AIDC
Alternative Information & Development Centre

Strengthening Alliances for a Wage-led, Low-Carbon, Sustainable and Equitable Development Path for Southern Africa

SUBMISSION TO PARLIAMENT ON THE FISCAL FRAMEWORK AND REVENUE PROPOSALS

26 February 2024

Hon. MJ Maswanganyi, MP, Chairperson: Standing Committee on Finance (National Assembly) and Hon. YI Carrim, MP, Chairperson: Select Committee on Finance (National Council of Provinces)
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ABBREVIATIONS

AIDC	Alternative Information and Development Centre
CPI	Consumer Price Index
CSG	Child Support Grant
FPL	Food Poverty Line
GDP	Gross Domestic Product
GEPF	Government Employees Pension Fund
GFECRA	Global Forum on Cyber Expertise Recognition and Accreditation
GloBE	Global Anti-Base Erosion
MTBPS	Medium-Term Budget Policy Statement
MTEF	Medium-Term Expenditure Framework
OECD	Organisation for Economic Co-operation and Development
PIT	Personal Income Tax
SARS	South African Revenue Service
SRD	Social Relief of Distress
UN	United Nations

1. Introduction

1.1. The Alternative Information & Development Centre (AIDC) is a grassroots-based non-governmental organisation based in Cape Town, South Africa. AIDC was established in 1996 to contribute to supporting social movements and trade unions to advance campaigns for a just transition to a wage-led, low-carbon development path.

1.2. The AIDC thanks the Select and Standing Committees on Finance for the opportunity to make a submission on the fiscal framework and revenue proposals tabled in the 2024 Budget on 21 February 2024. We want to use this submission as an opportunity to unpack how the fiscal framework and revenue trends will impact South Africa's economic trajectory; present a critique of the rationale underlying the budget cuts in the 2024 Budget; and outline policy alternatives which ought to have been explored in the 2024 budget.

1.3. The structure of the submission will therefore include a commentary and critique on the broader macroeconomic framework; the trends on the estimates of revenue and expenditure; a critique on the underlying rationale for implementing budget cuts; a list of alternatives to debt and austerity; and a summary of recommendations.

2. Macroeconomic Policy

2.1. Budget cuts in real terms will result in the further breakdown of service delivery in the country, the perpetuation of mass unemployment, and the continuation of unparalleled levels of inequality.

2.2. By introducing the idea of a fiscal anchor, the underlying problems of mass unemployment and stark hunger are sidelined in favour of chasing a primary budget surplus.

2.2.1. The use of the Gold and Foreign Exchange Contingency Reserve Account (GFECRA) has shown that it is possible to use alternative mechanisms to address the growing budget deficit while reducing cuts to social spending.

2.3. While we recognise low economic growth as a structural cause of budget cuts, we argue that an extension of these cuts will not address the underlying reasons for economic stagnation.

2.3.1. According to the 2024 Budget Review, economic growth has averaged only 0,8 percent since 2012. Estimated real GDP growth is set at 0,6

percent in 2023, which is lower than the 0,8 percent estimated during the Medium Term Budget Policy Statement (MTBPS). The revised estimate is caused by lower than expected household consumption and fixed investment.

2.3.2. South Africa's economic stagnation can in large be attributed to a lack of domestic demand. A further reduction in public sector spending will not only lead to worsened standards of living, but will also increase the dependence of households on the private sector for basic services, thus crowding out future household consumption as these services come at a substantially higher cost. This is a process that has already begun - many are increasingly reliant on private healthcare, private security, and now even private firefighting services due to the collapse in state capacity.

2.4. There is little evidence to suggest that budget cuts and austerity work. Keynesian, heterodox and feminist economists have criticised austerity practices for failing to achieve either economic growth or deficit and debt reductions, and for causing harm to the most vulnerable people in society (Perrons, 2017: 10). In contrast, evidence shows how austerity has led to increased unemployment, lower incomes and higher levels of inequality (Sibeko, 2019). In 2013, the IMF acknowledged that it had hugely understated the harm that spending cuts bring to a weak economy (Krugman, 2015). While it is true that debt service costs are rising at an unsustainable rate, it is also true that the debt crisis cannot be overcome without overcoming the lack of growth in the economy - growth to which austerity is a key obstacle.

