STAKEHOLDER FEEDBACK ON THE STANDING COMMITTEE ON APPROPRIATIONS

14 October, 2015

For an Equitable Sharing of National Revenue

PRESENTATION OUTLINE

1. Role and Function of the FFC
2. FFC Support During National Budget Process
3. FFC Support during the year
4. Strategies to Enhance Partnerships: Training and Research
5. Exploring Ways to Strengthen Systematic Oversight Over State Infrastructure Expenditure
6. Fiscal Policy: Constraints, Risks and Opportunities
7. Summary

FINANCIAL AND FISCAL COMMISSION

1. Role and Function of the Financial and Fiscal Commission

ROLE AND FUNCTION OF THE FFC

- What is the FFC?
  - Permanent statutory body established in terms of Section 220 of Constitution
  - Independent and subject only to Constitution and the law
  - Must function in terms of an act of Parliament
- What is the mandate of Commission?
  - Makes recommendations as envisaged in Chapter 13 of the Constitution
- How? Enabling legislation
  - Section 214 (2), 218(2), 228 (2), 229(5), 230(2) 230A(2) of the Constitution
  - FFC Act (No 99. of 1997) IGFR Act (No. 97 of 1997)
  - Provincial Tax Regulation Process Act, Municipal Fiscal Powers and Functions Act, Borrowing Powers of Provincial Government Act
- FFC in IGFR system
  - Municipal Finance Management Act, Municipal Systems Act, Money Bills Amendment Procedure and Related Matters Act, Intergovernmental Fiscal Relations Act

FINANCIAL AND FISCAL COMMISSION

Role and Function of the FFC [cont.]

- Commission mandate is defined around three interrelated pillars:
  - The Commission must make recommendations to Parliament and provincial legislatures on the equitable division of nationally raised revenue
  - The Commission can make recommendations on any other financial and fiscal matter
  - The Commission should contribute towards the creation and maintenance of an effective, equitable and sustainable system of IGFR
- Three pillar mandate executed through focused research, recommendations, policy advice and outreach activities (public hearings, training, briefings and publications)

FINANCIAL AND FISCAL COMMISSION

FINANCIAL AND FISCAL COMMISSION

2. FFC Support During the National Budget Process

Support Measures During National Budget Process: 3 Pillars

- **Providing recommendations to Committee 10 months before budget**
- **Making submissions on basis of IGFRA and MBAPRMA**
- **On request advise and ensuring value for money**

PILLAR 1: SUBMISSION FOR THE DIVISION OF REVENUE

- Submission made in terms of:
  - Section 214(1) of the Constitution (1996)
  - Section 9 of the Intergovernmental Fiscal Relations Act (1998)
  - Section 4(4c) of the Money Bills Amendment Procedure and Related Matters Act (Act 9 of 2009)
- **Submission is made to Parliament 10 months prior to tabling of the DoR by the Minister of Finance**
  - Contains recommendations/proposals for the following fiscal year and medium terms expenditure framework (MTEF)
  - Constitute key element of support to the Appropriations Committee

FINANCIAL AND FISCAL COMMISSION

Outline: Submission for the Division of Revenue 2016/2017

I. Macro-Micro and Fiscal Aspects of Public Investment Management

1. Responding to South Africa Infrastructure Challenges: Macro-Micro Dimensions
2. Economic Growth Effects of Municipal Capital Spending

II. Indirect Grants Proliferation, Design and Accountability in Public Infrastructure Management

3. A Review of Direct and Indirect Conditional Grants – Selected Conditional Grants
4. Accountability in Infrastructure Delivery – Case of Local Government Sphere

III. Improving State Capacity through Education and Productivity Innovations

5. Fiscal Arrangements for Financing Early Childhood Development Infrastructure
6. Public Sector Productivity – The Case of Secondary Education
7. Improving Government Operations Through Information and Communication Technologies

