

***Personal Income Taxation
and the struggle against inequality
and poverty in an era of crisis***



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In this booklet we argue that rampant corruption isn't an excuse for not increasing taxes on corporations and the rich. Tax dodging is a part of corruption. It takes place in the corporate sector. As for local government: tenders and outsourcing go together with corruption and a small public sector. The small public sector is a result of South Africa's low tax economy.

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Personal Income Taxation and the struggle against inequality and poverty

1. The personal, classes, apartheid legacy and nation

For privileged minorities, private ambulances only transporting those who can pay is not a problem. Or it doesn't disturb them enough to have them support high quality public services for all – an investment that would affect them through higher taxation on their personal incomes.

It seems that the richer you are, the greater is your resentment about “my hard-earned income” being taken from “me” to pay for “them.” This resentment is experienced on a personal level, but it is no doubt also a collective class-feeling, grounded in privileged consumption and wealth.

In South Africa, a deeply rooted racism adds to this feeling. Apartheid is alive in the minds of the people and in their daily lives. It is blatantly visible. And even if we now have a growing black middle class and black captains of industry; class division in SA is still coloured walong apartheid lines. More importantly, the change in colour of a part of the capitalist class will not rid us of class divisions. It is not the purpose of the BEE policy – this policy for creating a black business class has become the strategic axis of the ANC government, but does nothing for democratising the economy.

For the majority, a low-tax society means a poor level of public services, whether for health or education, and a denial of their democratic aspirations. It means that millions of citizens will continue to live in informal settlements, only having access to bucket toilets. It means failing housing programs, a lack of safe public transport, and that there won't be affordable electricity or piped water to all households. A list of our failed or absent public services and infrastructure would fill several pages. Twenty odd years after the end of apartheid, “service delivery protests” are a daily part of South African politics. Corruption is now endemic, spreading from the private to the public sector. But corruption is only part of the problem. Large resources are available for public services and social investment, but the government has chosen not to utilize them.

The “Personal” Income Tax (PIT)?

The personal income tax (PIT) is a good space for debating social services, inequality and social solidarity. The PIT both influences and is influenced by the dominating mind-set of society, reflecting how a society fits together, or how its social fabric is torn apart.

“The local is where we really feel it” was the title of an article written by Richard Pithouse before the local elections in May 2011.¹ In the article, Pithouse explains how gross inequality and corruption are “felt” on a local level. Yet changing taxation into a tool for the necessary and urgent redistribution of wealth and income from rich to poor would change “how we really feel it.”

The use of “we” in political talking is, however, problematic. Abysmal inequalities prevail and have increased in South Africa.² If individuals don’t feel a sense of belonging to any community—if they still only perceive people in their own apartheid category as exclusively constituting “the nation,” or if they only want to support their relatives, then they will regard taxation as an intrusion on their family economy.

Progressive taxation

Davis Tax Committee writes: “The concept of **vertical equity** states that those who earn more income should pay more tax in accordance with the **“ability to pay principle of taxation.”** Vertical equity has, at its heart, a redistributive effect on income. It also recognises the concept of the **“benefit principle of taxation”** which holds that wealthier members of society tend to enjoy greater benefits from government services and should accordingly pay more taxes for such enjoyment.” (*First interim report on mining*, July 2015, p. 16; emphasis added)

Taxing income according to the ability to pay

In most countries, systems of personal income tax (PIT) use the principle of progressive taxation. Currently in South Africa, the part of a taxable income³ that exceeds R701 300 (this is the highest tax bracket) is currently taxed at the top rate – 41%. After being reduced in 2000 and 2001 from 45 to 40%, this tax rate was again increased from 40 to 41% in the 2015 budget.⁴

¹ Richard Pithouse (7/4, 2011), “The local is where we really feel it.” <http://www.sacsis.org.za/site/article/651.1> (accessed 8 June 2011).

² Leibbrandt, M. et al. (2010), “Trends in South African Income Distribution and Poverty since the Fall of Apartheid,” *OECD Social, Employment and Migration, Working Papers*, No. 101, Paris: OECD.

³ The tax authorities allow already privileged people to deduct certain types of expenses that they have had from their total personal income, like medical expenses. What remains after such deductions is the lower *taxable income*. The tax statistics show that the total personal income, or gross income, is between about 8 to 13% higher than the taxable income for people with annual *taxable* incomes between R50 000 to R1 million (National Treasury & SA Revenue Service (2012), 2011 *Tax Statistics*, pp. 34, 60-74 and own calculations).

⁴ The share of taxable income paid in tax is measured in *per cent*, or written together, “percent.” As most readers know, the symbol is %. “Cent” is a Latin word that means “100.” In this context *percent* means “rands that are paid in taxes per every hundred rand of income.”

But how does a “graduated” or progressive tax work?

The part of a taxable income that exceeds R75 000 per year lies over the so-called “first tax bracket.” That part of the income will be taxed at the rate of 18%.⁵ This means that if you earn exactly R75 000 or less per year, you pay nothing in personal income tax (PIT). But if you earn R76 000 in taxable income, then this is R1 000 more than R75 000; therefore your tax will be 18% of R1 000, which is R180. So,

R76 000	- R75 000	= R1 000
[your earnings]	[1 st tax bracket]	[amount to be taxed]
18% of	R1 000	= R180
[tax rate of 1 st tax bracket]	[amount to be taxed]	[your tax]

Value Added Tax (VAT)

Everyone pays a 14% VAT (Value Added Tax) when they buy something at a shop. The VAT is added to the price of most goods and services.⁶ An item that would cost R10 without VAT, costs R11,40 with VAT. An item that would cost R100 exclusive of VAT, costs R114 inclusive of VAT. Internationally, VAT is a new tax. It was introduced in SA in the beginning of the 1990s.

Between the highest income level of R701 300 (the “sixth tax bracket”) and the lowest income level of R75 000 (the “first tax bracket”) there are four other tax brackets at four income levels. The *part* of the taxable income that exceeds each of these four levels is taxed in steps up to the next level at 26, 31, 36, 39 and 41%.

Progressive or graduated tax: a simplified example

Imagine a country where the first tax bracket starts at R50 000, the 2nd tax bracket at R100 000, the 3rd tax bracket at R150 000 and the 4th tax bracket at R200 000. The tax is 18, 25, 30 and 40% from one bracket to next bracket respectively. If an individual has R300 000 in taxable income, he or she will pay R0 in tax on the income between R0 and R50 000; 18% tax on the income between R50 000 and R100 000; 25% tax on the income between R100 000 and R150 000; 30% tax on the income between R150 000 and R200 000; and 40% tax on the income above R200 000. His/her tax will therefore be R0 + R9 000 + R12 500 + R15 000 + R40 000 = R76 500. The tax on the R300 000 in taxable income will then be 25.5% ($R76\,500 / R300\,000 = 0,255$).

⁵ The National Treasury, *2016 Budget Review*, p. 143.

⁶ Even informal shops set their prices at the same level as the legal formal shops, which add 14% VAT to the prices. Legal shops are obliged to pay the VAT money to the state, after subtracting the VAT they have paid themselves to the retailer of the goods they sell (as well as other services that keep the shop going, like electricity). **Indeed, a spaza shop owner in a township that buys the merchandise in bulk from a big supermarket buys at prices that include VAT. He/she then passes this cost on to the final consumer and adds a mark-up to the price in order to make a profit. VAT is a “consumer tax.”**

The government's budget year – or “the financial year” – runs from April in one year to March in the next.

Since the financial crisis of 2007/2008, tax on the business profits of companies, called Corporate Income Tax (CIT), has fallen as a share of the total budget revenue. In contrast, tax on personal income (PIT) and VAT have made up an increasing share of total tax revenue. Besides CIT, PIT and VAT, the remaining 20% tax revenue comes from other sources, like the fuel tax, which is paid when buying petrol and diesel.

In the 2010/11 financial year, VAT comprised 27.2% of the total tax revenue coming in to the national government. In 2014/15 VAT revenue was about 26.5%. In 2010/11, Corporate Income Tax (CIT) comprised about 20% of all tax revenue 2010/11, but fell to an 18.9 % share in 2014/15. In 2010/11 the personal income tax (PIT) comprised 33.8% of all tax revenue. In 2014/15 the PIT share of all tax revenue had increased to 35.9%. From the above we can see that as the revenue from CIT and VAT have decreased, the revenue from PIT has increased.⁷

History of progressive taxation

The principle of progressive taxation was first put forward in 1776 by Adam Smith in his book, *The Wealth of Nations*. Smith's book is generally regarded as the first book on economics, or at least the first serious book written in Europe on the subject. Progressive taxation, in fact, appears again as the second demand in the short 10-point program of *The Communist Manifesto* (1848), where the first three demands were about taxation:

1. Abolition of property in land and application of all rents of land to public purposes.
2. A heavy progressive or graduated income tax.
3. Abolition of all rights of inheritance.⁸

Progressive income tax is widely applied internationally. Nonetheless, it has never been popular among high-income earners and has, over the last 30 years, been under attack from neoliberalism.⁹ Some neoliberals argue for “flat taxes” set at a low rate. This means that the tax rate remains the same, no matter of how much you earn. VAT is, in fact, a kind flat tax, even if it is not charged on income: No matter their income, everyone

⁷ In its “First Interim Report on Base Erosion and Profit Shifting,” the Davis Tax Committee reports that tax revenue CIT fell from 6.8% to 5% of gross domestic product (GDP) 2007-2011. GDP is a measure for the value of new production of goods and services that are bought and sold.

⁸ Karl Marx & Friedrich Engels (1848), *The Communist Manifesto*, Chapter 2. <http://www.marxists.org/archive/marx/works/1848/communist-manifesto/ch02.htm> (accessed 24 January 2011)

pays 14% extra in tax for the majority of items they buy in a shop. Acknowledging this problem, and as a small tax relief, some 20 consumables, like paraffin, are exempt from VAT in South Africa. Many countries have different VAT on different items to protect people with low incomes and their children, for example, a lower VAT on books. VAT is a relatively recent introduction to the tax system, in South Africa and everywhere else. It makes each individual in a society a tax payer – even the very poor.

There is evidently a large amount of resistance from high income earners concerning their being taxed based on their ability to pay, compounded by the general tendency towards guarding personal incomes when social solidarity has been pushed to the side. Therefore, a moderate goal for progressive redistribution of incomes through taxation is to achieve what in the literature is called “quasi-compliance” – getting taxation to be more or less accepted in practice.¹⁰

But in a very unequal and divided society, such a shift of money – from individual consumption to social or collective consumption of public services or from private business and production for profit to public for-non-profit services – will be debated vigorously. This booklet is an intervention in that ideological and political struggle.

2. The goal of progressive tax policy

If too many workers are not organised – which is the case in South Africa, where about three out of four workers don't belong to a union – and if mass unemployment puts pressure on wage levels, then the working population's share in the national income will be smaller.

The bigger share of income then goes to shareholders or is put under corporate control. Society, thereby, becomes more unequal. This has been the case in South Africa for the past 15 years. The growth of outsourcing and labour broking, since 2000, has also contributed significantly to this inequality.

⁹ https://www.theguardian.com/books/2016/apr/15/neoliberalism-ideology-problem-george-monbiot?CMP=share_btn_fb (accessed 11 Aug 2016) George Monbiot writes: “**Neoliberalism** sees competition as the defining characteristic of human relations. It redefines citizens as consumers, whose democratic choices are best exercised by buying and selling, a process that rewards merit and punishes inefficiency. It maintains that “the market” delivers benefits that could never be achieved by planning. Attempts to limit competition are treated as inimical to liberty. Tax and regulation should be minimised, public services should be privatised. The organisation of labour and collective bargaining by trade unions are portrayed as market distortions that impede the formation of a natural hierarchy of winners and losers. Inequality is recast as virtuous: a reward for utility and a generator of wealth, which trickles down to enrich everyone. Efforts to create a more equal society are both counterproductive and morally corrosive. The market ensures that everyone gets what they deserve.”

¹⁰ “Quasi” means “kind of,” “close to” or “almost”: people “more or less” comply with tax laws and regulations. Lieberman, E.S. (2001), “National political community and the politics of income taxation in Brazil and South Africa in the twentieth century.” *Politics & Society*, 29(4): pp. 515–555.

The share of all new income going to wages – or of new national wealth produced every year, called the Gross Domestic Product (GDP) – has fallen from 55% in 1998 to below 50% today. Masking the extent of this growing inequality are the enormous salaries of senior managers and CEOs. Their salaries are deemed to be wages for statistical purposes.¹¹

The purpose of progressive tax and redistributive policy¹² is to enable the government to rectify and reshuffle the increasingly unequal primary distribution of income, wealth and minority monetary power.

Correspondingly, it is also used to pay for the so-called “social wage” of the majority – public healthcare and education, housing programs and affordable public transport.

But the economic system that dominates production and exchange in South Africa is a capitalist system inherited from colonialism and apartheid. It has its special features – it is infested with racism and sexism, and is dominated by mining, the production of electricity (from burning coal) and the selling of unrefined commodities.

