¹⁶⁶ Roos op cit (n165).

¹⁶⁷ Centre on Budget and Policy Priorities 'Chart Book: 10 Things You Need to Know about the Capital Gains Tax', 20 September 2012, available at <http://www.cbpp.org/cms/index.cfm?fa=view&id=3798>, accessed on 25 November 2014.

¹⁶⁸ Van Jaarsveld op cit (n128) 34.

¹⁶⁹ Ibid.

¹⁷⁰ Van Jaarsveld op cit (n128) 35.

¹⁷¹ Ibid.

of the asset will be the fair market value of such asset as at the date of distribution, sale, exchange or other disposition.¹⁷²

This means that whether the fair market value of a capital asset as on date of death or the fair market value of the asset six months later is used, it will in most cases result in a 'step-up' in the basis of that capital asset. This is known as the 'stepped-up basis'¹⁷³ (which was referred to earlier in Chapter 1) and means that any increase in value of such an asset is not subject to capital gains tax resulting in any significant capital gain not being subject to capital gains tax. The government's decision not to tax capital gains on death has been said to be the most serious flaw in the United States federal tax system.¹⁷⁴

The United States is thus similar to South Africa in its levying of death taxes in some respects. For example, both countries levy an estate tax while at the same time provide for an exemption level. However, South Africa levies capital gains tax on death against a deceased estate. The United States on the other hand, and similar to the United Kingdom albeit in a different way, has chosen 'forgive' capital gains tax at death.

¹⁷² Van Jaarsveld op cit (n128) 36.

¹⁷³ Ibid.

¹⁷⁴ Van Jaarsveld op cit (n128) 37.

CHAPTER 9 : DEATH TAXES IN CANADA

Unlike South Africa, the United Kingdom and the United States, Canada imposes a completely different system of taxation upon death. There is no estate duty levied on a deceased estate and capital gains tax is solely relied upon.

9.1 History of Wealth Transfer Tax

During 1962, a Royal Commission on Taxation (the Carter Commission) was appointed in order to re-evaluate the taxes which were being levied on the population at that time¹⁷⁵ as there was growing concern that the taxes, including the wealth transfer tax (under the Estate Tax Act of 1958), being charged were too high.¹⁷⁶ The Shoe Man Manufacturers' Association of Canada, for example, argued that 'the unreasonably high level of succession duties has been the largest single factor both in encouraging the sell-out of Canadian enterprises to foreign interests and in eliminating from the economic scene continuing independent family businesses. The Canadian Bar Association criticised the methods being used by the wealthy who would transfer their expensive properties to trusts thereby avoiding having to pay death taxes¹⁷⁷ and resulting in extensive economic damage to the economy. Contributing to this economic decline was the failure to tax capital gains on death.¹⁷⁸

The Commission published its report in 1967 and proposed that in order to create a fairer and more level playing field, taxes should be levied according

¹⁷⁵ D Duff 'The Abolition of Wealth Transfer Taxes: Lessons from Canada, Australia and New Zealand' available at <http://law.bepress.com/cgi/viewcontent.cgi?article=3046&context=expresso>, accessed on 25 November 2014 at 26.

¹⁷⁶ Duff op cit (n175) 27.

¹⁷⁷ Ibid.

¹⁷⁸ Ibid.

to a taxpayer's economic and wealth status and suggested the creation of a broad tax base according to which the 'all the net gains ... of each tax unit' should be subject annually.¹⁷⁹

A further submission by the Commission was that the tax base should include all gifts and inheritances for the year in which they were made as well as any capital gains made upon the disposition of property upon death. The Report suggested gifts and inheritances should be included in a taxpayer's income, which meant that separate wealth transfer taxes should be abolished.¹⁸⁰

The Canadian government agreed with the Commission's Report that any capital gains should be fully taxable at ordinary rates however disagreed that when property is transferred on death that capital gains tax should be levied upon a deceased estate. Instead the government stated that the beneficiary of the asset would be taxed as if he or she had purchased the asset at their cost from the deceased. With regard to gifts, the government proposed that capital gains should be taxable in the year that the gift was made and that the donee should be treated as having purchased the asset for its fair market value.¹⁸¹

In response to the Canadian government's suggestions, the Ontario Government made a few recommendations of its own. Firstly, it suggested that levying capital gains tax at a lower rate and included capital gains tax upon gains at death, and instead of repealing separate wealth transfer tax legislation, it stated that there should only be a reduction in these taxes.¹⁸² However, many critics argued that the levying of both capital gains tax and the estate tax was 'an attack on the middle-class values of hard work, thrift and initiative and a confiscation of the money and resources of the huge middle segment of the population'.¹⁸³

¹⁷⁹ Duff op cit (n175) 28.

¹⁸⁰ Duff op cit (n175) 29.

¹⁸¹ Duff op cit (n175) 34.

¹⁸² Duff op cit (n175) 35.

¹⁸³ Duff op cit (n175) 36.

Eventually in 1972 the Canadian government passed the Income Tax Act which levied capital gains tax at death when property is transferred as well as by gift. The legislation also repealed estate and gift tax to the provinces.¹⁸⁴ The government allowed certain provinces time to align their state legislation with the federal legislation and by 1985 succession duties, gift tax and estate tax were abolished in Canada.¹⁸⁵

9.2 Current Situation

There is no estate tax in Canada, however realised capital gains are taxed at death similar to the way in which South Africa taxes these gains.¹⁸⁶ Therefore, when a Canadian individual passes away, any capital asset owned by him or her at date of death is deemed to have been sold by him or her immediately before his death at a price equal to the market value of the asset at that time.¹⁸⁷ The estate or other person or entity that acquires the asset will be deemed to have acquired that asset at a cost equal to the fair market value of the asset as on date of death. The capital gain will be the difference between the price at which the asset is sold – which in this case is the fair market of the asset belonging to the deceased on date of his death and its original cost to the deceased.¹⁸⁸

Similar to South Africa's capital gains tax regime, capital gains tax will not be levied if the asset is transferred to a surviving spouse, minor child or to a spousal trust. When the surviving spouse dies, however, capital gains tax will be levied on his or her estate.¹⁸⁹

¹⁸⁴ Duff op cit (n175) 40.

¹⁸⁵ Duff op cit (n175) 47.

¹⁸⁶ JS Gans & A Leigh 'Did the Death of Australian Inheritance Taxes Affect Deaths' Topic in Economic Analysis & Policy, 6(1): 1-7 available at http://andrewleigh.org/pdf/DeathAndTaxes_BEP.pdf, accessed on 25 November 2014 at 1.

¹⁸⁷ Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/IEIT-2013/IEIT-CA.xml>, accessed on 12 December 2014.

¹⁸⁸ Van Jaarsveld op cit (n128) 24.

¹⁸⁹ Ernst & Young op cit (n187).

CHAPTER 10 : DEATH TAXES IN AUSTRALIA

Australia imposes a similar system of death taxes to Canada in some respects. For example, no estate tax or estate duty is levied on an Australian deceased estate (unlike in South Africa). However, it differs from Canada and South Africa when it comes to levying of capital gains tax on death.