PILLAR 2: SUPPORT DURING DIVISION OF REVENUE

- Regular, annual engagement with the Division of Revenue process takes three forms:
  - Commission produces recommendations on the equitable division of revenue among the three spheres of government (S 9(1) of IGFR Act). This is accompanied by a technical report and simpler policy briefs.
  - Minister of Finance must consult the Commission 14 days prior to the introduction of the Bill in Parliament and indicate in a memorandum accompanying the Bill what account was taken of the Commission's recommendations (Sections 10(3) and (4) of FFC Act)
  - The Commission then produces its third document, a submission on the Division of Revenue Bill to Parliament
- Another important advisory task relates to assignments among spheres of government
  - Before tabling a proposal for a national or provincial assignment to local government in general, the national or provincial Minister must consult the Commission
  - An assignment of functions or fiscal powers has no legal force until the organ of state making such assignment has indicated the extent to which it gave consideration to the Commission's views

FINANCIAL AND FISCAL COMMISSION

PILLAR 2: SUPPORT THROUGH MBAPRMA

- Money Bills Amendment Procedures and Related Matters Act (MBAPRMA) enacted in 2009. Sections making reference to FFC

Section 4(4C) requires that when committees on appropriations consider any money bill, the recommendations of the FFC must be considered/reported on

Section 9(7A) requires that in passing the annual division of revenue bill, the appropriations committees must consult with the FFC

FINANCIAL AND FISCAL COMMISSION

Support Through MBAPRMA [Cont.]

- MBAPRMA formalises a four stage budget process consisting of the
  - Medium Term Budget Policy Statement (MTBPS),
  - Fiscal framework which delineates revenue and expenditure aggregates
  - Division of Revenue Act
  - Departmental appropriations considered by the various portfolio committees
- Makes provision for FFC input to:
  - Finance committee cluster on the MTBPS and the fiscal framework
  - Portfolio committees drafting of Budget Review and Recommendations (BRR) reports

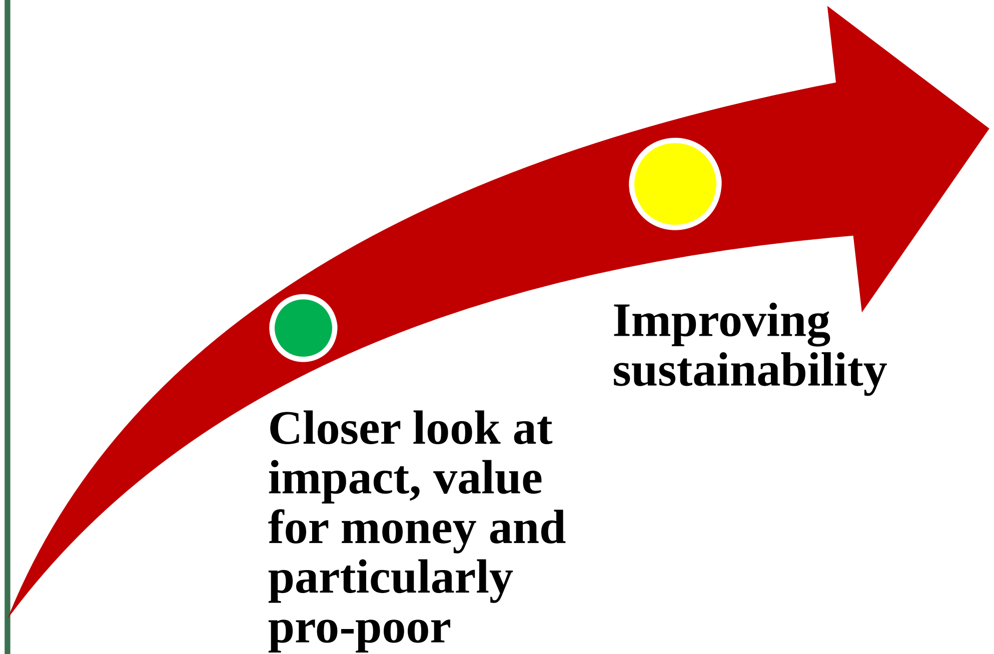
FINANCIAL AND FISCAL COMMISSION

Primary Outputs To Support The Committee Through MBAPRMA

- Submission on the Fiscal Framework and Revenue Proposals
  - Contains FFC's response to the fiscal framework and revenue proposals contained in the budget tabled by the Minister
- Submission on the MTBPS and Amended DoR and Appropriation Bill
  - Contains the FFC's response to the MTBPS and adjustments to the division of revenue
- Submission on the DoR Bill
  - Submitted to Parliament in February and outlines the FFC's response to DoR Bill and relevant annexures
- Submission on the Appropriation Bill
  - Submission made to the Standing/Select Committee on Appropriations
- Any other special reports made at own initiative or request by the Appropriations Committee

