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Discovery Life

## Medical Scheme Tax Issues

# Intro

- ④ NT accepts some form of tax subsidy for the moment [as an exception to the general principle that no tax benefits for private expenses].
- ④ The previous system of tax deductions benefitted the rich more than the poor. The current system is therefore a tax credit system, which assists lower earners more and is more equitable
- ④ Be aware that there is a lot of pressure to remove the tax credits altogether, as it is an expensive concession. Just the fact that it was not increased for inflation in this year's budget saved R1bn!
- ④ NB-if the tax credit system is dropped, up to 1.9m could leave medical aids...

# The New Tax Credit System-The current Law

## “Medical scheme fees tax credit

- ④ 6A. (1) In determining the normal tax payable by any natural person, there must be deducted an amount, to be known as the medical scheme fees tax credit, equal to the sum of the amounts allowed to that natural person by way of rebates under subsection (2), subject to subsection (3A)
  - ④ (2) (a) The medical scheme fees tax credit applies in respect of fees paid by the person to—
    - (i) a medical scheme registered under the Medical Schemes Act; or
    - .....
- that relate to benefits from that fund in respect of that person or of any person that is a dependent of that person

## Cont.

- ⊕ (b) **The amount of the medical scheme fees tax credit must be—**
  - (i) **R310**, in respect of benefits to the person, or if the person is not a member of a medical scheme or fund in respect of benefits to a dependent who is a member of a medical scheme or fund or a dependent of a member of a medical scheme or fund;
  - (ii) **R620**, in respect of benefits to the person and one dependent; or
  - (iii) **620**, in respect of benefits to two dependents and  
  
**R209** in respect of benefits to each additional dependent,  
  
for each month in that year of assessment in respect of which those fees are paid.

# Cont

- ④ (3) For the purposes of this section, any amount contemplated in subsection (2) that has been paid by—
  - (a) the estate of a deceased person is deemed to have been paid by the person on the day before his or her death; or
  - (b) an employer of the person is, to the extent that the amount has been included in the income of that person as a taxable benefit in terms of the Seventh Schedule, deemed to have been paid by that person.**

**NB-if employer pays a subsidy, in whole or in part, or simply gives the employee a salary, no real difference-all deductible to employer, taxable as a fringe benefit in employee's hands, and employee then claims the tax credit..**

## Cont.

- ④ (3A) Where more than one person pays any fees in respect of benefits to a person or dependent, the amount allowed to be deducted in respect of the medical scheme fees tax credit under subsection (1) must be an amount that bears to the total amount in respect of that person or dependent contemplated in subsection (2) (b) the same ratio as the amount of the fees paid by that person bears to the total amount of the fees payable.

“Subsection (3A) came into operation on 1 March 2018 and applies in respect of years of assessment commencing on or after that date.”

- ④ (4) For the purposes of this section a **‘dependent’ in relation to a person** means a ‘dependent’ as defined in section 6B (1).

# Definitions

“6B. For the purposes of this section—

- ④ ‘**child**’ means a person’s child or child of his or her spouse who was alive during any portion of the year of assessment, and who on the last day of the year of assessment—
  - (a) was unmarried and was not or would not, had he or she lived, have been—
    - (i) over the age of 18 years;
    - (ii) over the age of 21 years and was wholly or partially dependent for maintenance upon the person and has not become liable for the payment of normal tax in respect of such year; or
    - (iii) over the age of 26 years and was wholly or partially dependent for maintenance upon the person and has not become liable for the payment of normal tax in respect of such year and was a full-time student at an educational institution of a public character; or
  - (b) in the case of any other child, was incapacitated by a disability from maintaining himself or herself and was wholly or partially dependent for maintenance upon the person and has not become liable for the payment of normal tax in respect of that year;

# Definitions cont

⊕ **'dependant'** means—

(a) a person's spouse;

(b) a person's child and the child of his or her spouse;

(c) any other member of a person's family in respect of whom he or she is liable for family care and support; or