10.1 History of Wealth Transfer Tax

The move to abolish wealth transfer taxes in Australia began in 1970 when mounting support for its repeal began to build. The reasons for its abolishment included the fact that firstly, exemptions had not been increased to account for inflation, causing Commonwealth and State taxes to apply to relatively small estates. Secondly, there was a failure to combine the Commonwealth and state duties resulting in what many called double taxation. Thirdly, the costs involved in complying with the taxes were larger for deceased estates with small businesses than for most other sizeable deceased estates.¹⁹⁰ Lastly, the wealthier individuals were able to avoid having to pay these taxes by setting up instruments such as discretionary trusts which they could use to transfer assets from generation to generation avoid paying the tax,¹⁹¹ which resulted in the tax burden being placed more so on the small to medium sized estates.¹⁹²

At the government level, the death taxes were not bringing in the desired revenue when compared to government public expenditure. For example, in 1973, the government collected about AUS\$75 million from gift and estate taxes, which amounted to only 0.7 per cent of total tax revenues.¹⁹³

¹⁹⁰ Duff op cit (n175) 49.

¹⁹¹ Ibid.

¹⁹² Duff op cit (n175) 50.

¹⁹³ Ibid.

Therefore, as a result of mounting pressure, in 1977, some state governments decided to completely abolish estate taxes.¹⁹⁴ Other states followed suit by abolishing their own gift and estate duties. As one commentator reflected, 'by the early 1980s, the momentum against any death taxation in Queensland carried all other state death duties to the grave'.¹⁹⁵

10.2 Current Situation

There is no inheritance (or estate tax) payable in Australia. At death any assets transferred to beneficiaries of a deceased estate are deemed to be disposals and are subject to capital gains tax. Capital gains tax is levied in terms of the Australian Income Tax Assessment Act of 1997 and any asset acquired after 20 September 1985 is referred to as a 'post-capital gains tax asset'.¹⁹⁶

Generally in terms of this Act, capital gains tax is levied upon any change of ownership of a post-capital gains tax asset however, when it comes to levying capital gains tax on death, any capital gain made on a post-capital gains tax asset will be disregarded in the event that a taxable asset owned by the deceased passes directly to his legal personal representative or to a beneficiary, or in the event that such asset passes from the legal personal representative to a beneficiary.¹⁹⁷

If however the asset is bequeathed to a charity, superfund or foreign resident, any capital gain will be taken account of in the deceased's final tax return. Also, where a beneficiary is entitled to this kind of exemption, he or she would have to pay capital gains tax on any asset inherited when it is then subsequently sold. In this case, assets acquired before 20 September 1985 (a pre-capital gains tax asset) by the deceased will be deemed to have a base cost to the beneficiary equal to the market value of the asset as of the date of the deceased's death. Assets acquired after 19 September 1985 by the

¹⁹⁴ Duff op cit (n175) 51.

¹⁹⁵ Duff op cit (n175) 52.

¹⁹⁶ Van Jaarsveld op cit (n128) 25.

¹⁹⁷ Ibid.

deceased will be deemed to have a base cost to the beneficiary equal to the deceased's base cost.¹⁹⁸

The effect of the pre-capital gains tax asset gives a taxpayer a higher base cost without a corresponding capital gains tax liability for the estate of the deceased. The asset will however after it has been transferred to the beneficiary lose its pre-capital gains tax status and will be subject to capital gains tax when the beneficiary eventually disposes thereof. Van Jaarsveld explains that the Australian position with regard to capital gains tax on death is similar to South Africa's position (with respect to the post-capital gains tax asset) as capital gains tax will eventually have to be paid, however it differs in that the capital gains tax liability is postponed until that beneficiary decides to dispose of the asset at some date in the future, if ever, and if the asset has not been disposed of by the time of that beneficiary's death a roll-over will apply.¹⁹⁹

In summary, Australia differs materially from South Africa in its death taxes as it does not levy any estate duty on a deceased estate. Also capital gains tax is generally not levied upon death. Where in South Africa capital gains tax is levied on death, in Australia this is not always the case as different rules apply. A pre-capital gains tax asset will not be subject to capital gains tax and if this asset is held onto by a beneficiary until his or her death, the base cost of this asset will become the base cost equal to the market value of the asset as of his or her death without a capital gains tax liability for his or her estate. A post-capital gains tax asset will not attract capital gains tax if it is passed directly to his legal personal representative to a beneficiary or from the legal personal representative to a beneficiary.

¹⁹⁸ Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/IEIT-2013/IEIT-AU.xml>, accessed on 24 November 2014.

¹⁹⁹ Van Jaarsveld op cit (n128) 27.

CHAPTER 11 : DEATH TAXES IN INDIA

Previously, India used to conduct its taxes on death in a similar manner to that of South Africa, by levying an estate duty on a deceased estate. However, after certain legislative amendments, India decided to follow the example of countries like Canada and Australia and abolish its estate duty. Capital gains tax is also not levied against a deceased estate on death.

11.1 History of Wealth Transfer Tax

Estate duty in India was abolished in 1985. Prior to its removal however, this tax was levied on at a range of 7.5 per cent to 40 per cent of the total value of the estate, under the Finance Act of 1953.²⁰⁰ This tax was levied on the value of the assets transferred by the deceased sometimes at a maximum rate of 85 per cent. It included not only the assets at the time of the deceased's death but also the assets transferred in contemplation of death up to two years prior to the death of the person.²⁰¹ There were not many exemptions, except for one residential house being exempt.²⁰²

The move to abolish estate duty began for reasons such as difficulties in imposing the estate duty legislation and the ease by which it could be avoided, problems in valuing estates, the high costs involved in the administration of the legislation administrative costs plus the extensive litigation taking place in the courts made levying and collecting estate duty an expensive task for the government with the costs of collection exceeding the

²⁰⁰ Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/IEIT-2013/IEIT-IN.xml>, accessed on 24 November 2014.

²⁰¹ S Monani & G Zaoba 'It's a Bad Time to Bring Back Estate Duty', 19 February 2013, available at <http://www.dnaindia.com/mumbai/report-its-a-bad-time-to-bring-back-estate-duty-1801388>, accessed on 21 November 2014.