FINANCIAL AND FISCAL COMMISSION

PILLAR III: ENSURING VALUE – DEVELOPMENTAL IMPACT



- Allocative efficiency and value for money
- Focus on Inclusive Growth
- Adding more modules (gender, environment, and energy etc.)
- Poverty and inequality impact

FINANCIAL AND FISCAL COMMISSION

FFC Work Around Value For Money

- **Dimensions of value-for-money covered in FFC work:**
  - **Efficiency:** Achieving more output from the same input, while maintaining quality [Cost function work]
  - **Economy:** Reducing the cost of resources used as inputs [Consolidation]
  - **Effectiveness:** Achieving better outcomes by changing the nature of outputs [Wage Bill].
- Programmes not covered on the budget can be financed by reallocating spending from non-performing programmes
- Expenditure Limits and Quality

FINANCIAL AND FISCAL COMMISSION

3. FFC Support during the year (2014 and 2015)

FFC SUPPORT DURING THE YEAR (2015)

- **FFC had the interactions outlined below (with the SCOA)**
  - Presented on the submission of the 2016/17 Division of Revenue Bill
  - Briefing on the withholding of local government equitable share
  - Provided input on Eskom Special Appropriation Bill [B16-2015] and Eskom Subordinated Loan Special Appropriation Amendment Bill [B17-2015]
  - Commented on the Appropriation Bill [B6-2015]
  - Submission on the 2015 Division of Revenue Bill
  - Training of Parliamentary Researchers.

FINANCIAL AND FISCAL COMMISSION

FFC SUPPORT DURING THE YEAR (2014)

- **FFC had the interactions outlined below (with the SCOA)**
  - Briefing on the 2014 Medium Term Budget Policy Statement
  - Tabled the FFC's report on the 20th Anniversary Conference
  - Briefing on the 2015/16 Division of Revenue
  - Briefing on the Appropriation Bill
  - Briefing on the Division of Revenue Bill (B5-2004]

FINANCIAL AND FISCAL COMMISSION

FINANCIAL AND FISCAL COMMISSION

4. Strategies To Enhance Partnerships: Training, Research and Influencing Allocations

Enhancing Partnership Between FFC and SCoA

- FFC can provide advice, analysis and training to assist the work of the Committee
  - Specialised IGFR training to committee members and/or parliamentary researchers on request
  - Provision of recommendations that are founded on evidence based research
  - Technical support with respect to parliamentary fiscal oversight activities
  - Recommendations and reports readily available in the public domain

FINANCIAL AND FISCAL COMMISSION

IMPROVING BRRS THROUGH RESEARCH

- For Committees to influence budget allocations, timing of intervention is crucial
  - Efforts via BRR reports likely to yield much more impact than efforts applied later in the cycle.
  - Efforts applied to MTEF outer years likely to be even more successful if well founded.
- Some of the measures which could be considered include:
  - Sensitising committee researchers to the large array of source of independent analysis and research relevant to the BRR, including those from Chapter 9 Institutions Supporting Democracy and the FFC.

FINANCIAL AND FISCAL COMMISSION

Improving BRRs Through Research Cont…

- Some of the measures which could be considered include:
  - Encouraging an approach where recommendations for more money in one programmatic areas is accompanied by suggestions for reprioritisation, savings and increasing efficiency.
  - Identifying cross cutting themes (e.g. impact on vulnerable groups, employment creation or personnel related expenditure) that cut across all BRR Reports.