(d) any other person who is recognised as a dependant of that person in terms of the rules of a medical scheme or fund contemplated in section 6A(2)(a)(i) or (ii),

at the time the fees contemplated in section 6A(2)(a) were paid, the amounts contemplated in paragraph (a) and (b) of the definition of 'qualifying medical expenses' were paid or the expenditure contemplated in paragraph (c) of that definition was incurred and paid;

# Cont

④ “**disability**’ means a moderate to severe limitation of any person’s ability to function or perform daily activities as a result of a physical, sensory, communication, intellectual or mental impairment, if the limitation—

(a) has lasted or has a prognosis of lasting more than a year; and

(b) is diagnosed by a duly registered medical practitioner in accordance with criteria prescribed by the Commissioner;”

# Cont

⊕ **‘qualifying medical expenses’** means—

(a) any amounts (**other than amounts recoverable by a person or his or her spouse**) which were paid by the person during the year of assessment to any duly registered—

(i) medical practitioner, dentist, optometrist, homeopath, naturopath, osteopath, herbalist, physiotherapist, chiropractor or orthopedist for professional services rendered or medicines supplied to the person or any dependant of the person;

(ii) nursing home or hospital or any duly registered or enrolled nurse, midwife or nursing assistant (or to any nursing agency in respect of the services of such a nurse, midwife or nursing assistant) in respect of the illness or confinement of the person or any dependant of the person; or

(iii) pharmacist for medicines supplied on the prescription of any person mentioned in subparagraph (i) for the person or any dependant of the person;

## Cont

(b) any amounts (**other than amounts recoverable by a person or his or her spouse**) which were paid by the person during the year of assessment in respect of expenditure incurred outside the Republic on services rendered or medicines supplied to the person or any dependant of the person, and which are substantially similar to the services and medicines contemplated in paragraph (a); and

(c) any expenditure that is prescribed by the Commissioner (other than expenditure recoverable by a person or his or her spouse) necessarily incurred and paid by the person during the year of assessment **in consequence of any physical impairment or disability suffered by the person or any dependant of the person.**

# The Legislation

(2) In determining the normal tax payable by any natural person there must be deducted an amount, to be known as the additional medical scheme fees tax credit, equal to the sum of the amounts allowed to that natural person by way of rebates under subsection (3).

(3) The amount of the additional medical expenses tax credit must be—  
(a) where the person is entitled to a rebate under section 6(2)(b), [**65 or older**] the aggregate of—

(i) 33,3 per cent of so much of the amount of the fees paid by the person to a medical scheme or fund contemplated in section 6A(2)(a) as exceeds three times the amount of the medical scheme fees tax credit to which that person is entitled under section 6A(2)(b); and

(ii) 33,3 per cent of the amount of qualifying medical expenses paid by the person; “

# Cont

(b) where the person, his or her spouse or his or her child is a person with a disability, the aggregate of—

(i) 33,3 per cent of so much of the amount of the fees paid by the person to a medical scheme or fund contemplated in section 6A(2)(a) as exceeds three times the amount of the medical scheme fees tax credit to which that person is entitled under section 6A(2)(b); and

(ii) 33,3 per cent of the amount of qualifying medical expenses paid by the person; or

# Cont

(c) in any other case, if the aggregate of-

(i) the amount of the fees paid by the person to a medical scheme or fund contemplated in section 6A(2)(a) as exceeds four times the amount of the medical scheme fees tax credit to which that person is entitled under section 6A(2)(b); *and*

(ii) the amount of qualifying medical expenses paid by the person,

**exceeds 7,5 per cent of the person's taxable income** (excluding any retirement fund lump sum benefit, retirement fund lump sum withdrawal benefit and severance benefit), **25 per cent of the excess**.

- ⦿ (2) Para c comes into operation on 1 March 2014 and applies in respect of years of assessment commencing on or after that date.