²⁰² K Dalal 'Estate Duty: Sword of Damocles over India', 6 February 2013, available at http://articles.economictimes.indiatimes.com/2013-02-06/news/36949807_1_estate-duty-wealth-tax-financial-assets, accessed on 21 November 2014.

revenues generated.²⁰³ The government ultimately abolished the tax in 1985 although litigation involving previous estate duty matters continued to clog up the court rolls for a many years following the repeal.²⁰⁴

Recently, and in complete contrast to the situation in South Africa, there have been calls to reintroduce estate duty in India. The reasons for the calls for a reintroduction of the tax is as a result of the accumulation of wealth by a small minority of the population, the need for inter-generational equity and the need for an increase in the contribution to the national revenue. Proponents for the reintroduction of estate duty in India have argued that it is the only way to bridge the gap between the rich and the poor as recently India has seen a steady increase in the number of millionaires being created due to the economic growth and growing capital markets. Opponents against a reintroduction of the tax argue that since the wealthiest individuals make up only about 0.01 per cent of India's population, it is difficult to ascertain how much revenue could actually be collected from such a small percentage of the population in order to benefit society at large. They argue that what is needed is a framework of systematic reforms which could result in economic growth benefiting all classes of society.²⁰⁵

It is however, necessary to juxtapose the history and evolution of taxes in India against the contemporary economic state of the nation.²⁰⁶ When estate duty was still a part of India's tax legislation, individuals were subjected to extremely high levels of personal taxation, including income tax, gift tax and net wealth tax. During the 1970s income tax rates reached about 90 per cent and then about 50 per cent during the 1980s. Net wealth tax was imposed on almost all of the asset classes as was gift tax.²⁰⁷ During this time too, individuals were subjected to a high tax regime which gradually moved to become more of a moderate tax regime after the abolishment of estate duty.

²⁰³ Monani op cit (n201).

²⁰⁴ Ibid.

²⁰⁵ H Kotak & J Shah 'Union Budget 2013: Inheritance Tax May Make a Comeback', 28 February 2013, available at <http://firstbiz.firstpost.com/economy/union-budget-2013-inheritance-tax-may-make-a-comeback-36881.html>, accessed on 12 December 2014.

²⁰⁶ Monani op cit (n201).

²⁰⁷ Ibid.

Net wealth taxation was also amended to include only select asset classes. The reasons for this move was the belief that it would result in a drop in tax avoidance and encourage individuals to comply with the tax laws which would hopefully reduce the volume of litigation experienced by the courts ultimately lowering the costs involved in administering and ensuring compliance with the tax. These measures have not been in vain and over the last two decades have resulted in an increase in voluntary compliance and an increase in tax revenue.²⁰⁸

11.2 Current Situation

Currently in India, upon death, a deceased's assets are transferred to the beneficiaries through a mutation, without triggering any inheritance or estate taxes or income tax. A mutation is defined as 'the change of title ownership from one person to another when the property is sold or transferred'.²⁰⁹ However, any income which is derived from the asset inherited or in the event of sale of the asset, income tax will be levied thereon.²¹⁰

Until 2004, gift tax used to be levied on gifts made up of any movable or immovable property, without consideration, at the rate of 30 per cent. After 2004, any transfers without consideration were taxed in the form of income tax in the donee's hands on gifts with certain exceptions. Also, there is still an exemption on the transfer of property by way of gift. However, the difference between the fair value and the consideration paid by the donee is taxable for the donee.²¹¹

²⁰⁸ Monani op cit (n201).

²⁰⁹ Property Pulse "What is Mutation of Property and why is it Important?" 3 December 2013, available at <http://content.magicbricks.com/legal-taxation/what-is-mutation-of-property-and-why-is-it-important/60616.html>, accessed on 24 November 2014.

²¹⁰ VP Singh and P Chidambaram 'Inheritance Tax: Should India Introduce It?', 12 July 2011, available at http://articles.economictimes.indiatimes.com/2011-07-12/news/29765538_1_tax-gdp-ratio-inheritance-tax-wealth-tax, accessed on 24 November 2014.

²¹¹ Ernst & Young op cit (n200).

On subsequent transfer of the asset received by the donee as a gift, the difference between the sale consideration and the cost of such asset is taxable in the hands of the donee as capital gains.²¹²

Net wealth tax is also payable at 1 per cent if the value of an individual's net worldwide wealth exceeds an amount of 3 million Indian rupees. This tax is levied on the net wealth of a person and is calculated on 31 March of every year and is imposed under the Wealth Tax Act of 1957 as amended by the Finance Bill of 2012. However, if the individual is a foreign citizen, non-resident, or resident but not ordinarily resident, their assets located outside of India's jurisdiction will be exempt. Assets subject to net wealth taxation include 'residential houses, cars, yachts, boats, aircraft, urban land, jewellery, bullion, precious metals, cash and commercial property not used as business, office or factory premises'.²¹³

Unlike in South Africa, any transfer of a capital asset under a gift or a will does not attract provisions of capital gains tax. However, if the beneficiary were to eventually sell the asset, capital gains tax would then be levied.²¹⁴

In summary, India's system of taxation on death is remarkably different to the system followed by South Africa, with India not levying any estate duty or capital gains tax on death but imposes a net wealth tax on every individual.

²¹² Ibid.

²¹³ Ibid.

²¹⁴ DNA India 'How to Compute Capital Gains on your Inherited Property' 21 September 2011, available at <http://www.dnaindia.com/analysis/column-how-to-compute-capital-gains-on-your-inherited-property-1589601>, accessed on 24 November 2014.

CHAPTER 12 : DEATH TAXES IN BOTSWANA

Botswana death tax laws are similar to South Africa in some respects, in that an inheritance tax (or estate tax) is payable on the death of a deceased. However, unlike South Africa, it appears that capital gains tax is actually 'forgiven' at death due to certain provisions as contained in the Botswana Income Tax Act.

In Botswana, taxation on death is governed by the Botswana Income Tax Act of 2002. The Act does not specify whether or not the death of a Botswana taxpayer is regarded as a deemed disposal of a capital asset with a corresponding capital gains tax liability on any gain realised in respect thereof.²¹⁵

The Act does state however, that when a beneficiary disposes of an inherited asset which the deceased acquired before 1 July 1982, the acquisition cost (or base cost as it is referred to in South Africa) will be the market value as at 1 July 1982. Where the deceased acquired the asset after 1 July 1982 the acquisition cost shall be the market value as at the date of such acquisition. When calculating the market value of an asset, certain expenses incurred, taxes and duties paid may be taken into account.²¹⁶

Inheritance tax (meaning estate duty) is also payable by a deceased estate. This tax is payable by individuals upon the disposal by way of inheritance, donation, or other gratuitous disposals of property and is based on a sliding scale. The sliding scale values vary from 2 per cent to 5 per cent based on the net aggregate gains realised on the disposal of the property. Movable and immovable property, corporeal and incorporeal property wherever situated is subject to inheritance tax.²¹⁷

There are certain disposals which are exempt from inheritance tax, such as:

²¹⁵ Van Jaarsveld op cit (n128) 29.

²¹⁶ Ibid.

²¹⁷ KPMG 'Botswana: Other Taxes and Levies', 5 January 2013, available at <http://www.kpmg.com/global/en/issuesandinsights/articlespublications/taxation-international-executives/botswana/pages/other-taxes-levies.aspx>, accessed on 25 November 2014.

