CREATING OUR SHARED FUTURE

Strategic Considerations for a Comprehensive System of Social Security

DISCUSSION PAPER

Building a caring society. Together.

social development

Department:
Social Development
REPUBLIC OF SOUTH AFRICA

FOREWORD BY THE MINISTER

You will recall that in June 2006, the Department presented you with a document entitled Reform of Retirement Provisions: A discussion Document. In that report, we spelled out in great detail the strategic challenges and weaknesses of our system of retirement provision. The following year we presented a further report entitled "Reform of Retirement Provisions: Feasibility Studies". This was a technical report prepared by a team of highly skilled experts from our own country, who subjected our initial proposals to further scrutiny and feasibility assessment to ensure that our policy proposals are based on sound evidence. We were very pleased with the extensive comments and contributions we received from various stakeholders on these findings. We were also privileged to benefit from the input of internationally renowned social security experts, who examined all the proposals I am now presenting to you. The report they provided is also attached in this report that I am now presenting to you.

This discussion paper, entitled "Creating our shared future – Strategic Considerations for a Comprehensive System of Social Security" is the most comprehensive social security proposals we have presented to date, spanning both the social insurance or contributory side, and the non contributory or social assistance component of our social security system. The social insurance component now extends beyond retirement provisions, and also addresses the other contributory provisions relating to schemes such as the Unemployment Insurance Fund, Road Accident Fund, occupational injuries provisions and other coverage gaps that have been identified.

On the social assistance component, we are proposing the extension of coverage to various categories of people that are currently excluded from cover. We have identified specific vulnerable groups such as children over the age of 14, caregivers of children, unemployed youth, unemployed adults, and older persons who currently do not benefit from the state old age pension. We have also examined other interventions that government may consider to enhance the impact and effectiveness of our existing income support. In addition to these, we have given much consideration to the significant institutional shortcomings in the governance and supervision of our system, and we offer some far-reaching proposals for an institutional overhaul of our social security system.

These proposals are informed by a firm view that our social security system requires fundamental reform, and this cannot and should not be undertaken in a piece meal fashion. For this reason we would like you to consider the whole suite of proposals as components of one package of reform that will in the end result in an inclusive, affordable, sustainable and comprehensive social security system. This is our just offering to the citizens of this country, whom we believe will share our vision of a society where the needs of those who have endured many decades of debilitating poverty and pervasive exclusion are given priority, and those who have the means to contribute receive fair compensation and appropriate protection from the government they have appointed.

Of course, as is the nature of any policy development process, the consultation and deliberation is all-important if we are to achieve the kind of social security system that we all desire. So come let us reason together and continue in the same spirit of collective policy formulation that we have begun. What I am presenting to you today is an invitation to continue our dialogue, and extend our conversation by broadening our outlook to examine a more comprehensive suite of social security provisions.

As we have heeded your contributions in the past, we will continue in this same vein.

Ms Edna Molewa
Minister of Social Development

FOREWORD BY THE DIRECTOR GENERAL

Since the publication of the Taylor Committee of Inquiry into a Comprehensive System of Social Security, government has engaged in a concerted effort to crate a more coherent and integrated system of social protection in South Africa. Over the last twelve years, we have focused our attention on poverty alleviation through the extension of access to social assistance to more than 13 million South Africans, and improved our institutional capacity to render efficient, effective and equitable services to all eligible beneficiaries through the establishment of the South African Social Security Agency.

Over the last few years, we have begun to shine the spotlight on the contributory components of our social security system. Regrettably, we have found much that needs to be addressed. In 2006 we invited your input and comments on a discussion document entitled: "Reform of Retirement Provisions, a Discussion Document", which provided an extensive situation analysis of the key weaknesses and challenges in our retirement provisions. In 2007, we presented you with another document entitled: "Reform of Retirement Provisions: Feasibility Studies", where we detailed the research reports we had commissioned to examine the feasibility of key proposals we had made.

Many of our stakeholders took the opportunity to engage with us on the findings and proposals contained in these reports, by providing written submissions and also participating in various workshops and interactions throughout the country. I must sincerely thank all the stakeholders who have participated thus far, and inform you that your voices have indeed been heard. A key theme that has permeated all our interactions with you over the last two years has been the inextricable link between the contributory and non-contributory aspects of our social security system and the need to create a coherent system that enables all residents in the country to move seamlessly between the two as their circumstances change throughout their lifetimes.

It is for this reason that we have now consolidated all our proposals into one document, and named it "Creating our Shared Future", because we do indeed want to create a future in which all South Africans can have a stake, irrespective of their means, colour or creed. In our various interactions over the last two years, I was really struck by how close we are to each other in our goals, objectives and the principles that we propose to guide the reform agenda. This is particularly important, as it speaks to the nature of the society we want to create, and the values we want to inculcate in our communities. Those values are of course not new, as they are already enshrined in our constitution. We have heard the resounding call for social solidarity and inclusion, the need for us to recognize the rights-based approach espoused in our constitution, and the need to improve efficiency and transparency in our social security system.

We have devoted Section 1 and 2 of the report to these issues, beginning with a brief overview of the historical context of the proposed reforms, and then specifying some key aims and strategic objectives of a current social security reform evolving in the country. Section 3 is a description of the components of a comprehensive social security system. In section 4, we present a detailed analysis of the present socio-economic context within which our social security reform is currently being undertaken, and then describe in some detail the specific gaps in our social assistance, the absence of clear social insurance provisions and the related weaknesses in our institutional framework for social security.

Section 5 describe the way forward in terms of creating a social security system that address the non-existent of the contributory social security that affects many income earners in the country. It further extrapolates the non-integration of programmes that are geared towards alleviating poverty in many households in the country inclusive of the social assistance programmes.

Section 6 contains the detailed proposals on how our social assistance provisions need to be expanded in order to enhance the human development in the country. This includes extending social assistance to children up to age 18, caregivers of children, unemployed youth, unemployed adults, older persons from 60 years of age, people with disabilities of all categories and severely disabled children and their care givers. This amongst others will require a concentrated effort from the society in terms of creating a system of income support and redistribution which will ensure that the entire population will benefit from the economic growth.

Section 7 and 8 focus on retirement, and the death or disability of a breadwinner in the household. The key proposal is the introduction of mandatory contributions to protect income earners and their dependants, and some benefit design considerations to ensure some minimum protection against various contingencies. Related institutional challenges are also addressed, including the lack of coherence in the existing framework that leads to inefficiency and unintended consequences. Section 9 and 10 address challenges in the existing mandatory schemes, i.e the Road Accident Fund (RAF) and Compensation for Occupational Injuries and Diseases (COIDA).

The issues that we have presented in this report have emerged from the extensive interactions we have had with you over the last two years. The opportunity we have had to debate the first principles has provided an incredibly useful exchange which we have fed into the policy proposals we now present. I hope that you will recognize some of your contributions in the new proposals we are presenting to you now, as we invite you again to engage with us in what is proving to be a fruitful iterative process to arrive at the best fit for our country.

One rather embittered scholar of history has told us that “history teaches us that history teaches us nothing’. But I am sure you will agree with me that such cynicism has no place in our context. We can draw great lessons from our very recent history that the courage and commitment of a united civil society can win great victories against impossible odds. Fifteen years ago the odds were institutionalized racism, now the odds are poverty and underdevelopment.

Of course our present enemy is more insidious and harder to target, so we have to become sharper and more creative in our strategies. Of necessity, it means that we must commit to a continuous engagement, which requires both consistency and flexibility on both sides. Based on the extensive input we have received thus far, I am confident that there is enough commitment on both sides to continue this robust engagement.

Vusi Madonsela
Director General: Department of Social Development

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Definitions

Accredited Retirement Institution (‘ARI’): Private retirement arrangements companies that are authorised to manage mandatory individual accounts.

Basic Contributory Pension (’BCP’): A defined-benefit arrangement that is mandatory for all people with earnings above a designated income level.

Beneficiaries: Members or dependants of members who are entitled to social security benefits.

Ceiling: This refers to the maximum mandatory social security contribution level expressed in relation to an income level.

Contribution floor: The income level above which individuals are obliged to make social security contributions. If the contribution floor is R12 000 per annum, the social security contribution will be calculated only on income above R12 000 for all members. People earning below the contribution floor would not be included in the contributory social security system.

Contributors: Those persons or entities that are required to make a social security contribution, e.g. ‘members’, ‘employers’ and ’government’.

Defined benefit (‘DB’): A retirement arrangement where benefits are specified and are independent of the value of individual contributions.

Defined contribution (‘DC’): A retirement arrangement where benefits are dependent on the value of contributions plus investment returns, less the expenses for operating the arrangement.

Master Social Security Register (‘MMSR): It’s a registry that contains the most up-to date information on the population.

Minimum wage: A statutorily set minimum level of wages applicable to employees in the formal sector.

National Pension Fund (‘NPF’): A proposed statutory retirement fund to be established by government for the purpose of managing mandatory retirement risk benefits and basic benefit arrangements. It can also manage mandatory individual accounts placed with the fund.

Notional defined contribution (‘NDC’):	This refers to a defined benefit retirement arrangement that provides benefits calculated in the same way as a defined contribution arrangement.
Pay-as-you-go (’PAYG’):	Any system of retirement or risk benefits that are paid from current contributions.
Social security contribution:	A member’s legally required contribution toward a combination of social security programmes.
Social security benefits:	In the context of this paper this refers to both ‘retirement benefit’ and ‘risk’ benefit arrangements.
Social security Intermediary (SSI):	A public interface arrangement, which would consolidate the interface between the general public and the social security system within a single Agency.
State Old-age Pension (’SOAP’):	The existing means-tested social assistance benefit provided to females over the age of 60 and males over the age of 61.
Threshold:	In this report this refers to any contribution parameter defined as a percentage of the member’s gross income.
Universal Basic Pension (‘UBP’):	The non-contributory pension available to all qualifying residents in South Africa. This would replace the current SOAP.

1. OVERVIEW

1.1 Background

Starting with the publication of the report of the Taylor Committee of Inquiry into a Comprehensive System of Social Security in 2002, government has been considering creating a more coherent and integrated system of social protection in South Africa.

The way forward has been complicated by the following three factors:

1. The fragmented nature of the existing system of social security
2. The extent of inequality in our society at present
3. The present level of economic development.

These three factors can be overcome in a substantially improved system of social security. However, significant structural and institutional change is required.

With regard to the reform of social security, the central priorities are:

1. To ensure a comprehensive and affordable social assistance framework.
2. To introduce a contributory social security framework that will protect income earners
3. To introduce the appropriate redistributive measures (i.e. measures to share resources more equally) aimed at income earners.
4. To establish integrated, coordinated, efficient and responsive institutional arrangement of both the non-contributory and contributory schemes as a whole.

1.2 Purpose of this document

This document is intended to provide information on social security that can be discussed by the general public under the guidance of the Department of Social Development. The positions outlined in this report are not final; they represent options for the future that can be considered by all concerned. Certain social security policy areas, such as National Health Insurance ('NHI'), are not fully discussed in this report as they form part of separate consultation documents and processes.

2. AIMS OF SOCIAL SECURITY REFORM

2.1 Overview

The aims and objectives of the social security system indicate what needs to be done in order to effectively introduce this system. However, to date,these aims and objectives have not yet been formalised. This section therefore provides aims and objectives for consideration.

2.2 Composition of the social security system

The aims and objectives need to be directed at the social security system as a whole, rather than at certain parts of it. The system includes government departments; statutory institutions; regulated private institutions; regulatory authorities; and judicial and semi-judicial arrangements.

2.3 Aims

We propose that the aims of the social security system should be:

1. To integrate the social security system in such a way that no individual or family
   a. is forced to live below a reasonable level of income;
   b. suffers severe reversals of life circumstances due to any contingencies.
2. To promote the integration of all people and families into a well-functioning society.

2.4 Strategic objectives

Six provisional strategic objectives, consistent with the above aims, have been formulated. They are:

1. Income insufficiency should be eliminated and prevented, regardless of the cause.
2. Contributory social security should be structured to be as

inclusive as possible.

3. Subsidies of any form should be transparent and focused on the achievement of social security objectives.
4. Social security arrangements should apply equally to citizens and permanent residents, with the fair treatment of temporary residents.
5. Public and private social security arrangements should, without exception, be subject to adequate oversight, regulation and governance.
6. The social security system should, as far as possible, encourage employment creation and formal-sector participation.

3. GENERAL SOCIAL SECURITY CONSIDERATIONS

3.1 Introduction

The social security system is usually regarded as having contributory and non-contributory parts. Together these should provide income protection and access to services in the case of certain events, including early death; disability; old age; poor health; the need for health services (maternity etc.); and unemployment.

The significant social and economic changes taking place in South Africa suggest that we need to think about broadening social security beyond traditional approaches to include developmental objectives.

3.2 Non-contributory social security arrangements

Non-contributory social security arrangements (e.g. social assistance) aim at sharing our resources more equally and are normally funded from general taxes. Although they are important in all countries, such arrangements are more important in poorer countries since economic development in these countries often disrupts communities. Although these arrangements have a developmental purpose (in other words, are designed to build up the poorer parts of society) their effect is limited by a scarcity of resources. In the absence of proper organisation, they could also make human development more difficult, thus reducing the economic potential of the country over time.

3.3 Contributory social security arrangements

Contributory social security arrangements (in other words, funds into which people pay regular amounts over a period of time) are aimed at helping people to protect themselves by acquiring insurance policies that will ensure that they receive financial assistance in case of sickness, death and disability, for example. Contributory arrangements are aimed mainly at income-earning households and exclude households that do not have a regular income.

Contributory social security tries to share risk and smooth out an individual's income over his or her lifetime. This is typically not possible when arrangements are voluntary, for profit and unregulated. The establishment of contributory social security does not depend on the availability of national resources, but rather draws on a reasonable proportion of individual and/or family income.

Although contributory social security arrangements focus on apparently less vulnerable groups than do non-contributory arrangements, both are important.

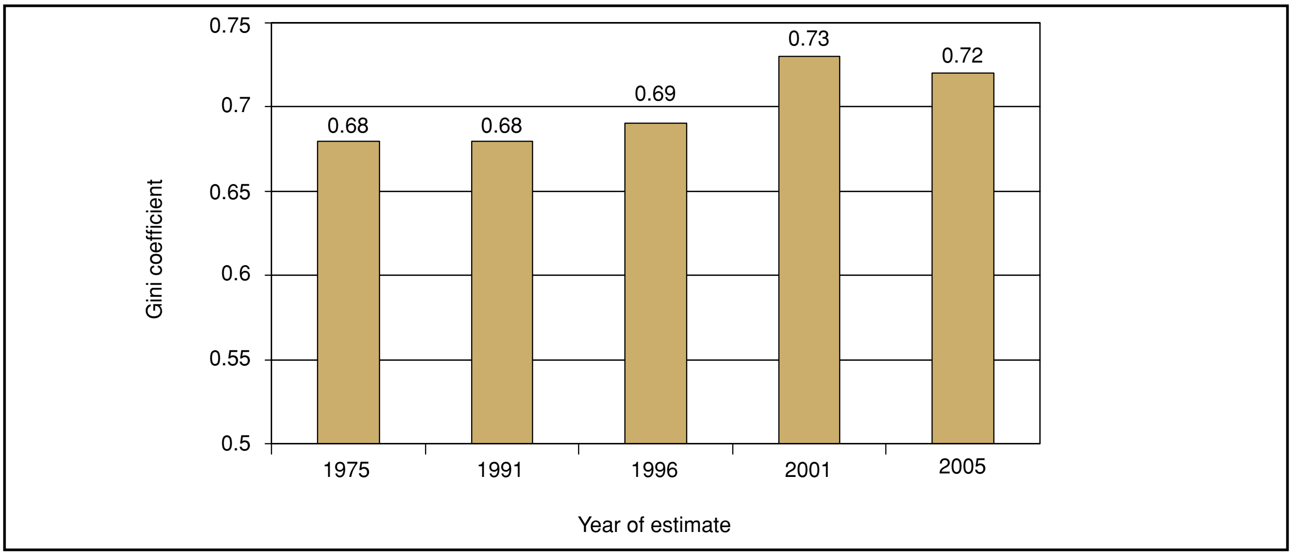
4. CONTEXT FOR SOCIAL SECURITY REFORM

4.1 Socio-economic context

South Africa is characterised by high levels of social and economic inequalities, with more than half the population not participating properly in the modern economy. According to the Income and Expenditure Survey (StatsSA, 2005/06), income inequality remains very high, with only 10% of the population receiving over 50% of household income from work and social grants. Over the past decade, income inequality has also worsened within all population groups, with the proportion of the population living in poverty showing no real improvement.

Of real concern is the increase in inequality within each population group, as well as an apparent break in trend, with inequality rising from 1996 (CSSR, 2004). The Income and Expenditure Survey ('IES') (StatsSA, 2008) further indicates that the level of income inequality in 2005/6 remains largely unchanged from 2001. These estimates furthermore suggest that, in the global context, South Africa is among the countries displaying the highest degree of enequality.

Figure 4.1:Gini coefficient estimates from 1975 to 2005



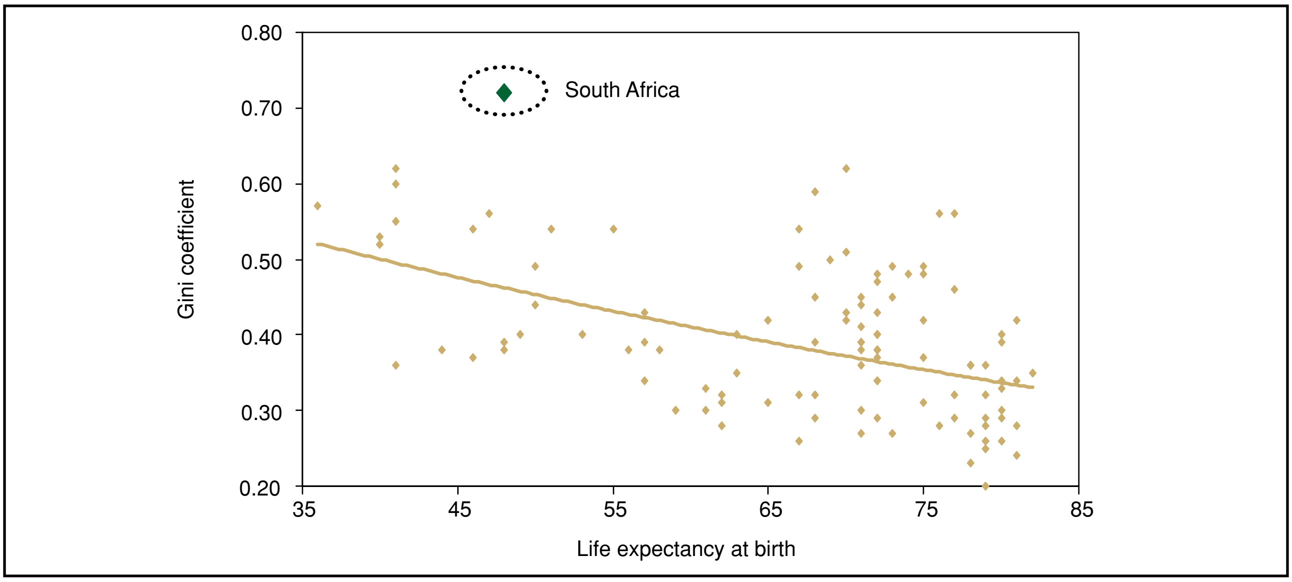
Sources: CSSR, 2004; HSRC, 2004; StatsSA, 2008

Box 4.1: Gini coefficient definition

The Gini coefficient is a measure of statistical dispersion most prominently used as a measure of inequality of income distribution or inequality of wealth distribution. The range is from perfect equality at '0' to perfect inequality at '1'.

