FEDUSA COMMENTS ON BUDGET 2014

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INTRODUCTION

- The delivering of the budget speech on the 26th of February 2014 came twenty years, since the advent of democ in 1994. South Africa as a Rainbow Nation has made steady progress in the areas of education, health, fighting the scourge against Vid/Aid economic growth widened, employment creation, income distribution, rural development, and housing, access to water, sanitation and electricity. However, not extensively has changed in the townships. The World Bank argues that during the apartheid period, slum clearance, harsh licensing, and strict zoning regulations rid cities of black-dominated informal sector niches.

- Two decades after the end of apartheid, spatial segregation remains, and investment in black-dominated areas is low. The legacy of separation also results in high transportation costs for the unemployed, who tend to live far from where the jobs are. South Africa's job creation problems may stem primarily from urban issues according to the World Bank report.

The focus in the budget speech was on the implementation of the National Development Plan (NDP) framework with the key priorities of public policy aiming:

- To eliminate poverty and reducing poverty,
- Focus on Social protection extension via NHI, UIF and Retirement reform;
- Creating a job creation trajectory,
- Making economic growth more inclusive,
- To create a growth path with a key focus on Infrastructure delivery.

INTRODUCTION (CONT)

- The directed NDP infrastructure roll-out is the main thrust of Budget 2014 as was in 2013 and is the most positive policy direction undertaken by Government since the downturn in the economy in 2007.

- The building of infrastructure is an imperative commitment to implement the National Development Plan to enhance capabilities and to promote active citizenry.

➢In our presentation FEDUSA will comment on the effects of the broader approach to solving our serious socio-economic problems, the fiscal framework and specific expenditure and tax measures announced in the Budget.

- FEDUSA remain concerned that the unemployment rate according Statistics South Africa persist to be high at 24.7 percent in the third quarter of 2013, with youth unemployment which stand at 55 percent.
- Budget figures for the 2014/15 financial year was already fixed in the October 2013 MTBPS. As such not any major surprises were expected, at least not from the expenditure side. All the different programs are in place to attain government's objectives of making inroads into our serious economic and social challenges of low and jobless growth coupled with structural problems and reflected in Budget figures.
- Budget estimates were however fixed in October 2013 based on assumptions regarding economic growth and inflation. Since October 2013 important global economic as well as domestic economic social and political developments taking place effected our growth and inflation and therefore necessitated certain adjustments in the 2014 Bufget figures.

ECONOMIC POLICY ISSUES

- Jobless growth, high unemployment with the resultant unequal income distribution and poverty remains South Africa's most serious socio-economic challenge.Government failed to make real inroads in our unemployment problem, although much was done in other areas. The question may rightfully be asked why the National Development Plan would fare better?

- What is however in favor of the National Development Plan is that an expert commission compiled it and drew on extensive research and wide consultation with different groups. The National Development Plan realize that it is a long-term strategy. The role of government, business and labour is clearly recognized. It further provides practical ways to take the Plan forward.

- Fedusa applaud government that the Plan is already part of the budget and that element of it is included in government's spending and revenue plans. There is a vast potential to increase the alignment between the Plan and the budget priorities.

- The National Development Plan analysed our socio-economic problems in a more systematic and pragmatic way than previous programs. The Commission identifies unemployment, income inequality, poor-quality education, poorly located and insufficient infrastructure, the resource intensity of exports and skewed spatial patterns as the main challenges facing the economy.

- FEDUSA also noted with satisfaction that consultation on the Budget took place within NEDLAC involving all the social partners and taking into consideration key policy interventions proposed by the social partners.

ECONOMIC GROWTH PROJECTIONS

- The IMF's forecasts that the South African economy would grow by a projected 2.8 percent in 2014 and 3.2 percent in 2015. The net effect of global and domestic developments is therefore somewhat slower growth and increased inflation for South Africa. The Reserve Bank downscaled its growth projections in line with that of the IMF for South Africa in 2014 and 2015 to 2,8 percent and 3,3 percent respectively, down from 3,0 percent and 3,4 percent in the previous forecast round.

- The estimates of Government are therefore more or less in line with this. The actual outcome will however be affected by both domestic and global developments such as the pace of tapering in the USA of its provision of providing liquidity to markets.