Tax policy will never be able to eradicate all the unacceptable economic inequalities that capitalism feeds upon (and, in turn, makes worse). For one thing, we need strong working class organisations, exerting pressure from below to bring about significant change. On the other hand, it is hard to see how a programme of transition away from capitalism, and towards economic democracy and social justice, can do without policies that tax the rich and their corporations, while blocking tax dodging and illicit (illegal) capital outflows. Such measures and programs need to be an integral part of progressive policies and the mobilisation towards mass action.

¹¹ Some researchers shave off one percentage point from the wage share (or “labour share”) of GDP, arguing that CEOs control their own salaries. The falling wage share of GDP was much debated during 2011 and 2012, for example in the Socio-Economic Report to the 11th Cosatu congress, September 2012 (pp. 18 and 19). Data that shows the falling wage share can be found in the national accounts, published in the Quarterly Bulletins issued by the SA Reserve Bank. A claim has been made by anti-union economists that increasing capital intensity explains why the wage share is falling. This is only relevant for very short periods. Heavily industrialised countries in the North (or OECD) are much more capital intensive than SA, meaning that they employ much more machinery and equipment per worker. Still, the wage share of GDP in all those countries is 15 to 20% higher than in SA, with the profit share of GDP correspondingly lower. The low wage share in SA is an indisputable indication of employees being super-exploited. This state of affairs is inherited from apartheid and colonialism (See Forslund, D. [2013] “Unemployment and the Low Wage Regime in South Africa.” *New South African Review*, No. 3, Johannesburg: Wits University Press.)

¹² In *redistribution*, the prefix “re” means “again”: **Most monetary incomes in our society are distributed under the control of employers. The government then uses taxes** to distribute the incomes one more time, as it were.

A missed opportunity

The fall of apartheid provided South Africa with an opportunity to attack economic inequality. But the tax reforms of post-apartheid South Africa have not been used for progressive redistribution of wealth and power. Tax policy has, in fact, contributed to the growing inequality in income and services, instead of rolling them back. The expansion of the social grants system that started 15 years ago has not been able to change this. Consistent with profits constantly beating wages in its share of national wealth, corporate profits have been taxed less and less. The tax on personal incomes has also become milder and milder. It is not only history and old crimes that are responsible for inequality and poverty in South Africa today.

Taxation is on the global agenda

At the beginning of the 1970s, the election manifesto for the British Labour Party advocated a “fundamental and irreversible shift of wealth and power in favour of working people and their families.”¹³ Those words are still relevant to our times, not least because, having spoken as the “left,” the Labour Party has subsequently acted decisively “right.” Today, beyond Britain and South Africa, global inequality has come to the fore as never before. The cleavage between the rich elite and the majority has grown into a gulf of epic proportions. International reports have started to highlight, or simply reveal, that “super-wealthy individuals”¹⁴ have been faring especially well through the worldwide economic crisis that has been with us since 2008; while the masses have been hit by growing unemployment, poverty and, even, hunger.

There has been a reaction to the sheer grossness of global inequality, in Africa and around the world. A debate has started on how to deal with tax cheating corporations and what the options are for taxing the rich. A Tax Justice Africa network has been established.¹⁵ The annual reports on illicit financial flows from Global Financial Integrity (GFI) are now widely read and acknowledged. In its 2014 report, GFI estimated that, in 2012, illegal outflows of money from South Africa amounted to 28.1 billion dollars US, the equivalent of over 300 billion rand.¹⁶ In 2015, the so-called “Panama Papers” were made public by a large team of journalists.

¹³ Harold Wilson (October 1974), “Labour Party Manifesto: Britain will win with Labour, by The Rt Hon. Harold Wilson, OBE, FRS, MP” Foreword. <http://www.politicsresources.net/area/uk/man/lab74oct.htm> (accessed 1 July 2012).

¹⁴ Wollgraaf, R. (24 June, 2011), “Africa’s rich get richer, faster.” *Sunday Times*, quoting the annual World Wealth Report from Merrill Lynch and Capgemini.

¹⁵ Tax Justice Africa was founded in 2007. www.taxjusticeafrica.net (accessed 3 July 2012). ¹⁶ The reports from Global Financial Integrity are published on www.gfintegrity.org

These papers revealed how one single law firm in Panama had helped individuals and transnational corporations (TNCs) hide billions of dollars in off-shore bank accounts.

Neoliberalism and dogma

Taxation is a vast and complex area, but the struggle over taxation is not technical at its core.¹⁷ Today's assumptions about what good economic policies are appear to be grounded in what is effectively a religion of inequality. This religion teaches its disciples that minority control over income and productive wealth is best. This religion is for the elite, who whole-heartedly believe in it, and for the majority to accept and pay respect to, even when in doubt.

It is this faith in minority control that we have to contest when arguing for increased taxation. For the whole period, from 2000 up until 2014, we saw a policy of corporate income tax cuts, some anti-avoidance measures and "further personal income tax relief." The official purpose of such neoliberal measures is always to "stimulate the economy," with the hope that some of the benefits that the minority receive will trickle down to the majority. But like everywhere else, in South Africa these measures have not accomplished the expected "support" to "inclusive growth and development" that they are claimed to bring about.¹⁸

Starting in 2015 when the state budget came under pressure from the global recession, we saw a hesitant increase by 1 percentage point of the PIT tax rates for all tax brackets except the lowest (i.e. generally, PIT rates were increased). Under additional pressure from the #FeesMustFall movement, and under intense pressure from the credit ratings agencies in 2016, the Treasury continued to take back a small part of the money that had been lost through the exaggerated upward adjustments of the tax brackets (i.e. the lowering of taxes) over the last 15 years. In other words, in 2016 the tax brackets were adjusted upwards by less than the inflation rate. This is discussed in detail below.

The positive measures taken in 2016 were, however, balanced by yet another increase of the tax rebate for private medical insurances. This signalled to creditors that the implementation of a National Health Insurance (NHI) was to be put on hold again. In fact, the net contribution to tax revenue from the different measures taken in the 2016 budget amounted to exactly zero.¹⁹ They cancelled each other out.

¹⁷ Myrdal, G. (1930/2007). *The Political Element in the Development of Economic Theory*, London: Routledge.

¹⁸ National Treasury (2/6, 2011), "Taxation Laws Amendment Bills 2011: General Overview." www.treasury.gov.za (accessed 8 June 2011), p. 1.

¹⁹ National Treasury, 2016 *Budget Review*.

In summary, the government cannot bring itself to radically change its tax policy. It still hopes that an end to the global crisis, the reining in of tax dodgers and a rebound of classical capitalist growth will save the income side of the budget, lessening the government's need to borrow money from the rich and private finance institutions. The policy of "too little too late" is informed by a decision to "wait and see," not by the much needed acknowledgment that "our policy has been wrong and now we will change it."

Two-legged tax strategy

Starting at the end of 1994, an extra 5% "Transition Levy" on yearly income above R50 000 (about R160 000 worth in today's prices) was in force for 12 months. It was a short-lived experiment. Since 1996, the strategy has been to balance tax cuts through an extensive growth of tax revenue.²⁰ Thus, more taxpayers, individuals and companies have been brought into the formal economy and the tax system. This has been combined with steadily decreasing personal and corporate income tax rates and reoccurring tax amnesties.²¹ In 2011 there was an amnesty to encourage greater compliance.²² Another one was announced in the 2016 Budget Speech.

Enormous inequality persists and has increased, not only between rich and poor but even within the best paid 20% of the population. If we believe the yearly surveys made by the Bureau of Market Research (BMR) at the University of South Africa (UNISA), then less than 2% of the population, aged between 15 and 64, receives close to 25% of the country's annual income.²³ Anything that disturbs this state of affairs will clearly be resisted.

3. The Negotiated Settlement and tax policy

Given the problem, since democracy, of providing good public sector services for all (and not only for the minority of people categorised as White), and given the permanent health, housing and education crises, why has the government pursued a strategy of lower and lower tax rates? The neoliberal theology of economics is a factor, as has been pointed out by many. For one thing, the government has opened South Africa to globalised markets and capital flows.

²⁰"Extensive growth": increasing the number of people and companies brought into the system.

²¹"Tax amnesty": the government sets a deadline for when tax dodges must declare their true incomes. If they do that, they will not be fined for breaking the tax laws or they will be fined less. ²²Ashman, S., Fine, B. & Newman, S. (2011) "Amnesty International? The nature, scale and impact of capital flight from South Africa." *Journal of Southern African Studies*, 37(1): 7–25.

²³ See again Leibbrandt, M. et al. (2010): This study also reports on growing inequality 1994–2008 (p. 25). The top 10% households (decile 10) have gained in income (1994 – 2008) at the expense of decile 3-9. Due to the expansion of social grants from year 2000, the household income of the poorest 20% of the households (decile 1 and 2), stayed the same during this period. The latest official survey of income from employment is "Monthly earnings of South Africa 2010" done by Statistics SA (www.statssa.gov.za). The new Stats SA "Household Income and Expenditure Survey" was published in November 2012.

This was done in accordance with the doctrine of “export led growth,” which these days is widely criticised, notably also by the United Nations’ Conference on Trade and Development (UNCTAD).²⁴ Proponents of “export-led growth” support the idea that exporting companies use low wage levels to boost their profits through competitive pricing, but this means that the domestic market is left with less demand for goods and services (because labourers cannot afford to buy these products). This leads to higher unemployment. Along with this, some aspects of neoliberalism have now, most remarkably, even been criticised by IMF.²⁵

The Negotiated Settlement on economic policy from before 1994 is most likely an additional factor. Breaking with neoliberalism in South Africa would mean breaking politically with corporate capital and challenging speculative capital flows – this would be the case anywhere in the world. But in South Africa we would also have to break a signed agreement about “not going too far” in reforming the economy.

The Freedom Charter of 1955 set out to frame what freedom would mean in a democratic South Africa. A core principle of the charter was that “The people shall share in the country’s wealth!”²⁶ Evidently a part of the settlement in 1994 entailed leaving the commanding heights alone. In practice this meant abstaining from touching the mines or the banks with nationalisation. At the same time, though, a rigid ceiling for tax revenue was probably also agreed upon. The purpose was clearly to protect the affluent minority from the threat of a redistribution of wealth and income.

This is what the historian Sampie Terreblanche argues in his seminal book, *A History of Inequality in South Africa*.²⁷ It also accords with the historical accounts presented in the works of Patrick Bond and Hein Marais.²⁸ In November 1993, when they applied for an 850 million dollar US loan from the IMF, the eight National Party and the eight ANC ministers in the Transitional Executive Council, individually signed an economic policy document. Among other things, the text, which has remained secret, most probably committed the signatories to ensuring that the size of the state, relative to the rest of the economy, remain at the same level as during the last years of apartheid.²⁹

²⁹ Terreblanche, S. (2002), pp. 96ff and 116–119; and a telephonic interview with Terreblanche in June 2012.

²⁴ UNCTAD. (2010). *Trade and Development Report, 2010: Overview*. New York and Geneva: United Nations. The export-led growth path dogma is also criticised in UNCTAD’s 2011 and 2012 report.

²⁵ <http://www.imf.org/external/pubs/ft/fandd/2016/06/ostry.htm> (accessed 5 July 2016).

²⁶ This section of the Freedom Charter reads as follows, “

²⁷ Terreblanche, S. (2002). *A History of Inequality in South Africa, 1652–2002*. Pietermaritzburg: University of Natal Press.

²⁸ Bond, P. (2000). *Elite Transition: From Apartheid to Neoliberalism in South Africa*. London and Pietermaritzburg: Pluto Press and University of Natal Press; Marais, H. (2011). *South Africa Pushed to the Limit: The Political Economy of Change*. Cape Town: University of Cape Town Press.

In 2013, former Minister of Security Ronnie Kasrils wrote:

From 1991 to 1996 the battle for the ANC's soul got under way, and was eventually lost to corporate power: we were entrapped by the neoliberal economy – or, as some today cry out, we “sold our people down the river.” What I call our Faustian moment came when we took an IMF loan on the eve of our first democratic election. That loan, with strings attached that precluded a radical economic agenda, was considered a necessary evil, as were concessions to keep negotiations on track and take delivery of the promised land for our people.³⁰

The most important and expensive “public service” provided to the black majority during apartheid was police repression. With the fall of apartheid in 1994, the public services and grants available for the white minority were to be expanded to all. The new government was confronted with a terrible backlog in housing, the need to eradicate informal settlements, the poor state of healthcare, the pernicious bantu education system that had been forced on the majority, a lack of social infrastructure in the townships and a desperate need to supply of sanitation, water and electricity. A public sector that could serve all, while addressing all the injustices of the past, would simply have to comprise a much larger share of the economy. To address the backlog, a radical redistribution of resources from private to public was a necessity, but it was effectively ruled out in the compromise.

