Submission by the Budget Justice Coalition

On the report of the panel of experts on mitigating the negative effects of the VAT increase for poor and low income households

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Submitted by:

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1. Introduction

This submission is made in response to the call by National Treasury for public comment on the report by the Panel for the review of the current list of zero-rated VAT items.

As raised in our submissions to Parliament on the 2018 Budget and the draft Rates and Monetary Amounts Amendment Bill, we are concerned about the negative effects the increase to the VAT rate is having on poor and low-income households. We are also concerned by the simultaneous increases in the fuel levy as this has resulted in higher transport costs – impacting negatively on food and public transport costs. As a result poor and low income households are struggling to afford nutritious food and transport to school, work and health facilities. The harsh spending cuts prescribed in the technical guidelines for the Medium Term Expenditure Framework will exacerbate the situation.

In this submission we again re-iterate our objection to the February 2018 decision to increase VAT and call on Treasury and Parliament to reconsider this decision. If Parliament ultimately agrees to the VAT increase by the passage of the Rates and Monetary Amounts Amendment Bill, we call on National Treasury and Parliament to implement <u>comprehensive mitigating measures</u> that recognise the full extent of the financial crisis being experienced on a daily basis by the majority of poor and low-income earners.

Zero-rating only an additional six goods as recommended by the Panel, will not amount to adequate mitigation. We recommend further items be considered by Treasury and Parliament as well as increased investment in social programmes that impact directly on the household budgets of poor and low income households. For additional items to be considered, further information will need to be supplied by the Panel: while the Report presents generous detail and demonstrates clear rigour of analysis regarding the eight items identified, it does not provide any information on the other 58 items. This makes it difficult for stakeholders to engage in informed debate with the Panel recommendations and methodology. For example, some of the 58 items may pass the more significant tests and therefore be good candidates for zero-rating. This detail would also enable a comparison with the items identified for zero-rating in recent research by the Institute for Economic Justice (IEJ). We therefore request the Panel make this detail public to promote a more informed debate going forward.

2. Factors leading to the VAT increase

On 17 August 2015, the Davis Tax Committee put out a media statement clarifying its position in relation to its first interim report on VAT.[1] In this media statement, it was outlined that the committee's interim position is that no explicit recommendations were made to increase the VAT rate. The interim report outlined that although from a purely macroeconomic standpoint, an increase in VAT is less distortionary than an increase in direct taxes, an increase in VAT would have a greater negative impact on inequality than an increase in Personal Income Tax or Company Income Tax. The DTC continued that should it be necessary to increase the standard rate of VAT, it will be important for the fiscal authorities to think carefully about compensatory mechanisms for the poor who will be adversely affected by the increase. The report finally emphasised that a VAT increase without a significant measure of recycling of revenue in favour of poorer people is inherently retrogressive.

However, in February 2018, the Executive announced that the VAT rate would be increased. There was no public participation process preceding this decision. This lack of public consultation is constitutionally problematic given the potentially negative impact of a VAT increase for poor and low income households.

The Budget Justice Coalition takes note of the National Treasury inputs at the Nugent Inquiry. Specifically we note that poor collection of tax by the South African Revenue Services (Sars) was offered as a contributing factor to the increase of VAT. We also take note that National Treasury has outlined that the underlying data didn't support the claim that it was sluggish economic growth alone that contributed to the revenue shortfall. Other testimonies at the Nugent Inquiry have outlined how the erosion of administration and governance at SARS took place and how the collapse of the Large Business Centre led to issues with collection of corporate taxes. We also take note of Judge Davis's input wherein he noted that the causes for the SARS under collection are complex and include slippage in tax morality- caused by broader levels of corruption- not just allegations at SARS. Various books have offered insights into the dismantling of SARS's investigative capacity and into tax evasion. This is as concerning to the Budget Justice Coalition as it is to National Treasury officials.

It is our contention that the VAT rate increase is one of the ways in which the cost of state capture and a lack of accountability is being visited upon citizens – in particular poor and low income households. This context needs to be borne in mind by Treasury

[1]Available at *http://www.taxcom.org.za/docs/20150817%20Clarification%20of%20points%20in%20DTC%20VAT%20First%20Interim%20Report.pdf*

and Parliament when considering the VAT increase and the extent and appropriate mix of mitigatory measures selected.

3. Re-iterating our call on Parliament to reject the February 2018 VAT increase

When the VAT increase was announced by the Minister of Finance in February 2018, we expressed our concerns with the way the decision was made by the Executive, in particular the potential impact on poor and low-income households and the lack of meaningful public participation prior to the decision being made.