3. Estimates of revenue

3.1. Mechanisms to enhance and maximize the progressivity of the tax system should be further explored to reduce cuts to the social wage and finance progressive economic development that prioritises the needs of working class and unemployed South Africans.

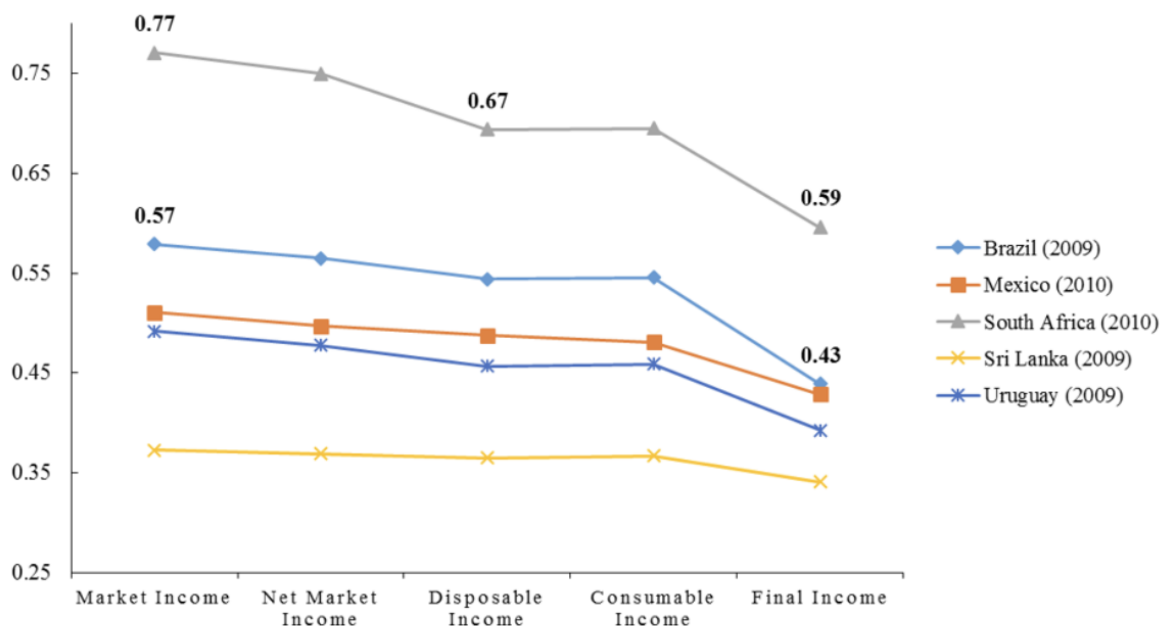
3.2. South Africa's inequality levels are far higher compared to any other country where data is available. Despite relatively high levels of distribution, inequality for final income (after taxes and transfers) significantly outweighs market income inequality compared to the countries depicted in Figure 1 below. This points to three arguments:

3.2.1. First, given the extent of inequality even after taxes and transfers, we should be taking additional steps to maximise the progressivity of the tax system.

3.2.2. Second, given the extent of market income inequality, it is important to promote better outcomes in the initial distribution of wages, salaries and capital income (Woolard et al., 2015).

3.2.3. Third, the decline in the provision of basic services as depicted in the real cuts to expenditure will reverse any reductions or improvements made in reducing the deep levels of inequality.