Jo-Ansie van Wyk speaks about an economic pact moulded together since the end of the 1980s which was established at an elite level before the democratic elections in 1994. So far, she argues, this pact has prohibited the necessary double transition – that is, a political as well as an economic transition from apartheid³¹

From a variety of income surveys and studies, we can conclude that this “economic pact” functions as a skewed social contract at the top, between Business and Government. The big business of the white minority signed-off on this “pact” from the start. Today, their junior partners, in the form of BEE capitalists, sign-off this contract when they become a part of mining corporations or start labour broking companies. Ideologically, the elite social contract rests on the assumption that the country will fall apart, unless the super-rich are allowed an undisturbed “Californian lifestyle,” to use an expression from Terreblanche’s book, and the newly rich must have the right to aspire to become super-rich.

³⁰ <https://www.theguardian.com/commentisfree/2013/jun/24/anc-faustian-pact-mandela-fatal-error> (accessed 25 July 2016).

³¹ Van Wyk, J. (2009). *Cadres, Capitalists, Elites and Coalitions: The ANC, Business and Development in South Africa*. Discussion paper 46. Uppsala: The Nordic Africa Institute.

4. The meaning of “tax pegging” and its history

Cutting taxes and the alternative

In an economy where the living standard improves for those who pay PIT, a larger part of these earners’ personal incomes will be paid in tax if the tax system is progressive. Of course, the majority of people in SA – that is, 70% of employees who earn less than the limit for PIT (R75 000 per year in 2016/17) – have not seen any real improvement in their living standards.³² On the other hand, the minority with higher incomes who are paying PIT have certainly seen improvements to their lifestyles. Moreover, if tax dodging people with high incomes were brought into the tax system, a much larger share of their personal incomes would inevitably be paid in taxes.³³

The “graduated” or progressive income tax system fits well with the absolutely crucial idea that the better off a person is, the more she or he should be able to contribute to the community, sometimes called “The Common” – the economy of common purposes. If annually this person increases her income more and more above a living wage, there should be no problem with that additional part of her income being taxed at a slightly higher rate.

When this process of increasing living standards among PIT payers takes place on a large scale, involving millions of individuals, a larger public sector can be financed without the government drowning in debt or changing tax policy. Tax revenue would not only be bigger in absolute rand terms, it would also comprise a larger and larger part of the whole national income (GDP).

A concomitant larger public service sector as a share of the GDP would almost inevitably be the result. “The Common” would become a more and more important part of the economy, when the individual needs and wants of the PIT payers have been met. They would no longer be able to reasonably protest against the redistribution of resources from their growing private incomes to public services.

³² Niall Reddy (2015), “Labour – twenty years after democracy.” Cape Town: Alternative Information and Development Centre.

³³ We write “a much larger share,” because **if you have a high income but escape the PIT, you still cannot avoid paying VAT.**

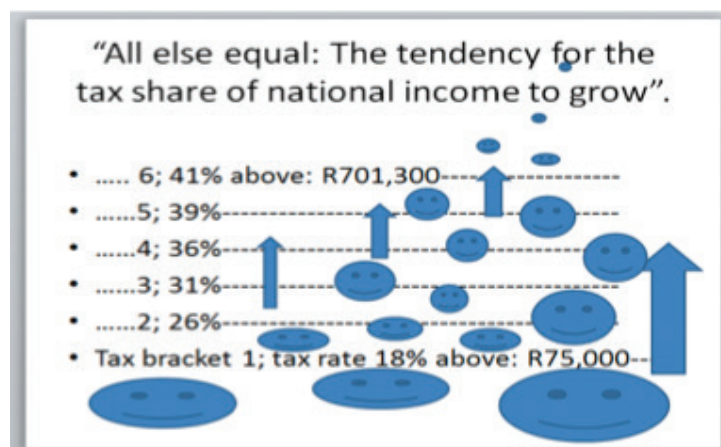


Figure 1: The tendency for the tax share of national income to grow. If we imagine that there is no inflation – or that tax brackets are adjusted upwards at the same rate as inflation, which amounts to the same thing – a growing living standard that is taxed in a graduated way means that a little larger share of the growing real income will be paid in taxes every year. This growth would come from individuals whose incomes climb in the system and in the whole system as such. If the working class majority also get real wage increased, then these individuals would finally also see the part of their income that falls above the first tax bracket being taxed at a rate of, presently, 18%.

The history of “tax pegging”

The tax revenue to GDP ratio³⁴ is a key measure of indicating what a government’s ambitions are for the quality and size of public services. It is also a key measure of how much of the whole economy the government allows to be placed under private control and production for profit. A policy of low tax to GDP ratio limits the financing of all public services and programmes, like health, education and housing, and gives more economic power to the capitalist sector.

For this reason, the tax to GDP ratio is referred to in debates about social welfare or when comparing “tax pressure” and the size of the public sector in different countries.³⁵ It is, however, unusual to sanction that the tax revenue to GDP should not exceed a certain ratio as the South African government did in the 1996 GEAR document and again in the Budget Speech of 2012. We call this policy “tax pegging.”

In budget speeches, finance ministers have argued that the reason for the yearly cuts in personal income tax is to compensate for the effects of inflation. But from the year 2000 (when the tax rate for the top income earners was cut in two steps from 45 to 40%) up until the 2008-2009 budget years, the upward adjustment of tax brackets have exceeded the amount required to compensate for inflation.

³⁴ A “ratio” compares two sizes to each other. Percent (%) is a measure of a ratio.

³⁵ See the National Treasury & SA Revenue Service’s *Tax Statistics* (2011) of any year since 2011.

In Figure 1 above, this policy would be illustrated by also moving the tax bracket “lines” upwards, but faster than the increase of real incomes (the upward movement of the “balloons” in Figure 1 that symbolise groups of people with different incomes).

Every year the *Tax Statistics* from the National Treasury and South African Revenue Services (SARS) illustrate this “over-compensation” for inflation in a diagram.

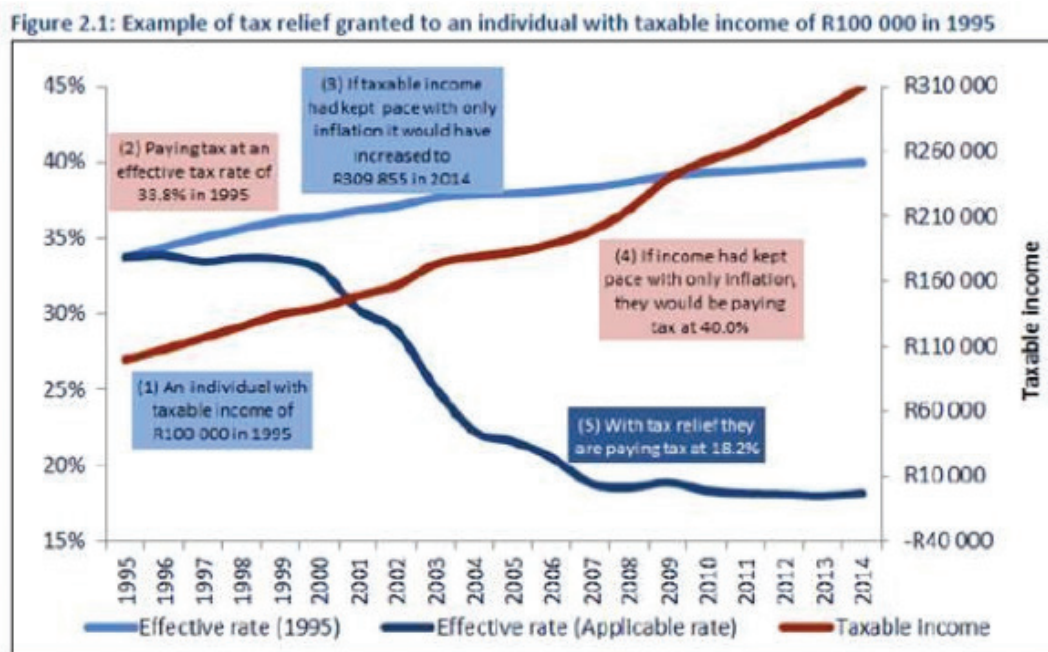


Figure 2.1 illustrates the impact of tax relief over a period of 19 years. (1) An individual with taxable income of R100 000 in 1995 (2) was paying tax at an effective tax rate of 33.8%. (3) If their income had only kept pace with inflation (4) this would have increased to 40.0% in 2014 if there had been no adjustments to the income tax brackets. The impact of the actual tax rate adjustments from 1995 for the same example (5) lowers the effective tax rate to only 18.2%.

Figure 2: “Tax relief” granted to an individual with taxable income of R100 000 in 1995

(Picture and text from the 2015 *Tax Statistics* published by the SARS and the Treasury. Note: point 4 in the explanatory text above confuses the matter somewhat: because of inflation, no government would freeze the tax brackets at the same levels for 20 years).

The important schedule in Figure 2 above (called “2.1.” in the *Tax Statistics*) is the falling dark blue schedule. The red schedule shows the effect of inflation on the value of money. The right scale in the diagram shows that a taxable income of R100 000 in 1994 is equivalent to R310 000 in 2014 in terms of buying power. This income level was taxed at 33.8% from 1995 to 2000, but only at 18.2% in 2014. As such, the idea of an increasingly harsh personal income tax is completely wrong. In fact, it is the complete opposite that is true.

The explanation for the diminishing PIT represented above is that it is actually part of the government's adopted policy. To keep the public sector small, the government has time and again granted huge tax reliefs to today's 5.5 million PIT payers.³⁶

We can see in Figure 2 (or "Figure 2.1") that the drastic fall of the tax rate (that is depicted by the dark blue schedule) was halted around 2008-2010. Unfortunately, this coincided with the government starting to use more and more of the tax revenue to pay interest on its growing debt.

In 2016, the government has decided to curb public sector services with a "wage bill freeze." First, it has announced a lowering of the so-called expenditure ceiling by R25 billion over three years "by reducing the compensation budgets." This refers to the total wage bill in the public sector.³⁷ Second, it has said that the costs for public sector employment will be fixed at 35% of total expenditure on public sector services (this is "the freeze"). Third, the government plans to grow non-interest public spending by less than the estimated growth of the whole economy over three years. This would mean 0.8% in real average growth of spending per year, as compared to the estimated 1.6% in real economic growth.³⁸ The service-delivering public sector would therefore comprise a smaller part of the economy if this becomes reality. The Treasury therefore optimistically writes: "the reductions in compensation budgets were designed to minimise the impact on frontline service delivery personnel, with the bulk of reductions applying to managerial and administrative staff."³⁹ The tertiary says this because the 35% "freeze" will inevitably lead to a fall in public sector employment.

The reason is this: individual wages in the public sector will, as a rule, always rise by the rate of inflation plus at least, say, one percentage point that follows the general rise of productivity in the whole economy. The government as an employer has to accept real wage increases. If not, many employees with skills, experience or higher education (teachers, doctors, clerks, electricians, nurses, managerial staff and the like) will start to look for jobs in the private sector. The so-called "wage bill freeze" is therefore a plan to reduce the number of people employed in the public sector.

³⁶ National Treasury & SA Revenue Service, *2015 Tax Statistics*, p. 51. The number of people registered by the SA Revenue Service exceeds 15 million, but the majority of them don't have incomes above the first tax bracket (R75 000 per year). They are not yet liable for paying PIT.

³⁷ National Treasury's 2016 Budget Review, page 55. "Expenditure" refers to everything but debt service. The public sector *wage bill* is simply the number of employed times the average wage.

³⁸ "Real" means after inflation is taken into account. The opposite is "nominal," which means that inflation has not been taken into account.

³⁹ National Treasury's 2016 Budget Review, page 55.

How is such a plan at all possible, given the pressing need for service delivery and the high number of vacant posts in local government? Statistics SA gives a total number of about 320 500 posts in local government in 2015, an increase from 2014; though about 41 500 or 13% were still vacant.⁴⁰

The austerity policy – decreasing public sector spending as share of the whole economy – also hits social grants, like childcare and pensions. For a number of years our social grants have been increased at less than the true inflation rate for poorer households. This has dire impact on the poorest in the country. In 2016/17 they were actually increased at less than the official rate of inflation, the so-called Headline CPI.⁴¹

What thousands of service delivery protests over the past 15 years and dramatic reports on the crisis in provincial health and education couldn't do – increase the tax revenue to GDP ratio to ramp up public services – the threat from finance capital, delivered via the credit ratings institutes, has now accomplished. The 2016 Budget Review provides the following picture of tax policy and government expenditure for 2012 to 2018 (Figure 3). The figure shows "the plan" from 2016.