FINANCIAL AND FISCAL COMMISSION

5. Exploration Of Ways To Exercise Systematic Oversight Over Infrastructure Expenditure

EXPLORE SYSTEMATIC OVERSIGHT ON STATE INFRASTRUCTURE EXPENDITURE

FFC conducted oversight visit to Limpopo province and therefore tables the following recommendations:

Financial performance

- Municipalities should ensure that they spend conditional grant funds to avoid having funds taken away. The municipalities should always remember that spending conditional grant funds properly is followed by incentive allocations.
- The municipalities should ensure that they comply with quarterly spending patterns and reporting requirements.

Non-financial performance

- The quality of projects that municipalities are rolling out should be of high quality. These projects should be viewed as the legacy of current generation for the benefit of future generations. Therefore, the municipalities and the Provincial Treasury and Department of Cooperative Governance, Human Settlement and Traditional Affairs should strengthen their monitoring and evaluation units.
- Municipalities should train and capacitate unskilled labour force.

FINANCIAL AND FISCAL COMMISSION

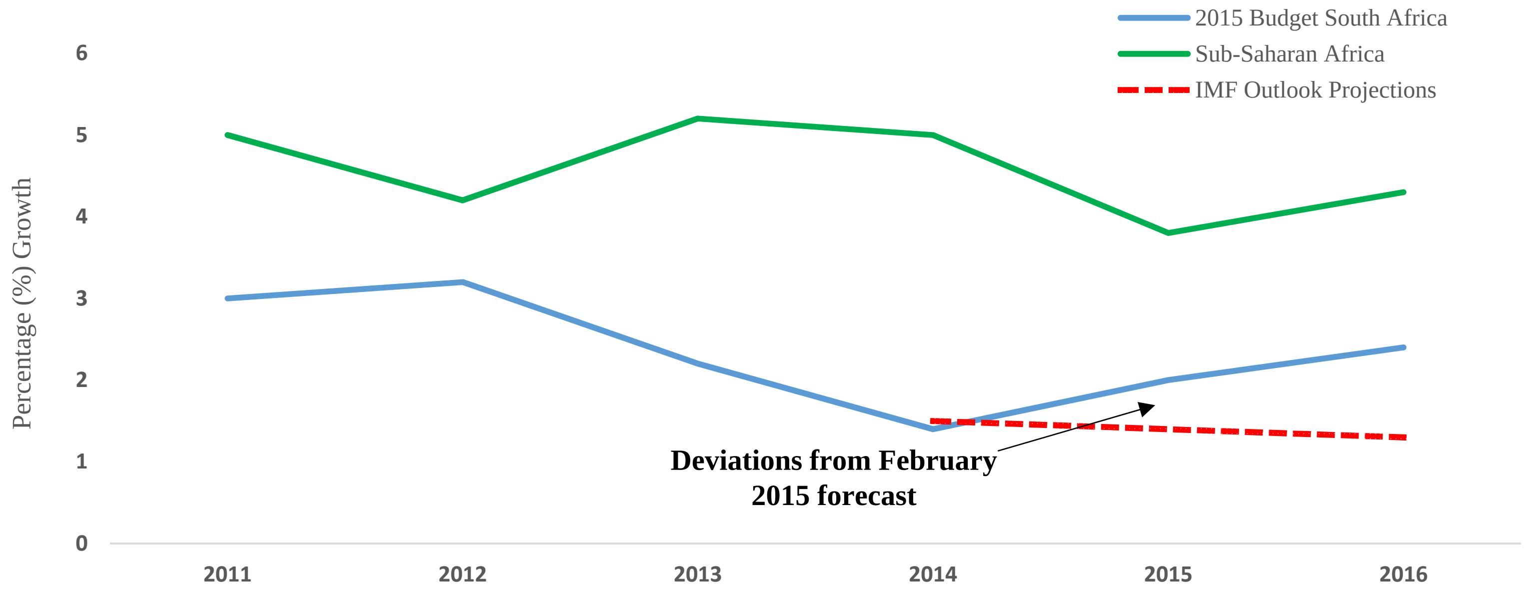
Matrix approach to Oversight

	Design	Implementation	Evaluation questions
▪ Targeting	▪ The right people?	▪ **Type I and II errors**	▪ Why is targeting failing? (protocols faulty, not being followed, corruption ..)
▪ Training / capacity building	▪ Right people? Is it appropriate? Mechanisms to ensure skills utilized	▪ Quality of delivery ▪ Skills / knowledge acquired and used	▪ **Have skills / knowledge changed? Are skills / knowledge being applied?** Do they make a difference to outcomes?
▪ Intervention delivery	▪ **Tackling a binding constraint?** ▪ Appropriate? ▪ Within local institutional capacity	▪ Delivered as intended: protocols followed, no leakages, technology functioning and maintained	▪ What problems have been encountered in implementation? When did first benefits start being realized? **How is the intervention perceived by staff and beneficiaries?**
▪ Behavior change	▪ Is desired BC culturally possible and appropriate; **will it benefit intended beneficiaries?**	▪ Is BC being promoted as intended (right people, right message, right media?)	▪ Is behavior change occurring? If not, why not?

FINANCIAL
AND FISCAL
COMMISSION

6. Fiscal Policy: Constraints, Risks and Opportunities

2015 Economic Outlook: navigating headwinds



- 2015 Budget emphasised fiscal consolidation in response to weaker than expected economic outlook
  - October 2015 mini-budget will occur against the background of further downward revisions to economic prospects of South Africa’s economy.