Figure 1. Gini coefficients by income type (Woolard et al., 2015)



Source: Inchauste *et al*. (2015). Note: The diagram shows the country-specific Gini coefficient for the different income concepts.
Market income = Income from wages, salaries, capital, private transfers and contributory pensions before paying taxes and receiving government transfers.
Net market income = Market income minus personal income tax and payroll taxes (direct taxes)
Disposable income = Net market income plus cash transfers and free basic services
Consumable income = Disposable income minus VAT, excises and the fuel levy (indirect taxes)
Final income = Consumable income plus value of health and education spending.

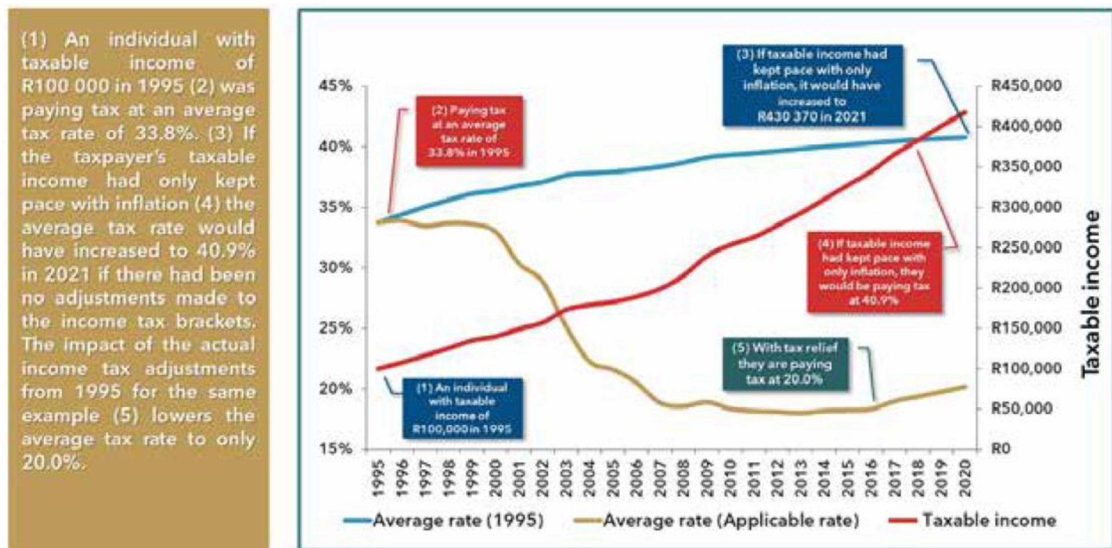
3.3. Personal Income Tax (PIT) collections have outpaced expectations and are expected to grow by 8,2 percent in nominal terms between 2023 and 2024.

3.3.1. PIT is growing faster than both GDP and CPI. Since GDP per capita does not factor in inequality and redistribution, the high growth in PIT could imply a post-COVID recovery for high-income individuals.

3.3.2. The removal of inflation adjustments to tax brackets is necessary and welcome, however, we would like to remind the committees that the R15 billion additional cost to taxpayers is minimal when compared to the R21 billion cut to social spending in real terms.

3.3.3. This is also insufficient in terms of rolling back close to 20 years of above inflationary adjustments to the personal income tax bands. Since 1995 there has been a massive reduction in effective personal income tax rates. Based on Tax Statistics South Africa (2022), an individual with a taxable income of R100 000 in 1995 was paying an average income tax of 33,8%, if taxable income had kept pace with inflation the average tax rate would have increased to 40,9% in 2021 (i.e. if there had been no adjustments made to income tax brackets). The impact of the actual income tax adjustments from 1995, culminated in a lowering of the average tax rate to 20% (SARS Tax Statistics, 2022: 38).

Figure 1. Example if tax relief granted to an individual with a taxable income of R100 000 in 1995



Source: SARS Tax Statistics (2022: 38)

3.3.4. In addition to rolling back approximately 20 years of above inflationary adjustments to personal income tax bands, there is potential to increase the number of high-net-worth individuals who are taxed. Table 1 shows the estimated number of individual taxpayers and taxable income from 2022 to 2024. The number of registered individuals for those earning above R1 000 000 per year has grown by more than 80 000 people between 2023 and 2024.