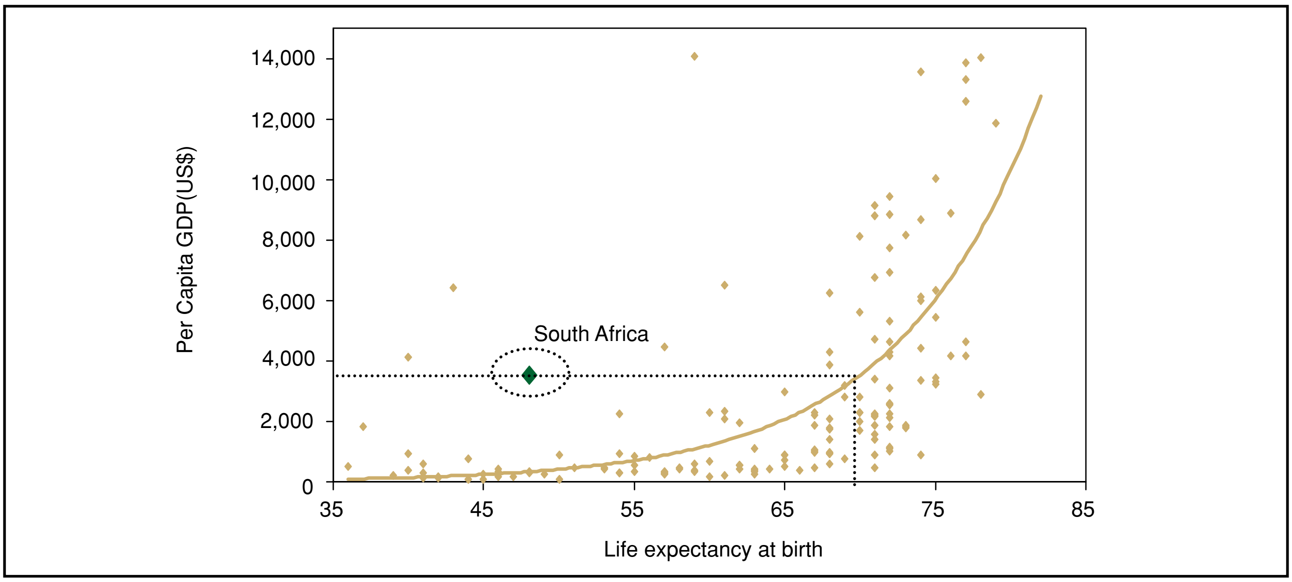
Although over the past decade access to certain basic services and social security has improved for some, human development has not shown any improvement. On the contrary, indices associated with human development have in fact gone into reverse. In 1990 the under-five mortality was 60 per 1,000 live births. By 2000 this had increased to 63, and to 67 and 68 for 2004 and 2005 respectively. Deaths from tuberculosis ('TB'), which were 64 per 100,000 of the population in 1980, rose to a high of 153.6 in 1997, and then improved to 71.7 by 2004. Thus deaths from TB were higher in 2004 than in 1980 (WHO, 2006). Internationally, South Africa is anomalous as regards both Life Expectancy at Birth, an important indicator of social well-being, and income inequality (Figure 4.2). Furthermore, Life Expectancy at Birth is out of line for a country with South Africa's per capita Gross Domestic Product ('GDP') (Figure 4.3). Although HIV/AIDS is a factor, it is possible that poor social and economic conditions are contributing to the worsening of the pandemic.

Figure 4.2: Gini coefficient estimates and Life Expectancy at Birth for a sample of countries



Sources: World Bank, OECD, and StatsSA 2008

Figure 4.3: Life Expectancy at Birth for a sample of countries compared to GDP per capita (US$)



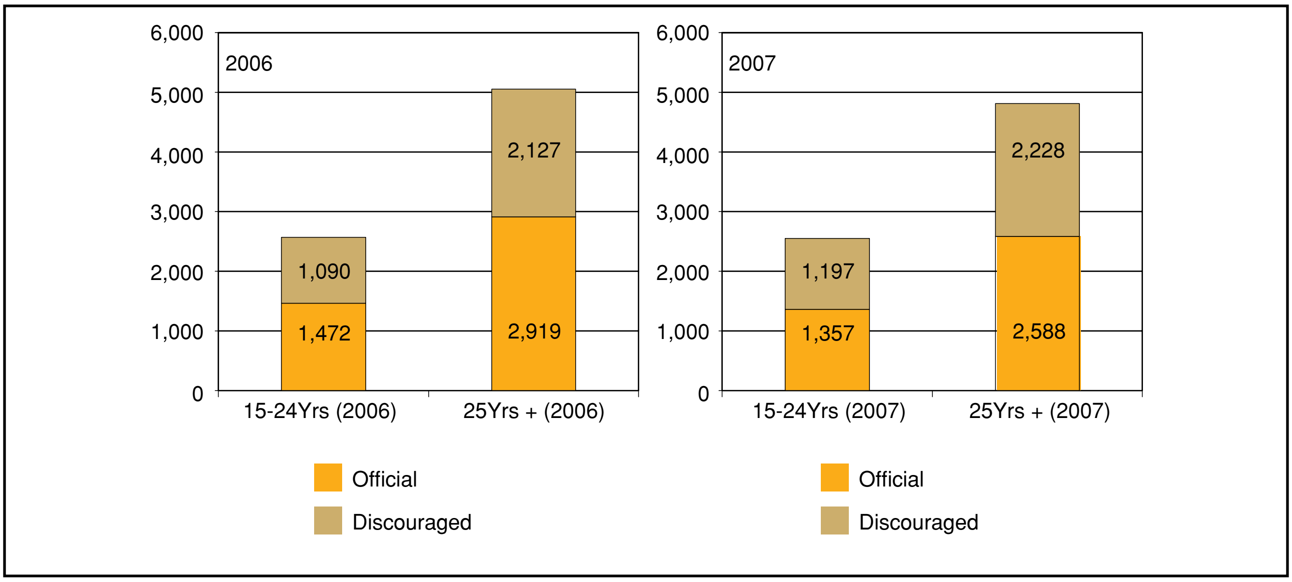
Source: OECD

South Africa's socio-economic conditions are largely caused by the structure of society and the economy, with the majority of the population living in conditions that effectively exclude them from advancement and SOAPortunities. Poor human development limits the extent to which many can be integrated into a positive and well-functioning society. High levels of unemployment, together with periods of high economic growth rates, indicate that there is a problem.

In 2007, there were more than 7.3 million unemployed and discouraged work seekers in South Africa (StatsSA, LFS, September 2007). Of this number, 35% were below the age of 25 (youth unemployed). In total, therefore, this level of unemployment impacts on the income security of more than 25 million people, including dependants.

The number of discouraged work seekers (those who wish to work, but have given up seeking employment) is broadly similar to the official calculation of unemployment (those who are actively seeking employment). The extent of youth unemployment, including those who are discouraged, is a problem that relates to the structure of society and the economy, and is unlikely to change if government does not actively deal with the problem.

Figure 4.4: Unemployment by broad age band in September 2006 and 2007, including discouraged work seekers (000)



Source: Labour Force Surveys, September 2006 and 2007.

Box 4.2: Youth unemployment

'… 51 per cent of all school-leaving first-time labour market entrants will fail to secure jobs, and this figure rises to 71 per cent per year for African first-time entrants. The primary contradiction here is that, as the school system has grown over the past decade, so the number of formal sector jobs available to school-leavers has shrunk. … There are a number of factors that determine this institutional disequilibrium. First, the fundamental problem facing the youth labour market is the low-growth, low employment scenario, characteristic of the South African economy. Second, it is likely that the actual or perceived poor quality of South African schooling … serves as a major disincentive on the demand side for employing large numbers of first-time entrants to the labour market, with qualifications equivalent to matriculation or less. This demand-side disincentive adds further fuel to the 'skewing effect' of the ever-increasing capital and skills-intensity in production.'

Source: Kraak, 2004

The evidence suggests that South Africa is not keeping up with its human development requirements, and is in fact going backwards in some cases. The problem may be that the economy is not able to draw more people into regular employment. When there are periods of economic growth, these seem not to contribute towards the development of human potential. This raises important questions about whether existing government programmes aimed at bringing about a more equal sharing of resources are working properly.

In summary, therefore, the fact that inequality has increased, despite positive short-term economic growth rates, means that government should carefully reconsider its allocation of resources. Strategies need to be coordinated in such a manner that meaningful progress is made in advancing the well-being of the vast majority of the population. In particular, these strategies need to make a real difference to the socio-economic context so that inequality is reduced and human development is improved. If this is not achieved, South Africa's long-term growth potential will be limited.

4.2 Social security system

4.2.1 Non-contributory social security

South Africa's system of social security has important non-contributory arrangements, including social assistance, public and subsidised schooling, and public health services. The non-contributory system is, by its nature, redistributive (i.e. aimed at sharing resources more evenly), and represents the most important pillar in achieving advances in human development and social integration.

Social assistance to low-income households is the most important way in which government tries to eliminate income poverty. There are approximately 13 million beneficiaries on the social assistance system, the largest part of which is the Child Support Grant ('CSG') with around 8.6 million beneficiaries. The next most important programmes involve provision for old age, the Older Person's Grant ('OPG') with 2.2 million beneficiaries, and the Disability Grant ('DG') with 1.4 million beneficiaries.
Although social assistance is a substantial programme with significant impact, many gaps remain. Using a poverty indicator of R552[1] (in 2005) per person per month, many people remain in poverty despite the existence of social assistance.

Value of benefits:

At best, the annual adjustments to benefits keep pace with general inflation rather than economic growth. As a consequence, the earnings gap for the lowest-earning households relative to higher-income earners widens systematically over time. In other words, because social grants do not keep up with economic growth, the gap between those earning a regular income and those who receive social grants gradually increases over time.

Programme shortfalls:

1. Children in poverty aged 15 to 18 receive no income support.
2. Caregivers of children in poverty receive no income support.
3. Males aged 60 years receive no income support.
4. Structurally unemployed youth (ages 19 to 25) receive limited or no support.
5. Structurally unemployed adults (ages 26 to 59) receive limited or no support.

Means tests:

1. The means tests are not adjusted consistently for general inflation or to cater for higher-income earners who are in need of income support.
2. The means tests unfairly exclude income categories in need of income support.

Access:

Although access to state institutions that assist those in need of social assistance and other essential services is improving, it remains inadequate.

1 This is based on the Taylor Committee's proposed poverty line (2002) adjusted to 2005. Although other poverty lines are lower, any income below R552 per month is clearly severely constrained.

Box 4.3: Means tests and the targeting of social assistance

'The rationale for means testing is primarily to save money. The evidence … highlights the many costs of targeting, particularly through a verified means test. These include not only the financial costs of the required administrative capacity but also political costs, social costs, economic distortions and the direct cost to the beneficiary. In addition, means testing can lead to the exclusion of the poorest – the people that the social protection policy aims to reach. While international experience offers evidence about many alternatives to means testing, including proxy means testing, geographical targeting, community-based targeting, and others, these generally cannot be implemented within a rights-based approach. Reforms to the means testing process are most likely to be feasible, cost-effective and rights-based if they move in a more universal direction.'

Source: Samson et al., 2007.

4.2.2 Contributory social security

Contributory social security in South Africa is almost non-existent. (This is a form of social security to which all those earning a regular income contribute.) Instead, use is made of private social security provision (pension and medical funds, etc.), which is only partially regulated by government. Therefore there is no form of social security in South Africa by which higher-income earners assist those in need. This is unusual even for a 'developing country'.

Box 4.4: Comments on the private system of retirement

'The adequacy of coverage provided through voluntary private provision is questionable. … An analysis … suggests that the industry-wide replacement rate [for private retirement] must be around 23.4%.'

'Consumers remain disempowered to a great degree by the current framework. Transparency is poor, with the value for money of products on the market deliberately opaque. Recourse in cases of abuse, although it exists, is unlikely to prevent many retirement funds and intermediaries from skimming from large numbers of the public.'

Source: Department of Social Development, 2006.

4.2.3 Institutional considerations

The social security system is not well integrated, and the non-contributory and contributory parts of the system do not work together as a single system. The responsibility and authority for an area of social security is often divided among several departments, usually along the lines of non-contributory versus contributory arrangements. Problems in the drafting of policy might also have contributed to the slow development of the social security system (see Table 4.1).

Furthermore, access to the social security system is uncoordinated, with each institution operating separately from the others, with low levels of integration, coordination, or cooperation. Users of the system have to deal with too many different access points and differing standards of service. This means that fewer people register for social services, often because they do not understand the system.

The management of the social security system is weak, with different approaches used for different organisations (e.g. UIF, SASSA, COIDA, etc.). Individual institutions therefore do not see themselves as forming part of a single integrated system with common values and aims. Existing SOAPortunities for cooperation and the sharing of resources and systems are therefore not being utilised.

Since social security is poorly controlled and managed, social security objectives in private markets are not being achieved, with the one exception of medical schemes. In many cases there is very little control, and many important private arrangements are exempted altogether from regulation (e.g. the Government Employees' Pension Fund).

Table 4.1: High-level summary of social security institutional arrangements

Specific Policy Area	Function	Institution	Reporting line	Policy Responsibility
Poverty alleviation for the Aged	Social assistance for those in old age without income	SASSA	MoSD	DoSD
Poverty alleviation for people with disabilities	Social assistance for the disabled without income	SASSA	MoSD	DoSD
Unemployment	Insurance against unemployment	UIF	DoL	DoL
Employment activation	'Various'	DoL	DoL	DoL/DoSD
Road Accident third-party insurance	Health, death and disability insurance	RAF	DoT	DoT
Occupational injuries and diseases	Health, death and disability insurance	COIDA	DoL	DoL
Occupational diseases	Health, death and disability insurance	ODMWA	DoH	DoH
Contributory retirement	Earnings-related savings for those in old age	Regulated private	FSB	Treasury
Contributory risk benefits	Death and disability insurance	Regulated private	FSB	Treasury
Healthcare services	Healthcare services	DoH	DoH	DoH
Contributory healthcare	Health insurance	Regulated private	CMS	DoH

Abbreviations:

CMS: Council for Medical Schemes
COIDA: Compensation for Occupational Injuries and Diseases Act
DoH: Department of Health
DoL: Department of Labour
DoSD: Department of Social Development
DoT: Department of Transport
ODMWA: Occupational Diseases in Mines and Works Act
FSB: Financial Services Board
SASSA: South African Social Security Agency
Treasury: National Treasury
UIF: Unemployment Insurance Fund

4.3 Concluding remarks

South Africa has a low level of general human development, and this is getting worse rather than improving. Government should do more to change this, therefore new strategies need to be developed. If South Africa's human development is not addressed, sustainable high rates of growth will not be possible in the future. Furthermore, one of the long-term effects will be the emergence of a permanent underclass, with people unable to lift themselves out of poverty and improve their SOAPortunities in life. Better social policies can change this and put South Africa on the path towards sustainable higher growth and development. Section 5 looks at the policy direction for social security.

5. SOCIAL SECURITY – THE WAY FORWARD

5.1 Overview

Section 4 considered important questions about the extent to which the short- and long-term developmental needs of South Africa are being met. What needs to be considered now is whether investment in South Africa's social security system is too concerned with short-term growth objectives or, alternatively, whether the social investment of the past 14 years has been slow to take effect.

Whatever is decided in this regard, it is certain that the socio-economic reality that exists now will be felt for many generations.

The social harm caused by the existence of widespread poverty, and consequent inadequate incomes, needs to be addressed now as part of a long-term development strategy. If no action is taken to address the extent of current social distress, it may take far longer for a virtuous cycle of improved economic growth and social protection to be achieved. (A virtuous cycle is the SOAPosite of a vicious cycle and refers to a process during which good things support each other to achieve still better things in the future.) It is also quite probable that existing social investment in education and healthcare will under-perform due to the state in which many households must exist.

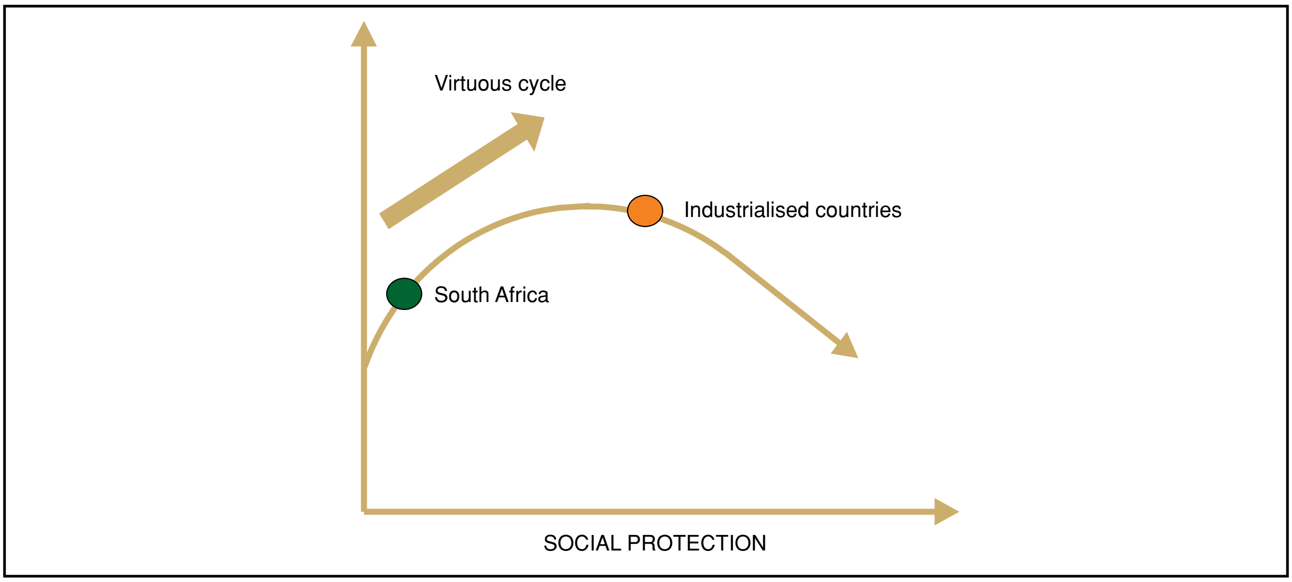
Strong evidence exists that dealing with social distress caused by a lack of income increases social and economic participation (Samson et al., 2007). Increased government grants to households in poverty have led to greater success in work-seeking behaviour and employment. This occurs because households are no longer merely trying to survive from day to day and can consider more positive, longer-term strategies (Figure 5.1).

Social assistance programmes, which try to change the circumstances within which many households exist today, have to be considered alongside other programmes that attempt to distribute society's resources more evenly. These include programmes dealing with housing, basic services, healthcare and education. How do we decide which programmes are more important and should be dealt with first?

In addition to social protection, contributory social security is virtually non-existent in South Africa, and this affects many income earners and the well-being of their households. Serious problems exist in private voluntary social security arrangements in areas such as healthcare, retirement, and the death and disability of a breadwinner. The needs of society as a whole have to be addressed, as is the practice internationally. Although South Africa's social security system will have some unique features, its aims are universal and essential to achieving a well-functioning society. Aspects that need to be considered include compulsory contributions and participation, protected minimum benefits and publicly accountable institutions.

Government, and the country as a whole, therefore need to carefully re-evaluate the quality of existing programmes and institutions, both public and private, that are focused on meeting these needs.

