



# SUBMISSION ON THE ADDITIONAL APPROPRIATIONS BILL 2012

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*“For an Equitable Sharing of National Revenue.”*

15 March 2012

Financial and Fiscal Commission  
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## 1. BACKGROUND

- 1.1 This submission is made in terms of Section 4 (4)(2) of the Money Bills Amendment Procedure and Related Matters Act (MBPARMA) of 2010 which requires Parliamentary Committees to consider any recommendations of the Financial and Fiscal Commission (FFC) (hereafter the Commission) during their processing of the Appropriations Bill<sup>1</sup>. It is also made in terms of the FFC Act of 1997 which requires that the Commission respond to any requests for recommendations by any organ of state on any financial and fiscal matters relevant to its mandate.
- 1.2 A special allocation of R5.75-billion is appropriated out of the 2011/12 National Revenue Fund for the requirements of the Department of Transport in respect of the 2011/12 financial year.
  - a. The allocation must be transferred to the South African National Roads Agency Limited (SANRAL) to pay off debt incurred for the completion of the Gauteng Freeway Improvement Project (GFIP).
  - b. The allocation is to be expended within the 2011/12 financial year as payback or settlement of debt incurred in-year, notwithstanding that the transfer may be rolled over for spending after 31 March 2012.
- 1.3 The submission consists of four sections. The second section gives a brief short-term assessment of the Bill. The third section looks at the longer term considerations for electronic tolling. Section 4 is the conclusion.

## 2. SHORT-TERM CONSIDERATIONS OF THE BILL

- 2.1. In his budget speech of 2012, the Minister of Finance explained that decisions around the tolling system were taken very late in the budget process. Accommodating this decision in the budget so late would have meant that payments on roads allocations and for PRASA's (Passenger Rail Agency of South Africa) provision of new rolling stock would have had to be decreased significantly.
- 2.2. The R5.75 billion amount was aimed at containing the SANRAL debt at a manageable level. The Cabinet took a decision around freeway schemes and the tolling in 2011. Subsequently it has come to light that willingness to pay that was

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<sup>1</sup> The Appropriation Bill is a piece of legislation that serves to appropriate money from the National Revenue Fund for the requirements of the national government in order to provide for subordinate matters incidental thereto.

assumed in 2007 when the project was approved was no longer there. This followed intense complaints from all sectors that the tolls would have a negative impact on the users. Government became attentive to these concerns at the last hour and offered this once-off payment<sup>2</sup>. It was also in response to the fact that the user-pay system was key to continue service delivery, as SANRAL would not meet its obligations by May 2012 if it was not supported financially.

2.3. While there may be unending discussions on whether or not this constituted a bailout, the Commission is of the view that this was a case of an agency failing to implement its original payment plan due to the threats of protests by the various stakeholders. The National Roads Regulations Act allowed SANRAL to borrow money, and with the Minister's approval to declare toll roads and raise a tariff. It was explicit that the tariff needed to cover the upgrade and the maintenance of the toll roads. The issue was therefore one of finding a political solution to address a technical matter. This raises three issues:

2.3.1. The first is concern with when inherent political risk associated with government action creates a contingent fiscal liability which then translates into an explicit claim on the fiscus. This illustrates that political intervention can impact the accountability framework for SANRAL and indeed any other agency in future exposing them to serious fiscal risk. The issue here one of time consistency and pre-commitment. As a result of this action, all other Private Public Partnerships (PPPs) or long term concessions attract additional and unnecessary risk premia. Such systemic risk issues are of concern in the light of government's strategy to prioritise social infrastructure on-budget but move economic infrastructure to State Owned Enterprises (SOEs) balance sheets. This moves the discussion into the realm of managing material contingent liabilities.

2.3.2. Second, government's strategy to prioritise social infrastructure on-budget but move economic infrastructure to SOEs balance sheets naturally means that administrative prices become an issue. This is so as the SOEs now try to pay off debts from charges for infrastructure use and this ends up feeding into higher consumer prices and eventually may impact negatively on poverty.

2.3.3. Third, it should also be emphasized that in most PPPs, concessions or other special purpose vehicles, banks as the financier play a critical role. This is one

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<sup>2</sup> Making it clear that this was a once off payment was meant to signal that it would not set a precedent.

avenue in the transmission mechanism for financial crises to spill over into a fiscal one as well.