- From a fiscal policy perspective the higher than expected revenue coupled with a re-allocation of expenditure and the usage of unspent funds gave Government some policy options, such as a somewhat smaller deficit of 4 percent against 4.2 percent and some tax relief for especially the lower income group and the re-allocation of its Budget to bring it in line with the National Development Plan (NDP) and to address urgent social and political needs.
- Governments in power worldwide, rightfully or wrongly, are usually accused of using the Budget for political gain specifically when it is electioneering time.
- This could take place by deliberately re-allocating funds to gain votes or merely by concentrating on aspects that could boost their image. In the light of the above, it is understandable that abundant election "campaigns" were included in this year's Budget to illuminate Government's achievements as was also done in the State of Nation 2014

ALIGNMENT WITH THE NDP

- As expected the NDP received considerable attention in this year's Budget. Elements of the NDP that was launched in August 2012, was already included in the 2013 fiscal framework and even in the 2013 MTBPS it was more aligned with the NDP.
- At this moment in 2014 the focus is on a range of policy areas, especially infrastructure, education, health care, social protection, building a capable state, and promoting accountability and fighting corruption.
- The NDP campaigns for a new approach to addressing the policy challenges that constructs on extended cooperation between the public and private sectors, labour and civil society. The Budget Review of 2014 utilizes various examples in this regard focusing on infrastructure, partnerships and education as backbones with a specific example the Renewable Energy Programme launched in August 2011. (Budget Review 2014, Chapter1, p 5). FEDUSA believe that the approach is the correct course to create a job trajectory but will not happen instantaneous.
- The Minister announced the introduction of the Employment Tax Incentive Act in 2013, also known as the youth wage subsidy, which came into effect on 2 January 2014. This piece of legislation is a significant step towards decreasing unemployment as it offers employers incentives to hire people between the ages of 18 – 29 years.
- The Act was unlikely to cause immediate stability or even instability in the labour market in the short term. FEDUSA expect that businesses are to start their planning processes with regard to the benefits that they can get in the long term, as it will take some time so it's without a doubt not going to have an immediate effect. Typically, wage subsidies of this nature take up to nine or 12 months before they take effect in the labour market according to economic experts.

- The Budget provides for an expenditure level (including interest payments) of R1 252.3 billion and revenue of R1099.2 billion, leaving the budget deficit at 4 percent, the same level as 2013/14. Government plans to lower the deficit further to 2.8 percent by way of strict expenditure control and larger revenue income as the economy picks up its growth rate.

- A positive development in this year's Budget is the further shift of its expenditure from current to capital expenditure. This will have a favorable effect on future employment opportunities. FEDUSA also commend Government on the priority given to Education and Health. Also on the steps (forensic reviews and investigations) taken to improve the quality of public services and cutting wasteful expenditure by proper controls developed by the Office of the Accountant-General.

- FEDUSA agree that Decent work is about both earned income and the living conditions of working people, as improvements in as well as increased access to services such as healthcare, education and housing can increase both productivity and employability.

- The growing dependency on the state is not a sustainable long-term solution to reducing poverty, inequality or unemployment.

SPECIFIC EXPENDITURE ALLOCATIONS

- FEDUSA welcomes the specific expenditure measures announced, namely the increase in social grants. Old age grants will increase from R1 270 to R1 350 per month from 1 April 2014. Child support grants will be increased from R300 to R310 per month in April 2014 and to R320 in October 2014.

- It is also noted that it was necessary to reprioritise across departments and to draw down on the contingency reserve to make additional allocations to priority areas and for the upward adjustment of the public sector wage bill, while maintaining the expenditure ceiling. FEDUSA would caution that this option would not always be open to Government. FEDUSA is therefore concerned about the sustainability of compensation expenditure. Compensation expenditure is a large component of Government's spending. For the current MTBPS period large increases in compensation expenditure is again envisaged. The Minister also admitted that a further deterioration in the inflation outlook would add to the wage bill and place additional pressure on the budget.

- The medium term expenditure priorities as set by Government allows for an average annual real growth in non-interest spending of 1.9 percent over the 2014/15-2016/17 MTEF period. The investment in line with the NDP strategic objectives (Budget Review Chapter 2014 (p 13-30) are welcomed by FEDUSA.