3.3.5. Table 1 below shows that real growth in tax payable (on average) far outweighs real growth in GDP per capita for most income groups, implying further scope to increase PIT. The uneven distribution of income growth is a symptom of the underlying structural inequalities and should be addressed through various redistributive frameworks. Both the growth in the number of registered taxpayers in the top income brackets and the growth in taxable income are promising signs of post-COVID economic recovery.

Table 1: Estimates of individuals and taxable income, 2022-2024

	Registered individuals			Taxable income (R billion)			Tax payable (R billion)			Real growth in tax payable (2023-2024)
	2022	2023	2024	2022	2023	2024	2022	2023	2024	
R0 - R91[1]	7 700 135	7 545 020	6 832 031	272,9	292,2	286,9				
R91 - R150	1 973 185	1 528 990	1 596 335	227,5	182,0	193,3	14,6	13,8	16,3	13%
R150 - R250	1 717 760	1 505 950	1 514 988	338,6	292,0	299,5	26,8	20,6	21,9	2%
R250 - R350	1 231 672	1 248 123	1 132 341	363,6	370,1	336,5	48,3	46,3	42,9	-12%
R350 - R500	1 158 117	1 233 846	1 315 092	478,2	516,3	548,9	83,6	86,2	92,5	3%
R500 - R750	756 629	842 653	988 658	456,7	506,4	599,6	104,6	110,3	132,2	15%
R750 - R1 000	274 963	354 263	371 316	237,7	305,1	322,3	66,3	82,1	87,6	2%
R1 000 - R1 500	199 837	244 586	292 810	238,1	294,3	351,4	75,3	90,3	109,1	16%
R1 500 +	133 230	163 702	197 866	425,0	493,6	605,1	168,4	190,6	236,2	19%
Total	7 445 393	7 122 113	7 409 406	2 765,3	2 959,9	3 256,7	587,9	640,3	738,7	11%
Grand total	15 145 528	14 667 133	14 241 437	3 038,2	3 252,1	3 543,6				

Source: Budget Review (2022, 2023 & 2024) and authors' calculations

3.4. Heading into the budget, a cause for concern was the R56,1 billion shortfall in tax revenue due to a sharp decline in corporate profitability, especially in the mining sector. This points to an underlying structural problem of the South African economy and its reliance on commodity exports, as a great deal of corporate income tax is tied to international commodity prices. As much as we call for economic transformation, so long as this structure is in place the tax system should be better placed to compensate for this volatility. For example, windfall taxes should have been introduced to capture the record profits of mining companies in 2021/22. Instead, that revenue boom was used to provide personal income tax relief, particularly for middle and high-earners.

3.5. The Treasury has included estimated revenue from its implementation of the OECD's 15% global minimum tax (the so-called 'pillar two'), which amounts to a paltry R8bn in additional tax revenue in 2026/27, compared to the outflows of an estimated R400bn due to illicit financial flows and profit shifting, the majority of which is due to tax evasion and offshoring by large corporations and high net worth individuals.

3.5.1. This is far from the promise made by Tito Mboweni and four other finance ministers in 2021, when they encouraged a hesitant Global South to sign on to a "global minimum tax that effectively puts an end to the race to the bottom and to aggressive tax planning by major international companies". We would like to request that the Treasury share the revenue modelling which was done in order to obtain this figure of R8 billion, and clarify which proportion of this is revenue expected from the implementation of the GloBE rules, as compared to revenue expected from the implementation of the Domestic Minimum Top-up Tax.

3.5.2. The AIDC, along with many other progressive organisations and South-based tax experts, have been advocating for countries to resist signing on to the OECD deal as it is fundamentally biased and gives little benefit to the Global South, which is in desperate need for additional tax revenues; instead we join the call for the coming UN tax convention to supersede the work of the OECD and deliver a more radical solution. We hope that the implementation of the GloBE provisions does not preempt South Africa from taking a leading role in advocating for a strong UN Tax Convention.