Figure 5.1: The interaction between growth potential and social protection



Source: Based on Samson et al, 2007, p.22

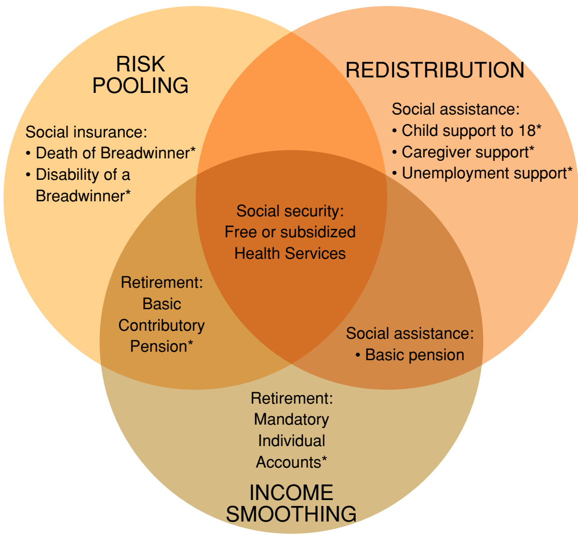
Box 5.1: The Virtuous Cycle

'The wealthiest countries in the world – as a group – have the most comprehensive systems of social protection. Social security is an essential basic service in all successful states that have experienced long-term sustainable growth rates alongside successful poverty reduction. This empirical regularity contradicts the notion of a negative trade-off. … The lower the level of social protection, the more likely will additional investments in social security promote economic growth.'

'A study by EPRI in 2004 found that workers in households receiving both pensions and child support grants looked for work significantly more extensively and intensively, and found employment more successfully.'

Source: Samson et al., 2007.

Figure 5.2: Social security priorities



*New policy area

To address social security effecyively, the following need to be considered:

1. The expansion of the range, value and benefits that have powerful redistributive effects (i.e. that distribute resources more equally) and are mainly non-contributory in nature (i.e. people do not necessarily have to contribute to these funds in order to receive benefits). Many of these programmes share risk and smooth income. However, the main aim is to include in these programmes households that would otherwise be excluded on the basis of income.
2. The strengthening of risk-pooling (the sharing of risks among groups) and income-smoothing where private markets are structurally inadequate (i.e. they do not address the needs of society as a whole). The main purpose of these interventions is to ensure the inclusion of groups that would be excluded from protection for reasons other than affordability.
3. Rethinking the institutional framework that supports social security as a whole. This would require the improvement of current programmes while also developing future programmes.

To ensure the ability of the social security system to assist the country's growth and development, bold steps will have to be taken in terms of both policies and institutions. This will be discussed later in this document.

5.2 Non-contributory programmes: social assistance

> *MEDIUM-TERM OBJECTIVE:*
>
> *To expand and develop the non-contributory system in order to ensure that it receives a balanced share of national resources, and is focused on improving the conditions of the most vulnerable.*

The achievement of this objective involves: allowing people greater access to non-contributory benefits, expanding programmes and benefits, and including all individuals and households vulnerable to income poverty.

Priority groups in this category that are particularly vulnerable include:

1. Children from the ages of 0 to 18
2. Caregivers of children
3. Structurally unemployed persons
4. The disabled
5. The aged.

In addition, basic infrastructure and services are required for communities in distress, including migrant communities that are substantially lacking in social goods and services.

Healthcare is also an important part of social security and requires careful and thorough planning and implementation. This includes the development and maintenance of complex public health infrastructure and services.

5.3 The contributory system

> *MEDIUM-TERM OBJECTIVE:*
>
> *To implement a contributory system designed to ensure maximum inclusion of all people reasonably capable of making a contribution, and benefiting from such a system.*

Expanded participation within the contributory system should be achieved through expanded social solidarity (i.e. where higher-income groups assist the more vulnerable) rather than reliance on voluntary private arrangements (i.e. where people who can afford to, choose to invest in medical and insurance policies, etc.).

The focus needs to be on strengthening risk-pooling and income-smoothing to assist with healthcare needs, old age, disability, early mortality and unemployment. Structural interventions aimed at achieving this include:

1. Mandatory (i.e. compulsory) contributions
2. Mandatory and protected minimum essential benefits
3. Statutory provision (i.e. providing a legal framework)
4. Regulated markets.

These aims can be achieved by providing the necessary legal framework and controlling and managing private markets more effectively. Arrangements that combine various approaches are becoming the norm in social security, but these require strong institutions with good governance and oversight.

5.4 Institutional considerations

MEDIUM-TERM OBJECTIVE:

To establish an integrated, coordinated, efficient, and responsive social security system able to address the requirements of both the non-contributory and contributory arrangements as a whole.

The development of an effective social security system does not require the combining of various entities into a single organisation. However, the authority for key social security areas needs to be clearly established and these areas have to be managed in an integrated way. This will ensure the development of effective policy, including the delivery mechanisms, over time.

Reforming social security to ensure effective delivery means that the following issues need to be considered:

1. Responsibility (and authority) for social security functions needs to be given to various bodies in such a way that both non-contributory and contributory elements are dealt with as a whole.
2. A decision regarding the organisations that should be assigned the authority to provide social security benefits, taking account of:
    a. Oversight and governance requirements (where possible, social partner approaches should be included)
    b. The establishment of specialised institutions that would simultaneously assist various parts of the social security system, with a particular emphasis on:
        i. Access to the system
        ii. Collection of contributions
        iii. Enrolment
        iv. Information management
        v. Administration
        vi. Adjudication.
3. Regulatory approaches that incorporate social security objectives.

5.5 Concluding remarks

The South African system of social security needs to be thoroughly restructured and overhauled. Central to this is the need to consider whether to raise existing levels of social assistance substantially in order to help low income households.

However, the contributory system of social security must also be developed in a way that helps those who currently have adequate incomes, but who may suffer a change of circumstances in the future. Both non-contributory and contributory systems should be developed simultaneously.
However, these objectives must be supported by the development of an institutional model appropriate for South Africa.

6. TOWARDS A SYSTEM OF MINIMUM-INCOME SUPPORT

6.1 Overview

Human development is badly affected by inadequate household incomes. Where income shortages result from short-term factors, such as short periods of unemployment, the household could be protected from undue hardship by using insurance arrangements and savings.

However, where unemployment is due to long-term structural factors, the long-term damage caused to affected households, such as the inability to send children to school and nutritional shortages, needs to be reduced. Failure to properly consider these issues in the South African context will result in a substantial and permanently excluded class of households, with limited prospects of advancement.

However, sometimes income protection mechanisms can lead to undesirable outcomes, such as people becoming dependent on welfare and not living and working effectively. Where benefits are very low, such negative effects are usually limited and outweighed by the positive gains (see discussion in Section 5.1). Nevertheless, in an economy with limited resources, careful consideration must be given to the identification and prioritisation of especially vulnerable groups.

Even though resources are limited, if there were no social assistance as a direct transfer to the poorest households, South Africa's Gini coefficient would be at 0.8 instead of the 0.72 (StatsSA, 2008). Social assistance therefore needs to be understood as the single most important mechanism for balancing the current extremely unequal distribution of income. Given the current socio-economic context, therefore, what needs to be considered is the expansion of social assistance as an important way of keeping household incomes at fairly constant levels. This would reduce the current levels of distress. However, there are numerous methods for targeting benefits, not all of which are efficient or fair. In an expanding system of income support, it is therefore necessary to carefully design and prioritise new benefits.

This section therefore considers an expanded system of income support for all households with very limited incomes. What is discussed is the possibility of targeting certain groups for increased benefits, starting with the most needy and gradually working towards a comprehensive system of social assistance. Each target group has a certain form of need, and these needs should be addressed in the proper order, dealing with the worst cases first. This also allows for the development of specialised programmes to support identified vulnerable groups, as well as the replacement of means tests as the main method of targeting.

6.2 Target groups

All families living in poverty constitute a priority target group for income support. However, these groups can be broken down into different categories of person, and these categories can be used to design programmes specifically for each of these groups, starting with the most needy:

1. Children from the ages of 0 to 18
2. Caregivers of children in the age groups 0 to 18
3. Unemployed youth from the ages of 19 to 24
4. Youth within the ages of 19 and 24 who wish to undergo further education
5. Unemployed adults (excluding caregivers of children) from 25 to 60
6. Older persons from the age of 60
7. People with disabilities of all age categories
8. Severely disabled children and their caregivers.

For the purposes of analysis, disability has been excluded. The resulting approximate headcount and poverty gap for people in the indicated target groups is shown in Table 6.1.

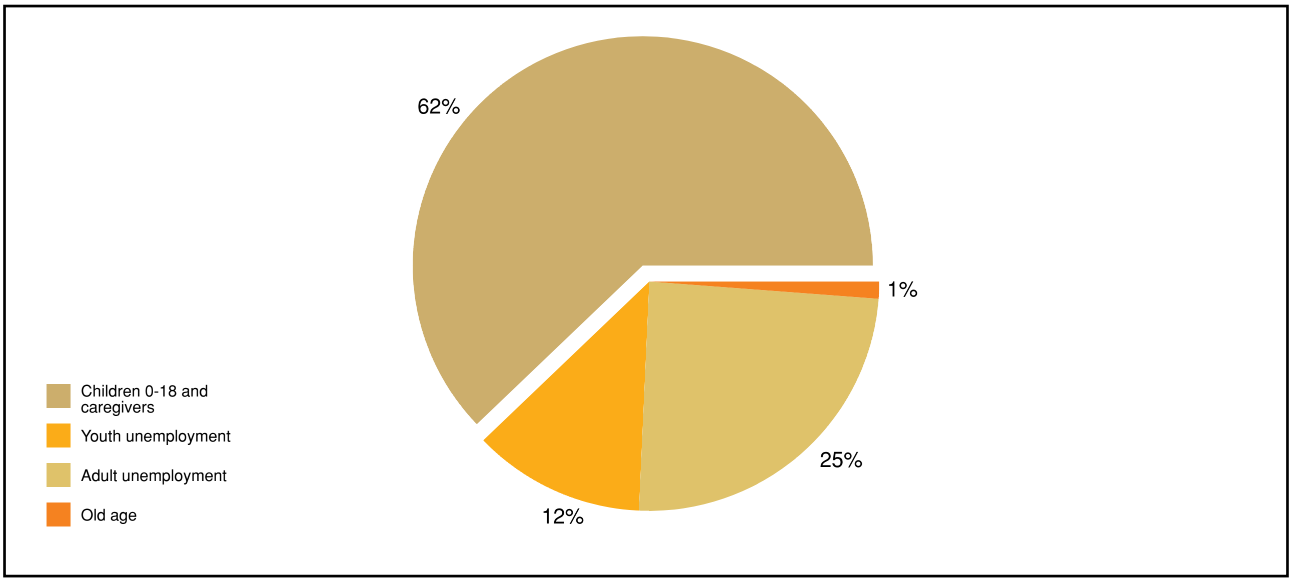
Table 6.1: Population in poverty by target group (2005)

PEOPLE IN POVERTY	Head count	% of total
Children 0-14	10,369,299	22.1%
Children 14-18	2,857,373	6.1%
Females 19-24 (excl. CG)	1,524,751	3.3%
Males 19-24	1,816,646	3.9%
Females 25-59 (excl. CG)	1,411,061	3.0%
Males 25-59	5,336,274	11.4%
Caregivers	3,894,417	8.3%
Old age	339,472	0.7%
Total	27,549,293	58.7%
Total population	46,913,000	

Source: Based on the GHS 2005

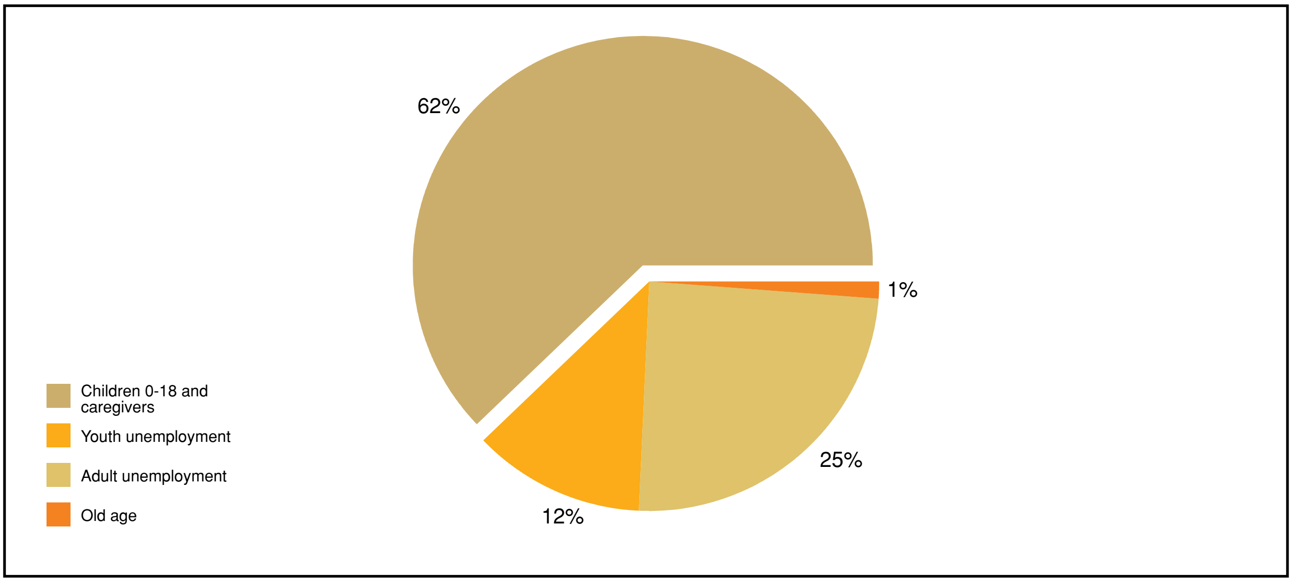
The above categories can be grouped according to related programmes: children in poverty grouped together with caregivers account for 62% of the poverty headcount and the poverty gap. Unemployed youth would account for 12% of the poverty headcount and the poverty gap. Unemployed adults outside of unemployed youth, children and caregivers account for 25% of the poverty headcount and 25% of the poverty gap. The aged (over the age of 60) in poverty account for only 1% of the poverty headcount and the poverty gap. (See Figures 6.1 and 6.2.)

Figure 6.1:Distribution of population in poverty (headcount) when grouped into main categories



Source: Based on GHS 2005

Figure 6.2: Distribution of poverty gap when grouped into main categories



Source: Based on GHS 2005

This indicates that if government were to expand assistance to children and their caregivers, 62% of people living in poverty would be reached. Programmes that seek to assist those who are unemployed would target the remaining 37% of individuals and the poverty gap. Unemployment support can usefully be divided into programmes designed for the youth and programmes focused on the needs of structurally unemployed adults. If the programmes aimed at the youth are successful, the number of structurally unemployed adults will decrease over time. Specific programmes for expanding social assistance will be discussed in Section 6.4. Before this, however, certain general considerations for reforming social assistance will be discussed in Section 6.3 below.

6.3 Reforming social assistance

Some of the target groups already have some degree of support, but many do not. Policy reforms should take into consideration the following:

1. The provision of a system of grants, supporting all the target groups, at values related to both need and what the meeting of this need would mean for society as a whole.
2. Where social assistance grants are provided, these should be steadily increased so that they remain above the inflation level.
3. Over time, grant values need to be improved in real terms to a level where they make a real difference to the beneficiaries and to society as a whole.
4. Income targeting needs to be implemented in the most efficient manner possible and should consider:
    a. Universal benefits subject to tax claw-back arrangements (In other words, the benefits are paid out in a given year, and this amount is then recouped in the form of taxes in the next year or two.)
    b. Means tests where no other approach is practical.
5. Where a means test is applied, the qualifying income threshold should:
    a. Be set at a level that does not result in the exclusion of people in need
    b. At a minimum be adjusted annually for the relevant inflation rate
    c. Be increased over time in excess of inflation to account for economic growth so that beneficiaries are able to change their lives, not merely survive from month to month.
6. These grants should be made subject to certain conditions, including:
    a. In the case of Child Support Grants, recipients should be in school or in further education.
    b. In the case of unemployment benefits, recipients should participate in labour programmes.

6.4 Recommended programme for the expansion of social assistance

6.4.1 Child support

The existing system of support for children living in households in poverty excludes children aged 15 to 18 years, does not support caregivers, provides a very limited benefit, and excludes many families in need due to the means test.

It is therefore proposed that a comprehensive system of child support be established as the ultimate goal. The following would need to be included:

1. All children up to the age of 18 (until the 19th birthday) should be covered.
2. All designated caregivers for child recipients of the CSG should receive a grant ('CCG') that is at least equal in value to CSG
3. The means test should be progressively increased, with the grant ultimately made universal.
4. Once made universal, the benefit should be funded either through a tax claw-back or any mechanism that achieves the same outcome.
5. The benefit amounts should be increased annually by a minimum of 2% in excess of the general inflation until such time as the grant value equals a designated, officially determined level of income sufficiency.

The progressive implementation of this framework will reach 62% of the people in poverty. If implemented, this programme will substantially impact on the most vulnerable households.

6.4.2 Unemployment support

Unemployment insurance already exists through the Unemployment Insurance Fund ('UIF'). However, this benefit lasts only a short time and, as a programme, does not adequately address structural unemployment.
The following should therefore be considered:

1. A continuation benefit should be available to any person coming off unemployment insurance who has failed to find suitable employment.
2. The continuation benefit should be provided for up to three years, subject to conditions.
3. The value of the benefit should be set at a fixed ratio to an officially determined minimum wage, with the following options:
   a. The minimum wage should be set at a value of R1,000 (2007 prices) and adjusted annually in accordance with an index of general wages.
   b. The continuation benefit should be set at 50% of the minimum wage.
4. All recipients of the continuation benefit would need to participate in labour activation programmes where these have been implemented. These could include:
   a. Skills development programmes
   b. Special employment projects with or without a skills development component
   c. Participation in surveys to evaluate the causes of continued unemployment.
5. For people from 25 to 59 years of age who have never been in formal employment, and consequently have never qualified for unemployment insurance, a conditional social assistance grant should be provided at a value equivalent to 20% of the UIF continuation benefit.
6. Conditions for acceptance of the grant should be equivalent to those for the UIF continuation benefit.

This programme, if implemented, would prevent households with unemployed breadwinners from slipping into extreme poverty while at the same time assisting their re-entry into formal employment.

Because the benefits would be below the proposed minimum wage, people would still prefer to find work rather than remain unemployed. The existence of a minimum wage will also improve income levels at the lowest end of the formal labour market.

Over time the institutions running programmes for the unemployed will also start to work together with those that are attempting to improve the employability of the unemployed. This will allow for the constant development and testing of new programmes aimed at reducing unemployment.

An indefinite continuation benefit is also an option. However, should this be implemented, it would take the form of social assistance, would need to be financed from general taxes, and would need to be offered at a lower value than a limited benefit in order to be affordable.

This proposed system could also incorporate a general unemployment benefit for the long-term unemployed. This would take the form of social assistance and would have conditions attached that are similar to those applicable to the UIF continuation benefit. However, the value of the benefit would need to be lower than the UIF continuation benefit in order to be affordable, and to ensure that people would still have the incentive to find work. It could also be de-linked from UIF.

Overall this strategy, if implemented fully, should address all adults in poverty from the age of 25 who are not caregivers of child recipients of the CSG. It would also boost the incomes of the lowest income earners in formal employment. At least 25% of the population in poverty would be assisted both financially and structurally.