## Cont.

- ④ (4) For the purposes of this section, any amount contemplated in subsection (3) or the definition of “qualifying medical expenses” that has been paid by-
  - (a) the estate of a deceased person is deemed to have been paid by the person on the day before his or her death; or
  - (b) an employer of the person is, to the extent that the amount has been included in the income of that person as a taxable benefit in terms of the Seventh Schedule, deemed to have been paid by that person**

# The Law-employer deductions

- ⊕ Section 11 I of the Act allows a deduction for: “any amount contributed by a person that is an employer during the year of assessment for the benefit of or on behalf of any employee or former employee of the employer... to any pension fund, provident fund or retirement annuity fund in terms of the rules of that fund...”
- ⊕ NB-Section no longer mentions contributions to a medical scheme. These are **therefore now deductible under section 11(a)**-the general deduction formula-”expenditure and losses actually incurred in the production of the income, provided such expenditure and losses are not of a capital nature”.
- ⊕ No limit here, but amounts must be reasonable, just like the test for all deductions
- ⊕ Note that the new tax credit system does NOT apply to the employer’s contribution-the employer still gets a full deduction for contributions as before

# Changes that came into effect from 1 March 2014

- ④ **“It is proposed that the remaining aspects of the deduction system for medical expenses be replaced with the tax credit system** in respect of all medical scheme contributions and qualifying medical expenses for all taxpayers. Under this system, a set level of credits will be allowed for medical aid contributions (with annual upward adjustments), with certain excess contributions and out-of-pocket expenses also eligible for tax credits (instead of deductions). “
- ④ **“All credits will remain non-refundable.** Like the current system for deductions, application of the tax credit system will fall into three categories: (i) taxpayers of age 65 and above, (ii) taxpayers with a disability factor under age 65 and (iii) all remaining taxpayers. “

## Cont- Taxpayers of 65 years of age and above

“It is proposed that taxpayers of 65 years of age [**on the last day of the year of assessment**] and above will become entitled to medical expenses tax credits in lieu of the current deduction system for all medical-related items. Other than the standard monthly medical scheme credits, **the credits will generally be set at a 33.3 per cent level**. More specifically, the medical credits will be calculated as follows:

- ④ The standard monthly medical scheme credits for the taxpayer, spouse and dependents;
- ④ 33.3 per cent credits for medical scheme fees that exceed three times the standard medical scheme credits; and
- ④ 33.3 per cent credits for all qualifying medical expenses (other than medical scheme contributions). “

# Cont

## ***Example:***

- ④ Jack is 65 years old. For the year of assessment commencing on 1 March 2014, he made contributions to a medical scheme of R2 000 per month on behalf of himself and his wife. By 28 February 2015, he had incurred R20 000 in qualifying medical expenses

# Calculation-Jack's tax liability for the 2014/2015 tax year would be reduced by R14 657 [NB-old figures!]

Type of deduction	Expense	Calculation	Value of credit
Standard monthly medical scheme credits	R2 000 p.m. x 12 = R24 000 p.a.	(R230 + R230) [now R310+R310] = R460 p.m. R460 x 12	R5 520 p.a.
Excess medical scheme fees		(R24 000 - (3 x R5 520)) = R7 440 R7 440 x 33.3%	R2 478 p.a.
All qualifying medical expenses	R20 000	R20 000 x 33.3%	R6 660 p.a.
<b>Total</b>	<b>R44 000</b>		<b>R14 657 p.a.</b>

# Taxpayers below 65 years of age (with a disability)

Like current law, a separate calculation exists for taxpayers below 65 years of age if **the taxpayer, his/her spouse and/or child is a person with a disability**. Other than the standard monthly medical scheme credits, the credits will generally be set at a 33.3 per cent level. More specifically, the medical credits will be calculated as follows:

- ④ The standard monthly medical scheme credits for the taxpayer, spouse and dependents;
- ④ 33.3 per cent credits for medical scheme fees that exceed three times the standard medical scheme credits; and
- ④ 33.3 per cent credits for all qualifying medical expenses (other than medical scheme contributions).