3.5.3. The AIDC will develop a more detailed submission on these points ahead of the hearings on the Global Minimum Tax Bill.

3.6. In its 2023 mid-term performance report, SARS noted that it "remains underfunded to give full effect to its mandate". This Budget does not alleviate this challenge: despite some additional funding in the short term, an average annual cut of 2% for the Revenue Service between 2023/24 and 2026/27 can be seen in the Estimates of National Expenditure, with an accompanying freeze in SARS' headcount during the same period. It is difficult to see how this can be justified given the need for additional tax revenue.

3.7. The 2021 Budget Review stated that SARS will focus on consolidating wealth data for taxpayers through third-party information. The feasibility and implementation of a wealth tax are necessary steps in addressing the deep levels of inequality in the country, yet no further steps have been taken for its implementation. The introduction of a wealth tax is also one mechanism to increase the tax-to-GDP ratio that has a self-imposed cap of 25 percent despite it being much higher in countries with strong welfare systems.

3.8. The growing deficit is partially a result of the need for increased spending and borrowing during the COVID-19 period. As expenditure rises to barely keep up with the needs on the ground, the tax-to-GDP has remained relatively flat which resulted in the growing deficit. Both the growing levels of income and wealth

inequality as illustrated above point to the necessity and possibility of raising this threshold.

4. Estimates of expenditure

4.1. Spending will decrease in real terms by R21 billion between the 2023/24 and 2024/25 financial years.

4.2. Once inflation has been adjusted for, these cuts to social spending include a R9,8 billion decrease in learning and culture and an R8 billion reduction in health. This means bigger classroom sizes and longer waiting lines at clinics.

4.3. This budget does not only show any sign of gender-responsive budgeting but in fact makes cuts in areas that disproportionately affect working class women. Sectors such as healthcare and education predominantly employ women, and by freezing posts in these key social sectors, more women become unemployed. Women also have differentiated and in some cases higher needs, such as the need for maternal health care and a disproportionate prevalence of HIV/AIDS.

4.4. While the permanent social grants have been increasing in line with headline inflation, this does not compensate for the drastic rise in food and electricity prices we have seen in past years. For example, while the permanent grants increased by 5% in 2023, food and electricity inflation was 11 and 12 percent, respectively. The Food Poverty Line (FPL), the minimum cost of the daily energy intake needed per person, is now expected to reach R798 in 2024. This means that the SRD and CSG is only able to cover 44 and 66 percent of the basic and minimum nutritional needs of an individual.

4.5. In 2024/25, R34 billion has been allocated to the COVID-19 SRD grant, which is R10 billion less in nominal terms than the amount previously allocated. The 2024/25 funding will only cover 8 million people out of the 16 million people whose income falls below the FPL. The implication of underfunding leads to intended errors of exclusion in the administration of the grant. This is a combination of barriers to accessing the grant; a qualifying threshold that is set too low; and administrative hurdles in administering payments, all of which serve to exclude as many people as possible from actually accessing the necessary social support.

4.6. The Budget Review makes a CPI inflation forecast of 4.7% for 2024/25. According to the 2023 public sector wage agreement, the wage increase must be precisely that in the coming fiscal year. Still, the Treasury has budgeted for a slight real cut in the total wage bill. However, in the crisis-ridden sectors of Public Health and Basic Education, the budget proposes real wage bill cuts of 2,5 and

2,2 percent. The only way to combine such a plan with the signed wage agreement for health and school staff is a further reduction of staff in their workplaces.

4.7. By asking most departments to absorb the wage increases resulting from the 2023 agreement within their baseline, the Budget Review presents the same dichotomy between wages and headcount which was made explicit in the 2023 MTBPS. An agreement on public sector wage increases should not come at the expense of worsening working conditions and service delivery through the freezing or reduction of headcounts. To do this is to undemocratically use the budget as a bargaining tool to discourage future wage negotiations.