REVENUE TRENDS AND INCOME TAX RELIEF

- Tax proposals for the 2014 Budget continue to prioritise economic growth, job creation and generating sufficient revenue to finance government spending in line with the National Development Plan (NDP) and the objectives of expanding the economy and reducing unemployment.
- Tax proposals for 2014/15 include personal income tax relief of R9.3 billion; steps to encourage enterprise development and household savings; measures to address acid mine drainage; and design adjustments to the proposed carbon tax.
- The first report of the Tax Review Committee, which examines how the tax system affects small and medium enterprises, will soon be published for public comment and FEDUSA look forward to the recommendations of the report specifically the aspects pertaining to the justifiable balance between direct and indirect taxes and the role of wealth taxes.

TAX RELIEF PROPOSALS 2014

Tax relief measures announced in the 2014 Budget which is regarded as positive are the following:

- Taxpayers will also find some tax relief on medical schemes contributions. Monthly tax credits will be increased from R242 to R257 per month for the first two beneficiaries and from R162 to R172 for each additional beneficiary with effect from 1 March 2014. The medical cost escalation has however been eroding benefits made in this provision;
- As was expected the proposed carbon tax and its alignment with desired emission-reduction outcomes were adjusted which is seen as a blow to dealing with emission reduction;
- The employment tax incentive amounting to an estimated R1 billion, introduced at the beginning of 2014, which will help unemployed youth gain skills and experience in the workplace is welcomed by FEDUSA.
- On the personal tax front, FEDUSA welcomes the personal income tax relief of R9.3 billion which will go largely to the lower income groups. The effect of this tax relief will however partly be neutralised by the increase in the fuel levy where Government will take back R2.6 billion by way of an increase in the fuel levy.

7 FINANCING OF THE NHI

- The ailing public health infrastructure and the move to improve infrastructure raise a concern about the apparent lack of consultation on the NHI process between the Department of Health and relevant stakeholders.
- To strengthen the health system, Government announced that an Office of Health Standards Compliance will be launched in 2014/15 as an independent public entity responsible for inspecting health facilities and improving the quality of health provision. The new office receives funding of R369.5 million over the medium term.
- In its 2012 Article IV report, the IMF pointed out that the approach of the NHI is to pool the risks and the funds so that equity and social solidarity will be achieved through the creation of a single NHI fund. As the Minister also indicated, the NHI will be implemented gradually over 14 years in three stages.
- The first phase (2011-15) will mainly include organisational changes to build capacity and pilot projects to assess the preliminary design. In the second and third phases from 2016-2020 and 2020-2024 the NHI will gradually take over the administration of the health functions.
- According to the IMF the cost is difficult to predict. In 2012 National Treasury estimated the cost of the NHI at 2 percent of GDP, going up to not less than 6.2 percent of GDP in 2025. Financing options include a payroll tax, payable by both employers and employees was considered, higher VAT, a surcharge on taxable income, or a combination were considered.

FINANCING OF THE NHI (CONT)

- The Department of Health's white paper on NHI and a financing paper by the National Treasury have been completed and will be tabled in Cabinet shortly.

- Further NHI pilot districts have been established in every province, supported by funding for NHI as a conditional grant. In addition to hospital and clinic building and refurbishment programmes, R1.2 billion has been allocated for piloting general practitioners' contracts.

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- It can therefore be accepted that the cost will be high. The implementation will therefore require that strict control on expenditure will have to be applied as well as a reprioritising of expenditure between functions to afford such a program.

FINANCING OF THE NHI (CONT)

- The NHI is to be phased in over a 14-year period beginning in 2012/13. The new system will provide equitable health coverage for all South Africans. Plans to begin the first phase of national health insurance, and initial funding requirements, are discussed with detail in Chapter 6 of the Budget Review.
- The budget review lack any detailed information pertaining to the NHI pilot projects. Integration of information would ensure greater participation in a process where the country as a whole is planning, evaluating and monitoring government performance.