In February 2018, we presented to the Standing Committee of Finance on the 2018 Budget and expressed alarm at the regressive taxation measures and social spending cuts being proposed. Of the additional revenue needed, the budget proposed that over 70% should come from three indirect taxes: VAT, fuel and excise (sin) taxes. Our submission provided evidence that this was regressive because the lowest income groups spend the highest share of their expenditure on these taxes, and because forms of tax which reduce inequality had not been effectively used to make the tax mix more progressive. We demonstrated that effective rates of CIT and PIT have fallen since 1999 and room thus exists for increasing these (direct and progressive) taxes. Our submission also countered the claim that South Africa's CIT rate is high by international standards – we rank 172 out of 213 countries for company tax contributions (where 1 is the highest). We also noted that taxes on property and wealth in South Africa are unacceptably low. The submission costed and proposed alternative revenue raising measures that would increase the progressivity of the tax system while ensuring that revenue shortfalls and social needs are met.

Our evidence showed that the real value of social grants has barely kept pace with CPI inflation in recent years and often not with food price inflation. This means that the modest increases to social grants proposed in the 2018 budget will not ameliorate the impact of the VAT rise. Neither will the zero rating of the current limited number of basic foodstuffs.

We cautioned that the revenue proposals, coupled with the planned expenditure cuts in essential services, would exacerbate the already unacceptably high levels of poverty and inequality in our country. We highlighted that tax and spending plans *must* be redistributive. This follows from Section 9 of the Constitution as well as the fact that reducing inequality and poverty is essential for inclusive economic growth.

Finally we called on Parliament to:

- withhold approval of the tax proposals;
- require Treasury to provide evidence for the claim that raising direct taxes would be more harmful to the reduction of poverty, inequality, unemployment and increased economic growth; and
- institute a meaningful process of public engagement on optimal revenue raising measures.

Following their consideration of the 2018 Budget and the concerns expressed during the public hearings, the Standing Committee of Finance recommended to the Minister of Finance, that future proposals to increase taxes, especially indirect taxes like VAT, should be tabled in the October MTBPS to allow for more transparency. They also recommended that Treasury should present alternative options and scenarios for raising revenue for consideration.[2]

> "The Committee notes that the processes of increasing taxes require more time for consultation with a wider range of stakeholders and civil society, outside of government, and that in future the MTBPS tabling can better prepare for such taxation changes. The Committee is fully aware of the market and other sensitivities about prematurely releasing tax increases figures, but believe more consultation is possible without undermining NT's concerns. The Committee recommends that NT presents quantified alternative measures, options and scenarios when introducing new or adjusting tax rates and utilise the MTBPS to enhance transparency of the budget processes, especially on indirect taxes which pose little risks for tax restructuring and avoidance. "

We believe this will also allow for meaningful and informed public participation prior to the decision being announced in the February budget speech. We appeal to the Minister of Finance to heed this recommendation with regards to future revenue proposals.

We were disappointed that the Standing Committee chose to accept the February 2018 VAT increase decision. We note the Committee's view that rejecting the VAT increase decision would be 'difficult' to do due to the tight timeframes, the onerous requirements of the Money Bills Amendment Procedure Act, and the Committee's interpretation of s7(4) of the VAT Act.

> "Should parliament reject the VAT increase through the Fiscal Framework we will have to propose alternatives to raise an estimated R22,9 billion during the 2018/19 financial year, instead of through the VAT increase. Given the tight timeframes and the onerous requirements of the

[2] Standing Committee on Finance, National Assembly.Report on Fiscal Framework. Pg 32

> Money Bills Act this is difficult to do. Even if we reject the VAT increase through the Fiscal Framework it will still be implemented on 1 April in terms of the legal provision in s7(4) of the Value-Added Tax Act. It will continue to apply for a 12-month period from the date of the budget and will only lapse at the beginning of the next financial year if it is not given effect through the passing of the Rates and Revenue Bill through which the VAT increase can be rejected."[3]

While recognising the constraints facing Parliament, we do not agree with the Committee's decision not to take on this 'difficult' task or their interpretation of the meaning of s7(4) of the VAT Act. Parliament could (and still can) have required Treasury to provide costed alternative options and scenarios for raising the required revenue, to ensure that Parliament had the necessary information to make an alternative decision.

