NATIONAL ECONOMIC DEVELOPMENT AND LABOUR COUNCIL

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RESEARCH REPORTS ON COMPREHENSIVE SOCIAL SECURITY AND RETIREMENT REFORMS (CSSRR)

KEY POINTS

Background

In 2014, Nedlac established a task team on Comprehensive Social Security and Retirement Reforms (CSSRR) to engage on a comprehensive social security and retirement reform system that is affordable, sustainable, and appropriate for South Africa. Engagements, however, could not be undertaken as the CSSRR Paper had not been tabled at Nedlac.

Engagements, therefore, started in 2017, following the tabling of the CSSRR paper, by the Department of Social Development (DSD). The task team engaged on the Government tabled paper between 2017 and 2019, which identified areas of agreement and required further discussion. To assist further engagement, research areas were identified, and Nedlac collaborated with the DSD and National Treasury to procure such research.

The research objective was to assist social partners in making informed decisions during their engagements on the comprehensive social security and retirement reform. The study was on the following research topics:

(i) Economies of Scale and value for money regarding the retirement system in South Africa by Neryvia Pillay commissioned by National Treasury.

(ii) The Financial Feasibility of Basic Income Grant (BIG) by Deloitte commissioned by Nedlac.

(iii) Informal Economy Retirement and Risk Benefits by True South commissioned by DSD.

(iv) Actuarial Sustainability of a proposed National Social Security Fund (NSSF) and, if established, its impact on the savings market – by International Labour Council commissioned by DSD.

(v) Impact on the investment environment and capital markets of the NSSF- by Deloitte commissioned by Nedlac.

1. ECONOMIES OF SCALE

1.1. The purpose of the research was to quantify the administrative efficiencies and economies of scale associated with the size of a retirement fund. It assessed whether the benefits of scale vary with fund characteristics, fund size, or across the administrative cost.

1.2. Summary of findings

1.2.1. There have been significant changes in the retirement fund industry between 2006 and 2018, with a decrease in the number of funds, an increase in the average fund size, and average administrative expenses per member.

1.2.2. Economies of scale do not meaningfully vary with fund size, except in 2007 and 2018, where funds established in 1996 achieved cost efficiencies with a funds size of 300,000 members.

1.2.3. Defined benefit and hybrid funds have higher administrative costs than the limited contribution funds, where the administrative costs of the defined benefit and hybrid fund were R9 269 and R4 380, respectively, in 2006. The administrative fee of the defined contribution fund in 2006 was R3 113.

1.3. **Recommendation**

1.3.1. Considerations should be given to increasing the operational scale of retirement funds to lower the average administrative costs.

1.3.2. More focus should be directed to ordinary, umbrella, pension, and provident funds to improve cost efficiency in the retirement system.

2. ACTUARIAL STUDY OF THE PROPOSED NATIONAL SOCIAL SECURITY FUND (NSSF)

2.1. This research focused on the costs of implementing an NSSF system in South Africa, with an expectation that the scheme will be effective from 2022. It modeled long-term population trends, employment, earnings, and claims on the NSSF, dependent on relevant qualifying criteria and associated benefits.

2.2. **Summary of Findings**

2.2.1. A 10% contribution rate towards the NSSF would not be sufficient to finance all the expenditures on a fully funded approach as total costs would exceed contributions from 2052, resulting in investment incomes being used to pay for the spending.

2.2.2. A contribution floor might need to be introduced as a new parameter in the scheme's design. The contribution rate would not apply to the first salary level on the SARS tax table, but benefits would accrue at this level. This will ensure that the scheme is less expensive regarding contribution rates for individuals with lower incomes.

2.2.3. Increasing the retirement age could positively impact the scheme's financial sustainability.

2.2.4. Population growth was an essential aspect of the NSSF: the higher the growth of the population, the more people available to pay for benefits.

2.3. **Recommendations**

2.3.1. The study recommended a 12% contribution rate fully funded approach.

2.3.2. It further recommended that the 12% contribution rate be doubled if the NSSF reached a 25% funding ratio.

3. FINANCIAL FEASIBILITY OF BASIC INCOME GRANT (BIG)

3.1. The purpose of this research was to assess the financial feasibility of providing income support to individuals between the ages of 18 to 59 in South Africa. The following factors were considered:

(i) The nature of income support (universal or means-tested, and conditional or unconditional);

(ii) The value of income support (cover nutritional needs, reduce poverty or provide a certain standard of living);

(iii) Links to the labour market;

(iv) The macroeconomic and socio-economic impacts; and

(v) The delivery mechanisms;

3.2. **Summary of Findings of the study**

3.2.1. Implementing a BIG can improve income equality in South Africa and possible economic gains through the multiplier effect. However, from a fiscal perspective, the cost of implementing BIG would be high.