1. donations to a spouse during the lifetime of that spouse (this provision is similar to the South African section 4(q) deduction);
2. gifts to a person on his or her marriage which does not exceed 5 000 pula;
3. household goods and personal belongings which have been inherited from a deceased person up to a value of 15 000 pula;
4. property disposed of to a non-resident and which is situated outside Botswana;
5. property disposed of for the purpose of maintaining or the education of a child to a maximum age of 21 years; and
6. casual gifts, which do not exceed 5 000 pula in value.²¹⁸

In summary, while an inheritance tax will be levied on a deceased estate in Botswana, it is likely that a beneficiary will escape having to pay any capital gains tax on an inherited asset. The reason for this is because a beneficiary is deemed to have received the asset at a value equal to the original acquisition cost thereof or at a value as at 1 July 1982. There is no provision in the Botswana Income Tax Act which states that an asset will be given a market value as on the date of the deceased's death.

²¹⁸ KPMG op cit (n217).

CHAPTER 13 : DEATH TAXES IN THE NETHERLANDS

Unlike in South Africa, nor any of the other countries examined above, neither estate duty nor capital gains tax is levied upon death in the Netherlands. Instead, assets acquired by beneficiaries of a deceased estate are subject to inheritance tax.

Inheritance tax is governed by the Inheritance Tax Act of 1956 and is levied on any assets received by a beneficiary from a deceased estate and is paid by the beneficiary and not by the estate. This tax is based on the residence of the deceased and is dependent on the amount of money a beneficiary would inherit.

Certain assets are included in this tax, for example gifts made by the deceased within 180 days prior to his or her death and proceeds of any life insurance policies for which the deceased paid the premiums while he or she was alive. The assets acquired through an inheritance is valued at the fair market value less any liabilities at the time of the deceased's death.²¹⁹

The tax rates that are applicable depend on the relationship between the heir and the beneficiaries, for example: Transfers to spouses, co-inhabitants and children are taxed on a scale between 10 per cent and 20 per cent. Transfers to direct descendants in the second or further degree, such as grandchildren, are taxed on a scale between 18 per cent and 36 per cent. Transfers to parents, brother, sisters and non-related persons are taxed on a scale between 30 per cent and 40 per cent.²²⁰

Where the law does contain similarities to South Africa and other countries described above, is when it comes to certain exemptions provided. For example, a surviving spouse is allowed an exemption of €523 667 for the 2014 year of assessment. A surviving partner of an unmarried couple who have been living together for at least five years is also provided the same

²¹⁹ Global Property Guide 'Inheritance Tax and Law' 12 May 2014 available at <http://www.globalpropertyguide.com/Europe/Netherlands/Inheritance>, accessed on 25 November 2014.

²²⁰ Global Property Guide op cit (n219).

exemption level. The exemption level is reduced proportionally if a couple have been living together for less than five years.²²¹

Other exemptions apply, for example, for children under 23 years, a deduction of €4 479 is provided for each year below the age of 23 years. For children older than 23 years, an exemption of €10 150 exists provided that the inheritance does not exceed €26 852.²²²

In summary, in the Netherlands, it is the beneficiaries of an estate that are responsible for paying an inheritance tax, whereas In South Africa, the tax is based on the value of the estate and estate duty is levied upon the transfer to the heirs and generally paid by the estate.

²²¹ CFE 'Inheritance Tax in the Netherlands' available at <http://www.cfe-eutax.org/taxation/inheritance-tax/netherlands>, accessed on 25 November 2014.

²²² CFE op cit (n221).

CHAPTER 14 : SUGGESTED ALTERNATIVES TO THE CURRENT REGIME

This dissertation has thus far investigated the various taxes imposed by South Africa and the other above mentioned countries on death, and has taken a look at what the various proponents and opponents of death taxes have to say. It has also explored the various issues South Africa has experienced in levying both estate duty and capital gains tax on death. Possible suitable alternatives to the current South African tax regime shall now be discussed, with an emphasis on the following alternatives currently being given the foremost weight:

1. Retaining estate duty and forgiving capital gains tax on death;
2. Abolishing estate duty and relying only on capital gains tax; or
3. Replacing estate duty with an inheritance tax.

14.1 Retaining Estate Duty and Forgiving Capital Gains Tax on Death

As in the case of the United States, United Kingdom, Australia, India and Botswana, capital gains tax is 'forgiven' at death. South Africa remains one of the few countries to levy both taxes at death, resulting in double taxation. In order to avoid this double tax imposition, it has been suggested that South Africa follow the example of the United States and the United Kingdom and only levy estate duty and not capital gains tax on the death of a taxpayer.

In order for this option to be implemented, Ostler²²³ suggests that the South African Institute of Chartered Accountants' ('SAICA') guidelines be taken into

²²³ L M Ostler *The Impact of Estate Planning on the Effectiveness of Estate Duty as a Wealth Tax in South Africa* MCom (Grahamstown) (2012) 89.

account. SAICA state that certain legislative changes would have to be made to the Estate Duty Act, including:

1. The administrative process which would have to be simplified in order to avoid the large costs involved in collecting the limited revenue generated.
2. The Act itself, as it is well-established and entrenched in South Africa's tax landscape and has been in operation since 1965. There is also much case law and precedent already in place to support its application.
3. An amendment to Section 5 of the Act which deals with the valuation of limited interests on death. Currently, people are able to escape having to pay estate duty through loopholes in this section and this section would have to be tightened.²²⁴
4. An exemption of up to a certain amount with regard to life insurance policies which are currently subject to estate duty. SAICA state that this would also assist the estate in paying the amount of estate duty owing by the estate itself.²²⁵

Apart from the above, Roeleveld adds that there are other major issues which need to be considered before adopting the approach of retaining estate duty and removing capital gains tax.

For example, an amendment to donations tax would have to be undertaken. Currently in South Africa, any disposals for a consideration below market value will be subject to both donations tax and capital gains tax. Roeleveld suggests that if estate duty was to be solely relied upon on death, donations should also be excluded from capital gains tax so that 'equity can be achieved'. Furthermore, capital gains tax legislation would have to be amended in that 'the market value used for the donations tax calculation and

²²⁴ Ostler op cit (n223) 90.

²²⁵ Ostler op cit (n223) 91.

not the consideration paid must be the base cost for the donee for a subsequent disposal. The reason for this is that ultimately, on death, the full market value is subject to estate duty. Capital gains tax can only be collected on disposals for a consideration and only on the increase in value since acquired by donation'.²²⁶

Roeleveld also suggests that no change be made to the value at which heirs and beneficiaries receive assets from a deceased estate. Currently, when an heir or beneficiary receives an asset he or she does so at market value. Capital gains tax has already been paid on this amount as has estate duty. It would not be fair for an asset to be given to an heir or beneficiary at its original base cost as this would result in double taxation, in other words, the estate having to pay estate duty on the full market value at death and then when the beneficiary or heir later disposes of the asset, he or she would be liable for capital gains tax on the increased value after death.²²⁷

Personal use assets are excluded from capital gains tax and Roeleveld suggests that they should also be excluded from estate duty. If they are to be included for estate duty purposes, then there should be an exclusion of up to a certain value to prevent the need of having to value small items.²²⁸

Lastly, Roeleveld suggests an amendment to Section 16 of the Estate Duty Act. She suggests that should foreign taxes paid on the same wealth this should be set off against a South African estate duty liability in respect of the same assets of the deceased.²²⁹

14.2 Abolishing Estate Duty and Relying only on Capital Gains Tax

²²⁶ JJ Roeleveld 'An Argument for Either Excluding Death as a Capital Gains Tax Event or Abolishing Estate Duty' (2012) *SA Journal of Accounting Research* Vol. 26 available at <http://www.sajar.co.za/documents/SAJAR-26-7-Roeleveld-final.pdf>, accessed on 26 November 2014 at 157.