# Example

- ④ Lerato is 31 years old. For the year of assessment commencing on 1 March 2014 she made contributions to a medical scheme of R2 000 per month on behalf of herself and her two children. Her son, Matthew is disabled. By 28 February 2015, she had incurred R20 000 in qualifying medical expenses.

# Calculation-Lerato's tax liability for the 2014/2015 tax year would be reduced by R14 659 [NB-old figures!]

Type of deduction	Expense	Calculation	Value of credit
Standard monthly medical scheme credits	R2 000 p.m. x 12 = R24 000 p.a.	(R230 + R230 + R154) = R614 p.m. [now R310+R310+R209] R614 x 12	R7 368 p.a.
Excess medical scheme fees		(R24 000 - (3 x R7 368)) = R1 896 R1 896 x 33.3%	R631p.a.
All qualifying medical expenses	R20 000	R20 000 x 33.3%	R6 660 p.a.
<b>Total</b>	<b>R44 000</b>		<b>R14 659 p.a.</b>

# Taxpayers below 65 years of age

Like current law, a separate calculation exists for taxpayers below 65 years of age in the residual category (if the taxpayer, spouse or children are not persons with a disability)

- ⊕ These credits will generally be set at a 25 per cent level. More specifically, these medical credits will be calculated as follows:
- ⊕ The standard monthly medical scheme credits for the taxpayer, spouse and dependants; and
- ⊕ 25 per cent credits of the value of the amount by which the aggregate of the medical scheme fees that exceed four times the standard medical scheme credits, and all qualifying medical expenses (other than medical scheme contributions), exceed 7.5 per cent of the taxpayer's taxable income.

# Example

- ❖ Curwin is 30 years old. For the year of assessment commencing on 1 March 2014, he made contributions to a medical scheme of R2 000 per month on behalf of himself, his wife, and his child. By 28 February 2015, he had incurred R20 000 in qualifying medical expenses. Curwin's taxable income for the 2015 year of assessment **is R200 000**. [Very low!]
- ❖ Therefore, Curwin's tax liability for the 2014/2015 tax year would be reduced by R8 618
- ❖ If Curwin's taxable income was R300 000 for the 2015 year of assessment, he would not be able to claim an additional credit, since 7.5% of his taxable income (R22 500) would exceed his qualifying medical expenses.

# Calculation-refer back to previous page [Old figures!]

Type of deduction	Expense	Calculation	Value of credit
Standard monthly medical scheme credits	R2 000 p.m. x 12 = R24 000 p.a.	(R230 + R230 + R154) = R614 p.m. [now R310+R310+R209] R614x 12	R7 368 p.a.
Excess medical scheme fees		(R24 000 - (4 x R7 368)) = -R5 472 No excess carried = R0	R1 250 p.a.
All qualifying medical expenses	R20 000	(R0 + R20 000) = R20 000 (7.5% x R200 000) = R15 000 R20 000 - R15 000 = R5 000 R5 000 x 25%	
<b>Total</b>	<b>R44 000</b>		<b>R8 618 p.a.</b>

# Main differences between “normal” taxpayers and over 65’s or people with a disability

- ⊕ Normal taxpayers have to exceed 4 times the tax credits
- ⊕ They also have to exceed the threshold of 7.5% of taxable income
- ⊕ They then only get a 25% credit
- ⊕ In most cases they will only get their monthly tax credits, nothing more

# Case Study 1-putting this all together

- ❖ X has a son who is classified as having a disability. He also pays for his parents' medical aid [they are not dependants on his scheme, but are supported by him]
- ❖ Normally, because his parents are factual dependants, he could claim the contributions he makes to the medical scheme for them as a tax credit. He would not be able to claim their out of pocket expenses as a tax credit unless he crossed the 7.5% threshold [very unlikely]
- ❖ However, because he has a son who has a disability, that makes all his out of pocket expenses subject to a credit- because they are incurred “by the taxpayer, his or her spouse or child, or any dependant of the taxpayer .” He therefore qualifies for a tax credit of “33,3 per cent of the amount of qualifying medical expenses paid by the person”-i.e.-a tax credit of 33% of all his out of pockets. **Does not need to cross 7.5% threshold.**