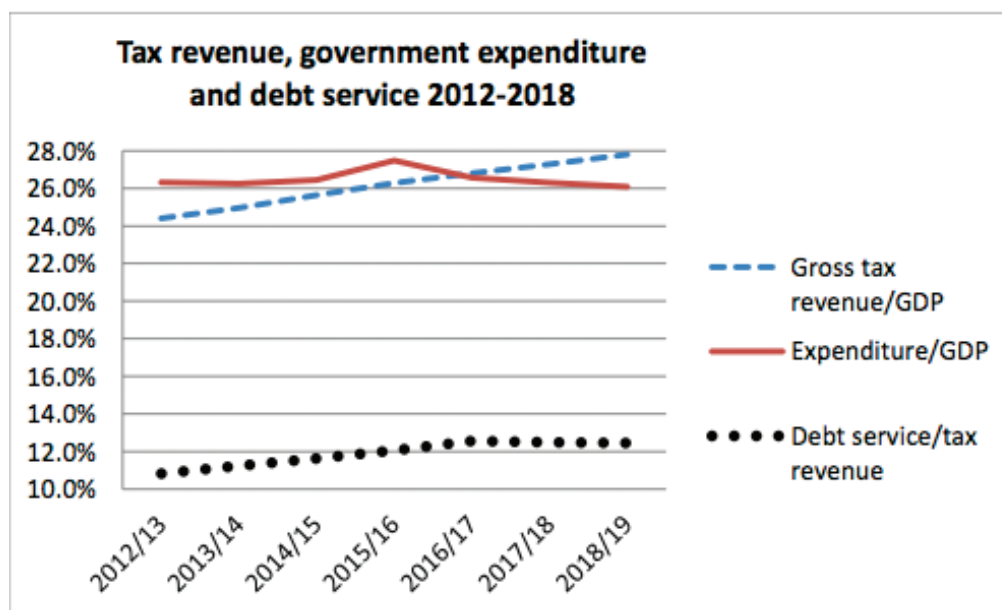


Figure 3: Tax revenue, government expenditure and debt service 2012-2018. While there have been cuts in public spending prior to 2016, direct "austerity" – a fall in the spending of local, provincial and national government – is now visible from the numbers in the 2016 Budget Review. The period after 2015/16 in the diagram is, of course, a prediction based on the government's plan.

⁴⁰ Media release from Stats SA, 7 June 2016, "Non-financial census of Municipalities." <http://www.statssa.gov.za/?p=7818> (accessed 6 July 2016): "The number of people employed by municipalities increased from 270 714 to 279 109 in 2015 (inclusive of councillors and mayors but exclusive of vacancies)." The highest number of unfilled posts in the technical areas was recorded in the environmental protection services (23%), followed by electricity departments (20%), while waste water managements departments and water reported vacancy rates of 16% and 12% respectively."

⁴¹ In the monthly Consumer Price Index (CPI) reports, Statistics SA also reports the rate of inflation experienced by the poorer households. SA households are divided into five groups ("quintiles"), according to how much they spend. Households that receive childcare grants spend the majority of their small income on goods that have for many years increased more in price than official inflation. These are goods like food and electricity.

While tax revenue and the payment of government debt to financial institutions and the rich constituency goes up (the majority of whom are in South Africa), the spending of national, provincial and local government as a share of all spending (GDP) goes down. Instead of “taxing the rich” the government has been “borrowing from the rich,” and is right now at peril of doing this at higher and higher interest rates. There has been an increase in interest payments on government debt, reflected by its increasing share in the GDP (from 2.6% to 3.5% between 2012/13 and 2018/19) and in terms of its share of the tax revenue (depicted in Figure 3, from 10.8% to 12.4%). This is the result of a rise in loan interest payments, from R88 billion to R179 billion on the growing state debt or with the same period.

Debt service will be more expensive if (1) the credit ratings agencies downgrade the government’s credit ranking, which would, in turn, increase the interest on the debt; and (2) if the government continues borrowing from the financial markets, instead of using funds under its control – most importantly, the R1.8 trillion Public Investment Corporation (but this and other reforms would be a subject for further discussion in another booklet).

It’s safe to say that Figure 3 indicates so-called “austerity” from the 2016/17 Budget. We have come to a point where the government’s fiscal policy undermines democracy. Communities, workers and students are increasingly met by violent police repression. In turn, social protests are also becoming more and more violent, either through manipulation from vested interests or simply in a desperate attempt to catch the attention of an unresponsive local state. Tax revenue as a share of GDP is now being allowed to grow, but to service interest payments to profit-maximising creditors. It is a tragedy that this is happening after 15 years of not using this tool to solve the long crisis in public services and fulfil longstanding promises, like free higher education.

The “25% rule” in the 1996 GEAR document

Available evidence indicates that the tax-pegging rule surfaced officially in 1996. The GEAR document from that year spelled out that the aim was to maintain a ratio of tax to GDP of about 25% for fiscal policy.⁴² The whole passage reads:

The improvement in economic growth, together with improved tax administration, should lead to a strong increase in tax revenue relative to GDP.

⁴² The Treasury. (1996). *Growth, Employment and Redistribution: A Macro-economic Strategy*, (GEAR), www.treasury.gov.za (accessed 9 June 2011), p. 8.

This will create considerable scope to effect further reductions in the rates of personal and corporate taxation, while maintaining a ratio of tax to GDP of about 25 percent.⁴³

The argument above proceeds in two steps: First, there will be higher economic growth and “improved tax administration.” Between the lines, “improved administration” means bringing tax dodgers and people in the informal economy into the tax system. This ongoing process is clearly visible in the statistics of the last 15 years, and it has contributed a lot to increasing tax collections. Still, hundreds of billions of rands continue to be lost: (1) to enormous illegal capital outflows, (2) to high-income South Africans remaining outside the system, and (3) to aggressive individual and corporate tax planning, engaging in transactions with bank accounts in the so-called “tax havens” to avoid taxation. The second sentence in the quote from GEAR puts forward a political choice; though it is not presented as a choice, but as a natural or “self-evident” outcome: The “considerable scope” provided by growing the national income through better tax administration would be used to cut tax rates for companies and individuals. This will, in reality, fuel social unrest: it will increase inequality and avoid a ramp up of public services. The thinking (in line with neoliberalism) is however that this would “attract investors” or enhance economic growth. This is how the government proceeded.

If tax rates had simply been left as they were, the “considerable scope” would have allowed for a larger and more efficient public sector as a share of the whole economy, providing a greater level of decent services. Instead, we witnessed the outsourcing of all basic services staff at higher education institutions from 2000, as well as the actual cutting of staff in public health between 2000 – 2005, to mention only two damaging repercussions of this decision.

Again, what was at stake was free higher education (already promised in the 1998 national election), the plan for a national health insurance (announced publically in the mid-2000s), overcoming the housing and sanitation crisis, and dealing with the primary education crisis (the legacy of Bantu education and overcrowded class rooms in public schools). Even so, this list is far from complete. At the very least, we needed a policy that would have read something like: *“This will create considerable scope to largely maintain the rates of personal and corporate taxation as they are, using economic and income growth to build a capable and larger public service sector as a share of the whole economy.”*

⁴³ The Treasury (1996), *Growth Employment and Redistribution*, (GEAR), p. 10.

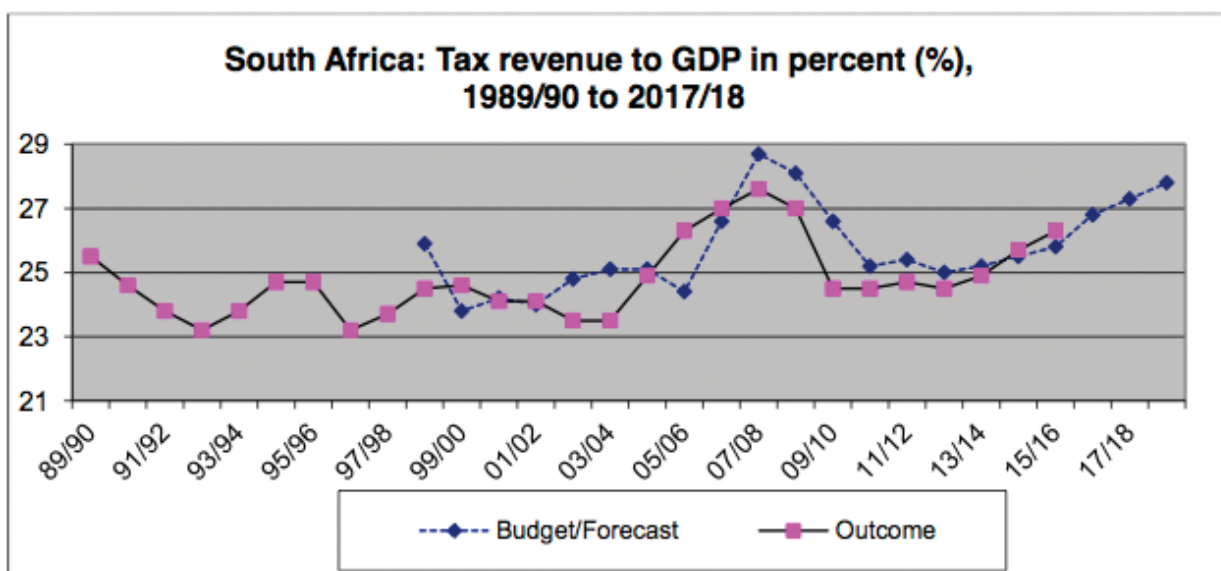


Figure 4: Tax Revenue to GDP in percent, from 1989/90 to 2017/18 (the last three years are forecasts). This is built on The National Treasury’s Budget Reports from 1989 and forward, available at www.thetreasury.gov.za). Table 1.6 in the 2015 *Tax Statistics* gives numbers that are about one percentage point lower for the period 1995/96 – 2015/16.

Former President Thabo Mbeki has argued that there was nothing “neoliberal” about government policy under his presidency, and he challenged his critics to prove the opposite.⁴⁴ But the passage quoted above from the GEAR document in fact confirms the neoliberalism of the ANC government, adopted under the presidency of Nelson Mandela and maintained throughout Thabo Mbeki’s presidency.

GEAR took a fork-in-the-road decision for fiscal policy. We are paying the price today. If there was ever any attempt at establishing “social democracy” through the ANC’s fiscal policy from 1994 to 1996, then GEAR ended any ambiguity or vacillation about which way the ANC was headed.

Tax pegging and the negotiated settlement

The tax pegging rule surfaced publically in 1996. Budget statistics show that the tax revenue to GDP was generally below 25% from 1989 onwards.⁴⁵ The bump in Figure 4, around 2007 - 2009 where the ratio exceeds 25%, is explained both by the economic boom of 2005-2007 (with higher profits and incomes) and the subsequent contraction of the economy in 2008/2009. When production of goods and services (or “GDP”) fall, tax revenue as a share of GDP can increase, because tax collections are “sticky,” meaning that for a while they

⁴⁴ <http://www.sahistory.org.za/archive/gear-and-neo-liberalism-part-2-thabo-mbeki-28-march-2016>

⁴⁵ Budget summaries from 1998 and 1999, published on www.thetreasury.gov.za (accessed August 2012), give data back to the 1989/90 fiscal year. They have been used in Figure 4.

continue as they were before, even when the economy contracts.⁴⁶ Thus, the retrenchment of over a million workers during the crisis only impacted on the collection of taxes, PIT and VAT, in subsequent periods (even though the vast majority of these workers' incomes were below the PIT threshold). In addition, more people and previously informal companies were brought into the system as usual, before and during the 2008-2009 crisis (the "administrative improvements" were not affected).

The 2012 Budget Speech

Either the 2006/2008 higher tax to GDP ratio was predicted in the government budget, or there was a temporary policy departure from GEAR during these years. Be this as it may, in 2012 Finance Minister Pravin Gordhan again felt obliged to confirm the 25% policy. It was as though he needed to reaffirm the sanctity of a small public sector – promised in 1993, confirmed in GEAR in 1996 and reassured by President Zuma's 2011 SONA speech that South Africa "is not a welfare state." In the 2012 budget speech, Pravin Gordhan re-announced the 25% tax to GDP policy, saying that one of the "key features of the budget framework include[s] ... tax revenue stabilising at about one-quarter of GDP."⁴⁷ Likewise, the budget review covering 2012/2013 budgeted for a ratio of 25.0% – to the exact decimal point.⁴⁸ Treasury officials, however, have denied (during public workshops and seminars) that there was ever any 25% tax revenue to GDP policy in place. And the rule has indeed subsequently been "violated" from about 2014, but now to finance growing interest payments on the state debt, not in service of a larger public service sector. We will discuss this further below. In 2010, COSATU was evidently unaware of the 25% rule or of its importance, when proposing a "solidarity tax" as well as increased taxation of the "super-rich."⁴⁹ But the People's Budget Campaign (PBC) – which joined together Cosatu, SANGOCO⁵⁰ and the SACC⁵¹ – raised the issue as far back as 2005. The PBC demanded that the tax revenue to GDP ratio be raised by three percentage points: "to 28.5%."⁵² However, the left and the labour movement seem to have been generally unaware of the small public sector dogma the government was following. Whatever the case, credit ratings agencies and corporate business economic policy watchers have most likely been aware of it.