3.2.2. Taking Covid-19 into account, the study revealed that implementing a BIG at the current special COVID-19 (R350.00) could address inequality in the country to increase the share of household income per capita. Furthermore, implementing the BIG could impact macro-level economic growth by boosting household productivity and employment, stimulating aggregate demand, affecting labour force participation, and influencing savings and taxation.

3.2.3. Basic income assistance would support investment into human capital development, for example, improved nutrition, health care, housing, and transportation.

3.2.4. If funded at the special COVID-19 Social Relief of Distress Grant level, it would result in an approximate average increase in effective tax rates (of 8.2% across taxable income bands considered for 2023/24). Meanwhile, the BIG at the Lower Bound Poverty Line (LBPL), the food poverty line plus the average amount derived from non-food items of households, would result in an approximate average increase in effective tax rates of 19.8% across taxable income bands considered for 2023/24. A BIG at the Upper Bound Poverty Line (UBPL), which is the food poverty line plus the average amount derived from non-food items of households whose food expenditure is equal to the food poverty line, would result in an approximate average increase in effective tax rates of 30.0% across taxable income bands considered for 2020/21.

3.3. **Recommendations**

3.3.1. It is recommended that cost-benefit analysis, determination of an appropriate tax base, and provision of comprehensive data on the pattern of wealth ownership in South Africa should be undertaken before a decision on BIG can be made. This assesses whether the tax revenue generated would exceed taxpayers' administrative and economic burden and the South African Revenue Service (SARS).

3.3.2. Alternative sources of taxation such as Personal Income Tax (PIT), Corporate Income Tax (CIT), and Value Added Tax (VAT) should be assessed for viability in financing the implementation of a BIG, partially or wholly.

3.3.3. Alternatively, the cost of implementing the BIG can be funded through the reallocation of public expenditure. This reallocation would require trade-offs from spending towards health, education, and social development, which currently accounts for 56% of government expenditure, as per the 2020 Budget Statement.

4. **IMPACT OF THE NATIONAL SOCIAL SECURITY FUND (NSSF) ON SAVINGS AND INVESTMENT**

4.1. The purpose of this study was to assess the potential impact of the introduction of the NSSF on savings and investment markets.

4.2. **Summary of findings**

4.2.1. The study revealed that the NSSF would have an impact on the following:

(i) Flow of funds between households, financial intermediaries, and government;

(ii) Consumption which includes the savings and investment behavior of households and firms;

(iii) Financing of business investment and in capital market flows and;

(iv) The existing retirement forms;

4.3. **Recommendations**

(i) It is recommended that the government subsidize wages to minimize disruptions to the labour supply-demand associated with the introduction of mandatory contributions.

(ii) The NSSF should be a defined-benefit social security fund in the form of a centrally managed public fund that aims to provide adequate retirement and risk-benefit for the working population of South Africa.

5. INFORMAL ECONOMY RETIREMENT AND RISK BENEFITS

5.1. The purpose of this research was to provide design options to extend mandatory contributory risk and retirement benefits to informal sector workers. Critical research areas included the appropriate type of benefits scheme for eligible workers who have irregular incomes; contribution collection and benefit payment mechanisms; flexibility provisions; benefit design; and an outline of the financial implications of such a scheme.

5.2. **Summary of findings**

5.2.1. Based on comparative analysis with other countries, a conceptual understanding and an operational framework of social security that transcends traditional approaches and boundaries was necessary for the successful coverage of informal workers.

5.2.2. The retirement and risk benefits designed for informal workers are challenging without systematically developed data. Furthermore, it would be challenging to undertake financial modeling given that the volatility of casual workers' earnings from month to month was unknown.

5.3. **Recommendations**

5.3.1. Comprehensive consultations should be undertaken with institutions representing informal economy workers before designing a retirement and risk benefits system for its workers.

5.3.2. Workers should be permitted to have a flexible payment approach, where they would pay the amounts affordable to them and as frequently as they wanted to, with no limitations. Furthermore, no penalties should be imposed on members who do not contribute for long periods.

5.3.3. The scheme for informal workers should be designed and operated as an extension of the National Social Security Fund (NSSF) as these combine economies of scale of two funds.