When we were invited to make submissions on the Draft Rates and Monetary Amounts Amendment Bill in April, we were uncertain as to why we should engage, given that the Standing Committee on Finance had already indicated its intention, in its Report on the Fiscal Framework, to agree to the VAT increase. We continued however to engage and presented a further submission. In this submission we re-iterated the points made in our February submission. While the most recent evidence[4] indicates that VAT in South Africa, due to existing zero-rating, is not in itself "regressive", increasing VAT makes the tax mix more regressive by increasing the tax contribution of poor and low-income households. It is also a more regressive tax than other options available. Further, it has the potential to dampen domestic demand and growth, and increase inequality. We further highlighted how a different management of the South African public debt and a strengthened focus on illicit financial flows and tax compliance could provide the necessary fiscal space to avoid the proposed VAT increase. We reminded the Committee that our February submission had contained evidence based alternative options for raising revenue other than via a VAT increase and we included these alternatives again. We called on the Committee to reject the VAT increase proposed in the draft Amendment Bill and amend the Bill to rather increase CIT, PIT and property taxes and to implement a comprehensive wealth tax to raise the required revenue.

4. Comment on measures to mitigate the impact of the VAT increase

If Parliament decides to accept the VAT increase for 2018 and beyond, we call on the Minister of Finance and Parliament to implement comprehensive mitigating measures to reduce the negative impact that the VAT increase is having on poor and low income earners and on the economy.

[3] Above Pg 33

[4] Gabriela Inchauste et al. (2015), 'The Distributional Impact of Fiscal Policy in South Africa'. The World Bank.

Given that the VAT and Fuel Levy increases have been in effect since 1 April, mitigating measures that involve increased budgetary allocation to social programmes need to be implemented as soon as possible, preferably in October 2018 via the Adjustment Budget. Due to the urgency of the financial crisis facing poor and low-income earners, we recommend that those mitigating measures that are able to reach poor and low income households immediately and directly, should be preferred, over measures that require further investigation before their effectiveness or success can be assured.

The addition of zero rated items and additional financial investment in social programmes should not be seen as an either/or. We recommend that a mixture of <u>both of these steps</u> need to be taken to fully reverse the negative impact of the VAT (and Fuel levy) increase on poor and low income earners. For example, a decision to take only one mitigating measure, for example small increases to social grants, would not directly assist people who are not receiving social grants. This includes the majority of poor people aged 18 to 60 who are completely left out of the social assistance programme. And a decision to zero-rate only a further six items and not also increase expenditure on key social programmes will have minimal impact taking into account both the VAT and Fuel levy increases and expenditure cuts to key social programmes.

4.1 Recommendations on additional items for zero rating

We support the Panel's conclusion that the current zero-rated item list should be kept as such. While some of the items may not, in a narrow financial sense based on the distribution of expenditure on these items, disproportionately benefit poor and low-income households, they should be retained for equity and health promotion reasons, in particular fruit, vegetables, milk products and lentils.

We support the six items identified by the Panel for zero-rating. The focus on items that will assist women and children is welcomed. However, the addition of only six items to the list will not sufficiently address the adverse impact of the VAT increase, especially if the increase is going to be retained beyond 2019.

A weakness of the panel report regards the methodology used to narrow the list of potential zero-rated items from the 66 considered to 8 - at no point are the results of the analysis of the 66 items given. The report considers:

1. Equity-gain ratios, comparing the gains to very-poor households in deciles 1-4 to those in very high-income deciles 9-10.
2. Relative benefit of tax reduction (based on relative current expenditure) accruing to households in deciles 1-4 vs. households in deciles 5-10.

3. Relative benefit of tax reduction (based on relative current expenditure) accruing to households in deciles 1-7 vs. households in deciles 8-10.
4. Whether or not zero rating would make VAT more or less progressive based on the ratio of VAT paid on a particular item as a share of income.
5. Socio-economic considerations that are vaguely defined as “items that are beneficial to the poor”.

The panel seems to place particular emphasis on the second criteria above, potential VAT savings of households in deciles 1-4 (the poorest 40%) compared to households in deciles 5-10.

The methodological approach is problematic in three ways.

Firstly, the report does not list how the 66 items faired with regards to these five tests. We are not informed whether items “passed” one or more of these tests, and which ones. An informed public conversation cannot take place on this basis (note, the report does give fuller results for existing zero-rated items).

Secondly, the special emphasis given to the second test above (deciles 1-4 vs. decile 5-10) is inappropriate. Concentrating on deciles 1-7 vs deciles 8-10 would have been far more appropriate as argued by the report compiled by the Institute for Economic Justice (IEJ).[5] 55% of South Africans are poor so deciles 1-4 do not capture all poor people, and exclude low-income households; almost all of the lowest spending/earning 70% earn below the income-tax threshold (see further reasons in the IEJ report). The Parliament’s Standing Committee on Finance strongly argued “that the list of zero-rated items needs to be expanded taking into account the needs of the *poor and low-income* earners”.

Thirdly, there is no evidence of gender or age sensitive analysis being applied to all the 66 items considered. The needs of women, children, mothers and pensioners at times differ from those of the general population and as these groups are the most vulnerable they should be given special consideration. The IEJ report offers detailed consideration of this, highlighting how zero-rating certain products would disproportionately benefit these groups.