6.4.3 Youth employment support

Youth entering the labour market for the first time face numerous challenges. If these challenges can be overcome, structural unemployment later on in life should be reduced. For this reason a specific youth strategy linked to a conditional social assistance benefit should be considered. It could have the following characteristics:

1. A conditional social assistance grant should be provided to unemployed youth, defined as persons from 19 to 24 years of age, at a value of 30% of the unemployment insurance continuation benefit
2. Conditions for the grant would include:

a. Assessments by a labour and skills adviser
b. Successful participation in skills-acquisition programmes
c. Participation in employment structured to enhance skills development
d. Participation in surveys to evaluate the continuation of unemployment.

3. Should a beneficiary fail to achieve set skills acquisition goals, up to 50% of the grant value could be removed for set periods, e.g. up to 12 months.
4. If a recipient does not participate in any structured programme at all, the grant should be removed completely for a set period.

If implemented fully, this programme will target 12% of the population in poverty. It will see to their immediate survival requirements as well as their structural exclusion from the labour market. If successful, this programme should impact on the employability of adults over the age of 25.

6.4.4 Old age

The poverty headcount for those in poverty over the age of 60 is relatively small (1%). It is nevertheless proposed that the existing Old Age Pension ('OAP') be adjusted to become universal, i.e. the means test is entirely removed. Already the qualifying age is being adjusted to 60 for both males and females. This reform should form part of the general reform of the retirement system discussed in Section 7.

6.5 Impact of expanded social assistance

If a comprehensive programme as outlined here, were to be implemented with existing social assistance programmes retained at their current grant values ('Scenario 1'), the social assistance budget would increase from R43 billion to around R67 billion at 2005 prices, which would amount to an increase of R24 billion per annum. The Gini coefficient would adjust from 0.72 to 0.68, with a 37% reduction in income poverty. Even though poverty would not be eliminated, every household in need of income support would receive assistance in one form or another.

Were the existing CSG and CGG to be increased by 20% in real terms, with all the other arrangements remaining the same ('sSenario 2'), the social assistance budget would increase by R30 billion to R73 billion per annum. This would achieve an improvement of the Gini coefficient to 0.66, with a 41% reduction in income poverty.

Table 6.2: Scenarios for an enhanced system of minimum income support (2005 prices and estimates)

	Expenditure (annual)	Poverty gap (income) (R'000)	Gini coefficient
Existing scenario	R43 billion	R123 billion (-0%)	0.72
Scenario 1	R67 billion	R78 billion (-37%)	0.68
Scenario 2	R73 billion	R73 billion (-41%)	0.66

The increased expenditure required for the above scenarios are shown as one-off increases for the purposes of illustration only. Given the large sums required, programmes would have to be introduced in order of priority. Such sequencing is possible: each element of the grant system can be extended individually, according to what can be afforded. It is recommended, however, that the system of grants make a real difference to the social and economic conditions of the poorest.

6.6 Grant extension prioritisation

A timeline for the expansion of minimum income support is provided in Figure 6.3. It is proposed that this occur over the period 2009 to 2015. The full grant system should be phased in in order to make it more affordable. Where affordability proves a problem in any given year, implementation could perhaps be deferred.

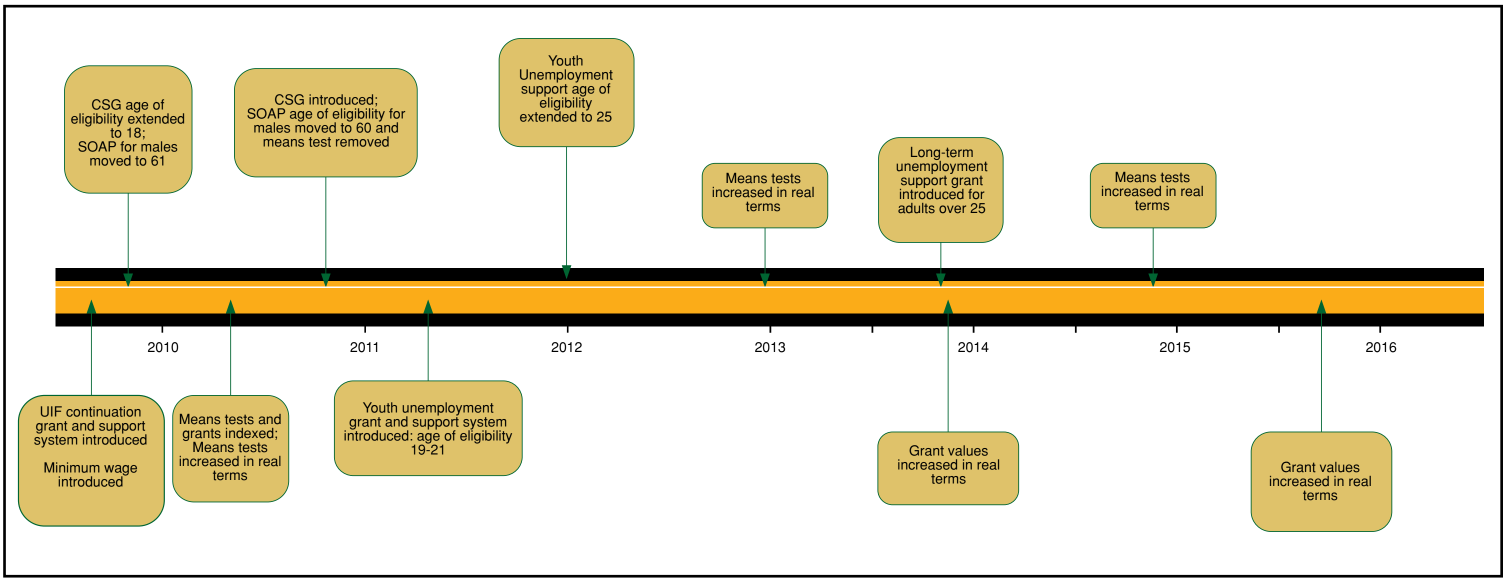
Priority in phasing is given to the CSG and the CGG. The youth unemployment programme for the age group 19 to 21 is prioritised for 2011. The process of modifying means tests and introducing the indexation of grant values is also proposed for early implementation.

The establishment of a UIF continuation benefit is also prioritised for early implementation. The implementation of a minimum wage would be linked to this programme. The minimum wage should be indexed to the wage index.

Adjustments to the means test thresholds and grant values should be considered every two to three years. The full implementation of the youth support system could be considered for 2012, while the basic system of unemployment support for people over the age of 25 could be considered from 2013.

It is important to emphasise that these proposals are for the purposes of consultation and discussion, and do not represent a final position. Nevertheless, the proposed programme illustrates how implementation can be introduced gradually and according to what is affordable.

Figure 6.3: Indicative timeline for the expansion of social assistance



6.7 Concluding remarks

The expansion of the social assistance system in South Africa is possible and will enhance human development, which will lead to higher levels of sustainable growth. Although immediate benefits are likely, the long-term impact should also be considerable. It will provide a reasonable system of income support and redistribution, which will ensure that the entire population is able to benefit from economic growth. It supports continuous improvements in social conditions and human development across the entire population. The programme could also be introduced in phases in accordance with what is affordable.

7. RETIREMENT AND OLD AGE – TOWARDS A COMPREHENSIVE SOLUTION

7.1 Overview

People in old age usually suffer a reduction in faculties and health, and therefore become more vulnerable. Their ability to earn an income declines dramatically after a certain age. This problem can be reduced if they have accumulated savings during their working lives. However, if they have not earned enough in their lifetime, hardship is inevitable.

Currently provision for old age is available both on a non-contributory and a contributory basis. The first is the State Old Age Pension ('SOAP'), while the second takes the form of voluntary private provision (private pension funds). The SOAP pays a fixed amount per month, adjusted subject to a means test, for all qualifying applicants. Aside from this, no contributory social security system is in place for retirement provision.

The means test excludes many people who are deserving of support through the SOAP and creates incentives for individuals to run down assets and income in order to qualify. The private contributory system does not provide adequate coverage and protection, as many income earners contribute intermittently or withdraw benefits early. Furthermore, administration costs are high, and this further reduces the benefit.

A comprehensive solution for retirement reform, involving both non-contributory and contributory retirement provision, is provided in this section. What is considered is a universal basic pension to replace the SOAP together with a mandatory contributory arrangement for formal sector income earners. The new system also proposes new institutional arrangements.

7.2 Design considerations

The central aim of any retirement reform is therefore to ensure that incomes of individuals and their dependants are protected once they reach advanced age. Those who have earned low incomes their entire lives need a minimum level of support. For those who have earned reasonable lifetime incomes, a system of protected income-smoothing is needed to ensure that an income is achieved that is reasonably related to lifetime earnings.

The reformed policy framework also needs to build, where possible, on the existing arrangements.

Benefits will decline over time from prevalent income levels. This situation will occur where final benefits are not appropriately indexed (i.e. linked to appropriate measures, such as the inflation rate).

Risk is an important aspect that needs to be taken into account in the design of the social security system.

Risks include:

1. Investment risk, which arises from fluctuations to account balances and portfolio values. In a Defined Contribution ('DC') system this is borne by the individual.
2. Longevity risk, which refers to the uncertainty of the period from retirement to death. This risk may be outsourced to an annuity provider, but is often shared by the retiree through product design or through opting out of purchasing an annuity.
3. Policy risk is the possibility of intervention by policy makers in the operation of the system, for example, through setting investment rules that are not in the best interests of all participants, or through failing to protect participants against the impact of potential future changes.
4. Agency risk arises from the involvement of the private sector in the pension system, and manifests in various ways: misappropriation of assets, conflicts of interest and negligence, or ignorance on the part of the provider or an intermediary.

Risk diversification (the spreading of risk) within retirement reform can be achieved by combining arrangements involving both benefits and institutional alternatives. In terms of benefit design, longevity risk needs to be balanced against investment risk, while institutional models need to consider allowing for a diversity of public and private players, subject to strong oversight, without excessively increasing the costs of the system.

7.3 Strategic overview

The framework considered here involves four tiers, with decreasing levels of protection associated with higher levels of income. Tier 1 focused on the poorest of the poor, offers the greatest certainty, whereas Tier 4, which affects the highest income groups, offers the least certainty.
It is proposed that all income categories participate in each of the first three tiers, although the degree of participation is expected to vary according to income.

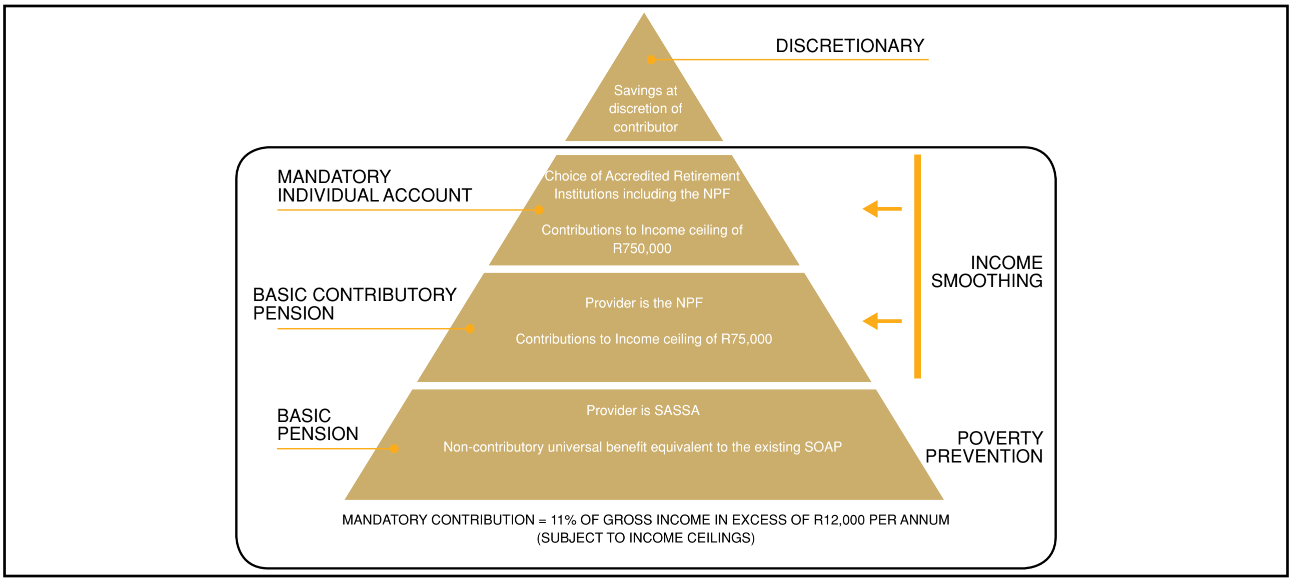
1. Strategic goal:
   a. Minimum income replacement rates of at least 40% must be achieved, with the possibility of higher targets for lower income groups.[2]

2 This would not eliminate the possibility of higher-income replacement rates, particularly for lower-income groups. (Replacement rate is the rate at which post-retirement benefits compensate for income lost when someone stops working.)

2. Tier 1: Basic pension:
   a. This provides for a universal minimum benefit available to all citizens and qualifying residents.
   b. The benefit provider would be the South African Social Security Agency ('SASSA'), which is at present responsible for administering all social assistance benefits.
   c. The objective is poverty prevention.
3. Tier 2: Basic contributory pension:
   a. This provides for a mandatory contribution towards either a Defined Benefit ('DB') pension arrangement, or a Defined Contribution ('DC') pension arrangement with legally guaranteed minimum benefits at least equivalent to the DB system.
   b. The provider would be a new statutory institution, the National Pension Fund ('NPF'), established to administer the mandatory contributory system.
   c. The income ceiling for mandatory participation would be R75,000 (2007).
   d. The objective is income-smoothing.
4. Tier 3: Mandatory individual accounts:
   a. This povides for a mandatory contribution toward a DC individual account arrangement with any accredited pension provider chosen at the discretion of the contributor.
   b. Accredited funds would include the NPF.
   c. The income ceiling for mandatory participation would be R750 000.
   d. The objective is income-smoothing.
5. Tier 4: Discretionary savings:
   a. Here contributors are free to make all decisions at their own discretion.
6. Mandatory contributions:
   a. The contribution floor below which no contribution is required is R12 000 per annum (2007).

b. The contribution rate/threshold would be 11% of gross income in excess of the contribution floor, subject to the income ceilings.

Figure 7.1: Strategic framework for retirement reform



7.4 Detailed options

7.4.1 Universal non-contributory basic pension

The existing SOAP should be revised to become a universal non-contributory pension ('Universal Basic Pension' or 'UBP'). Here the options involve:

1. Removal of the means test
2. Reliance on the tax system to claw back benefit from higher income groups to achieve income targeting
3. The shifting of the qualifying age for both males and females to 60
4. The indexation (linking) of benefits, at a minimum, to a relevant inflation rate, or wage rates, or a combination of inflation and wage rates, or any of the proposed permutations, depending upon which is the highest
5. The reconsideration of the secondary tax rebate applicable to individual tax payers over the age of 65. This needs to be restructured to be consistent with the implicit targeting mechanism replacing the means test.

7.4.2 Mandatory contribution to earnings-related retirement benefits

It is recommended that the following be considered: all persons in formal employment will be required to make contributions towards a retirement fund. However, the risks that will accompany this policy must be spread among a number of benefit configurations. It is proposed that the contribution be divided between Defined Benefit ('DB') and Defined Contribution ('DC') components with the following features:

1. The overall mandatory contribution should be set at a threshold of 11% of income above the first R1 000 ('contribution floor')[3] earned and subject to the following qualifications:
   a. BCP (Basic Contributory Pension): Contributions in respect of a DB arrangement must be made at a rate of 11% and subject to an annualised income ceiling ('Ceiling 1') of R75 000 (2007 prices).
   b. MIA (Mandatory Individual Account): Residual contributions in excess of Ceiling 1 and within the contribution threshold of 11% must be made to an accredited private or public DC arrangement, chosen at the discretion of the contributor or relevant employer (consistent with employer/employee agreements), subject to an income ceiling of R750 000 (2007 prices).
2. The official age of retirement should be set at 60 for both males and females, consistent with the Basic Pension. However, due to the early mortality of low income groups, consideration should be given to the following:
   a. A lower official retirement age, with automatic adjustments over time based on the aging of the general population to reduce longevity risk (i.e. the risk that the proportion of the population consisting of aged people becomes too large to support) (see Section 7.2)
   b. An early retirement dispensation, which would pay out a lower benefit.

3 The contribution is logically set at R1 000 per month (2007), as the non-contributory Basic Pension would in any case provide a universal entitlement in excess of an 80% replacement rate. Mandatory contributions to retirement provision would consequently result in replacement rates in excess of 100%. Such options could be considered if some benefit is to be derived from government transfers to households earning below R1 000 per month outside of the system of social grants. This option could also be tied to the establishment of a minimum wage at the same level.

Table 7.1: Options for the Basic Contributory Pension ('BCP')

Options	Comment
Option 1: DB only Scheme Here the benefit is set as an accrual based on lifetime earnings subject to automatic adjustment mechanisms to retirement age and benefit levels.	This option provides a high degree of benefit protection, with investment risk being carried by the statutory scheme. However, this option would mean that the vast majority of retirement funds would be directly controlled by the NPF, resulting in significant centralisation and reduced risk diversification.
Option 2: Single scheme that combines both DB and DC elements ('hybrid') This is a single scheme that combines both DB and DC elements (referred to here as a smoothed DC scheme). This arrangement can be underpinned by a guaranteed minimum benefit. The guaranteed minimum benefit can be equal to contributions multiplied by an index-linked factor equal to i. inflation plus a percentage or ii. wage inflation, or iii. GDP growth.	This option provides a similar degree of benefit protection as Option 1, but increases the SOAPortunity for private providers to operate at the level of the BCP. There is scope for an up side on investment returns through the application of smoothed bonuses based on a rolling average of market performance.

7.4.3 Benefits offered through the contributory system

The benefits proposed for the system should be related to the lifetime earnings of individuals, even where benefits are financed on a DB basis. The purpose of this is to reduce the effect of longevity risk on the sustainability of the retirement system. Nevertheless, the entitlements, and the risks associated with different entitlements, will vary depending upon whether they are DB or DC in nature:

1. A DB arrangement is based on an accrual of between 1% and 1.3%[4] of the qualifying income over the contributor's lifetime.
2. A Hybrid (mixed) alternative is based on contributions and guaranteed investment earnings less expenses over the contributor's lifetime.
3. A DC arrangements is based on contributions and investment earnings less expenses, with no guaranteed return on investment.
4. In combination: The minimum replacement rate achieved, when the Basic Pension (non-contributory) is included, should not be lower than 40%.

Benefits should take the form of a monthly pension and could be arranged as follows:

1. For accounts under the management of a statutory provider:
    a. A pension paid directly from the provider in respect of all accounts under its management, or
    b. a mandatory annuity which must be purchased on achievement of retirement age and

4 This level of benefit accrual is consistent with the policy target of a minimum replacement rate of 40%. The final required contribution rate to achieve this benefit target may be lower than those indicated. The figures presented should therefore be regarded as indicative rather than final.

c. a lump-sum benefit equivalent to a maximum of one-third of the value of the benefits at retirement, which must be drawn down over a minimum period of ten years.[5]

2. For mandatory accounts under the management of a private provider:

   a. An annuity equivalent to a minimum of two-thirds of the entitlement that must be purchased from an accredited private annuity provider on retirement age, and/or

   b. a lump-sum benefit, equivalent to a maximum of one-third of the value of the entitlement at retirement, can be provided with a minimum draw-down period of ten years.