FINANCIAL AND FISCAL COMMISSION

MAIN ISSUES AROUND ECONOMIC OUTLOOK

- Based on mid-year projections, SA's GDP growth will be 0.6 and 0.8% lower than originally forecast in February 2015 Budget.
- Dampened growth projections driven by internal and external dynamics
  - Externally: Volatile global economic conditions in which modest growth in advanced economies of Europe, North America and Japan has been tempered by economic distress in a number of emerging market and developing economies. The result is that in 2015 and 2016, respectively, global economy is expected to grow at 0.2% point below initial 2015 forecasts.
  - Internally: structural dynamics of South Africa's economy; labour market productivity and relations, and continued concern around SA's capacity to address pressing key infrastructure challenges

FINANCIAL AND FISCAL COMMISSION

RECENT EXTERNAL DEVELOPMENTS IMPACTING ON SA'S GROWTH PROSPECTS

- The anticipated lift-off in U.S. interest rates from zero lower bound
  - Impact on capital flows esp. to merging markets such as South Africa
  - Tightening external financial conditions (borrowing costs); currency depreciation (volatility in value of Rand)
- Growth slowdown in China: anticipated but larger than expected cross-border repercussions
  - China seeking less reliance on import-intensive investment and facing trade-offs as it seeks to strengthen role of market forces in adjusting its assets market
  - Slowdown reflected in weakening commodity prices (especially metals) and Chinese demand for manufactured goods thus limiting any potential gains from currency depreciation.
- Limited space to promote exports in alternative markets
  - Emerging countries (Russia and Brazil) and developing economies (oil/commodity exporting states in Africa and Middle East) are in midst of severe economic downturn

FINANCIAL AND FISCAL COMMISSION

INTERNAL DYNAMICS IMPACTING ON SA'S GROWTH PROSPECTS

- Severe pressure faced by mining industry
  - Significant drop in China's imports (14.6%) affecting SA for which over 80% of exports to China are commodities based
  - Currency deprecation offset by declining prices (platinum, gold, iron ore and coal) and slide in output.
  - Despite business, government and union compact, industrial tensions remain affecting productivity and heightening uncertainty
- Infrastructure bottlenecks remain
  - Need to solve electricity supply constraints still a top priority
  - More coordinated policies to enhance infrastructure delivery and address skills mismatch within labor market.
  - Enhance efficiency of infrastructure spend across the three spheres of government.