⁴⁶ The measure is a *ratio*. If the number below the line in a fraction becomes smaller and the number above it stays the same, the ratio increases – e.g. $\frac{1}{3}$ is smaller than $\frac{1}{2}$.

⁴⁷ Budget Speech 2012: www.thetreasury.gov.za (accessed 11 September 2012).

⁴⁸ The National Treasury, Budget Review 2012. Pretoria: Department: National Treasury, p. 48.

⁴⁹ Cosatu. (September 2010). *Growth Path for Full Employment*. www.cosatu.org.za (accessed September 2011).

⁵⁰ South African Non-Governmental Organisation Council.

⁵¹ South African Council of Churches.

⁵² People's Budget Campaign. (2005). *People's Budget 2006/2007*, p. 45.

The policy has thus far blocked a “fundamental and irreversible shift of wealth and power in favour of working people and their families,” to repeat Harold Wilson’s words. With this policy it was not possible to shift resources from private to public healthcare through national health insurance (NHI), to make higher education free or to insource outsourced workers at tertiary colleges and, more generally, in the municipalities. Indeed, when the tax cuts started in 2000, this went hand-in-hand with outsourcing and the freezing of posts.

In conclusion, it’s highly probable that a part of the secret agreement reached in the Transitional Executive Council in 1993 was to keep the relative size of tax revenue at more or less the same level as under late apartheid. This is in line with the cardinal requirement of neoliberalism worldwide that redistribution through taxation must be limited. In South Africa this means that the lifestyles and social values of the privileged white minority weren’t disturbed; though today the new black elite can also enter the same golden gate of low taxation on high incomes.

Alternative tax revenue “goals”

To borrow from the rich or to tax them?

Governments around the world always borrow money from rich citizens, financial investors and private companies that sit on huge amounts of cash.⁵³ Such loans – called state or government bonds – must be paid back together with interest (making the creditors richer⁵⁴). The idea is to use the borrowed money for investments in infrastructure. Loans from pension funds have also often been used for this purpose. Projects like the 1998 arms deal, Eskom’s two giant coal power stations or the plus R1 trillion plans for nuclear power corrupt this idea: Unnecessary weaponry produces no wealth, but is a pure cost, the pollution from coal energy is already very costly to our health and to the climate; nuclear power is extremely expensive compared to renewable energy and dangerous to us or to future generations that must take care of the toxic waste. In Europe, the idea of using state debt for the long term common good has been corrupted by bank crashes: governments have bailed out the bankrupted banks with borrowed money and are now paying back loans through cutting funding to public services.

⁵³ Such loans pay for the difference between the ordinary expenditures and incomes of the government. This difference is “the budget deficit.” In a growing economy, the government can pay back such loans over time if they are not too big. A benchmark ratio for budget deficits in Europe has been “3% to GDP.” For developing countries, a “6% to GDP” budget deficit was generally accepted by mainstream commentators before the global crisis. Their economies were expected to grow faster than the economies in the North, making it easier for governments to pay back loans. The budget deficit of the SA government is now over 4%. In the 2016 Budget Review, the Treasury has promised the credit ratings agencies that they will cut the budget deficit to below 3% by applying austerity measures.

⁵⁴ “Creditor”: the one who gives a loan.

If a future South African government decides to make a qualitative break with the old economic regime, and if corruption and “wasteful or fruitless expenditure” can be halted, then every increase in the provision of social services means that the state will need to replace or redirect some of the individual consumption and economic demands of the minority with the “collective consumption” of public services, such as education and healthcare.

One suggestion from the so-called Macro Economic Research Group (MERG) in 1993 was that the total government revenue should gradually be increased to about 32% of GDP by 2002.⁵⁵ MERG argued that sufficient redistribution of income – in order to deal with all backlogs, to deliver good public services to all citizens regardless of “colour,” as well as to provide enough extra support to the poor – would not take place otherwise.

The MERG report was supported by Cosatu but brushed aside by the ANC upon its publication in 1993.⁵⁶ From 1996 onwards, the new government embraced the neoliberal rejection of “the welfare state” and the fiscal priorities to which it gave rise.

Successive Budget Reviews, published every year ahead of the Budget Speech of the Treasury, show that “incomes other than taxes” (with royalties from mining being the most important) added between two and three percentage points to the total ratio of revenue to GDP. Keeping this in mind, an overall revenue of 32% to GDP actually means a ratio of tax revenues to GDP of about 29.5%. If the MERG recipe had been in place at the time of Gordhan’s budget speech 2012, the extra 4.5% would have added close to R150 billion in tax revenue to the 2012/13 budget.⁵⁷ This would have accounted for 15.5% of his 2012 budget, without taking the R89-billion of that year’s state debt costs into account. But if a greater portion of government expenditure had been financed by taxes instead of loans, these debt costs would be lower.

⁵⁵ MERG. (1993). *Making Democracy Work: A Framework for Macroeconomic Policy in South Africa: A Report from the Macroeconomic Research Group*. Cape Town: Centre for Development Studies, University of Western Cape. On page 40 in the MERG report, the argument is confused by a reference to tax revenue to GDP of about 32.5%. It is clear from other parts in the report though, that the authors mean total revenue and not only taxes. The confusion between tax revenue and total revenue is common. On the popular *Wikipedia* website (accessed 3 November 2012), a 26.9% “tax” to GDP ratio is given for SA, but this is the total revenue to GDP ratio. The fiscal policy chapter in the study by Robert Pollin et al. (2006), *An Employment-Targeted Economic Program for South Africa* (Amherst, USA: PERI and University of Massachusetts) pages 84ff, also focuses on the tax revenue to GDP ratio and suggests a very cautious increase, with a little more than one percentage point, to 26% odd at that time.

⁵⁶ Terreblanche, S. (2002), p. 86.

⁵⁷ Calculating with a GDP 2012/13 of R3200 billion: 4.5% of R3200 billion is R144 billion.

Could there be merit, therefore, in reviving the MERG standard of 29.5%, or even in completely disregarding tax pegging as a policy tool? Is it economically viable? Is it politically possible?

A variety of tax regimes over the world, in countries with different histories and with different pressing issues, show that it can be done. The question for us is whether it can be done in South Africa.⁵⁸ It is a political issue. The small South African middle class and top income earners enjoy a European middle class and upper class standard of living.⁵⁹ Can they really not afford the higher taxes of the usual European tax ratio to GDP, ranging from 30 to 45%?

5. More on the “tax relief” policy

Judging from history, since 1994 the government wouldn't have had to do anything special to increase tax revenue as a share of GDP. It merely had to refrain from making large tax cuts every year. The annual Tax Statistics publications provide us with enough data to illustrate this.

Tax brackets, progressive taxation and “bracket creep”

So far, we have seen the SA Revenue Service (SARS) and the Treasury, in the yearly Tax Statistics publications, provide an account for the reduction in tax pressure on individuals since the 1999/2000 budget. The recurrent line is “Fiscal drag relief.” This refers to the effect of inflation on tax rates.

We have also seen that if the six tax brackets in the tax system were not adjusted upwards with inflation, then a person would pay a little more in personal income tax (PIT) every year, even when their wage increases only follow inflation. The buying power of one's income before tax would stay the same, but a slightly larger part of the wage in rand would land above the next tax bracket. That part of the wage could then be taxed at a higher rate than before. The real tax pressure on a certain standard of living would then increase. This is called “bracket creep.”

⁵⁸ Table in Robert Pollin et al. (2006), p 86, shows a wide range of different “tax revenue to GDP,” from country to country. Currently, the USA – which has a very similar structure in its health system to South Africa – has a ratio of about 27% tax revenue to GDP.

⁵⁹ In their income reports, the Bureau of Market Research (referred to above) divides the SA “middle class” in 3 groups. For 2011, the BMR sets the “low emerging middle class” in the income range from R50 000 to R100,000, the “emerging middle class” from R100 000 to R300 000 and “the realised middle class” from R300 000 to R500 000 in yearly income.

Bracket Creep

A person earns R100 000 per year and stays in a country where you pay 20% in income tax for anything that you earn above R100 000. Let's say that inflation (the average price increases) is 5% over a year. Let's also say that this person gets a wage increase of 5%, so that he or she now earns R105 000. The extra R5 000 will not change the person's living standard, because the prices have also gone up by 5%. The tax on the R5 000 above the tax bracket will, however, be 20%, or R1 000, leaving him/her with R104 000 after tax. Consequently, taxation has become harder. This is called "bracket creep." If the tax bracket had also been adjusted by 5%, to R105 000, then the taxation on a certain living standard would have remained the same – the person would then continue to pay R0 in tax.

For 15 years South African finance ministers have spoken about "bracket creep" or "fiscal drag" in every budget speech. The notion of compensating for bracket creep has become an ideological fig leaf, covering up the reducing of overall tax pressure. The tax pressure on individuals has, in fact, dropped much more than the adjustment for "fiscal drag" or "bracket creep" can motivate.

In the 2016/17 budget, however, the government, for the first time since 1994, took a step in the opposite direction. It lifted the tax brackets for the four lowest income levels below the projected rate of inflation and even lowered the tax bracket for the two income levels at the top. However, we also saw that it increased the "medical tax credit relief." This tax subsidy benefits the medical insurance industry, by the way, because the usual 10% annual price increase on medical insurance becomes obscured and evades being politically challenged: Now it is not fully paid by the minority with private medical insurance, but by all South Africans, including the households that both see the real value of pensions and childcare grants decrease as a result of such arrangements and who anyway solely use public healthcare.

At any rate, the net effect of these two measures for a certain income level (or lifestyle) lowered the total income tax payable by R6.6 billion. For taxable incomes above R1 million, the average of about R2 100 – R2 200 in lower income taxes per year was the result of allowing higher medical aid deductions from the taxable income. For a fixed income at the top, the increased right to medical aid deduction effectively "won" over any gains achieved by lowering the two top brackets by 0.7% and 1.1% respectively.⁶⁰ The interested reader can study this table from the 2016 Budget Review, but should also note that the government plans to get back more than R6.6bn (R1bn more) when the PIT payers get their wage increases and are partially "hit" by bracket creep (when tax brackets are lifted less than the rate of inflation or when they are lowered).

⁶⁰ The Treasury, *2016 Budget Review*, p. 46f.

Table 4.7 shows how much tax is expected to be paid by individuals at different levels of taxable income for 2016/17.

Table 4.7 Estimates of individual taxpayers and taxable income, 2016/17

Taxable bracket	Registered individuals		Taxable income		Income tax payable before relief		Income tax and medical tax credits relief		Income tax payable after relief	
	Number	%	R billion	%	R billion	%	R billion	%	R billion	%
R0 - R70 000 ¹	6 619 854		178.2		-		-		-	
R70 001 - R150 000	2 583 046	36.3	271.9	12.5	12.6	2.8	0.6	9.1	12.0	2.7
R150 001 - R250 000	1 733 463	24.4	338.8	15.6	35.7	8.0	1.2	17.7	34.5	7.8
R250 001 - R350 000	1 071 798	15.1	317.9	14.6	49.5	11.1	1.3	20.0	48.2	10.9
R350 001 - R500 000	800 990	11.3	330.7	15.2	66.1	14.8	1.5	22.5	64.6	14.6
R500 001 - R750 000	497 722	7.0	300.7	13.9	75.9	17.0	1.1	16.3	74.9	17.0
R750 001 - R1 000 000	197 813	2.8	169.8	7.8	50.3	11.2	0.4	6.6	49.9	11.3
R1 000 001 - R1 500 000	136 782	1.9	163.4	7.5	53.6	12.0	0.3	4.6	53.3	12.1
R1 500 001+	94 578	1.3	276.5	12.7	104.0	23.2	0.2	3.2	103.8	23.5
Total	7 116 192	100.0	2 170	100.0	447.6	100.0	6.6	100.0	441.0	100.0
Grand total	13 736 046		2 348		447.6		6.6		441.0	

1. Registered individuals with taxable income below the income-tax threshold

Source: National Treasury

Figure 3: Table 4.7 from the 2016 Budget Review.

Figure 3 pertains to how an individual income within 8 levels is affected by these changes. The PIT system space within the realm of tax cuts. The game of tax gains and losses becomes complicated, but all the measures relating to the PIT summed up to plus-minus zero in the 2016 budget. 90% or nine out of every ten rand in tax income increases in the 2016 budget came from a R9.1bn increase of taxes on fuel, alcohol and tobacco. The two-legged strategy remains in place: fiscal policy continues to rely on growth and the hope of better tax administration, not redistribution.