4.8. It should also be emphasised that a quality public service requires motivated and skilled workers. In May 2023, the minister of Public Service and Administration noted that one of the chief challenges in filling certain vacancies within the public sector was "competition with the private sector", alongside budget constraints. A blanket wage freeze is as untenable as a blanket hiring freeze. If the Treasury insists on the other hand that a blanket increase also cannot be reconciled with the filling of vacancies, then a compromise must be obtained through negotiations with workers, not through the Budget process.

5. Critique of debt as a rationale for budget cuts

5.1. The rationale underlying the fiscal framework is that South Africa is facing an imminent debt crisis. However, we contend that South Africa is in fact facing a growth crisis coupled with a devastating social crisis - but not a debt crisis.

5.2. We recognise the rapid growth in debt servicing costs as a severe problem, but the framing of a 'debt crisis' implies that the government has lost any remaining fiscal space and is facing a potential default. We argue that this is premature, and fails to take into account the various alternatives that can be employed in order to maintain fiscal space, restore growth, and *avoid a future debt crisis (See AIDC publication Alternatives to Austerity - Dealing with growing levels of public debt in South Africa)*.

5.3. Given the rise in the debt stock during the years of 'state capture', it is essential that these debts are audited on the basis that they may be illegitimate debts. One extreme example is the World Bank's loan to Eskom in 2010, which was mainly for the building of the giant Medupi coal-fired power station, a project haunted by delays, steep cost increases and corruption. Conflicts of interest and other factors were known to both borrower and lender, with the Bank's later president explicitly being critical of the relationship between the Bank and South Africa. Given its contribution to climate change and the poor performance of the plant,

this loan was also clearly taken out against the interests of the population, making it a prime candidate to be investigated as an example of odious debt.

6. Austerity increases the liberalisation of the South African economy

6.1. Further, in relation to Eskom, the debt relief proposed must be assessed along with increased penetration of rooftop solar, businesses building solar PV and higher levels of private embedded. This is being enabled by a range of energy sector reforms, including the amendments to the Electricity Regulations Act and the establishment of an independent transmission grid. The independent transmission grid - the National Transmission Corporation of South Africa (NTCSA) - will be required to purchase power indiscriminately in a competitive energy market. Increased private sector involvement in the South African energy market will have direct and indirect costs. Eskom will continue to pay for electricity from private producers - primarily through expensive power purchase agreements. Moreover, a greater indirect cost is incurred due to reduced sales volumes for Eskom, leading to rising tariffs ultimately culminating in the acceleration of the Eskom death spiral. Government will also provide guarantees to private energy producers - which increases the contingency liabilities of the state.

6.2. The National Treasury mentions how the $3.3 billion dollars is to support climate change, energy and just transition objectives. These loans from multilateral development banks and international finance institutions like the World Bank, entrench policies aimed to privatise the energy and transport sectors. This entails the growth in the use of public-private partnerships (PPPs). The government argues that this will help to crowd-in private sector investment into infrastructure. However, in reality, PPPs are a mechanism to de-risk private sector investment and guarantee profits - placing the burden of risk onto the state.

6.3. Loans in foreign exchange locks in dependence on an export-oriented economic policy and the need for reduced capital and exchange controls - as was announced in both the MTBPS 2023 and the Budget Review (2024), further undermining fiscal, monetary and industrial policy sovereignty.

7. Alternatives to debt and austerity

7.1. The use of the Gold and Foreign Exchange Contingency Reserve Account (GFECRA) is one of the necessary ways the balance sheet can be used to increase the size of the pie and reduce the need for austerity policies. R150 billion is being proposed yet real cuts over the MTEF amount to R81 billion.

7.2. GFECRA has shown that it is possible to think outside the box in confronting the threat of an increasing deficit. Alternative ways of using the government's balance sheet should be strongly considered to both halt and reverse budget cuts.