The criteria used by the report are *at times* insufficient or inappropriate, it is unclear which tests are given more weight, and we are therefore essentially asked by the panel to take on faith that none of the other 66 items were appropriate candidates without

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[5] IEJ. (2018), *Mitigating the impact of the VAT increase: can zero-rating help?*

being presented with the evidence of this. An informed public debate cannot occur on this basis.

The Panel should be requested to provide this information, in an easy to understand manner, prior to the public hearings. This would allow us, and others, to compare the results with our own research. We would be able to consult with all coalition members and make a further short-list for consideration at the public hearings.

We would recommend in particular that the panel provide more detailed information on the results of their tests for the items contained in Table 1 below.[6] These items scored highly with respect to the tests applied in the IEJ research report.

Table 1 Candidates for further zero-rating

ITEM	Pass primary test?[7]	Benefits poor and low-income women more?	Socio-economic considerations	VAT forgone (R mn)
Cake and bread flour	YES	YES		491
Sorghum meal/powder and mabella	YES	YES		68
Poultry (incl heads and feet)	CLOSE BUT NO	NO	YES	3982
Mopane worms	YES	YES		3
Other canned fish	YES	YES		27
Whiteners (Cremora; Ellis Brown)	YES	YES		137
Amageu	YES	NO		26
Baby food	SOME, NOT ALL	YES	YES	395
Powder soup	YES	YES		187
Instant yeast	YES	NO		19
Soya product (excluding soy milk)	YES	YES		19
Tea	YES	YES		197
Infants and children's clothing and footwear (include school uniforms)	SOME, NOT ALL	YES	YES	4108
Candles and matches	YES	YES		116
Coal (including anthracite)	YES	YES		11
Hotplates	YES	YES		43
Soap	NO	NO	YES	1525

[6] Many of these match with items listed elsewhere, for example, PACSA notes that when prices increase: "Households prioritise the securing of foods which they cannot live without (maize meal, rice, flour, sugar, sugar beans, samp, cooking oil, salt, potatoes, onions, frozen chicken portions, curry, stock cubes, soup, teabags and yeast) and reduce or forgo or buy much cheaper, poorer quality nutrient-rich foods such as meats, vegetables and dairy products." In PACSA. (2017), *2017 PACSA Food Price Barometer, Annual Report, October 2017*

[7] The "primary tests" refers to whether zero-rating the item would disproportionately benefit deciles 1-7.

Medicine and medical services in public institutions	SOME, NOT ALL	SOME, NOT ALL	YES	309
Calls (including airtime for cellular phones)	NO	NO	YES	4180
Textbooks and stationery	NO	NO	YES	355
Disposable nappies	YES	YES	YES	685
Sanitary towels and tampons	NO	YES	YES	100
Agricultural own production	MOST, NOT ALL	SOME, NOT ALL		53

Source: Statistics South Africa, Living Conditions Survey 2014/15, IEJ calculations

Zero-rating most of these items would disproportionately benefit poor and low-income households. This includes: cake and bread flour; sorghum meal/powder and mabella; mopane worms; other canned fish; whiteners (Cremora; Ellis Brown); amageu; powder soup; instant yeast; soya product (excluding soy milk); tea; candles and matches; coal (including anthracite); hotplates; and disposable nappies. For most of these women benefit disproportionately.

Poultry is included because it is a major source of animal protein for poor and low-income households. South Africa's high (and increasing) stunting rates for children under 5 (27% of all children under 5) and high rates of iron deficiency for pregnant women (26%) indicate a need for increased access to foods high in protein. PACSA, leading experts in the monitoring of food prices and consumption, include chicken in the list of items that when food prices rise poor and low-income "[h]ouseholds prioritise the securing of foods which they cannot live without". Women in particular report chicken to be an item they "cannot live without". According to PACSA frozen chicken pieces saw a year-on-year price increase of 36% between 2016 and 2017 – suppliers and supermarkets have attempted to mask this by reducing the amount of chicken in each bag so it appears they are cheaper; women also reported that the quality of chicken had decreased.[8] We note that the panel could not reach consensus on this item with the majority deciding to exclude it from zero-rating. We do not agree that the reasons advanced for excluding chicken from the list out-weigh the socio-economic benefits (especially for pregnant women and children) of including chicken for further zero-rating and call for chicken to be added the list.