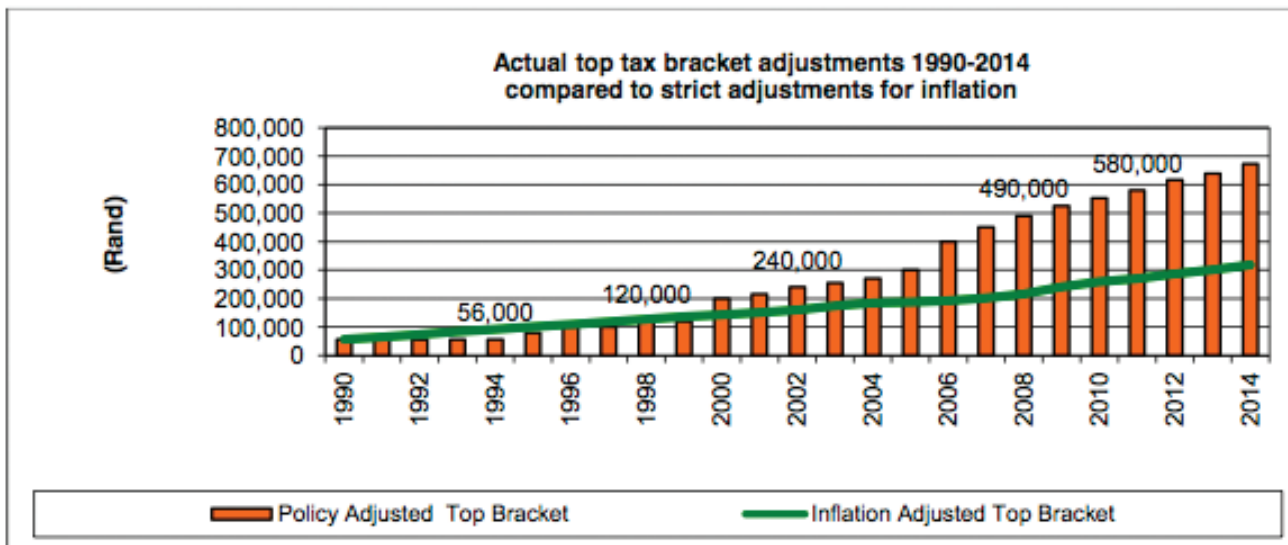


Figure 5: Tax cuts veiled as “adjustments of tax brackets for inflation” 2000-2014. (Source: The National Treasury’s Budget Reviews, Stats SA Consumer Price Index and own calculations)

If the highest tax bracket had been adjusted at the rate of the inflation only; then the 40% personal income tax would, in 2014, be levied on the income that fell above R318 000 per year, not R673 100

per year (Figure 2). The exaggerated adjustment for inflation started in 1999/2000, when the highest personal income tax rate was also adjusted from 45 to 40% in two steps.

Lower and lower “tax pressure”

If the government had stuck strictly to compensating taxpayers for “fiscal drag” or “bracket creep” since 2000, the politics of the system – which answers the question, “How much should we tax a certain life style?” – would simply have remained the same over the years.

The Tax Statistics publications, in fact, appear to argue that the politics of the system has been exactly that: the same. Every year, the authors state that it is “indicative of the effectiveness of combating fiscal drag through tax relief” that tax assessed as a percentage of taxable income has stayed “relatively stable around 21%.”⁶¹ We should now see that this is an error. Over the years, the living standard has increased among those who pay PIT, and most definitely among the higher income earners. If taxation on a given living standard had “remained relatively stable” during the whole period, the total sum of tax assessed as a share of the total taxable income would, inevitably, have increased. Most tax payers’ incomes have increased over the years and, all the more so, among high income earners. The Tax Statistics provide information that makes this claim irrefutable.

More than R190 billion in forfeited tax revenue in 2014 alone

R100 000 in 1995 and R310 000 in 2014 bought about the same amount of goods and services (Figure 2). If the tax policy had been fixed since 1995-2000, the same yearly income in real terms (15 to 20 years apart, but allowing for about the same life style) would have been taxed at 33.8% in 2014. It was actually taxed at 18.2%. The excessive tax relief, those missing 15.6 percentage points, corresponds to R48,400 less in tax paid on the same real income in income individual than would have been the case with a stable tax policy. The total of over R190 billion in forfeited taxes in 2014 alone can be roughly estimated by taking the tax cut in each income group and multiplying it with the number of people in that group as reported in 2015 *Tax Statistics*.

⁶¹ 2011 *Tax Statistics*, p. 25. The phrase “effectiveness of combating fiscal drag”... and so on, is repeated in the following years.

Table 1: Personal Income Tax (PIT) reductions since 1994/95

Table 2.2: Tax relief granted to individuals, 1995 and 2014

Taxable income		Tax at 1995 rates		Tax at 2014 rates	Effective rates		
Rand					Tax at 1995 rates		Tax at 2014 rates
1995 ¹	2014 ²	1995 ¹	2014 ³	2014	1995 ¹	2014 ³	2014
22 000	68 168	2 385	20 077	190	10.8%	29.5%	0.3%
25 000	77 464	3 225	24 074	1 863	12.9%	31.1%	2.4%
30 000	92 956	4 625	30 736	4 652	15.4%	33.1%	5.0%
40 000	123 942	8 225	44 060	10 230	20.6%	35.5%	8.3%
50 000	154 927	12 325	57 384	15 807	24.7%	37.0%	10.2%
100 000	309 855	33 765	124 002	56 347	33.8%	40.0%	18.2%
200 000	619 709	76 765	257 240	165 946	38.4%	41.5%	26.8%
300 000	929 564	119 765	390 477	289 510	39.9%	42.0%	31.1%
400 000	1 239 419	162 765	523 715	413 452	40.7%	42.3%	33.4%
500 000	1 549 273	205 765	656 952	537 394	41.2%	42.4%	34.7%
600 000	1 859 128	248 765	790 190	661 336	41.5%	42.5%	35.6%
700 000	2 168 983	291 765	923 427	785 278	41.7%	42.6%	36.2%
800 000	2 478 837	334 765	1 056 665	909 220	41.8%	42.6%	36.7%
900 000	2 788 692	377 765	1 189 902	1 033 162	42.0%	42.7%	37.0%
1 000 000	3 098 546	420 765	1 323 140	1 157 103	42.1%	42.7%	37.3%

1. Excludes the Transitional Levy.
 2. 2014 taxable income based on 1995 taxable income adjusted by inflation.
 3. This example assumes no fiscal drag relief over the period 1995 to 2014 (i.e., the tax rates are kept at 1995 rates).
 Source for Consumer Price Index (CPI) data: Statistics SA.

Table comparing tax pressure 1995 and 2014 (Treasury and SARS, 2015 Tax Statistics, page 33).

The information in 2015 Tax Statistics also allows us to estimate what the changed tax policy meant to PIT paying individuals in 2014, when compared to 1995-2000.

The two middle columns in section 2 and 3 are irrelevant and only confuse the matter. Instead, we simply “tax” the second column (labelled “2014”) in the first section with the “Tax at 1995 rates” (same tax rate as in 1995) and compare this with the “Tax at 2014 rates” to the far right. The taxable income of R500 000 in 1995 corresponds to a taxable income of R1 549 000 in 2014. Instead of letting the tax rate of 41.2% on this lifestyle stay put over the years, the tax rate on that buying power has decreased to 34.7% today (left and right columns in section 3; the middle column can be disregarded).

We can in fact plot the 15 different income levels provided by the table in 2015 Tax Statistics and create a “Tax Cut Manual,” as shown in Figure 6. It represents the political change in the PIT system.

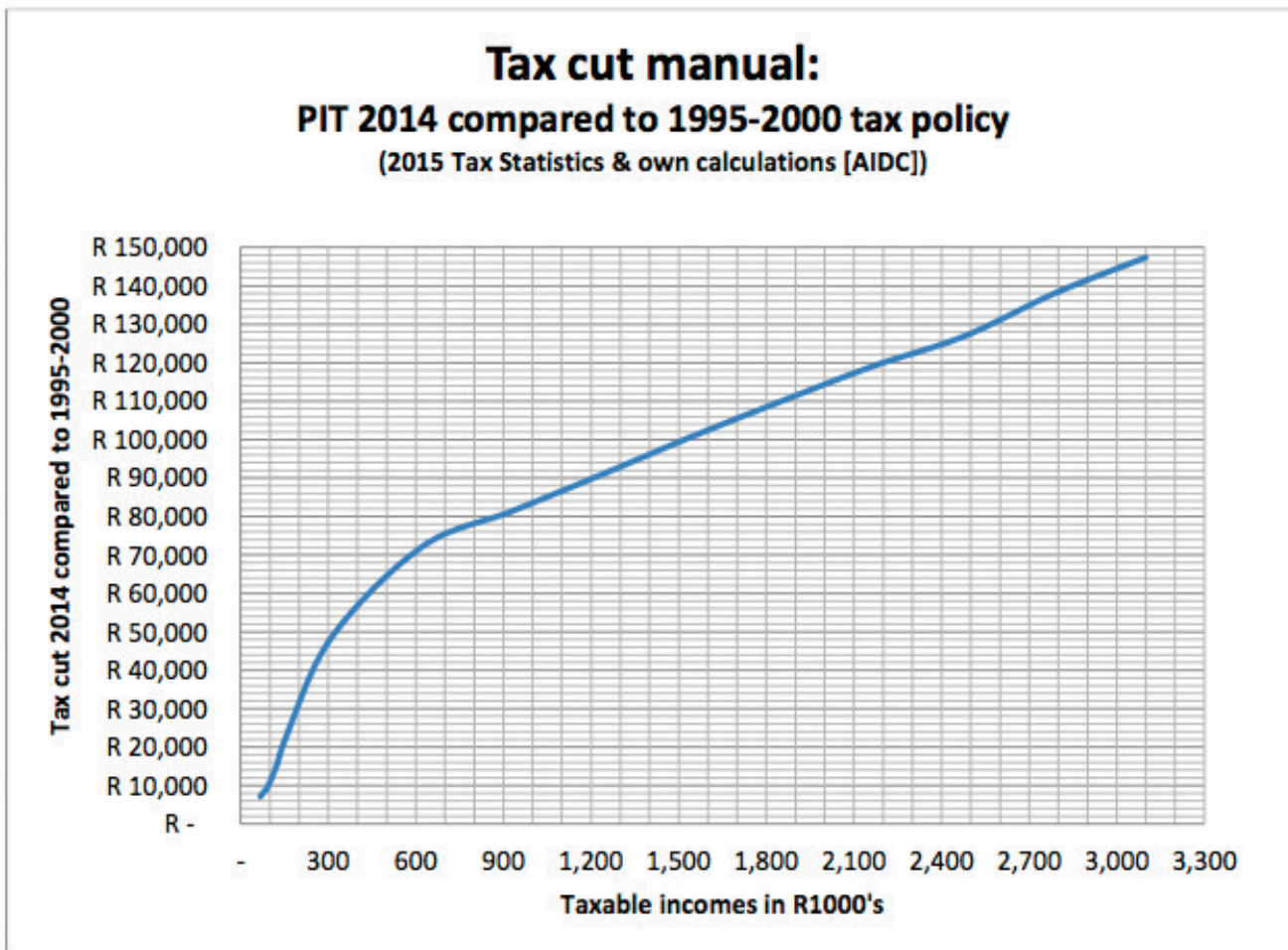


Figure 6: Calculation key to loss in tax revenue, 1994/5 as compared with 2013/14

Choose a taxable income on the horizontal line (where "1 500" = R1 500 000)! Go straight up to the corresponding point on the schedule. Read the lower tax when comparing 2014 with 1995-2000 on the vertical scale! A taxable income of R200 000 in 2014 is taxed R31,000 less as a result of the policy changes. A taxable income of R2mn is taxed at R114 000 less in 2014, compared to the rates of an unchanged tax policy (Source: Table 1). From the point of view of the public service sector, this "tax cut manual" is also a key to the 2014 loss in tax revenue.

Keeping personal income tax policy constant over the years – with no tax policy change – would have increased tax revenue as a share of the national income ("GDP") in the fiscal year of 2014/15 from 25.7% to 30.3% (i.e. by over 4 percentage points).⁶²

Is it politically feasible with today's realities to reverse the tax cut policy? A direct and immediate restoration of tax levels to from before 2000 for all income groups would mean that a worker with an yearly income R2500 over the first tax bracket (R77 500 per year) would pay R10 000 rather than R1,900 in PIT in 2014. But the lowest level PIT payer of today is also most likely supporting several other unemployed individuals, because of the very rapid growth in working class unemployment that we have been facing since before 2000. The "dependency ratio" (the number of people supported by one person's income) has increased

⁶² National Treasury (2012), Budget 2016, p. 45.

among the vast majority of employees. This makes it problematic for a government to embark on an “across the board” course.

By contrast, high unemployment is not a problem in middle and upper class families, which, moreover, have become even richer with the passage of time. A large increase in personal income tax for these groups would still leave them rich, by any standards.