7.4.4 Benefit indexation

The calculation of the DB benefit at retirement would require that the lifetime income of an individual be expressed as a present value at the time of retirement. The most appropriate escalation factor is the wage index rather than an index of general inflation.

The payment of benefits in retirement also requires the use of an index to escalate pension payments to properly account for annual changes in the cost of living. Options include

1. an appropriate indicator of general inflation, or
2. wage rates, or
3. a combination of general inflation and wage rates.

The provisional recommendation is to make use of an appropriate index of wages. This would keep pensions in line with wage trends.

7.4.5 Institutional considerations

Collection of revenue: The collection of all mandatory contributions should occur centrally via the tax system, through the South African Revenue Services ('SARS'). These funds should then be transferred to a National Pension Fund ('NPF'), where:

1. The account and benefit administration will occur in respect of the DB arrangement (or alternatively the hybrid arrangement), from where the funds will be transferred to an accredited retirement institution ('ARI')[6], chosen either by the contributor or his/her employer (in terms of an agreement collectively negotiated with employees), and which can include the NPF.
2. To the extent that a hybrid arrangement allows for some choice of individual accounts, the arrangement in (b) should also apply.

Opt-out arrangements: a number of opt-out arrangements could be considered, provided that these do not affect system-wide cross-subsidies and risk-pooling. The purpose of this is to:

1. Diversify (spread) the agency risk, which includes the statutory provider
2. Encourage tougher competition amongst existing service providers in respect of mandatory benefits
3. Improve the performance of the private sector in relation to supplementary financial products
4. Make constructive use of the existing, although poorly regulated, service provider system.

Through the 'opt-out' framework the private sector can continue to provide retirement services on a conditional basis. The alternative approach requires that the only service provider for the mandatory tier be the NPF. However, this may increase the implementation and agency risks associated with the policy.

The main reason for agency risks is that all retirement arrangements will be provided through a single institution. The implementation risks arise because, if all existing arrangements are to be replaced by one statutory provider, a massive effort would be needed to implement such a policy.

In addition to an 'individual' opt-out, certain service providers could perhaps be allowed to offer the full mandatory benefit to their members. Here primary consideration will have to be given to bargaining council arrangements[7] where they comply with certain conditions.

Oversight: All statutory and private retirement arrangements should be regulated without exception or exemption. This regulation would need to include appropriate semi-legal arrangements with clear areas of responsibility.

5 A lump sum has the advantage of a guaranteed transfer to a household, irrespective of the survival of the beneficiary. It has the disadvantage that it can be consumed well before death, leaving the household without an adequate source of income. Lump-sum payouts should therefore be limited to around two-thirds of the accrued entitlement at retirement and paid out over a number of years.

6 This is a proposed accreditation/licensing requirement, and does not exist within the present regulatory framework.

7 These are retirement schemes set up by statute for low-income workers employed in specific industries.

7.4.6 Unemployment benefits

Low income contributors to compulsory pension funds are more likely to face periods of unemployment and therefore may often need to draw on retirement benefits prior to achieving retirement age. This problem is partially reduced for those with access to unemployment insurance. However, many contributors are unable to access unemployment insurance or have used up their unemployment benefits.

The integration of unemployment protection and contributory retirement arrangements therefore needs to be considered. One solution is to expand unemployment insurance benefits to include a flat (in rand values) continuation benefit, provided that recipients participate in labour programmes.

To ensure consistency between any unemployment continuation benefit and formal sector wage rates, the implementation of a statutory minimum wage applicable to the formal sector needs to be considered. A value of R1 000, in 2007 prices, is seen as an initial point of departure for discussion.

This arrangement was discussed as part of the improvements to social assistance in Section 6.4.

7.5 Affordability of social security contributions and employment creation

Lowest-income earners (and in some instances their employers) could find it hard to afford any system of compulsory contributions. To alleviate this problem, such contributions could be subsidised in a way that does not significantly reduce the value of benefit entitlements.

Options include:

1. Option 1: Use of a progressive contribution structure (i.e. one that has different levels), with benefits calculated according to what an individual has contributed, or
2. Option 2: Subsidies paid to individuals and/or employers in respect of low- income earners.

A progressive contribution structure would have to be used regardless of what final arrangement is decided upon. Option 1 is consistent with a DB arrangement as the benefit need not be calculated strictly according to the contribution made. In other words, the benefit would be based on a specified uniform accrual rate (i.e. percentage of gross income above the contribution floor), but the contribution could be different for people who earn less than the specified income (R75 000 proposed in this report). This option has the advantage of being clear and efficient. The system would be paid for through a cross-subsidy from those paying the proportional contribution to those paying a lower contribution.

With respect to Option 2, households could be provided with subsidies above the level required to make contributory social security affordable. This would stimulate work creation through making employment more affordable to an employer at the low end of the wage scale. Employers may react to such a subsidy by altering their investment behaviour to favour labour-intensive technologies. Again, such an approach could be designed to target people earning up to R75 000 per annum. Option 2 would need to be assessed in relation to other potential government transfers, such as those discussed in Section 6.

7.6 Conclusion

The system of retirement reform described here is provided for the purposes of consultation. If implemented, this affordable system would considerably improve current conditions. The redistribution introduced into the contributory portion of the arrangement is a practical requirement to ensure that all income earners participate in the system. However, where this redistribution is more than is required to achieve inclusion within the contributory system, the programme should be assessed against competing programmes that attempt to achieve similar objectives.

8. DEATH AND DISABILITY

8.1 Overview

The death or disablement of a breadwinner usually results in great hardship for dependants and survivors within a household. Children, in particular, often suffer severely, and this affects their development and future prospects.

At present, households with low-income breadwinners are excluded from private insurance, while those with breadwinners earning informal incomes, or who are unemployed, are completely without protection. However, a social assistance grant (at the same value as the SOAP) does exist for disablement and is subject to the same means test. No protection exists against the death of a breadwinner.

Aside from these very vulnerable groups, many higher-income groups are structurally excluded due to poor risk-pooling SOAPortunities in private insurance markets. This leaves small employers and the self-employed vulnerable to excessively priced insurance and exclusion.

8.2 Considerations

As with the SOAP, the complete removal of any means test from the existing disability grant should be considered. This would mean that everyone would at least have a basic disability benefit. Additional potential benefits through the introduction of social insurance options could also be considered.

Although private markets typically exist for death and disability insurance, these often have gaps.
Those likely to face some form of structural exclusion from private insurance include:

1. Low income groups
2. The self-employed
3. Employees in small and medium-sized firms
4. People who change employment frequently.

The problems of an inadequate private insurance market can be addressed through expanded risk-pooling (in other words, drawing in larger numbers of contributors to share risks). Realistically, this can be achieved only by making risk-pooling arrangements compulsory by law. Some form of integration of existing private arrangements with the new mandatory benefit can be expected.

8.3 Social insurance options

Death and disability have different implications for a household. In the case of the death of a breadwinner, it is reasonable to expect any surviving spouse to get work at some point in the future, therefore income protection could be limited to a fixed number of years.

In the case of disability, however, the former breadwinner survives and will have little or no chance of being employed again. In such a case the benefits need to cater in a consistent manner for both the spouse and the former breadwinner. This is particularly true if the spouse becomes the disabled partner's caregiver. Given this, it may be reasonable to provide indefinite income replacement, and to regard the benefit as an acceleration of the retirement benefit.

In the case of both death and disability, child benefits may need to be improved to provide a small income stream until the child leaves formal education, with an upper ceiling age of 25.

In light of the above, the following should be considered:
Contingencies protected:

1. Death of a breadwinner
2. Disability of a breadwinner.

Contributions:
In order to achieve the recommended benefit levels, a contribution equivalent to 4% of gross income (combined for death and disability) in excess of the contribution floor should be considered.

Contribution floor:
The suggested contribution floor is the first R12 000 of annual income consistent with the approach applicable to mandatory retirement provision.

Benefits and beneficiaries:

1. Death of a breadwinner:
    a. Spouse benefit: This should be limited to a fixed number of years and should be related to the former earnings of the breadwinner.
    b. Child benefit: This should be provided up to the age of 18 years if the child does not continue with further education, or to the age of 25 if he or she does.
2. Disability of a breadwinner:
    a. Benefits should provide income replacement until the death of the contributor, with a continuation benefit for any dependent spouse upon the death of the contributor.

b. Contributions towards retirement provision should perhaps be adjusted, as this benefit will, in some instances, replace retirement provision.
c. Child benefit: This should be provided at a fixed replacement rate of the breadwinner's former income, up to the age of 18 years,where no further education is undertaken, and to a ceiling of age 25 where further education is undertaken.

8.4 Institutional considerations

The simplest way to achieve the risk-pooling of benefits would be to establish a statutory insurer. This could be the same organisation established to operate the mandatory retirement system.

The statutory insurer could also operate as a default insurance arrangement for death and disability cover in excess of any mandatory requirement. This would be to cater for those individuals or groups unable to access affordable insurance in the private sector for structural reasons.

8.5 Conclusions

The gaps in the current private insurance environment could be addressed by the system discussed here. The current voluntary system of insurance leaves certain groups with little chance of getting affordable death and disability insurance. A compulsory system of contributions and benefits, provided by a statutory insurance provider (the NPF), will address this problem. This new system should be integrated with existing private arrangements in order to ensure that it does not result in a problematic and unfair reduction in private provision.

9. THE ROAD ACCIDENT FUND

9.1 Overview

The Road Accident Fund ('RAF') is a mandatory third-party insurance system funded through a levy on fuel purchases, the purpose of which is to ensure that everyone driving a car is insured for civil liabilities (damages claims) arising from motor vehicle accidents. The RAF therefore provides a protection against the eventuality that a successful civil claim against an individual that caused a motor vehicle accident could not be paid due to lack of funds. The RAF therefore does not pay out in those instances where a civil liability would not arise, for instance, where fault can be attributed in the cause of an accident. The payouts from the fund include compensation for medical expenses; and the loss of future earnings. Benefits can take the form of lump sum payments and the direct reimbursement of expenses (in the case of medical expenses).

However, the narrow mandate of the RAF creates significant operational and social inefficiencies. The relationship to common-law rights of civil liability require that, before the RAF pays out, it must assess who was at fault in an accident and apportion a quantified set of benefits. The benefits are determined in relation to the loss suffered, rather than to a specific schedule of benefits. As a consequence the process of quantifying benefits involves many legal disputes concerning the payout in respect of both the apportionment of fault and the quantification of the benefits. The quantification of damages is also affected by income levels, with higher-income individuals suffering loss receiving higher benefits than low-income or indigent individuals.

Going forward, there is a need to assess what role the RAF should play within the system of social security. On the one hand it could focus its attention more on fulfilling a social security role, preventing severe hardship for families affected by the high medical costs associated with a road accident and/or the loss of income due to the loss of a breadwinner. Alternatively, it could merely streamline its operations in dealing with the insurance of third party liability claims. This would continue to underwrite third-party claims, preventing severe hardship when those facing a damages claim are unable to have a claim satisfied. However, these goals are very different and have a different focus. If the RAF focused on social security, it could improve the benefits for lower-income groups, but leave some people exposed to damages claims.

If the social security route is followed, it will become important to resolve the relationship between the RAF and mandatory social insurance death and disability benefits. Even if the present approach to the fund is followed, benefit entitlements in relation to mandatory social insurance will need to be taken into account in determining awards. Either way, therefore, the establishment of mandatory social insurance benefits for death and disability will potentially substitute a large portion of the benefits that are currently being paid out by the fund. However, this will not be the case with respect to coverage for medical expenses. Coverage for medical expenses involves benefits that potentially do not vary according to income, and can provide an essential basic universal protection in the case of a road accident.

9.2 Policy options

Aside from the considerable inefficiencies in the current scheme, the inevitable substitution of benefits between a mandatory social insurance scheme and the RAF necessitates its reform within the context of a comprehensive system of social security. An important outcome of this reform process should be: the removal of unnecessary inefficiencies associated with the provision of entitlements; the continued protection of access to medical care associated with all road accidents, and ensuring that families are protected from the loss of a breadwinner or caregiver. These protections are particularly important in relation to low-income groups. However, the mandating and pooling of third-party insurance for road accidents, where this covers any residual liability, after accounting for social security benefits, remains inherently rational. Without such central pooling, families could be exposed to severe losses resulting from accidents where these are resolved privately. In the absence of central pooling, inefficient private insurance products would become available, with variable coverage.

Taking these issues into account, the following framework can be considered to be compatible with a comprehensive system of social security:

1. The RAF continues to exist as a social insurance fund providing access to health care and income protection arising from the death or disablement of a breadwinner. Within this context, consideration needs to be given to regarding the death or disability of a caregiver as having a financial impact on a family for which compensation is payable.
2. The benefits should be defined in such a manner as to exclude any explicit coverage provided through either a private or social insurance arrangement.
    a. The RAF should clarify the exact manner in which the inter-relationship with other cover is to occur.
    b. It would be important to clarify which institutions, whether public or private, carry the principal liability for any substitutable benefits. In some instances it may be appropriate for the RAF to do so (e.g. in the case of medical expenses).
    c. For this to be carried out efficiently, it would be important for the institutions with substitutable benefits to integrate their information systems to prevent double-dipping (claiming the same benefit from more than one institution).
3. Survivor benefits should not be paid out as a lump sum, but should rather take the form of monthly payments. This would prevent the rapid exhaustion of the pay-out by a claimant.
4. The RAF should offer the following potential benefits on a no-fault basis:
    a. An earnings-related benefit in respect of the death and disability of a breadwinner or caregiver
    b. Medical indemnity insurance for all expenses incurred irrespective of whether treatment was provided in a public or private facility.
5. In those instances where a civil claim would occur despite the existence of no-fault benefits, the RAF should provide benefits on a fault basis.
6. The entitlements in relation to the RAF should be available only to permanent residents, citizens and certain classes on temporary resident. The inclusion of tourists could be considered for medical cover and repatriation only.
7. Contributions to the RAF should continue to be made in the form of a fuel levy, since the earnings-related death and disability benefits will ultimately be obtained from substitutive insurance arrangements rather than from the RAF. As a consequence the RAF will fund medical indemnity benefits, death and disability benefits for those without cover elsewhere, and any residual entitlements unavailable from other funds.
8. From an institutional perspective, consideration needs to be given to the following:
    a. A reconsideration of the Ministry to which it reports (Transport), which lacks the appropriate policy specialisation to deal with social security
    b. The implementation of a revised governance structure to strengthen its accountability
    c. The establishment of appropriate links between all

related institutions providing equivalent benefits to ensure coordinated operations.

The timing for reforms to the RAF could have some implications for its benefit design, liabilities and funding needs. However, many of the indicated reforms could occur prior to, or in conjunction with mandatory social insurance for death and disability benefits. Given this, the reform of the RAF should not be deferred in expectation of changes to other arrangements.

9.3 Medical benefits

Potentially the most important benefit offered via the RAF going forward involves the coverage of all medical expenses in respect of a road accident. Given that road accidents represent one of the most important drivers of the need for emergency care, and that in terms of the Constitution access to emergency care is an unqualified right, this aspect requires special attention. At present, benefits indemnify beneficiaries against expenses incurred. This implies that the fund must pay the full cost of treatment if patients are treated in a private facility, even where they are entitled to free treatment in a public facility.

However, in many instances, fear of non-payment by the RAF (due to the application of the fault provision) many patients are not referred to the nearest facility capable of providing the best care (especially as many public facilities are under severe stress). This reprehensible unevenness in the treatment of emergency cases should be eliminated through structural interventions that eliminate the incentives for differential treatment. Consideration should therefore be given to the following:

1. The RAF should develop a national network of accredited trauma sites which are funded prospectively. This network could include both public and private facilities. The prospective funding, which could include, where appropriate, a capital injection, should be in exchange for a contractual commitment to provide services in accordance with clear criteria.
2. Where any person is treated outside of the network, reimbursement should be on a fee-for-service basis against a standard tariff, established and gazetted by the fund, which should be the same whether the patient is treated in a public or private facility. In this way the medical liability for road accident trauma will be entirely underwritten by the RAF, irrespective of where treatment occurs.
3. The RAF would monitor the quality of care rendered within all hospitals providing contracted trauma services. Legislation should also provide the RAF with oversight capacity in respect of any hospital that treats any road accident victim, whether contracted in or not.
4. Where medical schemes reimburse any aspect of a road accident expense, the medical scheme will be entitled to reclaim expenses incurred from the RAF. However, the RAF would be entitled to reimburse only those claims it would have approved. Where a scheme has incurred residual expenses that would not have been approved by the RAF, they should have a claim against the relevant health providers.

The above framework would shift the focus of the RAF away from administering medical claims to overseeing services and contracts. Given that the RAF would have the authority to fund all road accident trauma, it should have sufficient scale and would be well placed to perform this function effectively. The revised system would result in a considerable improvement in access to emergency healthcare for a significant contributor to this morbidity (i.e. road accidents) and for the population as a whole.

Given the elimination of any fault-based assessment in relation to medical expenses, significant savings would be possible relative to the present situation. This arrangement would have the advantage of improving hospital services generally within both the public and private sectors. This approach to medical benefits should be considered as part of a joint arrangement with benefits provided in terms of the Compensation for Occupational Injuries and Diseases Act ('COIDA') discussed in Section 10.

9.4 Conclusions

A reform of the RAF holds many SOAPortunities for improved social security protection within the context of a comprehensive system of social security. This could be achieved through the rationalisation of benefits, a reduced inefficiency driven by the fault system, and the improvement in medical protection. Such a reform should see the fund change its focus away from assessments of fault and liability and toward protecting the most vulnerable. which would include those who do not have contributory protection against death and disability. Furthermore, it will contribute towards the establishment of a uniform national system for emergency services.

10. COMPENSATION FOR OCCUPATIONAL INJURIES AND DISEASES

10.1 Overview

Protection against occupational injuries and diseases is currently being provided through the Compensation for Occupational Injuries and Diseases Act ('COIDA'). As is the case with the RAF, the COIDA provides an insurance framework which compensates employees for injuries and accidents occurring within, or associated with the workplace. Benefits involve full compensation for medical expenses and for any permanent disability that prevents further employment.

The COIDA is administered by the state, with the director general of the Department of Labour operating as the accounting officer for the fund established for this purpose. The operational aspects of the Act are, however, delegated to the Compensation Commissioner, who takes direct responsibility for the day-to-day administration of the fund.

The following processes and regulations apply to the application of COIDA:

1. COIDA is administered by the State.
2. The rates of contributions and benefits are determined, and may be altered, by the State.
3. Effectively, as the fund is controlled by the State, the solvency of the fund is guaranteed.
4. It is compulsory that all employers and employees join the scheme, subject to certain exceptions.
5. The rates of contributions vary, but are standard between minima and maxima within the same occupational class or industry.
6. There is minimal individual underwriting of risks, except where a particular employer or occupational classification requires rating adjustments.
7. Disputes are handled in the first instance by the Commissioner, and not by the courts, although cases may be referred.

The contingencies covered in terms of the COIDA are:

1. The death of an employee
2. The temporary, total, or temporary partial disablement of the employee
3. The employee becoming permanently disabled
4. The employee requiring medical aid
5. The employee contracting an occupational disease.

Benefits are provided on a no-fault basis, except where an injury was deliberately self-inflicted. Contributions paid in respect of benefits are mandatory, are paid by employers and vary for different industries. Industries susceptible to higher rates of injury pay higher contributions relative to others. Overall, therefore, the system of compensation provides valuable protection for workers who would otherwise be vulnerable to working conditions that involve risk.

With consideration of a comprehensive system of social security which includes mandatory contributions toward contingencies covered by the COIDA, it becomes necessary to assess what implications this has for the present legislative and institutional framework.