In the IEJ report, not all forms of baby food, infants and children's clothing and footwear, and textbooks and stationery, pass the "primary test" (proportional benefits of deciles 1-7 vs decile 8-10). However, zero-rating these items would disproportionately assist women and advance the rights of children to food, dignity and education. Similarly,

[8] PACSA. (2017), *2017 PACSA Food Price Barometer, Annual Report, October 2017*

making sanitary products more accessible is a national imperative, both to ensure the dignity and health of women, and because of the benefit to improve school attendance by teenage girls.

Ensuring cheaper access to soap and medicines and medical services (limited to those in public institutions) would advance the rights to health, sanitation and dignity.

Airtime costs are also included in the list, on the understanding that a strong case can be made that access to communication and the internet is essential to participation in society, education and the labour market.

For almost all items, their inclusion in the basket of zero-rate items would make the tax mix more progressive. For more details, please see the attached research report by the Institute for Economic Justice, one of the Coalition members.

4.2 Recommendations for higher ad valorem excise duties and 25% VAT rate for luxury items

The IEJ report also shows that more than half of the costs of zero-rating the above items (R9.6 billion out of R17 billion) could be made up through imposing a VAT rate of 25% on a basket of luxury goods consumed by the rich.

South Africa currently has a limited range of *ad valorem* excise duties on luxury goods paid by the manufacturer or importer. These raise a limited, but not insignificant, amount of revenue – in 2017/2018 R3.8bn and projected to rise to R4.8bn in 2020/2021 (in nominal terms). However, they are projected to maintain their share in the overall tax mix. There is, therefore, room to further tax luxury consumption through the increase and expansion of *ad valorem* excise duties and the institution of a higher VAT rate on luxury goods.

"Luxury goods" could include those items bought only by the rich, as well as upper segments of other goods markets, for example, fancy cars, expensive fridges, and so on. Given the existing tax administration systems this can be feasibly implemented. Given that a higher share of luxury items is imported, this should not unduly dampen domestic demand and could modestly assist in closing the balance of payments. Access to luxury goods is an expression of inequality. The selection of items should not place goods that poorer households save for, beyond their reach.
Table 2 provides a sample of items that could be good candidates for a luxury VAT rate as well as the revenue this could raise. The test for inclusion is whether 70% or more of

expenditure on the item is spent by decile 10 (and more than 90% by deciles 8-10). The columns show additional revenue (over and above the existing 15% VAT rate) that would be earned from a 25% VAT rate on all goods in that category (the second last column).

Another test is applied to mimic a higher VAT rate on expensive versions of a particular good (the last column). Unfortunately, the data set is limiting and a luxury VAT rate cannot be properly applied to this data based on price differentiation, for example, levying a higher tax for cars selling for more than R500 000. For a selection of items, we have applied the 25% VAT rate only to the consumption of decile 10, on the loose assumption that decile 10 would purchase more expensive versions of this item.

Table 2: Indicative items for luxury VAT rate and fiscal benefit

Item	Percentage consumed by decile 10	Extra tax at 25% VAT rate applied to all goods in category (R mn)	Extra tax at 25% VAT rate applied to decile 10 consumption (R mn)
Security systems (including alarms; panic buttons)	80%	54	
Swimming pool maintenance (excluding wages of persons who maintain pools; but including chemicals)	83%	97	
Security services (including reaction services and neighbourhood watch)	86%	55	
Garden and patio furniture	79%	15	
Vacuum cleaners; polishers and carpet cleaning machines	72%	18	
Power driven garden tool (e.g. lawnmowers; etc.)	82%	30	
Garden water sprinkler (e.g. sprays; irrigation systems; etc.)	90%	34	
Other garden equipment	82%	7	
Aircraft educational trips	100%	8	
Aircraft other than educational	97%	157	
Aircraft for when away from home	91%	408	
Boat/ship for when away from home	78%	5	
Fax machines and telephone answering machines for household purposes	80%	1	
Boats (including outboard motors) aircrafts; go-carts	100%	59	
New caravans and trailers including motorised caravans	100%	4	
Quad bikes	84%	1	

Repairs and maintenance services to recreation; entertainment and sports equipment	92%	5	
Holiday tour package	75%	298	
Hotel	81%	397	
Bed and breakfast	81%	81	
Guesthouses	73%	85	
Lodges	70%	70	
Schools boarding fees in private institutions – Loans	77%	20	
Expenses occurred as owner of a holiday home i.e. after deduction of income received from letting	83%	32	
Motor cars	85%	5 201	4405
Station wagons	81%	325	264
Mini buses	100%	27	27
New bakkies	84%	638	532
New four wheel drive vehicles	89%	897	798
Used four-wheel drive vehicles	95%	363	298
Cameras; video cameras; projectors and flashes	73%	60	43
eReader	74%	4	2
Other consumables (e.g. toners; ink cartridges)	81%	9	7
Firearms and ammunition	85%	8	7
Special sports clothes and shoes	70%	49	35
Swimming pool equipment and repairs of equipment	75%	74	55
Loose carpets and rugs	52%		19
Refrigerators; deep freezers and refrigerator/deep-freeze combinations	19%		77
Refrigerators	24%		1
Washing machines; dishwashers and tumble dryers	26%		42
Stoves and ovens; including microwave ovens	20%		42
Heaters; air conditioners/fans	60%		16
Heaters (gas and paraffin)	31%		2
Kettles and percolators; coffee makers	26%		13
Cellular phones (pre-paid hand set)	24%		137
Cellular phones accessories e.g. chargers; pouches; earphones; prepaid sim-cards)	30%		6
Mobile device; Modems (e.g.3G; Wi-Fi)	44%		151

