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Calculating the real cost of the corporate income tax rate reduction

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On 24 February 2021, the then Minister of Finance, Tito Mboweni, announced that the corporate income tax rate would be reduced to 27%. While it was said that the reduction was intended to help businesses grow, it was also announced that the decrease would coincide with the broadening of the tax base by limiting interest deductions and assessed tax losses.

Image source: Le Moal Olivier – 123RF.com

The trade-off seemed like a fair deal. But the real cost of this 1% reduction requires further analysis.

South Africa's economy remains stagnant, inflation is up and business confidence is down. Apart from the prevailing global economic conditions caused by the Covid-19 pandemic and Russia's war on Ukraine, South African businesses have been subjected to local disruptions. These include the July 2021 civil unrest, the floods in Durban, which affected South African businesses nationally, and Eskom's ongoing inability to meet the nation's electricity needs.

As lower revenue often culminates in higher debt levels, many companies are shackled by debt and fragile balance sheet positions. According to a World Bank Research Paper, issued in November 2021, government and private debt levels rose to record levels in emerging markets and developing economies.

Against this backdrop, it appears that the National Treasury's amendments to the assessed loss provisions are another blow for corporate taxpayers. Ultimately, a corporate taxpayer with an accumulated tax loss balance carried forward from previous tax years will not be able to use the entire assessed loss balance. The usable loss will be limited to a maximum of either R1m or 80% of taxable income for that tax year.

The roll forward of assessed tax losses benefited many businesses as it was a means of preserving cash. This allowed companies to repay accumulated debt or to spend on necessary capital outlay when they returned to profitability. But, under the new rules, there will be less available cash for these purposes as income tax will be imposed on a portion of taxable income.

National Treasury is also tightening the rules around the deductibility of interest paid to certain lenders.

While the government recognises that the reduction of the corporate income tax rate is timely, the accompanying tightened rules may be detrimental to the recovery of many companies that suffered financial setbacks in the last few years.

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