10.2 Discussion and policy options

The vast majority of incidents that trigger benefits in terms of the COIDA, as in the case of the RAF, are trauma related and require some form of emergency treatment. Consequently, the medical aid requirements are very similar. At present all benefits are obtained from private sector providers, irrespective of the income of the employee. The prices paid for benefits are in terms of a schedule published each year in the gazette. The gazetted tariffs are set in negotiation with private providers.

The non-medical benefits provide compensation where an employee is no longer able to work due to an injury. Dependents will also be compensated in cases where the injury resulted in the death of the employee. All benefits are income related and are determined according to fixed limits related to the income of the employee at the time of the accident. In this way the COIDA provides very similar coverage to that likely to emerge from a system of mandatory death and disability insurance.

A reasonable accommodation between this legislative framework and that of a general system of contributory death and disability insurance should not undermine existing benefit levels available through the COIDA. However, in order to prevent double compensation the COIDA should focus on merely funding the residual between the benefit paid out by the general system and the possibly higher benefit paid out for occupational injuries and diseases. This would suggest some need to offset in terms of contributions required from employers.

Medical benefits offered in terms of COIDA would benefit from a joint strategy with the RAF, as both deal primarily with trauma and trauma-related events. A pooling of funds for a network of trauma centres and a common approach to contracting appears logical. Consideration should therefore be given to a joint strategy along the lines recommended in Section 9 for the RAF.

10.3 Conclusions

The implementation of a general system of mandatory insurance for death and disability will potentially substitute for some of the protection presently offered in terms of COIDA. As for the RAF, a degree of restructuring is required to eliminate inconsistencies between social insurance arrangements. Although some of this restructuring may be required only when mandatory insurance for death and disability is introduced, consideration needs to be given to a common strategy with the RAF to fund medical benefits. Significant efficiency gains will be possible if the two funds were able to combine their payment and oversight functions to achieve a national network of trauma facilities. The combined approach would go a long way toward establishing more uniform access to emergency medical services for much of the population.

11. INSTITUTIONAL REFORM

11.1 Overview

Institutions are large and complex structures and go beyond mere individual organisations. The administration of institutions requires proper legal frameworks, management and governance arrangements. In order to achieve this, the following aspects need to be considered:

1. Constitutional provisions outlining rights and obligations in relation to both entitlements and procedural fairness
2. Legislative arrangements, including entitlements and administration
3. The organisation of policy-making structures
4. Regulatory and oversight arrangements
5. Organisations and administrative systems
6. Governance arrangements
7. Judicial and semi-judicial arrangements.

South Africa's social security system evolved in an uncoordinated way over time, and its structures and mechanisms are disconnected and weak. Problems extend from the policy-making processes to service delivery. The benefits of a much larger, more comprehensive system have also not been realised.

South Africa's social security system is fragmented at almost every level, with very little coordinated decision-making and institutional development. Even if individual organisations were to function optimally, gaps would remain at a system level.

This section therefore offers a series of proposals that seeks to formalise the institutions of social security into an integrated system. However, organisational consolidation is not recommended. Instead, mechanisms for properly overseen and governed specialist social security organisations and institutions need to be established.

11.2 Policy considerations

11.2.1 Consolidation of the functional authority for social security

The authority to establish social security policy is currently divided amongst a number of different departments, not all of which have social security as their core business. Onsequently social security policy is not coordinated across departments, and often evolves slowly and inefficiently.

In order to promote the consolidation of social security policy, it is recommended that consideration be given to the establishment of a new Ministry and Department of Social Security ('MSS', 'DSS'), which would consolidate the authority to determine social security policy affecting the following areas:

1. Social assistance
2. Contributory social security, including:
   a. Retirement
   b. Social insurance
   c. Unemployment insurance
   d. Compensation for injuries and diseases incurred in the workplace
   e. Road accidents.

In relation to the above, policy with significant financial implications should be performed with the concurrence of the Minister of Finance as a matter of course. Where the regulation of voluntary contributory insurance and retirement needs to be properly integrated, regulatory changes with implications for any aspect of the social security system should occur with the concurrence of the proposed Minister of Social Security.

Were a DSS to be considered, it would consolidate policy capacity in relation to social security (apart from health) and allow for the development of a holistic approach to all contributory social security organisations and functions. It would also greatly improve the ability of government to apply consistent approaches and establish synergies that prove difficult when the authority for social security policy is split.

11.2.2 Oversight and governance of social security organisations

It is proposed that consideration be given to a three-tier social security system distinguishing between:

1. Oversight of the social security system as a whole
2. Oversight of organisations with the assigned authority to render specific social security functions
3. The executive level of organisations with the assigned authority to render specific social security functions.

The oversight of the social security system as a whole should be assigned to a representative Social Security Council ('SSC'), comprising the major social partners affected by the social security system: labour, employers, government, and civil society. This structure should oversee the boards of all key organisations assigned the authority to carry out social security functions.

Boards of two kinds should oversee organisations assigned the authority to carry out social security functions:

1. For organisations assigned the function to provide social security benefits, a representative board, incorporating the social partners in a manner consistent with the SSC, should be established.
2. For organisations assigned a supportive (shared) social security function, used by all social security organisations providing benefits, boards incorporating the board members and/or the chief executives of the supported social security organisations should be established.

The second kind of organisation requires oversight from affected agencies and organisations whose own delivery is affected by the shared service. This is preferable to boards made up of individuals with no direct interest in the ultimate performance of any social security organisation. Consideration could also be given to social partner participation, either via the boards of related social security organisations or through a distinct nomination and appointment process.

The powers, authority and responsibilities allocated among the three tiers need to be carefully considered. However, a proper balance should be achieved between executive independence and appropriate checks and balances.

The chief executive officer of each social security organisation should be appointed by its board. The premature removal of a chief executive should occur only with the agreement of the SSC.

Social security organisations need a sufficient level of discretion to determine their own operational priorities. For this to happen, these organisations should fall outside the civil service. However, organisational and human resource arrangements established by any social security arrangement should be approved by its board after consideration of a review provided separately by the Department of Public Service Administration ('DPSA').

11.2.3 Regulatory oversight

Regulatory bodies ensure that statutory arrangements are complied with through the independent exercising of oversight powers.

A coherent regulatory regime, incorporating multiple regulators, needs to be set up to intervene in the case of any social security institution, whether public, private or statutory. All related civil service social security arrangements should be brought within the ambit of an independent regulator.

All regulators should be independent and free from interference from any source. This would need to be achieved through the governance design of each regulatory authority.

11.2.4 Organisations with authority to deliver social security

A number of organisations are currently involved in the delivery of social security. These are:

1. The Unemployment Insurance Fund ('UIF')
2. The fund established in terms of the Compensation for Occupational Injuries and Diseases Act ('COIDA')
3. The fund established in terms of the Occupational Diseases in Mines and Works Act ('ODMWA')
4. The South African Social Security Agency ('SASSA'), which is assigned the function to administer social assistance
5. The South African Revenue Services ('SARS'), which provides the cross-cutting support function of collecting revenue generally for government as well as for the UIF
6. The Road Accident Fund ('RAF'), which provides universal third-party insurance in respect of damages claims relating to road accidents.

Proposed new organisations are:

1. A National Pension Fund ('NPF'), which will have the authority for the following functions:
   a. Administration of mandatory retirement and death and disability insurance benefits:
      i. Allocated to it by statute
      ii. Allocated to it at the discretion of individuals or employers
   b. The oversight, in conjunction with the regulator of retirement funds, of private retirement arrangements servicing the mandatory tier
   c. The oversight, policies, and allocation of investments
2. An agency to render National Health Insurance ('NHI')
3. A Social Security Intermediary ('SSI'), which would consolidate the interface between the general public and the social security system within a single agency. This organisation would provide the gateway into the social security system and would have the authority for the front-end portion of the following functions:
   a. Client interaction and service
   b. Front-end enrolment
   c. Education and awareness
4. A Master Social Security Register ('MSSR') of personal information required for all social security arrangements.
5. An agency ('Clearing House') established with the purpose of providing shared back-end operations for social security organisations.

In addition to the above, an expanded role can be envisaged for SARS, which should act as the collection agent for all social security contributions.

11.2.5 Public interface and enrolment

At present, each part of the social security system interacts with the public in its own way. However, despite having roughly the same public interface needs, the various parts of the system differ substantially in scale. Consequently this function, which is essential to ensuring proper access to social security, is not working properly.

To address this problem, the consolidation of the social security public interface function into a dedicated Social Security Intermediary ('SSI') is recommended. The SSI would support all the purpose-designed social security and related organisations and agencies.

It is proposed that the SSI operate as a national entity with branch offices and local walk-in centres. However, the SSI should not take responsibility for application approvals, as this function properly belongs to the entity with authority to fund and provide the benefits.

The purpose of the SSI should therefore be limited to assisting with enrolment, communication, advice, and certain related functions. The general public would therefore largely communicate with the social security system through the SSI.

11.2.6 Master registry

All social security systems rely heavily on registries of personal information relating to members and beneficiaries. Many social security institutions rely on similar sets of personal information to identify and validate beneficiary status.

However, each institution currently relies on its own information collection process to maintain these data. The new social security institutions will require richer information which will, among other things, need to include family relationships.

A master registry that contains the most up-to-date information on the population should therefore be set up. All social security institutions would then have the responsibility to ensure that the registry is up to date, while also using the registry to support their own registries.

It is therefore proposed that an agency be established to take responsibility for maintaining a Master Social Security Register ('MSSR') of the entire population. This registry would become the source of personal information used by all social security and related institutions. Validation of the MSSR would occur every time the personal information of an individual is checked by a related institution.

The MSSR would not replace the dedicated registries of each social security entity. It would merely serve as a source of accurate data by centralising/consolidating this function. The continuous process of validation would ensure that the information was accurate and reliable. Key private institutions that maintain registries of personal information and have frequent contact with clients could also form part of the validation process. This would include private retirement funds, insurers, medical schemes, banks and phone companies.

An important function of such a registry would be the maintenance of accurate information regarding family relationships. This could impact on more specialised social security entitlements that target dependants. Ultimately this registry could establish the basis for a smart-card identity system.

11.2.7 Administrative options

Certain back-office administrative functions could be combined by way of shared service platforms. Shared service platform should therefore be considered for account management, claims processing, and the management of investments (investment and reporting) in the form of a separate agency ('Clearing House').

It will need to be decided whether using such an agency would be made a requirement, or whether this will be at the discretion of each social security organisation.

11.2.8 Judicial and semi-judicial arrangements

At present each part of the social security system, some with questionable scope and independence, has its own semi-judicial procedure. Problems in this regard mean that matters are sometimes taken to court. However, the courts may find it difficult to deal with the specialised requirements of social security institutions.

Ordinary members of the public also experience difficulties accessing the courts due to the excessive expense involved. This places them at a disadvantage to public and private institutions, which do not face this financial barrier.

The specialised and full-time semi-judicial structures that have the power to decide legal matters therefore perhaps need to be expanded and strengthened. This can include the consolidation of some structures. The relationship with the courts can also be properly clarified.

11.2.9 Financing of social security

Non-contributory arrangements are typically financed from general tax revenue. However, contributory arrangements can be financed in a number of different ways. This may include mandating that contributions of some form must be paid to a private or statutory provider, or through the implementation of a payroll contribution collected through the system of income tax. The choice of system should be based on the approach that is most efficient and fair.

11.3 Conclusion

The institutional framework provided here is high-level and entails comprehensive strategic reforms to the system of social security. The proposals focus on changing how decisions are made and channelled within the social security system as a whole. Governance arrangements are central to the framework, as poor oversight weakens decision-making at every level of every organisation. Affected stakeholders (labour, civil society and employers) also need to be represented in oversight structures. Specialised agencies need to be set up to ensure operational efficiencies. Good governance arrangements are key to the success of the system.

12. CONCLUSIONS

Social and economic conditions in South Africa strongly indicate that social security needs urgent attention. Despite periods of reasonable economic growth, inequality and poverty have apparently worsened. Although efforts have been made to address poverty and unemployment, these have not prevented socio-economic conditions from worsening. If these trends are allowed to continue, they will undermine the development potential of the country.

An important consideration is whether there will be any negative trade-off between an improved focus on comprehensive social security, with particular emphasis on redistributive measures, and economic growth. The evidence suggests that South Africa will gain from social transfers to households, as this stabilises incomes and reduces destructive survival strategies. Although such programmes could have negative consequences when benefits are too large, it is unlikely that this will happen in South Africa, even with significant improvements in benefits in the medium to long term.

The social security infrastructure in South Africa is weak, with inadequate non-contributory programmes and a non-existent contributory system. With respect to the latter, income earners have little choice but to make use of voluntary insurance and retirement arrangements. The social security system requires expanded non-contributory programmes and the introduction of mandatory contributory insurance and retirement provision. Mandatory insurance is typically needed in relation to healthcare, death, and disability protection.

The expansion of non-contributory social security needs to prioritise households and individuals who do not have adequate income. Specific groups that require immediate consideration are: children in poverty not yet receiving a CSG; caregivers of child recipients of the CSG; unemployed youth; and unemployed adults. Children in poverty and their caregivers constitute 62% of the total number of people in poverty. Unemployed youth account for 12% of those in poverty, and adults in poverty (excluding caregivers) for 25%. Proposals include an unemployment insurance continuation benefit in conjunction with the implementation of a minimum wage of R1 000 per month (R12 000 per annum in 2007 prices).

The expanded system of social assistance also needs to ensure better access for larger groups of people. Barriers should not be created to accessing the benefits needed. Instead, these benefits should concentrate on achieving an enabling environment that allows individuals to access education and useful work experience. It would also be important to use information drawn from vulnerable households to design still further improvements in social assistance.

Contributory social security interventions include the implementation of mandatory retirement provision and death and disability insurance cover for all income earners above an income and contribution floor of R12 000 per annum (2007 prices). In total, contributions toward social security benefits, including unemployment insurance, should be approximately 17% of gross incomes in excess of R12 000 per annum (2007 prices), subject to various income ceilings. Retirement provision would involve a mixed approach, with a basic benefit offered through a statutory provider and supplementary mandatory benefits offered by an accredited provider, which would include the statutory provider, chosen by contributors.

The institutions responsible for driving social security need to be totally rethought. One proposal made here is the establishment of a range of oversight, governance and executive organisations. These include consideration of a Social Security Council; improved regulatory arrangements; a National Social Security

Fund; a reformed system of public interface; a specialised organisation to manage a social security registry supporting all social security institutions; and specialised adjudication arrangements. It is also proposed that a social partner model be considered in relation to the oversight of social security generally and in relation to key specialised organisations. The purpose of this approach would be to improve institutional responsiveness to affected stakeholders.

Since the recommendations provided here are provisional and are intended only to elicit feedback on South Africa's system of social security, the report has avoided great detail in many areas as this can only be decided once proper consideration has been given to the strategic framework.

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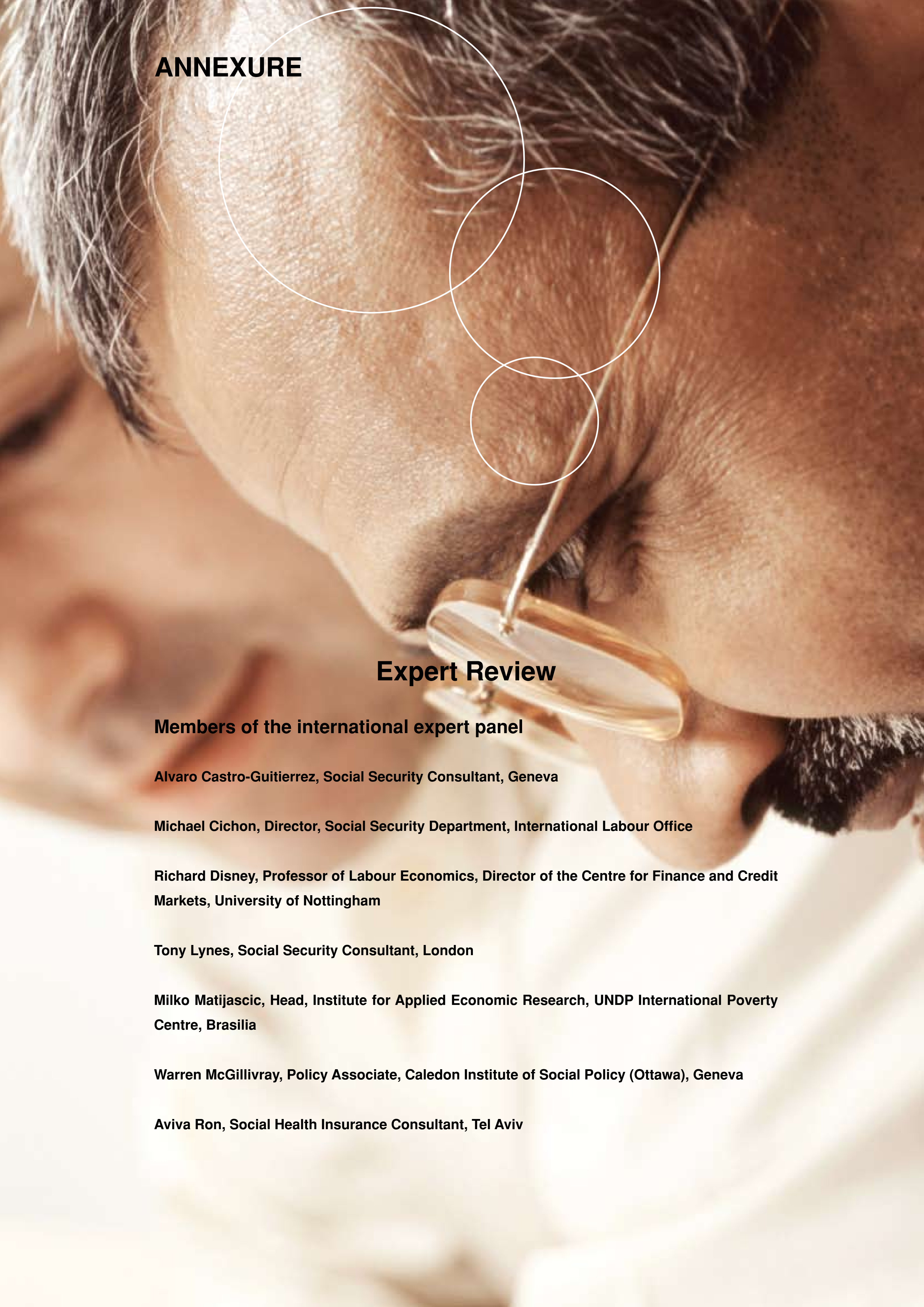

ANNEXURE

Expert Review

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Contents

CREATING OUR SHARED FUTURE

1. Introduction

1.1 Limitations, caveats and acknowledgements

This consultation report provides panellists' observations on the comprehensive social security reform plans of the South Africa Department of Social Development (DSD), which were presented to the panellists during 18-20 June 2008. The reforms are outlined in the discussion document ***Creating our Shared Future: Strategic Considerations for a Comprehensive System of Social Security (DSD, June 2008).*** The report, compiled by W.R. McGillivray, was based on submissions and reviews by the panellists, and prepared for distribution by the Social Security Department of the ILO.

The consultation report has to be read bearing in mind that much of the panel's analysis is based on documentation provided in advance, and on intensive, albeit brief, consultations over a period of three days. Some of the factual information that was provided to the panel may have been wrongly interpreted by the panellists. This report will not try to repeat or second-guess the excellent diagnostic work of the different elements of the existing social security system in South Africa that has been undertaken in recent years by the DSD and others.[1] The preliminary policy recommendations contained in this report should thus be considered as 'food for thought', rather than thoroughly researched policy recommendations. The views expressed by the panellists are personal and do not commit the institutions that they may represent.