²²⁷ Roeleveld op cit (n226) 158.

²²⁸ Ibid.

²²⁹ Roeleveld op cit (n226) 159.

Ger suggests that the best alternative to the current situation in South Africa would be to rely solely on capital gains tax by extending existing capital gains tax legislation and completely repeal estate duty.

14.2.1 The Advantages of Relying Solely on Capital Gains Tax

He states that this would be the best solution as capital gains tax is recognised worldwide and is much easier to collect and administer as it is usually governed by laws of income tax which are firmly entrenched. He argues that this would solve the problem where similar taxes are imposed on assets by two or more countries as most countries have signed double taxation agreements relating to capital gains tax and would contribute more significantly to government revenue as capital gains tax could bring in even more revenue if increased over time.²³⁰

Concurring with Ger, Jacobs argues that capital gains tax could be extended by making the following changes: expanding the classes of assets that attract capital gains tax, increasing the inclusion rate, and increasing the amount of tax payable in making the actual effective rate equal or higher to the actual effective rate of the tax to donations tax and estate duty.²³¹

Importantly, the National Treasury have stated that the revenue generated by estate duty is not worth the cost of administering the tax. As is evident from Table 5 above, estate duty revenue as a percentage of gross tax revenue on property has averaged 11.2 per cent from 2010/11 to 2012/13 and was 10.5 per cent in 2014. Total estate duty collected in 2013/14 was R1.1 billion.

As indicated in Table 3 above, for the 2013/14 fiscal year, capital gains tax of R11.6 billion was raised of which R7 billion was attributable to individuals and R4.6 billion to companies. This is an increase from the R7.2 billion raised

²³⁰ Ger op cit (n91) 60.

²³¹ Jacobs op cit (n95).

in 2012/13. A total of R61.7 billion has been raised since the introduction of capital gains tax in October 2001.²³²

The above data shows that capital gains tax collected R10.5 billion more than estate duty during the 2013/14 year of assessment. Should capital gains tax be extended, even more revenue could be generated, suggests Ger.

According to Roeleveld, this is not surprising as capital gains tax is considered to be a far more advanced tax for various reasons, some of which include:

The fact that it is recognised internationally and widely applied and covers a much larger range of taxable assets as opposed to estate duty. It treats a wider array of events as 'disposals' for example, becoming a resident or ceasing to be a resident for tax purposes, transferring assets and donating assets. Included in the events which trigger capital gains tax are donations, sales or any transfer of assets into trusts as well as the death of a taxpayer.²³³

Capital gains tax is easier than estate duty to collect as it is already administered under the Income Tax Act and has been successful in adding to the national budget since its implementation date in 2001. Also, the anti-avoidance provisions under the Income Tax Act can be used for capital gains tax.

It is argued to be a fairer, more just tax as the more assets a person has accumulated, the more tax he or she shall have to pay. Roeleveld states that in 2013 and 2014 taxpayers in the highest tax bracket, including individuals and special trusts, had to pay an effective tax rate of 13.3 per cent (10 per cent in 2012), while a taxpayer in the lowest tax bracket of 18 per cent had to pay 5.10 per cent (4.5 per cent in 2012) on the taxable capital gain or even no tax if the aggregate of their income and taxable capital gain was below the tax threshold. Companies and trusts had to pay an effective rate of 18.6 per cent

²³² Department of National Treasury '2014 Tax Statistics' available at <http://www.treasury.gov.za/publications/tax%20statistics/2014/TStats%202014%20WEB.pdf>, accessed on 26 November 2014.

²³³ Roeleveld op cit (n226) 152.

and 26.7 per cent respectively (14 per cent and 20 per cent respectively in 2012).²³⁴

Capital gains tax is a more modern and updated form of tax legislation, as opposed to estate duty and, as Roeleveld points out, the Estate Duty Act still refers to persons ordinarily resident. For example, the definition of a resident has changed for domestic income tax purposes. The Estate Duty Act was also created during the period when South Africa's tax legislation was based on a source based tax system, as opposed to the current recipient based tax system. Furthermore, for capital gains tax, the tests for establishing whether a person is ordinarily resident are different from those under the Estate Duty Act as under the latter assets of non-residents who become residents only on the basis of the physically present test do not fall into the estate duty net. However, for the purposes of capital gains tax, any gains made by these 'residents' are subject to capital gains tax under the Income Tax Act.²³⁵

Another difference between capital gains tax provisions and estate duty is that capital gains tax legislation includes gains made under indirect interests in immovable property for residents as well as non-residents. The Estate Duty Act does not cover this scenario and Roeleveld argues that this is significant as shares held at death in a foreign company owning South African immovable property will not be taxed for estate duty, while capital gains tax is imposed on the disposal of shares by non-residents who have a shareholding of at least 20 per cent in a company and where the market value of immovable property held by the company contributes at least 80 per cent toward the market value of the shares of the company.²³⁶

The most significant advantage of capital gains tax is that it is a globally recognised tax and is covered by most double taxation treaties on income and capital around the world. According to Roeleveld, South Africa has entered into almost 70 double taxation agreements with other countries and these cannot

²³⁴ Roeleveld op cit (n226) 152.

²³⁵ Roeleveld op cit (n226) 153.

²³⁶ Para 2(b) of the Eighth Schedule to the Income Tax Act 58 of 1962.

be renegotiated. The same cannot be said for estate taxes as these are not found in all countries as illustrated above. South Africa has only entered into five double taxation agreements which cover estate duty, and two out of the five have been entered into with the United Kingdom and the United States as these jurisdictions still impose estate tax as was explained above in chapters 7 and 8 respectively. These double taxation agreements are outdated as they were entered into when South African tax legislation was still imposed on a source basis and were drafted before the new, more modern tax treaties were created.²³⁷

14.2.2 The Disadvantages of Relying Solely on Capital Gains Tax

There are however certain problems with relying solely on capital gains tax. For example, when it comes to determining proceeds upon death, they are deemed to be based on the market value of the asset at the date of the deceased's death. The market value of an asset can be calculated in numerous ways, some of which are referred to as the discounted cash flow method, the economic profit method and cash value added method. These different valuation techniques can result in differing valuations for similar assets and unfortunately can be manipulated to suit the taxpayer or subject to calculation error. Calculating capital gains tax can be extremely difficult and this causes many headaches in determining tax liability.²³⁸

Capital gains tax is levied on unrealised gains which means that a person who ultimately is responsible for paying the tax may not be in a financial position to do so which could result in economic hardship being endured by persons who are required to settle capital gains tax costs before an asset can be transferred to them.²³⁹

²³⁷ Roeleveld op cit (n226) 153.