## Case Study 2

- ④ Jane is divorced. Her daughter is disabled and on her ex-husband's medical aid as a dependant. He pays the medical aid premiums, she pays the out of pockets.
- ④ Definition of dependant:
- ④ **dependant'** means—
  - (a) a person's spouse;
  - (b) a person's child and the child of his or her spouse;
  - (c) any other member of a person's family in respect of whom he or she is liable for family care and support; and
  - (d) any other person who is recognised as a dependant of that person in terms of the rules of a medical scheme or fund contemplated in section 6A(2)(a)(i) or (ii)...
- ④ Jane qualifies for a tax credit of "33,3 per cent of the amount of qualifying medical expenses paid- **"the person, his or her spouse or his or her child is a person with a disability"**-her own out of pockets qualify as well!

## Case Study 3

- ④ Fred and Jane are married. They have a child who is disabled. The child is in a home. They want the child on a separate medical aid, just to provide cheap hospital cover, as the day-day costs are looked after by the home. Is there any tax risk if they put the child on a separate medical aid?
- ④ No legal problem-child is still a dependant as defined, even if a major, and still defined as a child-"b) **in the case of any other child, was incapacitated by a disability from maintaining himself or herself and was wholly or partially dependent for maintenance upon the person..**" so would still all be subject to a tax credit- 33.3 per cent credits for medical scheme fees that exceed three times the standard medical scheme credits; and 33.3 per cent credits for all qualifying medical expenses (other than medical scheme contributions)
- ④ Problem in practice-have to prove this to SARS. Easier if remained a dependant on their medical aid...

## Some extras from SARS doc on website

- ❖ Taxpayer must be able to prove they actually paid contributions and expenses [unless paid by the employer]. “Taxpayers could be asked to prove that they have paid the amounts on the medical aid certificates.”
- ❖ “In cases where receipts have been made out in the name of a dependent, or contributions or fees in respect of a dependent have been made to a different medical aid to the one to which the taxpayer belongs, SARS will accept a sworn affidavit in which the taxpayer indicates that the contributions, fees or qualifying expenses claimed for the dependent, have actually been paid by the taxpayer (either directly or indirectly).”

## Cont.

- ④ The tax credit is a rebate limited to the tax payable, and therefore cannot create a refund, and any excess is not carried forward
- ④ Tax credit is deducted against employees tax for contributions paid, NOT out of pockets
- ④ If taxpayer not registered for tax, will have to register if have out of pockets not taken into account. Contribution tax credits normally taken into account by employer. [But could be excess contribution credits]. NB-if no tax liability, no refund. So system does not help taxpayers below the threshold.
- ④ Non-prescription medication NOT regarded as a “qualifying medical expense”

## Cont.

- ④ A person who wishes to claim an AMTC for disability expenses must complete a Confirmation of Diagnosis of Disability form (**ITR-DD**). The ITR-DD must not be submitted with the annual income tax return, but must be retained for compliance purposes in the event of a SARS audit. The ITR-DD needs to also be completed and endorsed by a duly registered medical practitioner every five years where the disability is of a more permanent nature. If the disability is **temporary**, the ITR-DD will only be valid for one year, which effectively means that a new ITR-DD must be completed for each year of assessment during which a disability claim is made
- ④ A disability will be regarded as being temporary in nature if that disability is expected to last for **less than** five years.

# Conclusion

- ④ Medical scheme tax is incredibly complex
- ④ Clients need to know what/when they can claim. Particularly important for family members with disability
- ④ Their tax advisors don't always know about family issues, and their medical aid advisor does not always understand tax, so slips through the cracks
- ④ SARS has great doc on their website on what qualifies as a disability