

INTERGENERATIONAL ASPECTS OF INEQUALITY: CHALLENGE FOR A DEVELOPING COUNTRY LIKE SOUTH AFRICA

PARALLEL SESSION X OF THE 4TH ITD GLOBAL CONFERENCE ON 'TAX AND INEQUALITY'

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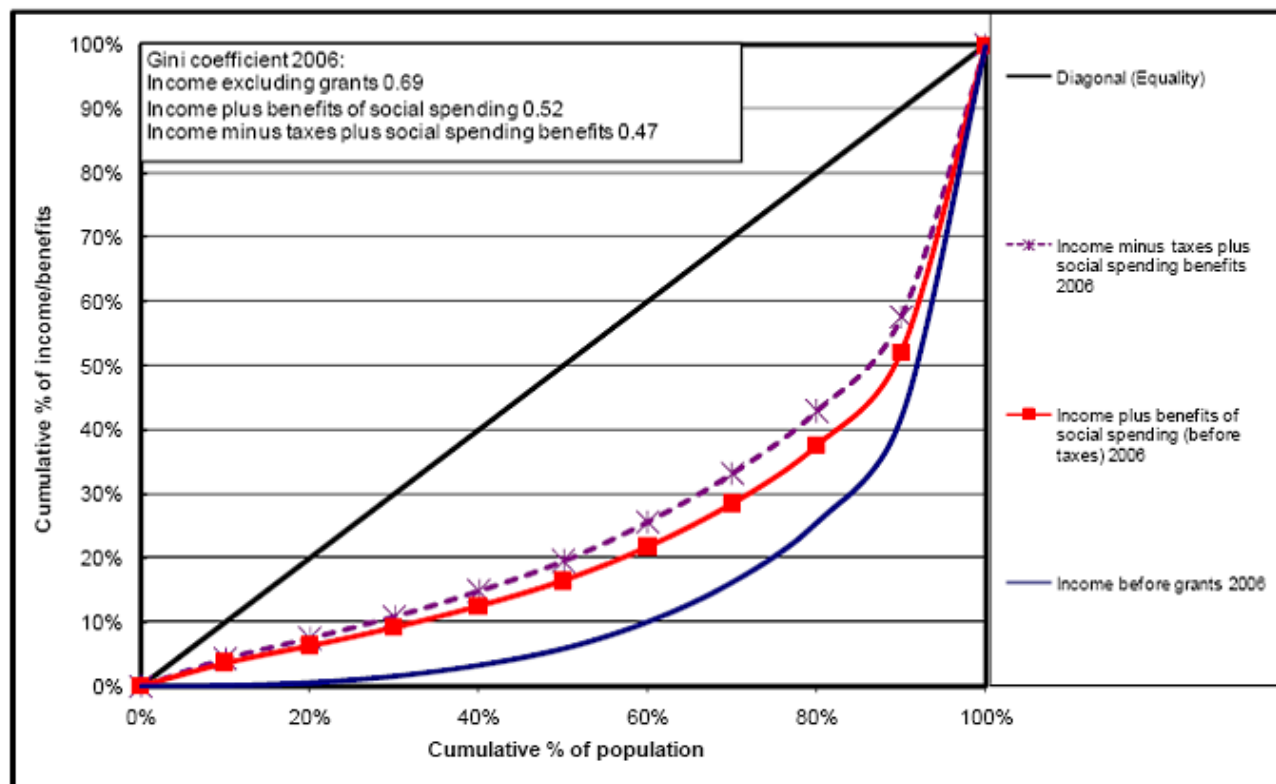
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INEQUALITY IN SOUTH AFRICA

- South Africa a developing country
- Unemployment around 25%, highly unequal
- High HIV/AIDS infection has lowered mortality rates
- Gini before transfers 0.69 in 2006,
- South African fiscal process is highly redistributive, dropping Gini to 0.52
- Tax system progressive, drops Gini to 0.47
- Social spending has a far larger impact on reducing inequality than progressive tax system
- Inequality is still extremely large even after redistribution and taxes
- There are limits to fiscal redistribution, need other mechanisms to reduce inequality more
 - Need much higher growth of 6% at least, instead of 2-4%, and generating many more jobs

Figure 7: Lorenz curves for three welfare measures in 2006: Pre-grant income, income plus social spending benefits, income minus taxes plus social spending benefits