Radios (including motor car radios) tape recorders; compact disk players; sound system; MP3 players; iPods and and similar equipment (including for cars)	26%		13
Television sets; decoders (e.g. M-net; PVR; Explorer; etc.); video recorders; Blu-ray and DVD player	27%		105
Aerials and satellite dishes	28%		12
Personal desktop computers (excluding laptops)	55%		39
Laptops/notebooks	40%		135
Tablets/mini tablets (e.g. iPad; galaxy tabs; etc.)	52%		98
Laptops; MP3 players; tablets for educational purposes in public institutions - Loans	33%		9
Laptops; MP3 players; tablets for educational purposes in private institutions - Loans	61%		7
Printers/scanners/copiers	52%		7
Modems	50%		9
Computer parts (e.g. motherboard; CPU; memory/RAM; graphics card; hard drives)	40%		4
Flash disks; SD cards and portable external hard drives	66%		6
Other musical instruments; sound equipment and accessories	29%		1
Musical instruments: Pianos; organs and other musical instruments	38%		11
Purchase of hunting dogs	63%		5
Video games CDs/DVDs/Blu-ray/downloaded apps (include downloaded games: X-box; Play-Station; Wii games)	62%		22
Fire works	10%		1
Firearms and ammunition (for security services)	29%		2
Tennis rackets and balls; fishing rods; soccer ball; bats; etc.	65%		13
Camping equipment (tents; sleeping bags etc.)	66%		16
Watches and personal jewellery	57%		126

4.3. Recommendations for further investments in social programmes

Social grants

We support the Panel's recommendations with regards to increasing social grants, in particular with regards to the Child Support Grant (CSG). The Panel proposes an additional R20/month be added to the CSG, taking it from R400 to R420. This would cost the fiscus approximately R3 billion and provide an additional R456 per year to households in decile 1 – the poorest decile. If this addition is made in October 2018, after the already promised R10 inflation increase, the CSG would total R430.

Our reasons for supporting this proposal are based on the following considerations:

- The CSG is South Africa's biggest and most successful poverty alleviation programme for children. Investing further in this programme is a 'sure-bet' due to the wealth of credible evidence on the programme's positive impact on reducing child poverty rates and improving nutrition, health and education outcomes.
- South Africa still has very high child poverty rates. Indicating that further investment in the CSG is much needed. Of the total population of 19.6 million children, 12.7 million (65%) lived below the Statistics South Africa upper bound poverty line of R1138 per capita in 2017.[9] The national average masks striking provincial and rural-urban variations in child poverty. For example, in KwaZulu-Natal, Eastern Cape and Limpopo, over 75% of children live in poverty while in Gauteng and Western Cape the rate is under 45%. Child poverty is the highest in the rural areas of the former homelands at 86% compared to 50% in urban areas.
- We agree with the Panel that further investment in the CSG has the potential to reduce urban/rural inequality due to its high uptake in rural provinces. The increased financial flows into rural areas will also stimulate the growth of rural economies.
- The CSG is particularly pro-poor. The Panel presents an analysis of all the social grants and illustrates that 74% of all households in decile 1 (the poorest decile) receive a CSG, compared to the next biggest contender, the Old Age Pension at 26%[10]. This means that further investment in the CSG will definitely reach the poorest of the poor.
- The CSG amount of R400 (April 2018) is significantly below the Stats SA food poverty line of R547/month in 2018 Rands. Approximately 7 million children (36%) live below this food poverty line,[11] meaning that they are not receiving sufficient food to meet their basic nutritional needs. Children living below the food

[9] Unless otherwise referenced, the data used in this section is sourced from Hall & Sambu 'Income poverty, unemployment and social grants' in Hall et al (eds) *South African Child Gauge 2018* Children's Institute, University of Cape Town *(forthcoming). The data is based on analysis of data from the General Household Survey 2017 (Statistics South Africa,* 2018)