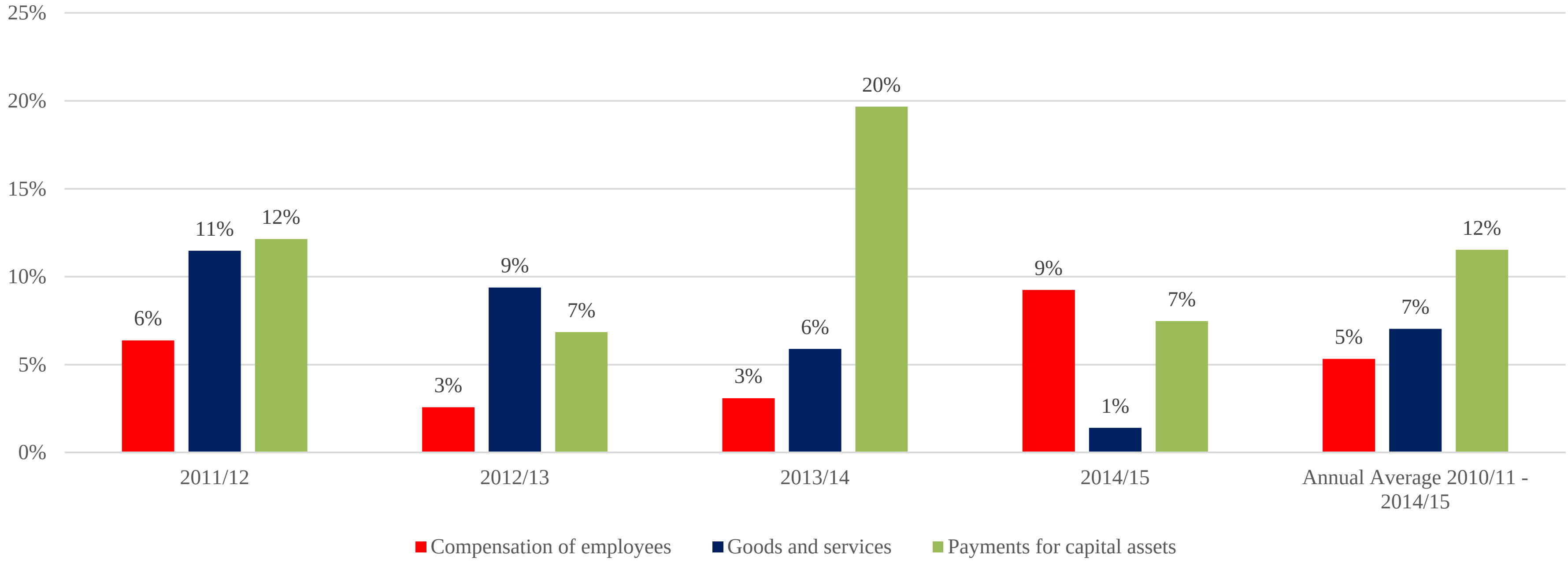
FINANCIAL AND FISCAL COMMISSION

Areas of Risk To Fiscal Framework

- Persistent weakness in the balance sheets of certain state owned companies (SOCs) could trigger calls for additional government support
  - Continuous cash injections to assist ailing SOCs places undue stress on the fiscal framework and redirects funding away from core service delivery areas
  - Also brings into question ability of SOCs to effectively drive infrastructure-led growth
- Intentions to reform health-care and social protection pose significant areas of impact on the national and provincial fiscal frameworks
- Salary negotiations still have to be concluded – poses significant risk. While compensation of employees (CoE) slows over MTEF period, projections only credible if salary increases close to inflation
  - If this does not materialise, underlying assumptions of the fiscal framework may need to be revised

FINANCIAL AND FISCAL COMMISSION

Areas of Risk To Fiscal Frameworks: Wage Bill Challenge



- Between 2010/11- 2014/15 real growth in wage bill amounted to 5% on average per annum
  - While the growth in wage bill was slower than goods and services and capital payments over the period, the size of the wage bill means the growth is significantly larger in absolute terms
  - The Commission welcomes efforts aimed at trying to find a long-term solution to the wage bill issue especially the setting up of the Presidential Public Service Remuneration to examine remuneration and conditions of service of public officials

MEASURES TO IMPROVE THE FISCAL FRAMEWORK

- Emphasis need not only be on reductions of expenditure ceiling
  - Growth in allocations must be aligned close to inflation rate or productivity to mitigate the risk of undermining hard budget constraint
- Expand own financing of capital expenditures and economic development
  - Options include improvements in expenditure efficiencies informed by ongoing expenditure reviews, maximising debt collection, user charges
  - Long-term problem to address is that the system of revenue-raising is highly centralised, especially at the provincial level
  - Decentralising revenue-raising responsibilities can be done in a way that does not threaten the integrity of the tax system by allowing provinces some say in setting their own tax rates on the same tax base used by the national government, using user charges more effectively etc

FINANCIAL AND FISCAL COMMISSION

Measures to Improve the Fiscal Framework [cont.]