In this regard, it is worth recalling that the immediate post-apartheid Government of National Unity introduced a Transition Levy (“to defray the greater part of the transition costs”) of 5% on incomes above R50 000 for individuals and businesses (a little more than R160 000 in 2014 value of money). This tax hike left the rich with quite a lot left, and it was not opposed. The extra tax lasted for 12 months, during 1994 and 1995. Given the much smaller number of people that were paying personal income tax, and the need to abolish tax rules that discriminated against women (for example by taxing the incomes of married women at a higher rate than the incomes of married men)⁶³, Finance Minister Derek Keys (coming from the strata of mining business executives and personifying the continuation of the economic regime) predicted in his budget speech that the extra tax on high- income earners and profitable firms would bring in R3.4-billion, the equivalent of about R10.5 billion in 2014 prices.⁶⁴

Conclusion: Lower tax pressure and less and less progressive tax system

Taxation on all personal income taxpayers has been greatly reduced since 1999/2000. The top marginal income tax rate for individuals decreased from 45% in 1999/2000, to 42% in 2000/2001, and then to 40% in 2002/2003. During this period, the personal income tax brackets were also significantly increased; this more than compensated for any fiscal drag.⁶⁵ The increase of the top tax bracket from R300 000 to R400 000, in one blow in 2005 (Figure 2.3), of course has nothing to do with “adjusting for inflation.”

To explain once again: Imagine a country with only one citizen. Imagine that he or she attains a higher and higher living standard every year (which is the case for over 5 million personal income taxpayers in South Africa, and especially the half a million of those at the top).

⁶³ And taxing married persons higher than unmarried persons: Together with the higher taxation for married women than “married persons” (“persons” is the word for “men” in the legislation) this effectively told women to stop doing paid work when getting married. Terence Smith (1999 [?]), “Women and tax in South Africa,” <http://www.internationalbudget.org/wp-content/uploads/Women-and-Tax-in-South-Africa.pdf>

⁶⁴ Derek Keys’ Budget Speech 1994, available together with other speeches at www.treasury.gov.za 65 2008 Tax Statistics, p. 29.

In a progressive taxation system this person inevitably pays a larger and larger share of his or her income in tax. He or she pays according to the ability to pay, and this ability is improving every year. The South African tax system is designed to be such a *progressive* system. However, if this one person instead pays a *constant* share of their income in tax, despite their real income getting bigger every year, the tax system is getting less and less progressive, and taxation of personal incomes is getting lighter and lighter. This is what has happened to personal income taxes in South Africa since 2000.

The fallacy of the “narrow tax base” argument

The more unequal the distribution of income in this country, the more irrelevant is the “narrow tax base” argument. As long as the current income distribution prevails, then personal income taxes (PIT) can only be paid by a small proportion of wage earners, as the poor get poorer or just see no change, but the rich get richer. Thus, there is a direct cause-and-effect relation between an extremely unequal income distribution and a narrow tax base. In 2010, about 58% of all individual income accrued to 10% of the population.⁶⁶ That is why they were also the population who paid more than half of the total income taxes. Their share of the PIT payments will increase as inequality increases! And the tax base for PIT will indeed be “narrow.” Ten percent of the adult population is paying over half of the personal income tax, because they earn over half of all the personal incomes in the country.

There is a strange general lack of awareness surrounding this matter-of-fact situation. The view commonly presented in the media is that a “narrow tax base” means these earners can’t possibly contribute more, because the base is “narrow.” This view conveniently ignores the reality of South Africa becoming increasingly unequal; that a minority have run away with their incomes and that the personal income tax is becoming less and less progressive. Most importantly, on the individual level, the rich and the small middle class have been paying a smaller and smaller share of their ever growing income in tax.

If, for argument’s sake, the entire national income went to one person only, a progressive tax system would tax him at a rate of 99.99%, even though he would likely complain about it being unfair to “overburden” him, as he is “such a narrow tax base.” But as the 0.01% that was left over would remain in his possession (it would very likely be a “he”), he would be extremely well-off and empowered by this money.

⁶⁶ See, for instance, McLeod, H. (August 2011). National Health Insurance Policy Brief 20, *The Tax Base in South Africa: Innovative Medicines*. www.imsa.org.za

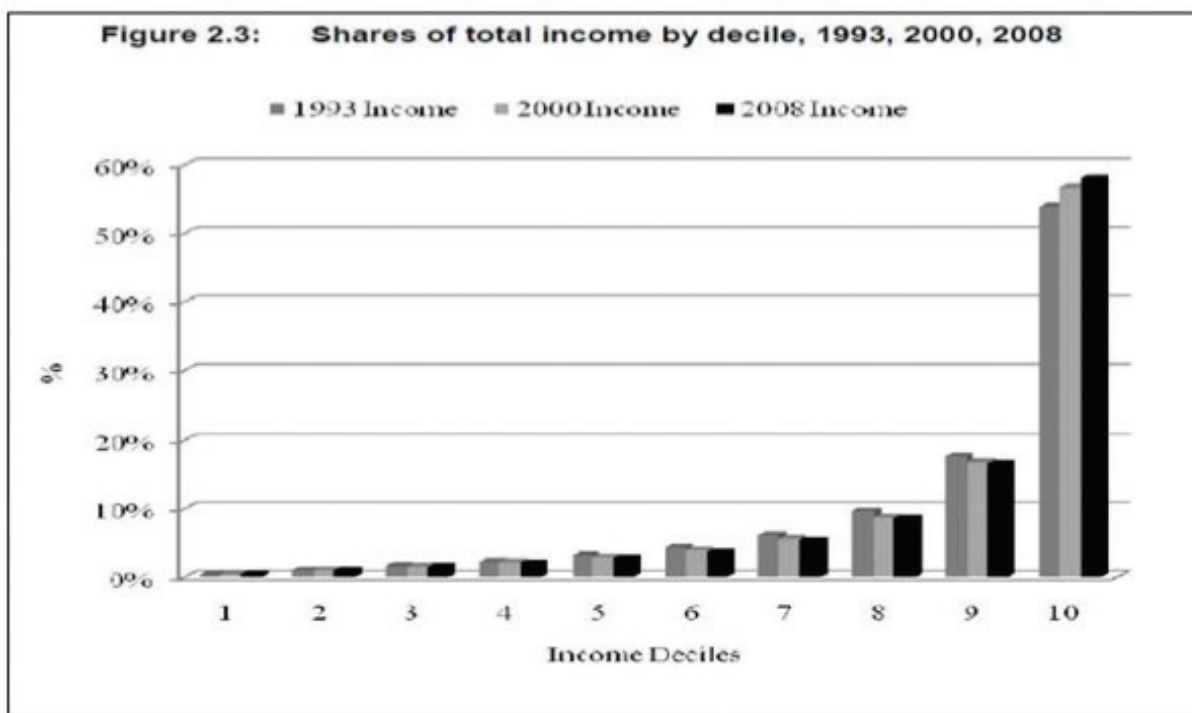


Figure 7: An unequal society produces a “narrow tax base” (Diagram from Leibbrandt et al (2010), page 25. This diagram also shows income decile 10’s (top 10%) growing share of the total income).

6. The missing “high net worth individuals” (HNWIs)

The Finance Minister was asked in Parliament on March 2012 about “9 300 South Africans,” suspected by SARS of evading personal income tax.⁶⁷ Although these individuals were assumed to have an annual income of over R7 million and/or of owning wealth of over R75 million, 7 000 of them are not even on the tax registers.⁶⁸

The Minister’s reply was significantly at odds with higher numbers already in the public sphere. But even if only using the 7 000 number, the tax loss in 2012 was at least R19 billion. SARS, however, found close to 30 000 HNWI’s during one year of investigation, 20 000 of them after contacting only one financial institution.⁶⁹ The number of taxpayers declaring taxable incomes above R5 million (close to the HNWI threshold) remained a little above 2 000 individuals in 2008, 2009 and 2010.⁷⁰ In 2015 they are about 4 200 individuals.

If every new batch of 10 000 tax dodging HNWI’s found by SARS starts to pay taxes (as do the 4 000 individuals who have a taxable income over R5 million), the state would collect another R40 billion per 10 000 super rich individuals, presently under the radar of the tax authorities. R40 billion is the equivalent to over 1% of GDP.

⁶⁷ Question number 260 (NW141E) from Mr G B D Mc Intosh (Cope) to the Minister of Finance.

⁶⁸ SA Revenue Service. (2011). “HNWI”; Power Point report (in our possession).

⁶⁹ In his reply in parliament on 9 March 2012, the Finance Minister forgot these 20 000 mentioned in the SARS’ internal report

⁷⁰ 2011 and 2012 Tax Statistics.

This begs the question: how many HNWI's are there really in South Africa?

HNWIs in South Africa

The Wealth Report 2010 issued by Knight Frank together with Citi Private Bank defines a HNWI as "a person whose investible property, excluding their principal residence, totals between \$1 million and \$10 million" – the equivalent of about R7 million and R70 million that year. According to the "Knight Frank Wealth Report," there were 96 000 such individuals in South Africa in 2009.

In its Global Wealth Report from November 2011, Credit Suisse expected the number of US dollar millionaires in South Africa to increase from the 71 000 in 2011 to about 243 000 by 2016. "According to Credit Suisse, 116 000 South Africans today are members of the global top 1% of wealth holders."⁷²

The political implication of the HNWI trail

Taking these estimates on board, the arithmetic of South African tax dodging becomes staggering.⁷³ Already, even if the SARS HNWI unit couldn't find more than 30 000 tax dodgers, the gain in yearly tax revenue from PIT from the dodgers would be well over R100 billion, or 2.3% of GDP in 2016.

The budgeted tax revenue for 2012/13 was R826.4 billion (all taxes), and all government revenue was R904.8 billion. State debt cost had increased by 16.6% from the year before; then in 2012/13 it was R89 billion, and by 2016/17 the debt service cost had reached R148 billion. Successfully combating super rich and corporate tax dodging in South Africa would allow for a completely different state budget.

These numbers do not only shed additional light on the "too narrow tax base" argument. The political implications of the SARS report, together with the interview with the head of the HNWI unit in January 2012, are encouraging. But then again, it would not be possible to reap such amounts of additional tax revenue from the super-rich without breaking the 25% tax revenue to GDP rule.

⁷² DLA Cliff Dekker Hofmeyer (2012), "TAX ALERT," Newsletter 20 January, p. 2.

⁷³ AIDC failed to get a comment from SARS on these calculation examples when the scandal exploded. The media officer answered that the calculations "might be wrong," and referred to The Finance Minister's answer in Parliament on 9 March 2012. SARS did not want to discuss the interview with Jonas Makwakwa, published on *MoneyWeb* in January or the internal report.

7. A critical test: NHI and the tax share of GDP

In 2011, the Department of Health (DOH) published a Green Paper.⁷⁴ It suggested that the public health sector should be doubled in strength between 2010 and 2025. Such a plan needs to be financed and there is a limit to possible reallocations within the budget. For one thing, already in 2011 it was extremely unlikely that economic growth will be above 3 or 4% every year for 15 years in a row. In 2016 the global crisis has diminished economic growth to below 1% per year. There have already had four years of growth below 3% per year since 2011 – indicating insufficient funds, in terms of the Green Paper calculation.

At any rate, if we take the cost estimations for the NHI, done by the DOH in its Green Paper, and if we assume a 3.5% average growth of GDP for the 14 year implementation period, then the cost share of Public Health to GDP grows with two percentage points, from 3.8 to 5.8%. Those extra two percentage points must be financed with taxes, which comprised 25% to GDP at the time of the Green Paper (2011) and 26.2% today. With today's average GDP growth being much lower than 3.5% per year, the reformed public health sector's share of GDP, as envisaged in the Green Paper, will be even bigger than 5.8% in 2025 (see Table 2).⁷⁵

⁷⁴ Department of Health (2011). National Health Act (61/2003): Policy on National Health Insurance, *Government Gazette*, 12 August 2012, No. 34523.

⁷⁵ The assumption of 3.5% GDP growth for 14 years in a row was indeed "optimistic." The Treasury projected a 4.2% GDP growth for 2012/13. Table 2 assumes "3.5% average growth in GDP." This is in the middle of the actual GDP growth rates during 2010/11 and 2011/12 and the Treasury's failed forecast for 2012/13. August 2012, GDP was expected to grow by less than 3% in 2012/13. August 2016, SA is close to zero growth.