### 3. LONGER TERM CONSIDERATIONS

- 3.1 Road pricing as a mechanism for infrastructure financing (for the internalization of external costs as well as for congestion reduction) has come into public focus in the last several decades. The motivation for the introduction of road pricing has changed over time. Nowadays, the connection between public budget and infrastructure expenses, the precarious private household situation, as well as the recent global economic crisis has brought road pricing into discussion as additional revenue source. As the SANRAL e-tolling has demonstrated, discussions on road user charges are always very controversial: Proponents argue for higher quality infrastructures, reduced travel times as well as cost-by-cause principle, whereas opponents especially point out social exclusion, overtrading of people and the freedom of mobility.
- 3.2 The economic foundation of road pricing has a long history with early contributors arguing that free access to public roads leads to a misallocation of resources because of external effects where drivers do not have to pay for the additional costs they impose on others<sup>3</sup>. Following the ground-breaking works, numerous publications on road pricing issues emerged in literature. Among the many topics which are treated by researchers and practitioners are the relation between investments in infrastructure and optimal tolling<sup>4</sup>. Only very few publications analyze distributional impacts of road pricing on households. Social research questions on equity and fairness of road pricing initiatives are seldom discussed in scientific publications.
- 3.3 An interesting illustrative study tested cordon schemes in three cities in the United Kingdom, Cambridge, Northhampton and Bedford<sup>5</sup>. The findings are that road pricing can be both regressive and progressive depending on the transport structure of the city, where people live and work, which travel mode they use and to what extent

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<sup>3</sup> See for example Pigou (1920), Knight (1924) and more recently Rouwendal and Verhoef (2006).

<sup>4</sup> The interested reader is referred to Mohring and Harwitz (1962) and Keeler and Small (1977). Surveys of the literature can for example be found in Small (1992).

<sup>5</sup> The study is by Santos and Rojey (2004).

compensation measures are used<sup>6</sup>. Compared to urban road pricing, literature on road pricing schemes for whole networks is very limited<sup>7</sup>.

- 3.4 For South Africa, very few studies exist on the distributional effects of car user road pricing schemes across different income groups. Some of the few studies in the context of fuel taxation conclude that, when a distance-based road pricing scheme in combination with revenue redistribution (i.e. tax reductions) is implemented, households are on average not made worse off than before. Households in lower income groups are less negatively affected because of their lower annual mileages and they will benefit from compensation measures most<sup>8</sup>.
- 3.5 An important objection to road pricing expressed in the recent street protests against e-tolling in South Africa is that it will make poorer households worse off. Government has rightfully addressed this concern through the implementation of exemptions in pricing of certain transportation modes and letting travellers choose between quicker but more expensive trips and remaining on pre-existing free alternatives that may now be less congested. Moreover, even unemployed individuals and off-peak commuters occasionally experience the need to travel during the peak. Road pricing lets these individuals travel quickly when their value of time is high. Furthermore, transponders have been programmed to allow discounted or free travel for the needy.
- 3.6 Systemic distortions of apartheid spatial planning created dormitory suburbs for black South Africans that deliberately segregated where people lived and where they worked, banishing them to the periphery of economic and life opportunity. Such spatial dislocations make blank e-tolling inequitable.
- 3.7 A common view is that – at least in the early stages of road pricing – prices should vary infrequently or not at all. But most of the value pricing projects do involve at least a peak/off-peak time differential. Furthermore, groups appear strongly opposed

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<sup>6</sup> This hypothesis is supported by Eliasson and Mattsson (2006) who analyze equity effects of congestion pricing in the city of Stockholm, using a sample enumeration model.

<sup>7</sup> An exception is Steiniger et al. (2005) who published a report in which they analyze, inter alia, the distributional effects across income groups of five different kilometer-based road pricing scenarios in Austria. The analysis is based on a passenger transport demand model. The macroeconomic impacts and individual effects on different household groups are analyzed with the Austrian Spatial Passenger and Income Transport (ASPIT) model, a computable general equilibrium model (CGE). Steiniger et al. (2005) show that road pricing in general is progressive, since households in higher income groups are more affected by the charges than poorer households. This is because they have a higher car mileage and rarely show themselves willing to use public transportation. Furthermore, Steiniger et al. (2005) states that road pricing based on the cost-by-cause principle is more equitable than a tax-based financing system.

<sup>8</sup> See van Heerden et al. (2007) and Chitiga et al. (2012).

to responsive pricing before it began operation. But elsewhere, responsive pricing is now accepted, and it has achieved a better balance between peak and off-peak periods. Indeed, Sullivan (2002:3) remarks that “There appear to be no differences in consumers’ acceptance or ability to comprehend any of these current systems, regardless of their complexity.” In part, drivers may accept responsive pricing because they value highly reliable travel times<sup>9</sup>.