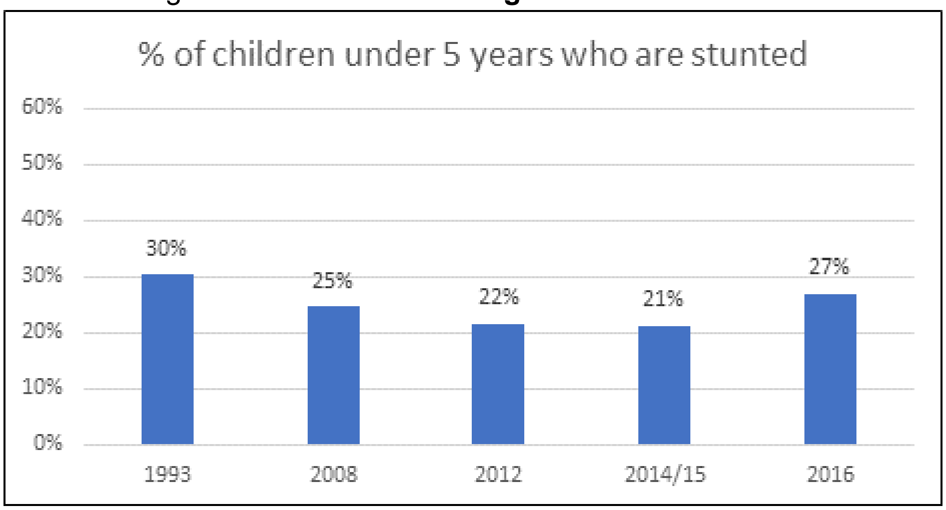
[10] Pg 71 of the Panel's Report

[11] Hall & Sambu 'Income poverty, unemployment and social grants' in Hall et al (eds) *South African Child Gauge 2018* Children's Institute, University of Cape Town *(forthcoming).* The data in the Child Gauge is based on analysis of data from the General Household Survey 2017 (Statistics South Africa, 2018

poverty line are likely to end up stunted (low height for age) as is evidenced by the stunting rate of 27% of all children under 5 years of age. Stunting has long term negative consequences for the affected child and the country's economy due to its negative and often irreversible impact on the child's ability to develop, learn and enter the labour market. Based on numerous research studies on the positive impact of the CSG[12], increasing the CSG amount is highly likely to reduce the number of children living below the poverty line and therefore also reduce the stunting rates.

- Analysis of trends in child nutrition show that while child hunger has been gradually declining over the past 15 years, the rates of stunting have not changed significantly over this period and are now starting to increase (see figure 1 below), indicating that people are less able to afford food of high nutritional value, especially protein. One of the reasons cited for this pattern is the low value of the CSG compared to rising food prices.[13]

Figure 1. **Trends in stunting for children under 5**



Source: Analysis by Sambu W, Children's Institute, UCT based on Project for Statistics on Living Standards and Development (PSLSD) of 1993; NIDS (2008); South African Health and Nutrition Examination Survey (2012); NIDS 2014/15; and South African Demographic and Health Survey (2016)

However, the Panel's proposal of an additional R20/ month is too little given the high levels of poverty and inequality. The proposal still leaves the value of the CSG at least R100 below the food poverty line.[14]

[12] Grinspun 'No small change: The multiple impacts of the Child Support Grant on child and adolescent well-being' in Delany et al (eds) *South African Child Gauge 2016* Children's Institute, University of Cape Town at 44

[13] Devereux & Waidler (2017)' Why does malnutrition persist in South Africa despite social grants? ' *Food Security SA Working Paper Series No.001*. DST-NRF Centre of Exellence in Food Security, South Africa at 16 – 17. Other reasons cited include deductions from social grants, inadequate nutritional knowledge leading to poor feeding practices and eating habits, and barriers to accessing quality health care services.

[14] The food poverty line was reported by stats SA to be R547 on 1 April 2018. The CSG is currently R400 and will increase to R410 in October 2018. An additional R20 increase in October would take it to R430.

We therefore recommend that the CSG amount be increased to at least the level of the food poverty line. An immediate increase in 2018 would mean increasing it by R150 from R400 to R547. In the alternative, an incremental approach could be adopted by phasing in the increase over a three year period with the aim of ensuring that the grant amount matches the food poverty line by 2020. The table below illustrates how this could happen.

	April 2018	**Oct 2018**	**April 2019**	**Oct 2019**	**April 2020**	**Oct 2020**
CSG	R400	R450	R500	R550	R600	R650
Food Poverty Line	R547		**R590*		**R640*	

*The food poverty line is not determined beyond the current year (2018). These amounts are speculative based on the trend over the past few years.