FINANCING OF THE NHI (CONT)

- The problem of budget under-spending remains prevalent in a country where we have rural citizens in dire need of essential services. Indeed, we have seen most of the NHI pilot sites underspending their allocated funds. Furthermore, it's not simply about getting officials to spend the money, but having the capacity to spend it wisely. Sound corporate governance in public health care has to enter the fray. We cannot only think of infrastructure development and forget about the skills utilizing it.
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- Hence, our message to government is to get the basics right first before introducing more bureaucracy to a system in which the administrators are already not coping. FEDUSA would like to reiterate the need for the following aspects to be included in the health reform system:
- i) Management training;
- ii) The placement (and retention) of doctors and professionals; and
- iii) Enhanced revenue management.
- Finally, FEDUSA is also calling for vast improvements in infrastructure in rural areas – particularly in the form of roads, bridges and communications – as many of our country's citizen's battle to gain access to health care facilities.

SOCIAL PROTECTION AND RETIREMENT PROVISIONS

FEDUSA acknowledging that retirement fund coverage is poor for low-income workers and employees in small firms. FEDUSA engaged with Treasury at NEDLAC on the 28th of February 2014 to discuss the proposals in considerable more detail.

- It was announced that tax-preferred savings accounts, first mooted in the 2012 Budget Review as a measure to encourage household savings, will now proceed. The lack of personal savings remains a serious problem in South Africa.
- The Social Protection spending plans in line with the NDP focus on the introduction of tax-free savings accounts in 2014 which will create a mechanism to increase household savings and support financial inclusion is applauded by FEDUSA.
- The encouragement to save in tax-preferred savings accounts, tax exemptions for interest, dividends and capital gains will be granted for investment of not more than R30 000 per annum per individual. Investments in bank deposits, collective investments schemes, and exchange traded funds and retail savings bonds will be allowed to be offered in these savings accounts by banks, asset managers, life insurers and brokers.
- FEDUSA also welcomes the adjustment of lump-sum pension payments, which would help individuals to save for their retirement. Pre-retirement withdrawals, mainly because of resignation will be tax-exempted up to R25000, while lump-sum receipts of up to R500 000 at retirement will be tax-exempted.
- The rates for these lump sums are to be adjusted to limit instances where lower income taxpayers are required to pay tax on lump sums even though they did not benefit from a deduction for contributions to the retirement fund because their taxable income was below the tax threshold. The adjustments will have the effect that a lump sum payable on retirement will be tax free if the amount is R500 000 or less.

SOCIAL PROTECTION AND RETIREMENT PROVISIONS (CONT)

- The Finance Minister indicated that Government will seek to improve coverage and preservation of retirement funds and lower costs in the system. They are currently consulting with NEDLAC on measures to cover the six million employed South Africans who do not enjoy access to an employer-sponsored retirement plan. Government indicated that it will move progressively towards a mandatory system for retirement provision for all employed workers.

- The Minister also indicated that a document that briefly describes the retirement reform changes up to this point and sets out anticipated future reforms will soon be released by Government.

- FEDUSA naturally welcomes any policy initiatives that would improve the material well – being and quality of life of workers and would therefore in principal support the retirement fund and the NHI.
- Government however is cautioned that both schemes could have far reaching financial and other implications, both for the public and private sector. At this stage an important goal of Government is to bring down its deficit by keeping its expenditure level at a sustainable level. Any large program such as the NHI would therefore have to be tackled with caution.

- It is noted that in his 2013 MTBPS and 2014 Budget speech the Minister indicated that authorities will proceed cautiously with pension reforms and the implementation of the National Health Insurance to ensure their affordability and consistency with fiscal sustainability.

SOCIAL PROTECTION AND RETIREMENT PROVISIONS (CONT)

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- The formula used to estimate the taxable contribution amount in defined benefit funds was legislated in 112013. The methodology of calculating the formula will be detailed by way of regulation in 2014.

- The policy approach for the timing of accrual of retirement fund benefits will be reviewed to provide certainty and ease practical application. It would appear that what the Finance Minister has in mind is a review of the requirement that taxpayers must annuitize when they retire, even if they embark on a second career and do not need a pension at that time.

- Agreement has been reached with the Association of Savings and Investment of South Africa (ASISA) on a way forward to reduce the level of charges for retirement savings products. Draft regulatory reforms will be published shortly.