3.8 Several points indicate that an increase in the cost of road transport would have ambiguous effects in South Africa as follows:

- a. The percentage of total household expenditure on transport rises with income.
- b. Remote areas are dependent on trucking and public transport, and would not suffer disproportionately from a rise in the cost of road transport due to exemption.
- c. Local roads and services are funded primarily by regressive fuel taxes.
- d. Lower-income households have older and more polluting vehicles, and they often have rigid work hours that prevent them from avoiding peak-period tolls.
- e. At this stage and given recent experiences of the GFIP, the prospect of extensive road pricing in the form of tolls appears to have been weakened and compromised in South Africa. Stronger preferences for public funding are one factor. Another is unpopularity displayed by recent mass protests against the proposal. If this assessment proves to be wrong, and tolling does become widespread, the question then arises whether roads would be self-financing.

3.9 Climate change is another important factor because South Africa is in favour of ratifying the Kyoto Protocol. It is an open question whether or not the country will stick to its current position if the other influential countries refuse to ratify the protocol and aid promised to developing countries remains unforthcoming, and if so whether greener policies will be pursued more vigorously. If South Africa does follow through with its Kyoto commitment, there will be a strong impetus to reduce vehicle travel. This will presumably mean a reduction in the base for fuel taxes. But it also means less expenditure in the long run on construction and maintenance of roads. Moreover, global warming could complicate transport in South Africa because it may lead to adverse weather effects, and provide further costs on road maintenance.

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<sup>9</sup> Supernak *et al.*, 2003) and Lam and Small (2001) offer evidence corroborating this view.

Overall, this leaves the net implications of climate change for financing roads ambiguous.

#### 4. CONCLUSION AND RECOMMENDATIONS

- 4.1 The Commission is of the view that while the special appropriation of R5.75-billion for 2011/12 for SANRAL's GFIP was a necessary step taken by government in light of the negative effects expressed by the public in general and the fact that Cabinet had acceded to the proposal earlier, it will be important going forward that more rigorous scrutiny has to be applied before such large infrastructure projects are implemented. The measures should include thorough consultation processes with possibly affected parties. The Commission welcomes government intervention to avoid potentially negative impacts of GFIP on the South African economy. However, the Commission is also of the view that government should strengthen the accountability framework relating to decisions taken by public entities to ensure that negative impacts are minimised.
- 4.2 The SANRAL GPIF e-tolling short experience has allowed identification of "irreversible" national decisions concerning short-term implementation/further development of electronic tolling. In the absence of meaningful changes to present national fuel taxation schemes under consideration at national level, a *business as usual scenario* best describes the context in which the level and structure of road infrastructure charges will continue to be set. With conditions in place to charge motorists as a function of mileage performed on GPIF, Gauteng should be used as the test field for "second-generation" national approaches to make 'road users and polluters pay' in South Africa and for using resulting revenue to expand capacity and standards of transport networks. Then, progressively, other provinces will start introducing electronic tolling in their practice, largely based on domestic considerations, but letting this become established practice. Ensuring political acceptability will really not be in the agenda in this period, except in Gauteng that has introduced tolling in the first generation. Only later, when systems go through their adolescence and start receiving political acceptability, will the pressure for expansion of electronic charging systems be considered. There will be support for this pressure from the Gauteng experience if it yields positive outcomes, with that experience invoking how much helpful they could be to solve all those problems the system set

out to solve. The conclusion is, there will be solutions available to provide full political acceptability, but conditions to achieve it must be ripe both from the demand and from the supply side.

- a. Toll road pricing needs to be linked to the systemic distortions of apartheid spatial planning which created dormitory suburbs for black South Africans that deliberately segregated where people lived and where they worked, banishing them to the periphery of economic and life opportunity. The absence of viable public transport is critical (especially in the light of cities' role), and there should be some form of synchronization in this respect. For commercial freight there should be better rail and port options available.
- b. All contingent fiscal liability through road tolling and infrastructure funding in general that creates an explicit claim on the fiscus needs to be declared well in advance before the project is approved.
- c. The impact on administrative prices, particularly when the decisions are made individually but their impact is cumulative on the consumer should be made clear before the project is approved.

4.3 In the interim, the National Department of Transport should set out guidelines for e-tolling of facilities that have private sector involvement in financing, delivery or management. From the Commission's perspective, at the very least, these guidelines should include:

- Only major projects that result in significant increases in capacity will be subject to tolling.
- Tolls will be implemented only if there are clear, demonstrable net benefits for the users.
- Tolls will be implemented only if a reasonable untolled alternative is available. The public has a right to a basic level of toll-free access.
- The level of tolls and limits on the amount and frequency of increases will be established in advance. This is intended to provide certainty to the public.
- Tolls will be used to generate revenue for transportation projects.
- The Financial and Fiscal Commission should be consulted prior to implementation of the e-tolling projects.

These guidelines are generally consistent with the user-pays principle, and appear to be designed to gain political acceptability.



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15 March 2012

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