Media Release

SUBMISSION FOR THE 2010-11 DIVISION OF REVENUE

18 February 2010

Financial and Fiscal Commission
Montrose Place (2nd Floor), Bekker Street,
Waterfall Park, Vorna Valley, Midrand,
Private Bag X69, Halfway House 1685
www.ffc.co.za
Tel: +27 11 207 2332
Fax: +27 388 3965

For an Equitable Sharing of National Revenue

[**18 February 2010, Cape Town**] On May 28 2009 the Financial and Fiscal Commission tabled its Recommendations for the Division of Revenue for the period 2010/2011 in compliance with Chapter 13 Section 214 (2) and section 9 of the Intergovernmental Fiscal Relations Act of (1997) and related legislation. The focus of the recommendations was on the provincial equitable share formula, provincial infrastructure investment and sectoral issues in the areas of health, social security, the built environment including housing and road transport infrastructure and also access to water and sanitation and local government capacity building. On Wednesday 17th February 2010 the Minister of Finance presented the budget which among other things contains national government's response to the Commission recommendations to the 2010/11 division of revenue. This media briefing by the Commission details its response to the Division of Revenue 2010/11. This is in compliance with Chapter 13 section 214 (2) and section 9 of the Intergovernmental Fiscal Relations Act of (1997) and related legislation.

The Commission's submission touches on three areas, namely a response to the various clauses contained in the Bill, comments on the fiscal framework (including conditional grants), and finally on views to Government's response to its recommendations made on the 2010 Division of Revenue.

The Commission has for some time been of the view that the Division of Revenue Act represents a strategic document capable of linking priorities with outcomes. In its 2009 Submission, the Commission noted that the Division of Revenue Act was becoming increasingly complex, voluminous and too wide-ranging in terms of the issues it covers. The potential danger of the Act becoming a "hold-all" document, and thus losing strategic focus and transparency, was identified. The Commission recommended a review of the Bill with a view to streamlining and reducing its volume. The Commission also notes that the Division of Revenue Act preceded other pieces of legislation relating to the management of public finances such as the Public Finance Management Act of 1999, Municipal Finance Management Act of 2003 and the Intergovernmental Relations Framework Act of 2005. Certain issues that have since been addressed in these pieces of legislation may still be finding their way into the Division of Revenue Act, which could be addressed through the proposed review. For example, an important issue that this review will need to consider is whether the annual Division of Revenue Act is simply meant to address the technical elements of the division of revenue and not with any elements of responsibility or accountability for the use of funds. In this case the current "objects" section needs no review. However, if the legislation is interpreted to include responsibility and accountability for use of the funds transferred there is a need to review and probably expand the objects section of the legislation). The Commission is of the latter view.

The Commission welcomes the fact that the 2010 Bill is significantly streamlined, without having lost strategic coherence. In the current Bill for example, a number of specific clauses that deal with allocations are now appropriately dealt with, within the relevant grant frameworks.

Following consultations with the Ministry of Finance, it has been agreed that the Commission will lead a process for a comprehensive review of the Division of Revenue Bill in preparation for the 2011 division of revenue. It has been further agreed that the work should be completed by June 2010.

The Commission notes the priority areas guiding government's allocation decisions over the 2010 medium term expenditure framework. A concern from the Commission is the apparent lack of intergovernmental structures such as MinMecs and Clusters for coordination of the employment creation and rural development priorities. These two priority areas are very important and cut across the three spheres of government and as such require a very strong intergovernmental structure to coordinate the various strategies from the different sectors and spheres of government.

More broadly, the view of the Commission is that the impact and aftermath of the global recession just witnessed, has added further challenges to attainment of government's priority objectives. As part of its work for the 2011 division of revenue, the Commission is investigating measures that could assist in the cushioning of the impact of similar recessions while at the same time preparing the country for future growth through the division of revenue process.

Another key aspect in ensuring progress in the attainment of these objectives is in the area of actual service delivery. As part of its work, the Commission has developed a budget analysis tool that allows it to assess performance amongst the three spheres of government.

Finally with respect to priorities and division of revenue, improved health care and the fight against HIV and AIDS require that personnel, utilities and infrastructure in the area of health, are able to cope with the demands placed upon them. The anticipated introduction of the National Health Insurance scheme has the potential to be a key input in this. However, it should be noted that the details of the system have not been made available to the Commission. The Commission can only comment once the formal proposal has been forwarded to it by government.