OVERVIEW OF TAX REVENUES IN SA-CONTINUED

Tax revenue by instrument as a % GDP									
	1984/85	1994/95	1999/00	2004/05	2006/07	2007/08	2008/09	2009/10	2010/11
Individuals	6.8%	9.0%	10.3%	7.8%	7.7%	8.1%	8.4%	8.4%	8.3%
VAT	5.2%	5.9%	5.8%	6.9%	7.3%	7.2%	6.7%	6.0%	6.7%
Companies	5.0%	2.7%	2.5%	5.0%	6.5%	6.7%	7.1%	5.5%	4.8%
Fuel levy	0.2%	1.7%	1.7%	1.3%	1.2%	1.1%	1.1%	1.2%	1.3%
Specific excise	1.5%	1.1%	1.1%	0.9%	0.9%	0.9%	0.9%	0.9%	0.8%
Customs duties	1.2%	0.9%	0.8%	0.9%	1.3%	1.3%	1.0%	0.8%	1.0%
STC	0.0%	0.3%	0.4%	0.5%	0.8%	1.0%	0.9%	0.6%	0.6%
Sub Total	19.9%	21.6%	22.6%	23.3%	25.7%	26.3%	26.1%	23.4%	23.5%
Three (PIT, VAT, CIT)	17.0%	17.6%	18.6%	19.7%	21.5%	22.0%	22.2%	19.9%	19.8%
Tax/GDP	21.0%	22.8%	24.0%	24.9%	27.0%	27.5%	26.9%	24.4%	24.5%

AGE DISTRIBUTION OF TAXABLE INCOME IN SOUTH AFRICA

Table A2.1.4: Assessed individual taxpayers: Taxable income and tax assessed by age group, 2006 – 2009

Tax year	2006 [90.2% assessed]			2007 [84.9% assessed]			2008 [75.3% assessed]			2009 [69.0% assessed]		
Age group (years)	Number of taxpayers	Taxable income (R million)	Tax assessed (R million)	Number of taxpayers	Taxable income (R million)	Tax assessed (R million)	Number of taxpayers	Taxable income (R million)	Tax assessed (R million)	Number of taxpayers	Taxable income (R million)	Tax assessed (R million)
Below 18	19,886	844	124	19,101	990	141	18,059	1,223	199	16,804	1,205	187
18 - 24	129,906	8,797	1,160	138,018	10,266	1,249	114,706	10,541	1,390	119,432	11,971	1,552
25 - 34	913,875	109,886	21,196	897,907	120,951	22,336	782,896	127,057	24,319	819,132	143,765	27,479
35 - 44	1,180,487	168,225	37,168	1,146,047	187,297	40,430	1,011,380	201,510	45,177	1,022,240	222,490	49,906
45 - 54	922,367	134,174	31,532	903,020	152,971	35,102	822,047	170,108	40,301	834,820	186,362	44,205
55 - 64	527,284	66,558	16,146	514,038	78,640	18,802	479,856	90,025	22,121	488,030	98,940	23,979
65 and older	312,661	23,063	4,003	298,012	26,383	4,672	283,633	32,089	6,146	284,085	35,789	6,746
Total	4,006,466	511,547	111,330	3,916,143	577,499	122,730	3,512,577	632,551	139,653	3,584,543	700,523	154,053
Percentage of total												
Below 18	0.5%	0.2%	0.1%	0.5%	0.2%	0.1%	0.5%	0.2%	0.1%	0.5%	0.2%	0.1%
18 - 24	3.2%	1.7%	1.0%	3.5%	1.8%	1.0%	3.3%	1.7%	1.0%	3.3%	1.7%	1.0%
25 - 34	22.8%	21.5%	19.0%	22.9%	20.9%	18.2%	22.3%	20.1%	17.4%	22.9%	20.5%	17.8%
35 - 44	29.5%	32.9%	33.4%	29.3%	32.4%	32.9%	28.8%	31.9%	32.3%	28.5%	31.8%	32.4%
45 - 54	23.0%	26.2%	28.3%	23.1%	26.5%	28.6%	23.4%	26.9%	28.9%	23.3%	26.6%	28.7%
55 - 64	13.2%	13.0%	14.5%	13.1%	13.6%	15.3%	13.7%	14.2%	15.8%	13.6%	14.1%	15.6%
65 and older	7.8%	4.5%	3.6%	7.6%	4.6%	3.8%	8.1%	5.1%	4.4%	7.9%	5.1%	4.4%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