²³⁸ P Fernandez 'Company Valuation Methods. The Most Common Errors in Valuations', 2004, available at <http://www.iese.edu/research/pdfs/DI-0449-E.pdf>, accessed on 26 November 2014 at 1.

²³⁹ Dubay op cit (n96).

Also, the tax can be avoided through the creation of trusts. An important feature of a trust is that it is everlasting. This means that if a deceased acquired all of his or her property in trust, after he or she dies there is no deemed disposal or transfer of those assets as he or she was never the owner of the property in the first place. According to Van Gijzen, these tax-free transfers 'could continue indefinitely and the fiscus would never earn any revenue from transfer taxes or the capital gains tax'.²⁴⁰

Lastly, according to Dubay, capital gains tax could result in a shortage of investment and savings as the tax encourages people to rather spend their money today and avoid being taxed on it at a later stage.²⁴¹

14.3 Replacing Estate Duty with an Inheritance Tax

There has been another suggestion that the current system of estate duty in place should be scraped and that a totally new system based on inheritance tax should be levied on the beneficiaries inheriting assets from a deceased estate, instead of the estate itself.

Maartens-Dorey provides reasons as to why a system which taxes the recipient of an inheritance would have certain benefits. These include the suggestion that double taxation would no longer be a problem as capital gains tax would be paid by the estate and inheritance tax by the beneficiary. The beneficiary would most likely be in a position to pay the tax as he or she would have inherited an unearned benefit. Inheritance taxes are seen in a more favourable light as being a form of transfer tax as opposed to a death tax and could be seen as an incentive to distribute inheritances to more beneficiaries.²⁴²

²⁴⁰ F Van Gijzen 'Is Breaking a Trust for Tax Gains a Good Idea', 22 February 2013, available at <http://www.gaaaccounting.com/is-breaking-a-trust-for-tax-gains-a-good-idea/>, accessed on 26 November 2014.

²⁴¹ Dubay op cit (n96).

²⁴² R Maartens-Dorey *The Survival of Estate Duty as a Wealth Transfer Tax in South Africa* MCom (Pretoria) (2011) 54.

Ger, on the other hand, states that while inheritance taxes are common in other jurisdictions, such as the Netherlands, he argues however, that this tax would result in South Africa needing to create a brand new piece of legislation.²⁴³ In addition, the legislation which would need to be drafted and passed ultimately delaying the resolution of the current problems.

14.4 Conclusion

This chapter has looked at possible options that are currently being assessed by the legislature which is looking to possibly amend the current tax system imposed on death in South Africa. Judging from Table 4 above, although estate duty does not contribute as much as the other taxes on property to the annual fiscus, it is nonetheless an important contribution, however small it may seem, especially in light of the South African government's goals of addressing wealth redistribution, alleviating poverty and inequality.²⁴⁴

Should the legislature elect to abolish estate duty, it would need replace this income in one way or another, without replacing this loss in revenue with a tax that in any event results in the middle or lower income classes being taxed on a higher scale.

Also, with South Africa's fast growing population and high unemployment rate, it is evident that a greater emphasis should be placed on the current revenue collected from estate duty before repealing or amending such a tax permanently. It would not be possible for the required replacement tax to be apportioned to all South Africans equally through increasing income tax for example, as the level of wealth inequality in South Africa is too great and would negatively affect the poorer sections of society.

Bearing these important goals in mind, it may not be ideal to place so much weight on death taxes being the answer to correcting the problems of

²⁴³ Ger op cit (n91) 60.

²⁴⁴ Department of National Treasury 'The Role of the National Treasury' available at <http://www.treasury.gov.za/nt/info.aspx>, accessed on 26 November 2014.

redistribution, inequality and social policy. According to Prasad, over the last decade the redistributive impact of taxes and social transfers has generally not been able to address growing income inequality found in many countries and have instead become a more important source of government revenue.²⁴⁵

Were the government to choose an alternative method of taxing wealth on death, it is submitted that relying solely on capital gains tax would be the best option available due to the international recognition that this tax has on a global scale, and the fact that it is a more modern form of tax legislation and is already incorporated into South Africa's Income Tax Act. There are however, as already mentioned, problems which would be encountered in choosing this alternative. Nevertheless, whichever course of action the Legislature decides upon, it will involve a weighing up and balancing of its goals with the resources it currently has at its disposal and whether they would be able to be realistically achieved.

Taking all of this into account, it is submitted that the problems currently being experienced by South Africa do not economically justify any tax being repealed at this time. Abolishing either estate duty or capital gains tax, or implementing an inheritance tax, would necessitate major changes to current legislation, including not only to the Income Tax Act and Estate Duty Act, but as well as to donations tax.

Furthermore, and often overlooked, the legislature have already made certain concessions as a result of the criticisms levied against the death taxes imposed. For example, current legislation includes, but is not limited to:

1. Any capital gains tax liability is an allowable deduction in the hands of an estate;
2. There is an annual exclusion on death of R300 000 for capital gains tax purposes;
3. There is a R3.5 million primary rebate for estate duty purposes;

²⁴⁵ N Prasad 'Policies for Redistribution: The Use of Taxes and Social Transfers' available at http://www.ilo.org/wcmsp5/groups/public/---dgreports/---inst/documents/publication/wcms_193159.pdf, accessed on 27 November 2014.

4. There is up to R7 million roll over relief granted to surviving spouses for estate duty purposes;
5. An annual exemption for donations tax in the amount of R100 000 for assets donated during a deceased's lifetime, which used efficiently could minimise the amount of tax payable by a deceased estate; and
6. Certain exemptions, deductible expenses and excluded property under the Estate Duty Act reducing the amount of estate duty payable.

Moreover, before any changes are made to the current tax regime, it needs to be assessed whether the South African Revenue Service and the Master of the High Court would have the necessary resources, time and capacity to train staff, educate taxpayers and update their current systems in order to successfully implement these changes and efficiently process deceased estates.

CHAPTER 15 : CONCLUSION

The main purpose of this dissertation has been to determine whether estate duty should be retained or abolished in South Africa and whether other alternatives should instead be relied upon.

It is submitted that the aim of the research was met as in coming to a decision, various elements relating to taxation were examined and considered. In Chapter 1, a global history of taxation was provided as well as an outline of the various kinds of death taxes that are implemented around the world.

Chapter 2 examined the general objectives of taxation, which included the need to generate revenue, redistribute resources and contribute to economic growth. Chapters 3 and 4 documented the death taxes currently imposed in South Africa, being estate duty and capital gains tax. Of significance were the problems highlighted in Chapter 5 in imposing both estate duty and capital gains tax on death in South Africa, with a main emphasis being placed on the issue of double taxation that sometimes arises. Another problem that was discussed was that of estate duty and capital gains tax avoidance – as many wealthy individuals who have access to lawyers and accountants are able to implement estate planning techniques in order to minimise or avoid having to pay these taxes. The South African Revenue Service has also raised another problem being that estate duty does not collect a substantial amount of revenue and is burdensome to administer.