- Commission agrees with the thrust of the adopting the user pay principle as part of a menu of options for financing economic infrastructure
- Such funding mechanisms should work in tandem with other elements of the developmental strategies to raise efficiency
- Examples include:
  - User charges which encourage people to reduce congestion or factoring social and environmental "externalities" into prices
  - Putting in place measures to improve acceptability of the user charge principle for higher levels of infrastructure services
  - Differentiation within the user charge principle and/or ensuring costs are aligned with willingness to pay
  - Based on *evidence* about people's willingness to pay, obtained through a transparent and robust examination

FINANCIAL AND FISCAL COMMISSION

MEASURES TO IMPROVE THE FISCAL FRAMEWORK [CONT.]

- Two-pronged financing approach with respect to SOCs, specifically Eskom
- In 2013/14 and 2014/15 Government guarantees in respect of Eskom amounted to R350 billion per annum
  - Provision of guarantees give rise to contingent liabilities for Government
  - The total amount of borrowing (exposure) made against the Eskom guarantees: R125.1 billion in 2013/14 and R144.5 billion in 2014/15
  - Relative to the amount actually borrowed by Eskom, the large state guarantees should be reviewed and adjusted annually as this could create a perverse incentive to borrow more than required
  - Budget Review 2015 notes that expanded infrastructure investments have led to a steady increase in the asset base of SOCs (with Eskom and Transnet accounting for 79% of SOC's net asset value). Government should explore the possibility of a two-pronged financing approach - providing limited guarantees whilst also allowing SOCs/Eskom to leverage financing on the strengthen of their balance sheet
    - Where guarantees are considered they should be based on stringent requirements around improvements to governance and performance

FINANCIAL AND FISCAL COMMISSION

MEASURES TO IMPROVE THE FISCAL FRAMEWORK [CONT.]

- Improving expenditure efficiency and government-wide commitment to long-term planning and efficient resource utilisation
  - Long-term planning remains purview of selected infrastructure grants and an elusive goal across three sphere of government
  - No fiscal parameters to measure extent to which resources are used efficiently
  - In Submission on 2014/5 Division of Revenue, FFC recommended that interface between planning, budgeting and outcomes be improved through the newly adopted outcomes-oriented delivery approach
  - Chief procurement officer should develop spending efficiency indicators against which spending agencies can be measured

FINANCIAL AND FISCAL COMMISSION

Measures to Improve the Fiscal Framework [cont.]

- Efforts to improve the fiscal framework should ultimately be premised on re-igniting growth
  - Current economic growth estimates fall short of required growth rate to fulfil National Development Plan (NDP) expectations and compares unfavourably with other developing economies
  - South Africa should focus its strategy for reigniting growth on improving education expenditure outcomes in particular, increasing skills bases, maintaining strong growth on social safety net spending and increasing productivity of public infrastructure
  - Efforts should be intensified to structurally transform the economy by diversifying exports away from raw mining commodities, deconcentrate the vertical market structure of the economy and move towards a low carbon economy

FINANCIAL AND FISCAL COMMISSION

SUMMARY

- FFC looks forward to supporting the Standing Committee on Appropriations
- Support during National Budget Process through submissions
- Other forms of support:
  - Strategies for coordinated and regular briefings
  - Partnerships with regard to training, research and identification of training, mentorships and visits
  - Ways on systematic oversight over infrastructure expenditure
  - Continue to advise on fiscal policy, fiscal and DoR frameworks.

FINANCIAL AND FISCAL COMMISSION

FFC's Website: www.ffc.co.za