Table 2: NHI as a share of GDP 2010-2025 in 2010 prices, assuming that GDP grows 3.5% per year on average from 2012 (GDP figures for 2010 and 2011 are given)

YEAR	Going from Public Health in 2010 to NHI in 2025, according to DOH (constant 2010 prices, R billion.)	Assuming 3.5% growth in GDP (in constant 2010 prices, R billion).	Percentage points increase in public health sector's share of GDP	NHI as a share of GDP
2010	101,0	2663	-	3,8%
2011	110,0	2745	0.2	4,0%
2012	125,4	2844	0.6	4,4%
2013	134,8	2944	0.8	4,6%
2014	144,4	3047	0.9	4,7%
2015	156,2	3153	1.2	5,0%
2016	166,7	3264	1.3	5,1%
2017	177,7	3378	1.5	5,3%
2018	189,1	3496	1.6	5,4%
2019	201,0	3619	1.8	5,6%
2020	213,6	3745	1.9	5,7%
2021	227,1	3876	2.1	5,9%
2022	236,0	4012	2.1	5,9%
2023	245,3	4152	2.1	5,9%
2024	255,0	4298	2.1	5,9%
2025	255,8	4448	2.0	5,8%

Source: Department of Health Green Paper on NHI (August 2011), 2012 Budget Review, and own calculations (GDP figures for 2010 and 2011 are given)

The same logic was followed by Di McIntyre and John Ataguba in their 2012 study.⁷⁶ They used a more sophisticated model and made their calculations using higher NHI costs than were projected by the DOH's Green Paper. Their study forecasted an even bigger increase in public health's share of the GDP when the NHI is fully implemented. They forecasted a 2.4 percentage point increase. Indeed, they assume as much as 4.5% average growth of GDP from 2014, taking this forecast from the Treasury's 2010 Budget Review. We know today that this forecast was completely wrong. The NHI will therefore have to be implemented in a period of protracted crisis.

If the whole economy will be smaller in 2025 than has been predicted by a 3.5 to 4.5% average growth rate, then the reformed public health sector will inevitably take up a larger proportion of the economy than 5.8 to 6.5%. The lower the GDP growth rate turns out to be, the more we will be forced to exceed the old "25% tax to GDP" ratio to implement an NHI to the standard that the DOH has set out in the 2011 Green Paper.

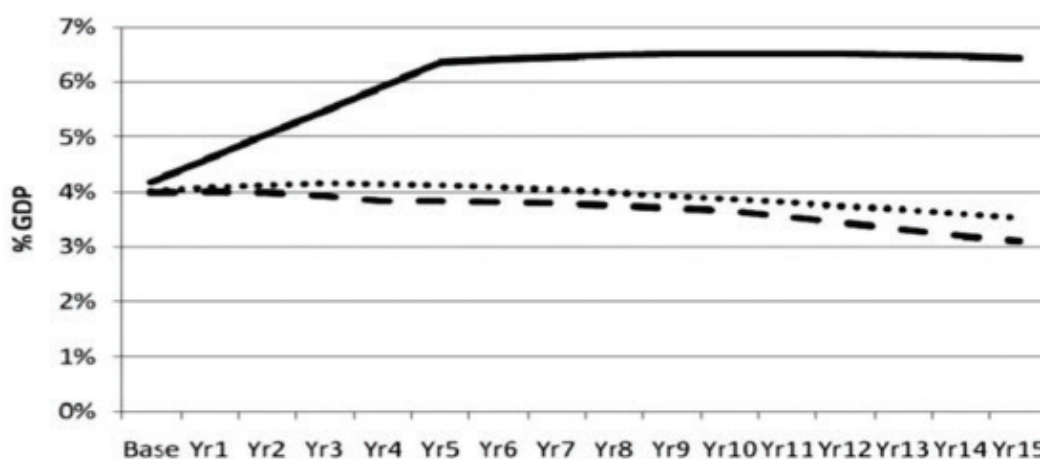


Figure 8: Public Health Services' future share of GDP, following McIntyre and Ataguba (2012: page i107).

McIntyre and Ataguba indicated that they have assumed a constant tax to GDP ratio in their model, and that they favour a reallocation of expenditures in the budget. However, their model demonstrated that tax revenue as a share of GDP must increase. In their conclusion they also "partly" advocated increasing taxation as a means to finance a NHI.

This discussion about the necessity of growing the size of public health in relation to the rest of the economy doesn't necessarily mean that in 2025 public and private healthcare together will comprise a bigger share of GDP – i.e., the annual production of goods and services – than today's 8.1%.

⁷⁶ McIntyre, D. & Ataguba, J.E. (2012). "Modelling the affordability and distributional implications of future health care financing options in South Africa," *Health Policy and Planning* 27: i101–i112, doi:10.1093/heapol/czs003.

To the contrary, the NHI presupposes a *shift* of resources from private to public health care, via cuts in tax subsidies to the private health sector and via a shift of demand for healthcare, from private to public.

This shift is more likely to happen when the public health sector improves its standard and reputation. Today about half of the healthcare provided is public, and it serves 84% of the population. Half of health spending, though, is private and serves 16% of the population.⁷⁷ Let us play with the thought that public health should, in the future, be used by 99% of the population, and that most of the spending on health will be public.

The drawn-out global crisis and continued low growth will perhaps also make it necessary to shift resources within reformed public healthcare itself, from high-tech hospitals and big institutions to primary healthcare and tens of thousands of unpaid community health workers.

This has for some time been suggested by the People's Health Movement: Not as an "austerity" measure, but as a move to towards a much better public health system. Indeed, if the crisis within housing, sanitation and water was to be addressed – something which can only be done by expanding the public service delivery sector – then less people would get sick. Similar arguments can be made in relation to outsourced workers, unmonitored violations of the Basic Conditions of Employment Act in the private sector (from labour broking to mining) and poverty wages (from farm workers, to domestic workers or women working in supermarkets). Public health is breaking under the pressure of the unfair and unequal society that in turn creates a sick population: poverty and inequality means bad health and early death.

Different alternatives for financing an NHI

There have been no other suggestions of how to finance NHI, other than through taxation. Universal coverage means that everyone will be insured. But the poor, the low-paid workers and the unemployed cannot reasonably be forced to pay for insurance in addition to taxes such as VAT and the Unemployment Insurance Fund (UIF). UIF, in practice and for that matter, is more like a tax on the formally employed. It serves only in part as insurance. Yearly, the UIF fund underspends R8- billion to R12 billion per year, despite more than 4 million people being officially unemployed.⁷⁸

⁷⁷ Di McIntyre at the International Public Health Movement Conference, 6 July 2012, UWC in Cape Town. This number has, however, been in the NHI debate since the Green Paper 2011.

⁷⁸ The underspending has been going on for many years, and is also budgeted forward in the yearly Budget Reviews. The accumulated UIF surplus is over R100 billion in 2016!

VAT?

An increase in VAT would increase the tax burden on workers and the poor more than it would for high income earners, who do not spend all their income on consumption and can save a lot of it. For this reason it should be ruled out. According to McIntyre and Ataguba, VAT would have to increase from the current 14% to 17%, if it were used to fund the NHI. In 2016, the Treasury indicated that an increase of VAT could be on the cards, but currently they are concerned about servicing the state debt with additional funds, not building the NHI.

Payroll tax?

A new payroll tax, in addition to the unemployment insurance fund (UIF), would, in practice, be paid by all employees – much like the current 2% UIF contribution. A payroll tax is, in the end, paid by employees, regardless of whether or not employers formally contribute half of it (as is currently the case with UIF). This is because the payroll tax is taken into consideration in wage bargaining. To the employer it is a labour cost, just like the wages. Thus the part of a payroll tax formally paid by an employer ends up being paid by the worker via forfeited wage increases.

Progressive income tax?

A surcharge added to the ordinary personal income tax appears to be the best alternative. This would uphold the widely accepted principle of progressive taxation: those who earn more can afford to pay a higher share of their income in taxation and, indeed, should pay a higher tax. The surcharge could be added to the ordinary PIT at increasing percentage points; this is sketched as one alternative in the article by McIntyre and Ataguba.

8. Consequences of low taxes and a small public sector

At any given level of expenditure, a government must borrow what it doesn't have in income. A policy that limits the tax revenue share of GDP increases the need for government to borrow. If the government indulges in tax cuts, as it did since 2000, and if the economy lands in crisis (where we are now, with no end in sight), the government will suddenly find itself paying more and more of its income towards servicing its debt. The tax pegging policy originates publically in 1996, in the so-called GEAR document, but was probably in place before 1994. It was cited, again, as "a part of the budget framework" in the 2012 Budget Speech. It is now impossible to keep it at this level, but the increased tax share of GDP will largely be used to pay back

debt, a situation that has been created by the tax cut policies implemented since 2000.

First, it is arithmetically impossible to finance a national health insurance system, the NHI, and also keep the public sector small. This has been demonstrated by comparing the exaggerated GDP growth rates that were forecasted in the Department of Health's budget plan 2010 to 2025 with where it in reality lies today.


Second, calculations based on Tax Statistics 2015 show that the government would have had, at least, an additional R190 billion more in tax revenue in the 2014/15 fiscal year alone compared to 1994/95, **if it had refrained from big cuts and political interventions in the personal income tax.**

Third, free higher education would cost close to R30 billion today. This is only one of a range of pressing needs, including the battle against unemployment, which demands a much larger public sector. These needs should determine tax policy, not some pre-decided rule that tax collections mustn't exceed a certain size in the economy.

The Economic Freedom Fighters (EFF) has launched the popular slogan "Economic Freedom in our Lifetime!" What we have argued for here is the less ambitious **Economic Security, Safety and Protection**. Total economic freedom is only for the super-rich, who can command a helicopter to come and fetch them with a phone call – and it has economic serfdom for the majority as its basic condition. Indeed, a progressive government would take away that kind of economic freedom from the minority in order to organise economic security for all. It would "Tax the Rich so that the Poor Can Live!" as one slogan reads.

9. Conclusion

South Africa is "not a welfare state," President Jacob Zuma said in his 2011 State of the Nation address. South Africa is, though, a country with a HIV prevalence of over 11% and, at least allegedly, a plan for an NHI. We have millions of citizens living in shacks, an immense investment backlog in social infrastructure, a growing state debt and a huge climate change problem. At the same time we have a finance minister who feels he has to appease the international credit institutes when he speaks in Parliament, as he did in 2012 when reaffirming the 25% tax-pegging rule, initially publicly pronounced in the GEAR document of 1996. In 2016, when the threat of a so-called credit downgrade is imminent, the Treasury feels it has to say things that are completely detached from the political reality and the urgent needs of the majority:



The Treasury on Friday evening welcomed S&P's decision to affirm the ratings, saying it would give SA more time to demonstrate concrete implementation of reforms to raise growth levels and place public finances on a sustainable path. The rating outcome demonstrates that South Africans can unite, especially during difficult times, to achieve a common mission.⁷⁹

"A common mission," "South Africans united," in 2016? How many can recognise themselves in that statement? To continue the neoliberal dream of a small public sector when students are protesting at Fort Hare with slogans like "We are hungry!" as they did in June 2016, is truly delusional.

This report has deliberately limited itself to personal income taxation and highlighted one basic political rule that has guided the government's fiscal policy from 1996. How it is possible that more than two-thirds of all registered companies (in all branches of industry) in South Africa declare a loss or zero result every year and that they have no taxable corporate income will be the subject of another report.⁸⁰

As more and more people become aware of the trickery involved in "keeping the government poor," as well as what taxation means for service delivery for schools, hospitals and the reduction of extreme poverty, the public pressure on the government can be expected to grow. What will happen then is still unwritten history. The student movement that shook the government in October 2015 confirmed again that it is the people who make our history. As this booklet goes to print in 2016, students have started to protest against the upcoming fee increases.

The majority of students and their families cannot afford the cost of higher education, but society as such can afford it if the resources are pooled together according to the principle of progressive taxation: The principle of taxing income according to the ability to pay.

⁷⁹ Hillary Joffe. *Business Day*, 3 June 2016, "Credit rating affirmed but S&P sends warnings."

⁸⁰ *2011 Tax Statistics*, p. 75 and the corresponding table in the Tax Statistics publication any year up until 2015.

A note on corruption

Corruption undermines the legitimacy of taxation and destroys public services and social investments. Part of the premise of this booklet is that corruption must be undermined strategically through the insourcing of services and functions to the local state.

The curtailed capacity of the public sector is the very point of departure for the whole tender system. It brings the private sector into a game of tenders. The bloated tender system turns the delivery of basic services and the building of social infrastructure into a costly for-profit endeavour, haunted by big business' price collusion, low quality products, service failures, the bribing of officials and nepotism.⁸¹

Almost by definition, corruption is located where the private and public sectors meet. Today they also meet inside the very institutions that are supposed to regulate the private sector. Nowhere is this problem more evident than in the mighty Department of Mineral Resources.

Legislation that forbids elected politicians and state officials from engaging in private business is necessary, even if this by itself will not end corruption. Insourcing in the municipalities that rely on outsourced services, maintenance and repairs is another measure, at the very least in order to give the workers decent wages and working conditions. This too demands a larger public sector as a share of the whole economy.

As for tender patronage, the half a billion rand cost of burning down 24 schools in Vuwani, Limpopo, in May 2016 after a court decision on municipal demarcation, seems to indicate what is wrong with the management of services in local governments. It is the organisation of services by for-profit business: "Certain important people already have tenders with Makhado municipality and, if the area is moved under another municipality, they will lose out."⁸²

⁸¹ "Nepotism": to give favours to your relatives and close friends.

⁸² <http://mg.co.za/article/2016-05-13-00-forces-behind-the-vuwani-fire>





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