RETIREMENT TAX ADJUSTMENTS

- The Finance Minister announced adjustments to the retirement fund tax tables with effect from 1 March 2014. The tax tables were introduced in 2007 and have not been adjusted since, with the exception of the retirement / death tax table which was adjusted by 5% in 2011.
- It is proposed that the lump sum brackets be increased by about 10%. The single biggest adjustment is the increase in the retirement / death tax table of the tax-free amount from R315 000 to R500 000. The tax-free amount in the withdrawal tax table has also been increased from R22 500 to R25 000. The large increase in the bottom bracket of the retirement / death tax table is to avoid instances where low income workers may be required to pay tax on their lump sum, even though they did not benefit from a deduction due to their taxable income falling below the tax-free threshold.
- FEDUSA naturally welcomes any policy initiatives that would improve the material well-being and quality of life of workers and would therefore in principal support the retirement fund and the NHI. Government however is cautioned that both schemes could have far reaching financial and other implications, both for the public and private sector. At this stage an important goal of Government is to bring down its deficit by keeping its expenditure level at a sustainable level. Any large program such as the NHI would therefore have to be tackled with caution.

TAX INCENTIVES TO ENCOURAGE HIRING OF YOUNG WORKERS

- The youth tax incentive is welcomed together with the Special economic zones tax incentives focussing mainly on job creation and social impact businesses.
- FEDUSA want to caution government to design the tax incentive scheme for special economic zones with great care in order to avoid unintended consequences like was the case with Atlantis and Butterworth.

CREATING A SAVINGS CULTURE AS TAX INCENTIVE WELCOMED

- The tax relief afforded to the lower end of the tax-payers, no doubt provides an opportunity to save.
- FEDUSA have been calling for years for household savings to be increased.
- The discussion document published will provide more details on creating a savings culture. It is a reality that with the high debt levels and the low savings levels the nation are consuming today what we have not yet earned tomorrow.
- To encourage greater savings among South Africans, tax-preferred savings and investment accounts are proposed as alternatives to the current tax-free interest-income caps. This will encourage a new generation of savings products.

2014 GOVERNMENT PRIORITIES AND BUDGET VOTES AND THE GENDER LENS

- Following the national outrage and debate around the high number of incidents of violence against woman, many arguments criticizing the very structure of our patriarchal society have been raised.
- Considering that South Africa is a signatory to international human rights conventions such as the Convention on the Elimination of Discrimination Against Women (CEDAW) it would be expected that such outrage and international attention would re-energize the state's commitment to the pursuit of gender equality, and a safer society in which women can work and live.
- FEDUSA must question the gender lens, or absence thereof in the Budget 2014 delivered by the National Treasury.

- Furthermore, again in reference to the recent outrage expressed by not only the general public, but by the President himself and a number of political leaders in South Africa, the lack of commitment to addressing gender based violence recognizable throughout the Budget, and especially in Vote 8: Women, Children and People with Disabilities is deplorable. FEDUSA wishes to categorically state its disappointment with the National Budget to produce tangible and actionable budgets for addressing the gender inequality inherent in our patriarchal society, which is no doubt the primary contributor to the unacceptable rates of rape and sexual violence in this country, and urge all Ministries, especially Health, Women, Children and People with Disabilities, Labour and Social Development to restructure their programmes and budgets to include urgent efforts in this regard, and the financing thereof.

CONCLUSION

- As in the past, the yearly Budget contains a lot of information.
- It is only possible to comment on a few aspects.
- The time scheduled for the public hearings are as always problematic and does not allow for intensive and objective comments.
- FEDUSA hoped that the establishment of the Budget Office will be able to bring change to the budgetary process and input from social partners.
- FEDUSA believes that the most important aspect in 2014 is probably the implementation of the National Planning Commission strategies and the reprioritizing of expenditure towards infrastructure to steer the economy on a sustainable growth and employment creation path.
- We would like to thank the joint committee for the opportunity to present our initial comments on the Budget 2014.
- A well – balanced Budget under challenging global economic as well as domestic economic, social and political circumstances. The current fiscal stance of keeping a secure reign on expenditure and lowering the deficit as economic growth and therefore revenue picks up.