SOURCE: Tax Statistics 2010

PERSONAL INCOME TAX AND ESTATE DUTIES

- Six income tax brackets with marginal tax rates increasing from 18% to 40%
- After the tax liability has been calculated various age-related rebates can be deducted.
- Estate duties apply to the estate of a deceased person. The duty is levied at 20 % on the value of the estate, with a number of adjustments and deductions. There are three important deductions.
 - General deduction of R3,5 million.
 - Additional deduction of up to R3,5 million for the value of property that is transferred to a surviving spouse.
 - All debts due by the deceased can be deducted.

CHALLENGES FACING YOUTH

- Youth Unemployment close to 50% in SA (ages 15 to 24)
 - OECD : other middle-income emerging market economies employed about 80% of their working-age youth in 2007
- Social spending is not as effective as it should be
- Public school education of poor quality, even though there is comparatively high funding on a per capita basis
- Labour market challenges for a highly unionised country
- Proposal for a youth wage subsidy to incentivise youth employment
- Large expenses often made in early 20's to fund education – when this can be funded by the current (older) working population (through progressive taxation or funded by parents) an important and significant intergenerational transfer takes place

RICARDIAN EQUIVALENCE THEOREM

- Central hypothesis: when taxes are cut and government spending is held constant, a deficit arises. Taxpayers foresee that this deficit will have to be funded through future taxation, and will therefore curtail consumption and increase their savings in anticipation of future tax liabilities.
- Limited empirical evidence that this is the case (usually premised on the assumption that the tax cut is temporary)
- The requirement that individuals offset governments' deficits with their own savings is often breached (although there is some evidence that corporations increase their savings when governments increase deficits – this could be due to business cycle factors)
- When the hypothesis does not hold (which is the case in most circumstances), then current deficits will not be borne by current taxpayers. The deficits will be borne by future taxpayers.

OLD AGE RETIREMENT CHALLENGES

- Tax system supports pension and retirement savings
- But most employed South Africans do not save sufficiently for retirement
- There is a modest non-contributory state old age pension fund for those over 60 years
- Problem of high fees for retirement and savings funds mean that even those who save, do not benefit to the extent that they should
- As elsewhere, for those with jobs, income is not distributed evenly over the life cycle of a person. Income is low in early phases (20's), builds (30's), peaks (40's, early 50's) and declines (late 50's and 60's)
- Middle class also squeezed further when it opts to use private education and health services

SUSTAINABILITY OF GROWTH

- Key question: Will future generations experience the same levels of growth that the current (or past) generation does? If not, then public debt (funded by future taxes) burdens future generations in an inequitable manner.
- Sustained growth depends on:
 - Sustainability of financial flows and investment in infrastructure
 - Improvements in education and labour force participation
 - Environmental sustainability
 - Sustainable growth in new business ventures
 - Sustainable improvements in productivity of all factors of production
- Fiscal policy must maintain an optimal balance between:
 - Current expenditure / investment on public goods and services that will enhance future growth (can also use equivalent tax expenditures in some cases)
 - Funding current expenditure in a manner that doesn't saddle future generations with a debilitating tax burden

LONG TERM FISCAL CHALLENGES

a. Pensions

- Large pay-as-you-go social pension / social security systems imposes a large burden on future tax payers (given demographic shift)
- Returns on underlying assets rely on future economic growth - therefore it is crucial to ensure that future economic performance is not impeded by current decisions / policies

b. Health care

- Generous existing public health systems will have to be funded from tax revenue – this burden will grow as the population ages.
- Large pay-as-you-go public health insurance systems impose a large burden on future tax payers (given demographic shift)
- Medical expense inflation continues to outpace general measures of inflation

CONCLUSION

- Developing country like SA faces ADDITIONAL challenges to the normal challenges between generations
- Limits to fiscal redistribution to reduce inequality
- Unemployment makes inequality worse
- Ineffective public services squeezes the middle class and delays the possibility of reducing inequality
- Specific challenges to deal with youth employment, and prepare for retirement