7.3. Utilising the Government Employee Pension Fund, which has had annual surpluses of approximately R50 billion for the past 10 years, is just one of the steps that can be taken to mitigate austerity. For example, the GEPF could be compelled to purchase bonds at concessional rates so as to reverse the growth of debt servicing costs. This would not endanger pensions nor the solvency of the fund, given the fact that the GEPF is more than fully funded and pays out defined benefits.

7.4. Furthermore, removing and reducing tax rebates for high-income earners could raise the required revenue needed for the prioritisation of service delivery and growth. South Africa's world-beating inequality means that the reduction of tax expenditure on high earners is not only a fiscal imperative but also a moral one.

7.5. The fundamental problem underlying this budget is the lack of meaningful, job-creating and inequality-reducing growth and development in the South African economy. Without a comprehensive public investment strategy, the alternatives above would only be sufficient to stave off austerity for a few years. A progressive government will need to utilise these funding mechanisms, among others, to drive meaningful and inclusive growth and outpace debt interest costs in the long term.

8. Summary of recommendations

8.1. Reject the future proposal of a binding fiscal anchor. There is a risk that the fiscal anchor will enshrine the requirement of a primary budget surplus into law above the need to keep public expenditure at least in line with inflation.

8.2. Ensure that public expenditure grows by at least the level of inflation and population growth.

8.3. Introduce further mechanisms to enhance and maximize the progressivity of the tax system and increase the tax-to-GDP ratio, this should include reviewing a range of tax rebates - which redirects resources back to the most affluent people in society and results in billions in foregone revenue. This also includes the exploration of the establishment of a progressive net wealth tax on the wealthiest 1 percent of the population.

8.4. Windfall taxes should be introduced to capture the future profits of mining companies during commodity booms and look to increase effective corporate income tax rates.

8.5. Treasury should share the revenue modelling which was done in order to obtain the figure of R8 billion from the implementation of the OECD's Pillar Two global tax and clarify which proportion of this is revenue expected from the implementation of the GloBE rules, as compared to revenue expected from the implementation of the Domestic Minimum Top-up Tax.

8.6. Join the call for the coming UN tax convention to supersede the work of the OECD and deliver a more radical solution to corporate tax avoidance and evasion.

8.7. Adopt gender-responsive budgeting to ensure equality of outcomes in the budgeting process.

8.8. Increase the budget for the COVID-SRD grant and ensure that both the SRD grant and the CSG are set at the FPL as a minimum, and towards the establishment of a dignified basic income grant of at least R1500 per month.

8.9. Increase the interim qualifying threshold of the SRD grant to at least the Upper-Bound Poverty Line.

8.10. Ensure sufficient investment in public services, this includes sufficient resources to adequately compensate employees and provision of funding to fill vacancies in education and health..

8.11. Audit debts that accumulated during the 'state capture' years on the basis that they may be illegitimate debts.

8.12. Place a moratorium on borrowing in foreign exchange.

8.13. Strengthen capital and exchange controls to reduce the risk of capital outflows and to help mitigate against illicit financial flows, base erosion and profit shifting.

8.14. Shift the Eskom debt relief from the fiscus to the GEPF - increasing Eskom's total liabilities to the GEPF and freeing up fiscal space for increased social spending.

8.15. Compel the GEPF to purchase bonds at concessional rates so as to reverse the growth of debt servicing costs. This would not endanger pensions nor the solvency of the fund, given the fact that the GEPF is more than fully funded and pays out defined benefits.

8.16. Reverse proposals to increase private sector involvement in the energy sector and the creation of a competitive energy market. Maintain a fully vertically integrated public energy utility and provide adequate resources for the effective operation of the utility. This includes financing for operations, maintenance and investment in new generative capacity.

8.17. Prioritise a comprehensive public investment strategy to utilise funding mechanisms to drive meaningful and inclusive growth and outpace debt interest costs in the long term.

WE ARE REQUESTING TO MAKE AN ORAL SUBMISSION.

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