In this report social security is defined to be the mechanisms that a society applies to provide income security and access to health care for its members. It includes universal tax-financed income transfer schemes, means-tested tax-financed social assistance schemes, social insurance schemes and employer liability provisions, as well as mandatory or voluntary private schemes.

The panel is indebted to the national experts who made presentations and provided valuable insights. This group was led by Selwyn Jehoma, Deputy Director General: Social Security, DSD and included persons named in the annexed programme of the seminar.

1.2 Context: A sense of urgency

South Africa is probably the country with the most unequal income distributions in the world. The Gini coefficient is in the order of 0.72. Life expectancy and health status varies widely among ethnic groups. There is no agreed poverty line but, depending on the measurement used, the poverty headcount varies between 33 and 43 per cent. A cash transfer programme to older people and some children has reduced poverty significantly among some subgroups. Nevertheless, poverty data show that poverty is a problem that affects families, notably single-parent households with children and households with unemployed household heads. Unemployment remains high; the lower rate (ILO definition) is around 25 per cent while the broader estimate in the order of 43 per cent. Youth unemployment is in excess of 50 per cent. Economic growth in the order of 5 per cent during recent years has not had significant employment effects. The recurrent influx of jobseekers – mostly low-skilled workers – discouraged workers, other non-labour-market participants and school leavers has led to a situation where employment gains have not resulted in a reduction in the level of unemployment.

The social situation has two particularly worrying aspects. Firstly, poverty and unemployment are concentrated in the Black community. Secondly, indicators of aggregate poverty levels, aggregate unemployment levels, and inequality figures have worsened since the 1994 democratic change.

High levels of crime, an increasing 'brain-drain' migration and recent xenophobic violence signal that there is a need to stabilize society by fostering social peace and inclusion. It is reasonable to assume that these factors curb the country's growth potential, and in turn sub-optimal economic performance lessens the 'economic space' to reduce poverty and unemployment. Current challenges to maintaining living standards – rising food and transportation costs – will aggravate the situation, especially for the poorer segment of the population. The poverty reducing 'trickle-down' effect of economic growth is too slow to provide the relief that the society needs. A rapid reduction of poverty and inequality and attempts to address alienation from

1 Reform of Retirement Provisions (DSD), Gaps in the System of Comprehensive Social Security and an Assessment of the Policy Options (DSD, 2007), Social or National Health Insurance (McIntyre/van den Heever), Employment, Wages and Social Security (National Treasury, 2007).

the country and the political and social system among elements of the younger generation can alleviate some of the country's security problems and can be an investment in economic growth. The most rapid means of addressing poverty and inequality is through social transfers that demonstrate that the country cares for disadvantaged and excluded persons. While improved social transfers combined with conditionalities or other measures that enhance employment levels will combat poverty and affirm an explicit constitutional right in South Africa, there can be no guarantee that these actions will be successful or will pay off in economic terms, or that they will be implemented early enough to realize their full potential. However, the panellists generally saw virtually no alternative strategy.

South Africa has a public expenditure ratio of about 27 per cent of GDP at a per capita GDP level of about US$4 000. The Government currently maintains a budget surplus (which it considers to be non-structural) of about 1 per cent of GDP. Total social expenditure is not recorded through national accounts or a social budget. International Monetary Fund statistics indicate that many countries at the same level of GDP per capita as South Africa spend more on social transfers. This suggests that there may be fiscal and policy space for enhanced social expenditure in South Africa.

2. General observations on the reform process

2.1 The existing system and the need for reform

The existing social security system is fragmented. It consists of tax-financed grant systems (old-age and child support grants), a social insurance scheme (the Unemployment Insurance Fund (UIF)) providing unemployment benefits and short-term illness, maternity, death and adoption benefits), private insurance arrangements for pensions and health care, an under-funded public health system, special pensions and health care schemes for public servants, as well as a Road Accident Fund (RAF) and an employer-financed fund for occupational accidents and diseases (COIDA). It performs well in some areas (e.g. the provision of benefits to the unemployed in the formal sector and the delivery of minimum benefits for the elderly to prevent old-age poverty), but fails in other areas (e.g. the alleviation of poverty among families with children). The initiative of the DSD to develop and implement a coherent, effective and efficient national social security system that embraces the existing social assistance and social security benefits and seeks to introduce a new social security pension scheme is thus a timely effort that should be accelerated.

2.2 The scheduling of reforms

Since the envisaged reforms touch on the competencies of several government ministries (Labour, Social Development, Health and the Treasury), the UIF and the provinces, rapid progress in implementation of a comprehensive and coherent package of reforms is unlikely. It is therefore desirable to sequence individual components of the reform package without losing sight of the envisaged long-term overall architecture of the national social security system and the overall social budget of the reform.

It appears that amendments to the social grant systems can and should be pursued as a matter of priority. The following sections deal with reforms of individual components of the existing systems. Reforms of the RAF and COIDA are not dealt with in this report.

2.3 The financing of reforms

The DSD estimates the cost of the proposed reforms of the social grant system at R24 billion. The cost of modifications to the grant system is in the same order of magnitude as the expected consolidated national budget surplus in 2010/11.[2] The cost of introducing a new social insurance tier in the pension system could be partially offset for employers by reductions in the private voluntary tier and by a reduction in the UIF contribution rate. A detailed financing plan for reforms to the grant system, the social insurance component of the pension system and a social health insurance scheme should be drawn up in a social budget (see Section 9).

In order to enhance the transparency of social spending in South Africa, a social assistance fund could be set up that would cover

2 See 2008 Budget Review, p. 46, Table 3.3.

some or all of the expenses of the grant system and possibly subsidies for the social health insurance contributions of the poor. The fund could receive income from general revenues and earmarked taxes. One form of earmarked tax is the General Social Security Tax on income which was introduced in France as an expression of social solidarity. It appears that contributions to the UIF can be reduced, and the reduction could be the basis for a general social security tax. An earmarked increase in consumption taxes (either as a whole or partially through taxing only certain goods and services, such as alcohol and tobacco) could be considered. Part of the resources that are currently envisaged for the wage subsidy could be allocated to a social assistance fund. Alternative sources of funds can be identified in the context of a social budgeting exercise.

3. Social assistance reform (other than old-age and disability grants)

The DSD suggests filling in the major gaps in the social grant system by:

(1) Improving support for children and care givers through

- extending the upper age limit for the child support grant (CSG) from 14 to 18 years (the new entitlement could be made conditional on school attendance or attendance in an occupational training programme);
- gradually increasing the amount of the CSG to the level of 'income sufficiency';
- making the CSG universal (i.e. not subject to a means-test);
- providing designated caregivers of children receiving the CSG with a grant that is at least at the level of the CSG benefit; and
- achieving the targeting or income-relating of social assistance benefits by introducing an income tax 'claw-back' of payments made to higher-income earners.

(2) Improving income support for unemployed persons not entitled to UIF benefits through providing social assistance grants for unemployed persons related to the proposed monthly unemployment continuation benefit (50 per cent of the minimum wage – see Section 4):

- Unemployed persons aged 19-24: 30 per cent of the continuation benefit (i.e. 15 per cent of the minimum wage)
- Unemployed persons aged 25-59: 20 per cent of the continuation benefit (i.e. 10 per cent of the minimum wage).

The panel supported all the above proposals since they would effectively reduce gaps in South Africa's social assistance provisions. The levels of the suggested non-UIF monthly unemployment benefits – 10 per cent or 15 per cent of the minimum wage – are questionable, since it is doubtful that a benefit of R100 to R150 would provide a sufficient incentive for the unemployed, notably the young, to undergo a demanding skills training programme.

A schedule for the introduction and improvement of the grants should be determined by a budgeting exercise that would map out a strategy for financing the benefits. The present schedule follows a gradual approach based principally on fiscal prudence. It also envisages the universalization of the old-age grant at a relatively early stage – before the introduction of youth unemployment support – which, though desirable, may not reflect the most urgent need given the relatively extensive coverage of the existing old-age grant system.

The panel advocated, as matter of priority, the early introduction of meaningful child support, caregiver grants and unemployment assistance benefits, combined with a highly visible, well-endowed and carefully monitored public works programme. The benefits and the public works programme could be substantially financed by resources that are currently envisaged for the wage subsidy programme.

Social assistance grants should be increased periodically to reflect increases in the general level of wages or the cost of living. These increases can be measured by an index of average earnings or by an alternative measure of living standards. Over a period of rising real incomes, the use of a price index will result in a widening gap between the incomes of grant recipients and other sections of the population.

4. Unemployment benefits and the Unemployment Insurance Fund (UIF)

The sole social insurance scheme in South Africa is the Unemployment Insurance Fund. In addition to unemployment insurance benefits, the UIF provides maternity, sickness, adoption and death benefits. Several years ago, the system was virtually bankrupt. Systemic reforms in 2002/03, including the extension of insurance coverage to persons above the contributions ceiling, inclusion of groups of new members and radical and successful administrative reforms turned the financial situation around. This is a unique success story by any international standards.

The scheme now has about 7.2 million contributors (including domestic workers). Annually the UIF pays benefits to about 420 000 unemployed persons, 30 000 sick persons and 96 000 women on maternity leave, and it pays approximately 24 000 death benefits. In 2006/07 the UIF had expenditures of about R2.7 billion and an excess of contributions over expenditures of about R6 billion. Recent surpluses have resulted in the UIF holding reserves of about R21 billion at the end of 2007.[3]

The UIF reserve has reached a level of about seven times its annual expenditure. This is several times higher than is required for a reasonable and prudent reserve. Social insurance schemes such as the UIF are risk-pooling and redistributive mechanisms, not capital accumulation schemes. Unemployment and short-term cash benefits require only contingency reserves. A contingency reserve should have sufficient funds to meet expenditures in order to provide time for a scheme to adjust its contribution rate and/or benefit levels in the event of adverse experience, for example, unexpectedly high unemployment benefits resulting from a rapid economic downturn. A contingency reserve level of about one year's expected annual expenditure is generally regarded as appropriate.

The UIF pays benefits to about ten per cent of the approximately four million unemployed persons in South Africa. However, its reserves effectively take about R18 billion away from possible redistributive measures which could be introduced to alleviate hardship due to unemployment not covered by the UIF or caused by other contingencies.

3 Of the R21 billion, about R15 billion is invested in government bonds.

The UIF recognises that there is a need to improve its coverage and concurs with the DSD that a number of improvements can be made. Measures suggested include:

- increasing the maximum number of benefit days the unemployment benefit is payable from 236 to 300;
- de-linking the benefit entitlement in the different benefit categories (for example, allowing women to receive the maximum number of daily unemployment benefit payments after having received the maternity benefit);
- improving the malfunctioning placement service and developing effective active labour market services (e.g. demand-oriented training and retraining services);
- extending for an unlimited period the payment of a continuation benefit of 50 per cent of the minimum wage (i.e. a monthly benefit of around R500) to beneficiaries who have exhausted their normal unemployment benefit entitlements, subject to their being available for work and following required measures to qualify for the benefit (e.g. participation in skills assessment and training programmes);
- increasing the lower limit of the graduated benefit replacement rates (currently 38 to 70 per cent) to 45 per cent; and
- including self-employed persons and civil servants.

The panel agreed in principle with the above measures, subject to the following qualifications:

- The period of payment of the continuation benefit should be limited in order to avoid creating dependency. This should not create hardship if a social assistance benefit for unemployed persons is introduced (see Section 3).
- The development of an effective active labour market policy is a matter of urgency. The services can be made available to the wider group of unemployed persons, with the cost of services to the uninsured reimbursed by the state.
- To avoid manipulation of the scheme, self-employed persons cannot be covered for unemployment benefits.
- The inclusion of civil servants is a matter of national solidarity.
- In the short to medium term, the above measures will not reduce the reserves of the UIF to the level of one time the expected annual expenditure. Thus, for a number of years, it would be possible to reduce the contribution rate. This would

free funds for financing urgently needed social assistance benefits.

The provision of social assistance benefits for the uninsured unemployed is a high priority. It may be observed that the introduction of a rural employment guarantee scheme (such as has been introduced in India) that provides one person per household with 100 days of employment per year paid at the minimum wage, would probably cost in the order of R6 000 per annum per recipient. This means that the annual surplus of the UIF alone could finance such a scheme for about one million youths. Furthermore, the part of the wage subsidy that is not earmarked to offset the introduction of a new social insurance scheme could be used to finance such a system, which would have a much more tangible outcome in terms of reducing unemployment. However, it was pointed out that the implementation of a 100-day employment guarantee scheme would not be an appropriate alternative to the proposed social assistance grants for unemployed persons (see Section 3).

5. Pension reform

The panel fully supports the principles of statutory national pension schemes: universality, equity, pooling of risks, mandatory participation, administrative efficiency and solidarity, as well as the objectives of adequacy, affordability, benefit predictability and financial sustainability.

With respect to the predictability of benefits, ILO Convention No. 102 requires a minimum replacement rate of 40 per cent (of the last or a defined reference wage) for old-age pensions after 30 years of contributions. This benchmark sets the minimum target level of income that people need for planning their retirement. Whether the benchmark is achieved or not, depends on the mechanism used to provide pensions, and on how investment, demographic and other risks are handled.

The DSD suggests a national pension system with the following components:

Tier 1: A flat-rate universal pension grant of approximately R940 per month (in 2008 terms) financed by general revenues. There would be no means-testing. This is a modification of the existing old-age and invalidity grant system whereby it is incorporated as a component of the statutory national pension scheme.

Tier 2: A contributory pension scheme with two components:

- Tier 2a: A defined benefit (DB) scheme – covering persons with annual incomes under R75 000, a contribution rate of 15 per cent of earnings and a pension benefit accrual rate of approximately 1.5 per cent per year of contributions.
- Tier 2b: A defined contribution (DC) individual savings scheme – covering persons with annual incomes of between R75 000 and R750 000 and a contribution rate of 15 per cent.

Tier 3: Supplementary voluntary savings, possibly subsidized by tax credits.

5.1 Tier 1: Old-age and disability grants

The universalization of the old-age and invalidity grants and the envisaged benefit levels are supported by the panel. They are crucial tools in the continuing battle to avoid poverty in old age and during invalidity. When there is a high income threshold for a means-test which results in most persons qualifying for the benefit, the cost of administering the means-test can be higher than the savings ahieved through means-testing. Since the present income threshold for the means-test is relatively high and population coverage of the grant is wide, it is desirable to abolish the means-test.

When there is an income threshold for contributions, there may be questions of equity between persons whose earnings were below the threshold and who consequently did not contribute, and those who contributed since their earnings were slightly higher than the threshold. Persons who made relatively low contributions might not receive any (or only a small) additional benefit, compared to others who made no contributions. An equitable approach would be to levy contributions only on earnings above the threshold.

5.2 Tier 2

The panel recommends that, before formulating a specific proposal for Tier 2 and seeking a national consensus, the

DSD should consider national pension scheme design issues, including the following:

The principal retirement benefit should be a pension:

- It may be necessary also to provide a modest lump sum at retirement (particularly for low-income earners).
- Drawdowns of retirement benefits before retirement should be limited. Contingencies that create the need for such drawdowns should be met by other benefits.
- Disability and survivors' pensions should be related to the retirement pension in payment or accrued pension rights.

Tier 2 should provide retirement benefits based on earnings up to a ceiling:

- The ceiling should be set at a level to include all the earnings of, say, 80 per cent of the insured persons.
- The ceiling should be adjusted annually to take into account increases in average earnings.

All income earners, including civil servants, should participate in the Tier 2 scheme:

- The inclusion of all income earners in the national pension scheme gives effect to the principles of universality, risk-pooling and solidarity.
- There should be no exemptions (e.g. for alternative schemes which have benefits equal to or better than the statutory scheme). The Tier 2 scheme would be 'carved out' of existing occupational schemes.
- Existing schemes would provide supplementary benefits by applying accrual rates in excess of the statutory scheme accrual rate and for earnings above the statutory scheme earnings ceiling.

A target Tier 2 replacement rate for a full-career participant should be set (e.g. an accrual rate of 1 per cent per year would produce a 40 per cent replacement rate after 40 years of contributions):

- Earnings for the calculation of pension should be career average adjusted earnings (i.e. earnings adjusted annually according to the increase in average wages).
- There is no reason to limit participation to persons over the age of 25 years (especially if Tier 2 is a DC scheme).
- A replacement rate under 50 per cent leaves room for Tier 3 voluntary occupational and personal pensions to top up the statutory benefit.

A Tier 2 contribution rate of 15 per cent has been mentioned:

- A possible 15 per cent increase in labour costs is not insignificant and, to the extent that the cost falls directly or indirectly on employers, has potentially serious implications for employment in a situation where a severe unemployment problem already exists.
- A 15 per cent contribution rate will generate funds for investment which may be more than can be absorbed by the domestic capital market and could affect interest rates and asset values.
- Foreign investment is an alternative, but this is unpopular; funds withheld from consumption should be used to build South Africa.

Retirement age for males has been reduced to the female retirement age of 60 years. This will create problems in the future:

- It is simple to lower retirement age, but extremely difficult to develop the consensus and political will to raise it, and any such raise generally has to be phased in over extended periods.
- Retirement age should be raised to maintain a constant ratio of expected period in retirement to expected contributory period.
- Provision for an automatic increase in the retirement age as life expectancy at retirement age increases could be legislated.

Tax relief may not encourage persons to opt for voluntary (e.g. occupational) retirement schemes, but it would be inequitable to tax these schemes on a TTT basis:[4]

- Acceptable alternatives are EET (i.e. tax deferral) or TTE. Under the EET system, the personal income tax payable on the pension is generally at a lower rate than the tax relief on the contributions and investment income.
- Ceilings can be applied to any tax-relief arrangements.

4 TTT means that contributions, investment income, and benefits are subject to income tax. EET (exempted, exempted, taxed) means that contributions and investment income of reserves are exempted from income tax, while benefits are taxed

The structure of a national pensions system for South Africa, consisting of a basic Tier 1 flat rate universal pension, a social insurance (DB) Tier 2a and a voluntary private insurance (DC) Tier 3 was supported by the majority of the international panel. One member suggested a structural modification to Tier 2, which is set out in Section 5.2.2 as Option 2.

The panel made a number of specific comments on the design of Tier 2. Suggested modifications and alternative options are outlined below. Option 1 refers to Tier 2a, a DB scheme operated by a government agency. Option 2 discusses Tier 2b, a mandatory DC scheme operated by private sector managers.

5.2.1 Tier 2 Option 1: Defined benefit scheme

The Tier 2 scheme could consist of only a social insurance DB scheme (i.e. only Tier 2a), with a 1 per cent (or slightly lower) accrual rate for retirement pensions, and could include the risk benefits (invalidity and survivors' pensions). The ceiling on insurable earnings would be set at 2.5 times average annual earnings (i.e. R75 000 per annum, according to information provided to the panel). The reference wage would be calculated on a career average adjusted earnings basis using revalued annual earnings. Benefits in payment would be indexed to take into account inflation since they were awarded.

A DB scheme has predictable replacement rates and thus enables personal financial planning. After 30 years of contribution, a pension formula that guarantees 1 per cent of the reference wage per year of contribution would, along with Tier 1, lead to a total replacement rate for the average earner approximately at the 40% level set out in ILO Convention No. 102. After 40 years of contribution, the replacement rate would be around 50%.