Chapter 6 examined the arguments put forward by both opponents and proponents of levying death taxes, problems which have been experienced by countries the world over. Selected countries' taxation systems were then documented from Chapters 7 to 13 and it was revealed that there is not one universal system that is followed in levying death taxes. Some countries choose not to levy capital gains tax on death and impose only estate duty or a variation thereof, such as the United Kingdom, the United States, Australia, India and Botswana. Others, like Canada, choose not to levy any estate duty whatsoever and rely solely on capital gains tax upon death. Then, as is the

case in the Netherlands, some countries have decided to only implement inheritance tax, which is a tax levied on the beneficiary of the inheritance, instead of estate duty.

Chapter 14 discussed three viable options available to the South African Revenue Service as replacements to the current system of taxation upon death which are currently implemented in the countries discussed above. The first option was the retention of estate duty and 'forgiving' capital gains tax on death. The second option was to abolish estate duty and rely solely only on capital gains tax upon death. The third option was to abolish estate duty in favour of an inheritance based tax.

It was submitted that the best alternative of the three mentioned would be to rely on capital gains tax and abolish estate duty, given that capital gains tax is a globally recognised tax and already well established and incorporated in the Income Tax Act, bearing in mind its downfalls. Ultimately however, it was decided that while the levying of estate duty and capital gains tax upon death does result in double taxation and other problems, these taxes should not be abolished or amended at this point in time. The possible alternative options discussed were found to be impractical and unlikely to be implemented due to the fact that it will be cumbersome for either new legislation to be drawn up or current legislation to be amended. Furthermore, it remains unclear as to whether particular governmental departments such as the South African Revenue Service and/or the Master of the High Court would be in a position to educate its staff and taxpayers as to the necessary changes and successfully implement a new system of taxation upon death. The possible negative impact these changes could have on the current system in place potentially outweigh any benefit they could seek to achieve.

It remains uncertain what the Davis Tax Committee will propose in its review of the tax system and estate duty's role and continued relevance, however, these issues should not be overlooked, nor should the concessions already provided by the legislature.

BIBLIOGRAPHY

Primary Sources

Statutes

South Africa

1. The Estate Duty Act 45 of 1955.
2. The First Schedule to the Estate Duty Act 45 of 1955.
3. The Income Tax Act 58 of 1962, as amended.
4. The Eighth Schedule to the Income Tax Act 58 of 1962.
5. The Matrimonial Property Act 88 of 1984.
6. The Taxation Laws Amendment Act 24 of 2011.
7. The Employment Tax Incentive Act 26 of 2013.

The United Kingdom

1. The Finance Act of 1965.
2. The Inheritance Tax Act of 1984.
3. The Taxation of Chargeable Gains Act of 1992.
4. The Finance Act of 2014.

The United States

1. The Economic Recovery Tax Act of 1981.
2. The Economic Growth and Tax Relief Reconciliation Act of 2001.
3. The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010.
4. The American Taxpayer Relief Act of 2012.

Canada

1. The Estate Tax Act of 1958.

2. The Income Tax Act of 1972.

Australia

1. The Australian Income Tax Assessment Act of 1997.

India

1. The Finance Act of 1953.
2. The Wealth Tax Act of 1957.
3. The Finance Bill of 2012.

Botswana

1. The Botswana Income Tax Act of 2002.

Netherlands

1. The Inheritance Tax Act of 1956.

Secondary Sources

Books

1. DM Davis, C Beneke and RD Jooste *Estate Planning Issue 38* (1998) LexisNexis, South Africa.
2. D Meyerowitz *The Law and Practice of Administration of Estates and Estate Duty* 7ed (2007) The Taxpayer CC, Cape Town.
3. B Victor & K Ronald *Estate Planning & Fiduciary Services Guide 2013* (2013) LexisNexis, South Africa.

Journals

1. B Ger 'Time for Estate Duty to Go?'(2012) May *De Rebus* 59-60.
2. JJ Roeleveld *An Argument for Either Excluding Death as a Capital Gains Tax Event or Abolishing Estate Duty* SA Journal of Accounting Research Vol. 26 : No. 1 : 2012 pp 143 – 164 available at <http://www.sajar.co.za/documents/SAJAR-26-7-Roeleveld-final.pdf>, accessed on 26 November 2014.

Articles

1. A Ebeling 'IRS Announces 2015 Estate and Gift Tax Limits', 30 October 2014, available at <http://www.forbes.com/sites/ashleaebeling/2014/10/30/irs-announces-2015-estate-and-gift-tax-limits/>, accessed on 24 November 2014.
2. B Roach 'Taxes in the United States' (2010) available at http://www.ase.tufts.edu/gdae/education_materials/modules/Taxes_in_the_United_States.pdf, accessed on 10 December 2014.
3. C Dubay 'The Economic Case Against the Death Tax', 20 July 2010, available at <http://www.heritage.org/research/reports/2010/07/the-economic-case-against-the-death-tax>, accessed on 24 November 2014.
4. Centre on Budget and Policy Priorities 'Chart Book: 10 Things You Need to Know about the Capital Gains Tax', 20 September 2012, available at <http://www.cbpp.org/cms/index.cfm?fa=view&id=3798>, accessed on 25 November 2014.
5. CFE 'Inheritance Tax in the Netherlands' available at <http://www.cfe-eutax.org/taxation/inheritance-tax/netherlands>, accessed on 25 November 2014.

6. D Block and S Drenkard 'The Estate Tax: Even Worse Than Republicans Say', 4 September 2012, available at <http://taxfoundation.org/article/estate-tax-even-worse-republicans-say>, accessed on 24 November 2014.
7. Department of National Treasury '2014 Budget Speech' available at <http://www.treasury.gov.za/documents/national%20budget/2014/speech/speech.pdf>, accessed on 26 November 2014.
8. Department of National Treasury '2014 Tax Statistics' available at <http://www.treasury.gov.za/publications/tax%20statistics/2014/TStats%202014%20WEB.pdf>, accessed on 26 November 2014.
9. Department of National Treasury 'The Role of the National Treasury' available at <http://www.treasury.gov.za/nt/info.aspx>, accessed on 26 November 2014.
10. D Duff 'The Abolition of Wealth Transfer Taxes: Lessons from Canada, Australia, and New Zealand' (2005) 3 *Pittsburgh Tax Review* 72 available at <http://law.bepress.com/cgi/viewcontent.cgi?article=3046&context=expresso>, accessed on 25 November 2014.
11. DNA India 'How to Compute Capital Gains on your Inherited Property' 21 September 2011, available at <http://www.dnaindia.com/analysis/column-how-to-compute-capital-gains-on-your-inherited-property-1589601>, accessed on 24 November 2014.
12. D Roos 'How Capital Gains Tax Works' available at <http://money.howstuffworks.com/personal-finance/personal-income-taxes/capital-gains-tax.htm>, accessed on 25 November 2014.