Annual increases beyond October 2020 would be based on keeping pace with the food poverty line or food price inflation, whichever is the highest.

We also recommend that the comprehensive review of social security be finalised as a priority. In particular the non-existence of basic income support for the majority of poor people aged 18 to 60 needs to be addressed. In the absence of this, whole households will continue to have to collectively rely on the social grants received by the elderly, disabled and children.

Sanitary products

We agree with the Panel's proposal for greater investment in providing sanitary products directly to poor women and girls. However, we note the Panel's concerns with regards to the state's capacity to effectively distribute these products so as to ensure they reach the intended beneficiaries. We therefore recommend further details be provided by the responsible departments as to how they would use the increased investment in the programme and that there should be public engagement on these detailed proposals. This participation process should include direct engagement with women and girls and with civil society organisations representing these groups. We offer our assistance in promoting such a participatory exercise.

School Nutrition Programme

The Panel's proposals on increasing the school nutrition programme are not clear, besides recommending that all schools have a food garden. We recommend further details on this proposal be provided before we can engage meaningfully.

While the panel provides figures on how much such an investment would give back to poor and low income earners, it fails to mention that only a portion of this increased investment would actually reach poor households because much would be diluted by the supply chain process due to the multi-layered nature of the programme.

Another way of investing further in the school nutrition programme could be by zero-rating the food items that are most used in the programme. This would reduce the cost of the programme for the Department of Education, enabling it to reach more children with its current budget. Peanut butter for example would be a good candidate for zero-rating for this reason. It would also assist all households to increase their protein intake.

The school nutrition programme does not reach children below the age of 5 years. To reach these children with improved nutrition, there needs to be greater investment in both the Child Support Grant and the Early Childhood Development Subsidy. See above for our comments on the Child Support Grant. With regards to the ECD subsidy, the per capita amount is currently too low to cover the basic nutritional needs of a child.[15] It is required by the ECD programmes to cover rent, management and teacher salaries, equipment and food. Increasing the subsidy amount would improve not only children's nutrition but also the salaries of the ECD practitioners. ECD practitioners tend to be women who are receiving wages below the minimum wage level and who are likely to be a category exempted from the minimum wage. Investing in the subsidy therefore also has a positive gender impact.

Public and scholar transport

Poor and low-income households spend a disproportionately high amount of their income on transport due to the legacy of spacial inequalities. Public transport costs have increased substantially in 2018 due to the fuel price increases and the wage increases (which in turn were higher due to the need to compensate employees for the VAT increase). We therefore recommend that state programmes aimed at subsidising public transport be considered for further investment.

With regards to scholar transport we recommend that Equal Education's call for a conditional grant for scholar transport be supported and implemented by April 2019. This will ensure that funding allocated by national treasury for scholar transport reaches scholars in need, and is not allocated by the provinces to other education costs as is currently happening. We also recommend that the allocation to this conditional grant be adequate to fund the number of learners who need subsidised scholar transport.

[15] Berry L & Proudlock P (2014) *Children's rights to basic nutrition: A review of South Africa's subsidy for ECD programmes.* In Proudlock P (Ed) South Africa's progress in realising children's rights: A law review. Pg 50 -51 and 54

5. Summary of recommendations on mitigating measures

Zero rating

- Retain the existing 19 items that are zero-rated.
- Zero-rate the six items identified by the Panel.
- Include chicken in the basket of zero-rated items.
- Consider zero-rating the items that scored highly in the IEJ report and the Panel's analysis (information not yet available), with priority given to: sorghum meal/powder and mabella; other canned fish; powder soup; instant yeast; soya product (excluding soy milk); tea; candles and matches; and coal (including anthracite).
- Investigate peanut butter for zero-rating given the role it plays in the school feeding scheme and ECD centres, and generally as a source of protein for children.

Luxury rating

- Implement a higher VAT rate of 25% on luxury items.

Social programmes

- Increase the amount of the Child Support Grant to the level of the food poverty line (R400 to R547).
- Pioritise the finalisation of the policy on comprehensive social security and commit to timeframes for implementation (including providing income support for 18 to 60 year olds).
- Commit to direct provision of sanitary products to women and girls in poor and low-income households and initiate a meaningful participatory process to identify the most effective distribution mechanisms.
- Commit to implement a conditional grant for scholar transport by April 2019, with a budget adequate to ensure subsidised transport for all scholars in need.
- Investigate increased subsidisation of public transport.
- Clarify the details of how the school nutrition progamme could be expanded to improve its reach and impact to enable meaningful engagement on the proposals.
- Investigate increasing the per capita ECD subsidy to improve nutrition for children under 5 and salaries for ECD practitioners who are currently working below the national minimum wage.