For the 2010 budget, an additional R112 billion has been added to the fiscus to finance the priorities. Of this, R33.3 billion (or
38.3 per cent) goes to national government, R 45.5 billion (or 52.3 per cent) to provinces and R7.8 billion (or 8.9 per cent) to municipalities. The Commission's reaction to this division of revenue amongst the three spheres is that:

- Whilst the local government sphere receives the smallest share of total revenue relative to the other two spheres, it exhibits the fastest growth

- With respect to provinces, conditional grant allocations grow faster than allocations made via the provincial equitable share

- Allocations to national departments are expected to show an annual average growth rate of 4.7%.

The Commission notes that there is an increase in the debt service cost compared to other items of the budget. In this respect it is also important to note the rapid increase in the public sector wage bill. This scenario might imply that significant amounts of the debt service costs increases are driven by personnel expenditure. If this is indeed the case, it would be important that this development is reversed as soon as possible. Large amounts of debt that are driven by current consumption as opposed to the financing of capital assets are known to ultimately compromise future economic growth and destabilise the domestic financial system. The Commission's submission for the 2010 division of revenue emphasised the need to, where possible, restrict long term borrowing to the financing of infrastructure investment in order to secure a better life for future generations.

Turning now to conditional grants, this year sees the introduction of at least 4 new conditional grants to provinces, despite previous recommendations of the Commission's highlighting the need to reduce the number of conditional grants. Two of these new grants are in the education sector. Other new grants are the Expanded Public Works Programme for the Social Sector (a once off allocation of R57 million in 2010/11), the Secondary School Recapitalisation Grant and Dinaledi Schools Grant for the purchasing of mathematics and science teaching material, and the grant (discussed previously) to facilitate the transfer of FET colleges to national government.

The Commission welcomes funding of the EPWP Incentive Grant for the Social Sector. However, there will be a need to standardise the employment framework for the sector including conditions, wages and progression across provinces and municipalities. The Commission is also concerned with the difficulties still being experienced with the transfer of the Expanded Public Works Programme Incentive Grant to Local and Provincial Governments. The general challenge with this grant is that provinces and municipalities still find it difficult to integrate it through their infrastructure programmes. The Commission welcomes the certainty in funding shown by firm allocations for Public Transport Improvement & Systems Grant over the MTEF. However, the Commission is still concerned about the vague allocation criteria for this grant. Of importance is that funding for the transport sector needs to be urgently reviewed. There are pockets of funding for transport in the fiscal framework (Equitable Shares, Infrastructure Grant to Provinces, Municipal Infrastructure Grant, Rural Transport Services and Infrastructure Grant and the PTIS), yet no coherent fiscal strategy for the long term sustainability of public transport services is in place. The Commission is currently reviewing the whole system of conditional grants and will be making recommendations in the submission for the 2011 Division of Revenue.

Key developments with respect to local government conditional grants include the discontinuation of three grants (namely the Backlogs in Water and Sanitation at Schools and Clinics Grant, the Backlogs in the Electrification of Clinics and Schools Grant and the Electricity Demand Side Management Grant: and the introduction of one new grant (the Rural Households Infrastructure Grant). In general, with respect to conditional grant allocations the Commission recommends that as a matter of standard and ongoing practice:

- Independent exit reviews of discontinued grants be conducted in order to evaluate their performance relative to objectives, and provide lessons for the ongoing improvement to other conditional grant programmes

- A design and implementation planning review be conducted for new grants (in this instance the Rural Households Infrastructure
Grant), and

- There be independent mid-term grant performance reviews for all grants in the system.

Finally, the Commission would wish to note government's response to the recommendations contained in the 8 chapters of its 2009 Submission referred to at the beginning. The Commission's reaction to Government's response that is contained in annexure W1 can be summarised as follows:

- The Commission welcomes the fact that Government has accepted almost all of its recommendations.

- Furthermore the Commission is committed to ensuring ongoing improvements with respect to the relevance and quality of its recommendations

- In this spirit, the Commission proposes further consultation with National Treasury (and relevant government departments) following the tabling of the national budget.

The Commission thanks its stakeholders in government and the legislatures for the support provided over the current research cycle.

Dr Bethuel Setai
Chairperson/CE
Financial and Fiscal Commission
February 18 2010

Interested parties can acquire the electronic version of the Submission document on the FFC's website:
www.ffc.co.za
Printed copies can be obtained directly from the FFC's offices. Please contact:
Financial and Fiscal Commission
First Floor
Montrose Place
Waterfall Park
Bekker Street
Midrand
Tel: +27 861 315