13. E McCaffery 'Grave Robbers: The Moral Case against the Death Tax', 4 October 1999, available at <http://www.cato.org/sites/cato.org/files/pubs/pdf/pa353.pdf>, accessed on 24 November 2014.
14. Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1mages/taxguides/IEIT-2013/IEIT-US.xml>, accessed on 24 November 2014. (US)
15. Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1mages/taxguides/IEIT-2013/IEIT-GB.xml>, accessed on 24 November 2014. (GB)
16. Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1mages/taxguides/IEIT-2013/IEIT-CA.xml>, accessed on 12 December 2014. (Canada)
17. Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide---XMLQS?preview&XmlUrl=/ec1mages/taxguides/IEIT-2013/IEIT-AU.xml>, accessed on 24 November 2014. (Australia)
18. Ernst & Young '2013 International Estate and Inheritance Tax Guide' available at <http://www.ey.com/GL/en/Services/Tax/International-Estate-and-Inheritance-Tax-Guide--->

XMLQS?preview&XmlUrl=/ec1images/taxguides/IEIT-2013/IEIT-IN.xml, accessed on 24 November 2014. (India)

19. F Van Gijzen 'Is Breaking a Trust for Tax Gains a Good Idea', 22 February 2013, available at <http://www.gaaaccounting.com/is-breaking-a-trust-for-tax-gains-a-good-idea/>, accessed on 26 November 2014.
20. Global Property Guide 'Inheritance Tax and Law' 12 May 2014 available at <http://www.globalpropertyguide.com/Europe/Netherlands/Inheritance>, accessed on 25 November 2014.
21. G Ruffenach 'Coming Soon: More Estate Tax Battles', 29 April 2013, available at <http://blogs.marketwatch.com/encore/2013/04/29/coming-soon-more-estate-tax-battles/>, accessed on 25 November 2014.
22. H Kotak & J Shah 'Union Budget 2013 : Inheritance Tax May Make a Comeback', 28 February 2013, available at <http://firstbiz.firstpost.com/economy/union-budget-2013-inheritance-tax-may-make-a-comeback-36881.html>, accessed on 12 December 2014.
23. HM Revenue & Customs 'Inheritance Tax – the Basics' available at <http://www.hmrc.gov.uk/inheritancetax/intro/basics.htm>, accessed on 24 November 2012.
24. Independent Green Voice 'Abolish the Death Tax' available at <http://www.sovereignty.org.uk/features/articles/manifesto07/iht.html>, accessed on 24 November 2014.
25. J Jacobs 'Is the Capital Gains System about to Replace Estate Duties?', 24 February 2012, available at <http://www.moneyweb.co.za/moneyweb-tax/estate-planning-and-deceased-estates>, accessed on 3 December 2014.

26. J Garber 'Overview of 2014 Estate Tax, Gift Tax & Generation Skipping Transfer Tax Laws' available at <http://wills.about.com/od/2014-Estate-Tax-Rules/fl/Overview-of-2014-Estate-Tax-Gift-Tax-amp-Generation-Skipping-Transfer-Tax-Laws.htm>, accessed on 25 November 2014.
27. JS Gans & A Leigh 'Did the Death of Australian Inheritance Taxes Affect Deaths' Topic in Economic Analysis & Policy, 6(1): 1-7 available at http://andrewleigh.org//pdf/DeathAndTaxes_BEP.pdf, accessed on 25 November 2014.
28. K Dalal 'Estate Duty: Sword of Damocles over India', 6 February 2013, available at http://articles.economictimes.indiatimes.com/2013-02-06/news/36949807_1_estate-duty-wealth-tax-financial-assets, accessed on 21 November 2014.
29. KPMG 'Botswana: Other Taxes and Levies', 5 January 2013, available at <http://www.kpmg.com/global/en/issuesandinsights/articlespublications/taxation-international-executives/botswana/pages/other-taxes-levies.aspx>, accessed on 25 November 2014.
30. L Emanuel, S Drenkard and R Borean 'State Estate and Inheritance Taxes in 2014', 28 May 2014, available at <http://taxfoundation.org/blog/state-estate-and-inheritance-taxes-2014>, accessed on 25 November 2014.
31. M Graetz 'It's Fair, and We Need the Revenue', 20 September 2010, available at <http://online.wsj.com/articles/SB10001424052748704358904575477593075638722> , accessed on 24 November 2014.
32. National Treasury (Republic of South Africa) 'Tax Statistics', 21 October 2013, available at

<http://www.treasury.gov.za/publications/tax%20statistics/2013/TStats%202013%20WEB.pdf>, accessed on 20 November 2014.

33. N Prasad 'Policies for Redistribution: The Use of Taxes and Social Transfers' available at http://www.ilo.org/wcmsp5/groups/public/---dgreports/---inst/documents/publication/wcms_193159.pdf, accessed on 27 November 2014.
34. P Fernandez 'Company Valuation Methods. The Most Common Errors in Valuations', 2004, available at <http://www.iese.edu/research/pdfs/DI-0449-E.pdf>, accessed on 26 November 2014.
35. Property Pulse "What is Mutation of Property and why is it Important?" 3 December 2013, available at <http://content.magicbricks.com/legal-taxation/what-is-mutation-of-property-and-why-is-it-important/60616.html>, accessed on 24 November 2014.
36. S Monani and G Zaoba 'It's a Bad Time to Bring Back Estate Duty', 19 February 2013, available at <http://www.dnaindia.com/mumbai/report-its-a-bad-time-to-bring-back-estate-duty-1801388>, accessed on 21 November 2014.
37. The National Archives 'Finance Act 2014' available at <http://www.legislation.gov.uk/ukpga/2014/26/contents/enacted>, accessed on 9 December 2014.
38. VP Singh and P Chidambaram 'Inheritance Tax: Should India Introduce It?', 12 July 2011, available at http://articles.economictimes.indiatimes.com/2011-07-12/news/29765538_1_tax-gdp-ratio-inheritance-tax-wealth-tax, accessed on 24 November 2014.

39. W Finestone 'United States: 2014 Estate and Tax Planning', 13 February 2014, available at <http://www.mondaq.com/unitedstates/x/292812/Capital+Gains+Tax/2014+Estate+And+Tax+Planning>, accessed on 24 November 2014.

Theses

1. C Bornman *Estate Planning: The Impact of Estate Duty and Capital Gains Tax on Offshore Assets* MCom (North West) (2010).
2. E Muller *A Framework for Wealth Transfer Taxation in South Africa* PhD (Pretoria) (2010).
3. J Van Jaarsveld *The Levying of Capital Gains Tax at Death* LLM (Johannesburg) (2013).
4. L M Ostler *The Impact of Estate Planning on the Effectiveness of Estate Duty as a Wealth Tax in South Africa* MCom (Grahamstown) (2012).
5. R Maartens-Dorey *The Survival of Estate Duty as a Wealth Transfer Tax in South Africa* MCom (Pretoria) (2011).

Newspapers

1. W Hutton 'The Case for Keeping Inheritance Tax' *The Observer* 7 October 2007 available at <http://www.theguardian.com/commentisfree/2007/oct/07/comment.inheritance-tax>, accessed on 24 November 2014.