pcfinance 161122

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

2016/11/21

Motivation to comply with sections 8(5) and 11(3) of the Money Bills Amendment Procedure and Related Matters Act, 2009 for amending the Taxation Laws Amendment Bill, 2016, as tabled by the Minister of Finance on 26 October

Introduction

The Taxation Laws Amendment Bill, 2016 (TLAB) was tabled in Parliament on 26 October 2016. On 15 November 2015 the Minister of Finance requested that the Standing Committee of Finance (SCoF) consider amendments to the Bill, specifically relating to the proposed caps on the Employment Tax Incentive and effective dates for amendments to definitions. Since the Bill had already been tabled in Parliament, any proposed amendments made or approved by SCoF must comply with the Money Bills Amendment Procedure and Related Matters Act, 2009, including sections 8 and 11 of the Act. This followed the SCoF hearings on public comments on 9 November 2016. A draft response document to the TLAB was presented by the National Treasury on 15 November 2016. This note provides the information to help inform the requirements in sections 8(5) and 11(3) of the Money Bills Amendment Procedure and Related Matters Act, 2009.

The proposed amendments

The proposed changes to the tabled version of the TLAB in relation to the cap on the Employment Tax Incentive reflect the outcome of discussions of the potential impacts of the proposed cap on job creation initiatives. When the draft legislation was published on 25 September 2016, National Treasury invited comments on the potential impacts in order to elicit inputs from affected employers. During the comments phase and the parliamentary hearings comments on the cap were received from business groupings, claiming employers and labour federations. The majority recommended removing the cap.

After consideration of the comments received and after discussions with interested parties, the Minister of Finance recommended that the SCoF amend the TLAB to revert to the original design of the ETI by removing the proposed cap.

During the comments phase it also became apparent that the proposed effective date for implementation of the change to the definition of "monthly remuneration" cannot be facilitated by payrolls in time to comply with the proposed amendment by 1 October 2016. We therefore suggest that the effective date be moved to the start of the next tax year (i.e. 1 March 2017). This is a purely administrative change.

Potential impact of the amendments

Section 11(3) requires that the amendment considers:

- The revenue raised (to be consistent with the fiscal framework)
- Equity, efficiency, certainty, ease of collection
- The composition of tax revenues
- Regional and international tax trends
- The impact on development, investment, employment and economic growth

Section 8(5) requires that the amendment considers the impact on the fiscal framework, including elements of revenue, expenditure and borrowing.

The only policy change is the removal of the proposed cap per employer. This would meant that this year's TLAB amendments become a pure extension of the existing scheme. This reversion to the current policy design means that there is minimal disruption to current practice.

The postponement of the effective date for amendments to the definition of 'monthly remuneration' is purely administrative.

1. Removal of cap on ETI claims

Employment growth is a key aspect of government's inclusive growth objective. During the SCOF hearings a compelling case was made by claimants that the proposed cap would come at the cost of higher levels of employment. This presents 2 options for the cap: increase the level of the cap or delete the proposal for a cap. Our analysis indicates that a higher cap would affect only a handful of claimants, and would therefore be ineffectual. National Treasury proposes to retract the proposed cap during the next phase of the ETI, given the need to address rising unemployment. This will also lend support to the emerging commitment by key stakeholders to extend employment to a large number of young work seekers – including a commitment to support work seekers with structured training programmes. SARS and the National Treasury will monitor the affordability of the programme as an input to the fiscal framework. Should cost containment of this programme be required the imposition of a cap will be reviewed.

Tax revenue implications

The removal of the proposed cap will affect tax revenues for the duration of the period of the extension of the ETI, namely tax years 2017/18 and 2018/19. Tax year 2016/17 is not affected, since the effective date for cap was 1 March 2017.

In terms of a more micro-assessment to estimate the tax revenue impact, one can consider the latest claims data as a base for analysis. Had the proposed cap of R 20 million per employer been applied in the 2015/16 year, it would have affected claims of 16 claimants and resulted in savings of revenue foregone to the amount of R 557 million.

The estimated revenue foregone due to scrapping the cap would be R0.63 billion in 2017/18 and R0.67 billion in 2018/19. In each case it amounts to less than a percent of PIT revenue and a negligible percentage of total tax revenue.

Deviations to tax revenue estimates	2017/18	2018/19
Estimated revenue foregone		
R millions		
Lower bound	R 532	R 563

Upper bound	R 628	R 665
Relative size of impacts		
Percentage of total		
On PIT revenue	0.11%	0.11%
On total tax revenue	0.05%	0.05%

There are two sets of uncertainty that underlie this calculation, namely (1) the margin of error in overall revenue realization and (2) the margin of error in estimating tax expenditures.

- The MTBPS estimates the tax revenue that is likely to be collected over the MTEF period. While this is a precise estimate at the time of the MTBPS, it is subject to some margin of error.
- Estimates of tax expenditures – like the ETI – are dependent on the behavioural responses from claimants, which are difficult to quantify precisely. This adds an extra layer to the margin of error.

Equity, efficiency, certainty and ease of collection

The equity of the tax instrument would be impacted through different channels on the horizontal and vertical equity of the tax system.

- Vertical equity of employees: Removal of the cap is likely to support greater stimulation of hiring of low-income workers, therefore it is a progressive fiscal measure.
- Vertical equity of employers: Employers can claim the ETI in proportion to the number of employees that are eligible for the ETI. This means that larger employers stand to claim larger absolute claims, though the proportion of claims to taxable income is not likely to be biased in favour of large employers. The cap would have limited the absolute value of claims to R20 million per employer per year, which would have biased the ETI in favour of smaller operations. The removal of the cap restores neutrality of the ETI to size of employers.
- Horizontal equity of employees: Not affected.
- Horizontal equity of employers: Not affected.

The cap was proposed as a measure to improve the cost-efficiency of the programme. The comments on the cap indicated that this improvement in the efficiency of the programme would have come at the cost of effectiveness of the programme, by limiting the potential for job creation. Since the ETI is still more cost-efficient than other job creation programmes, its potential scale takes precedence over the potential efficiency gain.

Certainty and ease of collection are both improved, since the cap was a new design feature which required systems changes.

Composition of tax revenues

Given that the revenue impact on Personal Income Tax is quantitatively small, there would be no impact on the composition of tax revenues, including between direct and indirect tax revenues.

Regional and international tax trends

Not affected.

Development, investment, employment and economic growth

The amendment follows the comments from claimants, who indicate that the cap would have stifled further employment. The removal of the cap will therefore have a positive impact on employment growth, which is a key component to inclusive economic growth.

The fiscal framework

The aforementioned sizes of the impacts relative to total tax revenue (0.05%) and PIT revenue (0.11%), the size of deviations fall well within acceptable margins of error – and therefore the fiscal framework is not affected.

2. EFFECTIVE DATE OF AMENDMENT TO DEFINITION OF 'MONTHLY REMUNERATION'

Tax revenue implications

None. The amendment is intended to clarify the amount of remuneration that feeds into the calculation of the value of the incentive. It does not represent a change in policy design. Both the amendment itself and the move of the effective date would only have affected the precision of the monthly claims by employers. The amendment and move of effected date allows for great precision, which merely lowers the risk of penalties and interest charged on incorrect claims. This does not form part of tax revenue.

Equity, efficiency, certainty and ease of collection

There are no impacts on equity and efficiency of the tax instrument. Certainty and ease of collection is improved.

Composition of tax revenues

No impact.

Regional and international tax trends

No impact.

Development, investment, employment and economic growth

No impact.

The fiscal framework

No impact, since there are no revenue implications.