A statutory DB national pension scheme would be partially funded. The ultimate guarantor of the benefits is the Government. The initial contribution rate could be set taking into account the capacity of contributors to contribute, the amount of reserves that will be accumulated, and the possibility of investing the reserves productively. Subsequently, depending on the initial contribution rate, the rate may have to be periodically increased according to a benchmark that triggers an increase. A 40 per cent replacement rate after 40 years of contributions could be financed with a contribution rate much lower than 15 per cent.

A partially funded Tier 2 DB scheme would also allow:

- redistribution through the benefit formula or contribution rate (a progressive contribution rate structure is preferable to a wage subsidy);
- payment of risk benefits (disability and survivors' pensions) by the scheme;
- crediting of insurance periods for periods of sickness, maternity, caring (which will become more important in South Africa in the coming years) and unemployment;
- 'grandmothering/fathering' in older workers without having to wait decades before the first full pensions are paid; and
- diversification of risks among a flat rate Tier 1, DB Tier 2a and voluntary DC Tier 3.

The Tier 2 DB scheme would be operated by a government agency. A Tier 2 DC scheme would be operated by competing private sector managers. It is not clear what advantage there is in having a DC scheme and private managers given the following considerations:

- Competition among private DC scheme managers is largely illusory. Rather, private investment institutions could be contracted to invest tranches of the reserve funds accumulated by a partially funded DB scheme. This would create real competition.
- Private DC scheme managers typically have much higher expense ratios (including commissions and profits) than a well-managed, publicly administered DB scheme where the expenses should be below 5 per cent of contribution income.
- Risk benefits (payable in the event of disability or death) must be financed separately in a DC scheme.
- A DC scheme requires contributors to make important decisions about financial products for which they are totally unqualified, and they are often influenced by advisers who have a pecuniary interest in their decisions.
- Annuitization of DC balances at retirement to produce a lifetime stream of periodic payments has been a problem

for DC schemes. Also, unless the provider(s) of annuities have access to indexed bonds (almost exclusively issued by the Government), pensions cannot be adjusted to automatically take into account inflation. If indexed bonds are available, there is no point in pretending that competition exists among annuity providers.

Mandatory membership of DC schemes requires that a stringent and effective regulatory authority must be set up. When contributions are mandated, regulation must be stronger than for voluntary schemes, since the Government has an implicit obligation for the performance of the mandatory DC scheme. The cost of regulation is ultimately borne by scheme members in the form of lower pensions.

If there is some form of government guarantee of pensions, the Government might just as well operate a DB scheme.

5.2.2 Tier 2 Option 2: Mandatory defined contribution scheme

It is not clear why Tier 2 should have both a mandatory social insurance programme (Tier 2a) and a mandatory fully funded defined contribution component (Tier 2b). Such a combined programme would require additional contributions and (if successful) would imply substantial transfers across the life cycle from working age to old age.

Existing defined contribution pension funds in South Africa suffer – to a greater or lesser extent – from problems of excessive fragmentation and high administrative costs which reduce the effective return to participants. Much of the potential return to the more diversified portfolio that can be offered by such a scheme relative to a traditional 'pay-as-you-go' scheme is therefore eroded and not available to plan participants in the form of higher pensions.

If a policy of mandatory defined contribution pension coverage is implemented – whether to supplement Tier 2 earnings-related coverage or as an alternative to that programme – the structure of the DC component must be carefully thought through. In particular, it should avoid the pitfalls of excessive administrative charges, fragmentation of funds and over-complexity of investment choices that might arise in such circumstances.

One strength of a proposal for a mandatory tier of this kind – especially if backed up by the possibility of public contributions in the form of individual tax reliefs (up to some ceiling) and, possibly, supplementary contributions for low earners, is that the sheer size of the potential flow of investments gives the Government some bargaining power vis-à-vis private providers. Mandatory DC plans open up a whole new market to private providers, and it is important that the Government exploits its role in the process to maximize social welfare rather than simply the profitability of providers. This bargaining power should make it easier for the relevant government department to negotiate on issues such as capping administrative charges, limiting complexity and exploiting the economies of scale in investment arising from a limited number of providers.

One model of such a structure would be for the Government to act as a 'clearing house' in collecting mandatory contributions from employers (as with a standard public programme) and then transferring these contributions to nominated providers. This would save on the administrative and marketing costs that arise when individual providers seek to negotiate contracts with individual contributors. The Government could establish an open tendering process by which a limited number of established private pension providers (which could be from the South African market, or external providers with international experience of similar arrangements) are invited to manage the investment funds arising from these contributions. Contributors could choose which of (say) the four or five providers approved by the Government would manage their contributions; the Government itself could act as a default provider by investing the proceeds in government securities.

Approved providers would have to satisfy stringent conditions concerning ceilings on administrative charges, transparency of portfolios and reporting arrangements, and easy access to information and advice for members. To keep administrative costs under reasonable control, the range of investment options offered by these companies to contributors should be decided in advance by the Government and kept to a strictly limited number of alternatives (e.g. 100 per cent bonds, 25 per cent equities + 75 per cent bonds, 50 per cent equities + 50 per cent bonds). Experiments undertaken in conjunction with the introduction of the new Personal Accounts in the UK suggest that potential contributors find it difficult to make choices beyond four or five portfolio options, and that their choices are highly influenced by whatever 'default option' is offered as the portfolio that will be assigned if the contributor does not make an 'active' choice. The role of the Government in this process should also permit it to rule out what it considers to be 'anti-social' investment strategies and to pursue its own social goals in deciding on approved investment strategies. However, care should be taken in ensuring that the pursuit of social goals does not outweigh the provision of satisfactory returns to contributors which, after all, is the primary object of the reform.

With such a scheme in place, the residual role for Tier 3 investment in discretionary pension funds is that it permits certain groups in the population – particularly those with surplus investment funds – to invest in portfolios which may diverge from the limited choice envisaged for the Tier 2b. The extent and diversity of these arrangements would then depend on the success of the Tier 2b pension investments. One could envisage a successful Tier 2b as leaving only a residual role for discretionary investments with the inevitable attrition of much of the existing – fragmentary – multiplicity of pension schemes. Indeed the nominated Tier 2b providers might have a dominant market position in Tier 3 as well as Tier 2b, which re-emphasizes the need for effective regulation and control of the private pension sector.However, if returns earned in Tier 2b were relatively modest (due, for example, to the Government and contributors choosing rather conservative investment strategies), then the scope for a large Tier 3 would be greater. Either way, effective regulation of the private pension industry must extend to Tier 3.

5.3 Tier 3

Tier 3 would comprise voluntary private and personal pension schemes that would largely consist of existing occupational schemes. Occupational schemes would have to be modified depending on the form of the specific Tier 2 scheme that they would supplement. Regulation of Tier 3 schemes should be strengthened.

6. Health care

6.1 The need for change

The case for change in health care financing in South Africa through the introduction of mandatory social health insurance is both strong and urgent. Despite discussion of various proposals, there does not appear to be a clear proposal that could now be submitted for consultation and discussion with stakeholders and high level decision-makers.

The case for change should also be considered in the light of the lack of achievement of the Millennium Development Goals (MDGs) for health in the past decade, and the stagnation and even deterioration in mortality rates, as noted in the DSD document Creating our Future: Strategic Considerations for a Comprehensive System of Social Security (Chapter 4: Context for Social Security Reform, Socioeconomic context, p. 13).

The mechanisms employed to reach the suggested change could be accelerated by stressing several issues, in addition to the noted problems and cost escalation in the voluntary medical insurance system and public-private mix of providers. These issues are:

- Inequity in access to health care, with the majority low-income population seeking and receiving less care than the minority high-income population
- Differences in health indicators across population sectors (e.g. by income levels, urban and rural residence, insured persons in private schemes and the rest of the urban population)
- The lack of comprehensive health care benefits in the existing private medical insurance schemes, and failure of these schemes to introduce health promotion and preventive services
- The failure of the substantial revenue generated through the medical insurance schemes to contribute to improvement in health and health care services throughout the country.

6.2 Principles of mandatory social health insurance

From the outset, the principle of universality should be stressed in the change in health care financing, mainly through the introduction of a mandatory social health insurance system with affordable levels of contribution and social assistance for those who cannot contribute. Universality is not likely to be achieved immediately and may take up to a decade. The process will require:

- Legislation of a mandatory social health insurance system for all economic sectors, including both public and private sector employees and their dependants, as well as the self-employed and informal economy workers and their dependants
- Adjustment of the Government Employees Medical Service (GEMS) to the design of the new mandatory system
- The sharing of contribution payment between employers and employees for the employed population as a percentage of salary, with appropriate ceilings
- Appropriate mechanisms to facilitate registration and contribution collection from persons in the informal economy and consideration of state subsidies for the low-income families in this population to replace employer participation
- Mandatory social health insurance for all the contributing sectors, without exemption of persons covered by existing private health insurance schemes
- Coverage of the indigent and non-economically active population with the same entitlement to benefits as the contributing population, and the cost covered by the state budget and through the same system
- Coverage of a package of health insurance benefits which includes both ambulatory and in-patient care, with primary health care in the community and home, specialist care covered as ambulatory and in-patient benefits, and covering an appropriate defined range of technology and pharmaceutical drugs and medical supplies
- A defined allocation of health insurance revenues for health promotion and prevention at the individual and population levels in addition to government funding of preventive services
- Provider-payment systems that are not volume based, that is, moving from fee-for-service to capitation fees or a combination of provider-payment mechanisms with the necessary quality assurance mechanisms to assure appropriate health care
- Provider-payment mechanisms that are identical for all categories of providers for essential health insurance benefits
- Appropriate legislation and regulatory tools to implement and enforce all of the above, and covering all aspects of contributory and non-contributory membership, benefits, provider contracts and payment, as well as governance and management structures.

6.3 Prerequisites to assure effectiveness of a mandatory health insurance scheme

The development of private health care in South Africa has not followed a national health system development plan, but rather has followed economic SOAPortunities in a for-profit service industry. The majority of the population will remain dependent on the public health care system, which needs to be strengthened as part of the process of the introduction of health insurance. Several activities or interventions are suggested to reach this stage:

- Allocation of additional resources from the state budget for necessary improvements in infrastructure, including equipment, in public health centres and hospitals
- Review of the system of provincial level allocations for health care to assure improvement in recruitment and a stable supply of all resources, particularly human resources
- Development of national and provincial plans for the establishment, licensing and continued accreditation of all levels of health care facilities (including health centres, specialty clinics, diagnostic facilities and hospitals)
- Strengthening of the management and financial accounting functions of providers, particularly the public hospitals at all levels, to enable the retention of revenue from health insurance at the provider level, rather than the

current transfer of user charges to the provincial health departments. With appropriate guidelines, this process should lead to financial autonomy of providers.

- The extension of coverage to persons in the informal economy may involve a number of alternatives, from the development of capacity in a state health insurance system to cover this population to contracts with associations or cooperatives to operate as satellite schemes. Care should be taken to develop regulations for the extension of coverage to this population in order to avoid the establishment of a wide variety of unregulated community-based initiatives.
- If user-fees in public hospitals are eliminated, then mechanisms will be needed to encourage membership of the mandatory health insurance scheme. The implementation of mandatory social health insurance should result in providers being financially compensated for health care provided to all population groups.

6.4 Regulation of existing structures

The current voluntary health insurance coverage involves a large number of medical insurance schemes which are statutorily non-profit entities served by commercial agencies to handle the contracting and payment of for-profit providers of medical services. While some proposals for regulation have been made, it is suggested that criteria for the accreditation of the agencies should first be developed, and that the government authorities responsible for each group (e.g. medical insurance schemes, commercial agencies, private health providers) be defined as part of the regulatory reform process.

6.5 The role of the existing private health insurance schemes and providers

The role of the existing medical insurance schemes has to be clarified as a first stage in development of a proposal. It would be unfortunate if 14 years after the democratic change in South Africa, a two-tier system were developed, that leaves the higher-income population covered by the existing private structures, with a new public system for the low-income and indigent population. The existing schemes could play an important role in insuring benefits beyond essential health care on a voluntary basis, and could facilitate the provision of non-essential services, including direct access to specialists without referral and private in-patient accommodation. The expertise of the larger existing schemes should be tapped to assist in the development of the mandatory social health insurance system.

Private hospitals would gain from contracting with the mandatory insurance scheme to cover defined populations under the same provider-payment conditions, and this could increase their current low occupancy rates without major cost increases. At the same time, the private providers would be able to charge for non-essential services, such as private accommodation, directly to the patients or through the voluntary insurance component.

6.6 The development process for a mandatory health insurance scheme

Following the vast amount of research and work already done, it should be possible to develop a sound proposal within two to three months. The proposal could be in the format of a master plan for mandatory social health insurance for South Africa, developed by a task force including representatives of the agencies that participated in the seminar organised by the DSD. Assistance could be given by providing examples and an outline for a master plan.

The master plan should be a document for review and consultation, and subsequent submission for approval to the highest-level authorities, along with appropriate orientation on the principles of social health insurance and the multiple objectives of the proposed changes in health care financing in South Africa.

Parallel to the master plan, a plan for the legislative and regulatory tools required for mandatory social health insurance should be prepared by the same task force, but with the assistance of individuals familiar with the Constitution and legislative tools required for such mandatory systems for social services. This plan would help to provide a realistic time-frame for the development of the health insurance system.

Much of the groundwork has already been done, and the suggested documents could be drafted within a short time.

7. Wage subsidies

The Treasury has suggested that the introduction of a contributory social insurance scheme should be eased by wage subsidies for low-income workers. The wage subsidies would be paid to employers, and should serve a dual purpose: firstly, to offset workers' social insurance contributions and, secondly, to create incentives for employers to hire low-skilled workers. The panel considered that reduced contribution rates for low-income workers would be a better and simpler alternative. Under a defined-benefit pension scheme these subsidies could be financed by the community of contributors on a solidarity basis without any subsidy from the Treasury.

The amount of the wage subsidy that exceeds the amount needed to offset the social insurance contributions would be a subsidy for low-skilled labour. Given the low amount of monthly subsidy a low-skilled worker would receive (possibly in the order of R100 per month), the panel questioned whether the subsidy would be a sufficient incentive to significantly increase employment of low-skilled workers. Rather, there is risk that this subsidy would lead to considerable dead-weight losses and would embody a hidden tax relief for employers.

8. Institutional reform, governance and administration

It was suggested by the panel that:

- It should be recognized and accepted that existing social security institutions are unlikely to be replaced or amalgamated. The focus should be on rationalizing social security programmes and introducing new ones in order to ultimately produce a coherent (non-duplicative) and comprehensive system of statutory social security protection.
- It should not be possible to receive two benefits due to the occurrence of one contingency ('double dipping').
- The regulation of voluntary occupational (and personal) pension schemes must be strengthened. (See publications and activities of the International Organization of Pension Supervisors (IOPS) and the Financial Affairs Division, Directorate for Financial and Enterprise Affairs, Organization for Economic Co-operation and Development OECD.)
- A system of specialized social security tribunals should be set up to deal with appeals against decisions made on a claim for a benefit or other matters. (See the systems in the UK and Germany.)
- Any social security scheme should be simple to understand. Complex schemes may (theoretically) produce better protection, but if the scheme is not understood by those it is designed to protect, it will not be appreciated. A simple scheme facilitates simple and efficient administration by the social security institution(s).
- Collection of contributions to all social security programmes along with income tax can reduce collection costs and is a sound approach, provided that:
  - The tax collection agency is efficient, and able and motivated to collect contributions on earnings between the social security schemes' contribution threshold(s) and ceiling(s), and to perform social security verification, oversight and enforcement functions
  - The tax collection agency transmits data on contributors and contributions to each social security scheme administration promptly
  - The tax collection agency has the legal right, personnel and motivation to enforce social security contribution conditions.
- A common threshold and ceiling for contributions to all social security schemes would simplify contribution collection and employers' compliance. Thresholds and ceilings should be adjusted annually to take into account increases in average earnings.
- A centralized agency to maintain basic data on scheme members is a sound approach, but each scheme still needs its own specific data (for claims adjudication, actuarial valuations, etc).
- Each scheme should adjudicate and pay its own benefits. Offices comprising all government operations (e.g. social security schemes, vehicle licenses, business licences) are a modern approach ('one-stop shops') and should be used to provide information and advice to social security scheme members.

9. By way of conclusion: Further technical work is needed

The panel concluded that social security reform in South Africa should move forward based on a set of principles and priorities. The key principles are:

- Keep it simple.
- Do no harm; ensure that reforms are, and are perceived to be, equitable.
- Act quickly to do what can be done.
- Take time to ponder what requires longer-term planning.

Social security reforms that would help to stabilize South African society should have first priority. Improvements to the social assistance grant system will have an immediate effect on poverty and inequality, and can be undertaken immediately. They can be financed in the short term from the current surplus, transitional borrowing at a modest level and/or a reduction in tax credits for voluntary occupational or private pensions and health insurance. In the medium term the increased resources can be financed by borrowing from the pension scheme until such time as the tax to GDP ratio is increased by appropriate measures, or increasing growth creates the necessary fiscal space. The establishment of a social assistance fund (to finance the grant system) in parallel with a social insurance fund (to finance social insurance pensions) and a possible national health insurance fund would create a transparent financial structure of the overall social security system.

To create maximum 'buy-in' and wide acceptance of reforms, institutional upheavals should be minimized. While existing institutions may be assigned new or additional tasks in a comprehensive reformed system of social security protection, major reforms of the institutions themselves would result in a political cost that should be avoided in a situation where broad consensus is necessary. The functional part of the private pension and health insurance schemes should be maintained, and these schemes should be given space and roles to ensure that they can maximize their social utility and minimize potential discontent.

Establishing or reform of social insurance pension and health insurance schemes is a longer-term undertaking. The full effects of the schemes are evident only after years – in the case of a pension scheme, after generations – and the analysis requires extensive statistics. Much groundwork to set up these schemes has already been done, and it should be possible to prepare the suggested documents within a short time. Through the seminar organised by the Department of Social Development in June 2008, the major stakeholders have been identified and have demonstrated their willingness to participate in the process.

Following the endorsement of mandatory social health insurance by the ANC in November 2007, this process should move ahead as soon as possible to take full advantage of the current political commitment. The process should first focus on the major equity, health status and health system issues, and then on the financial aspects and institutional elements. The proposal should be kept as simple as possible and should provide a rational time-frame for the required changes, drafting and passing of legislation and the extension of coverage to the entire population to reach universal coverage.

Reforms of important societal institutions, such as social insurance and social assistance schemes, must be based on the greatest possible transparency and full information to the public on the expected long-term development of contribution and tax rates and levels of benefits. Based on complete information, an informed policy debate on the pros and cons of alternative solutions could take place and be brought to a consensual conclusion. Full disclosure of all information and assumptions can result in a robust consensus in an interest-ridden policy area like pension reform. The process will take time, but such an approach can create national ownership and consensus and avoid subsequent governments reopening the reform package, thereby creating uncertainty.

The ILO is available to support the process by providing the Government and social partners with a structural financial analysis of the social security systems, including the pension systems, on the basis of demographic, economic and labour market scenarios provided by a tripartite working group. The outcome of this analysis would be a projection of the social budget[5] of South Africa, which would provide a sound basis for a discussion of different options. The analysis could be established under the guidance of a multi-party steering group (including representatives from concerned government agencies, employers, workers and civil society) which would help to set the assumptions and identify design alternatives which could then be tested to assess their social desirability and fiscal feasibility.

The members of the panel and the International Poverty Centre are ready to support aspects of the reform process through individual or collective inputs.

5 A social budget model would encompass all branches of social insurance, the health insurance scheme, and the social assistance schemes as well as the government budget in order to model the financial and fiscal relationships and impacts of the overall social security system.

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