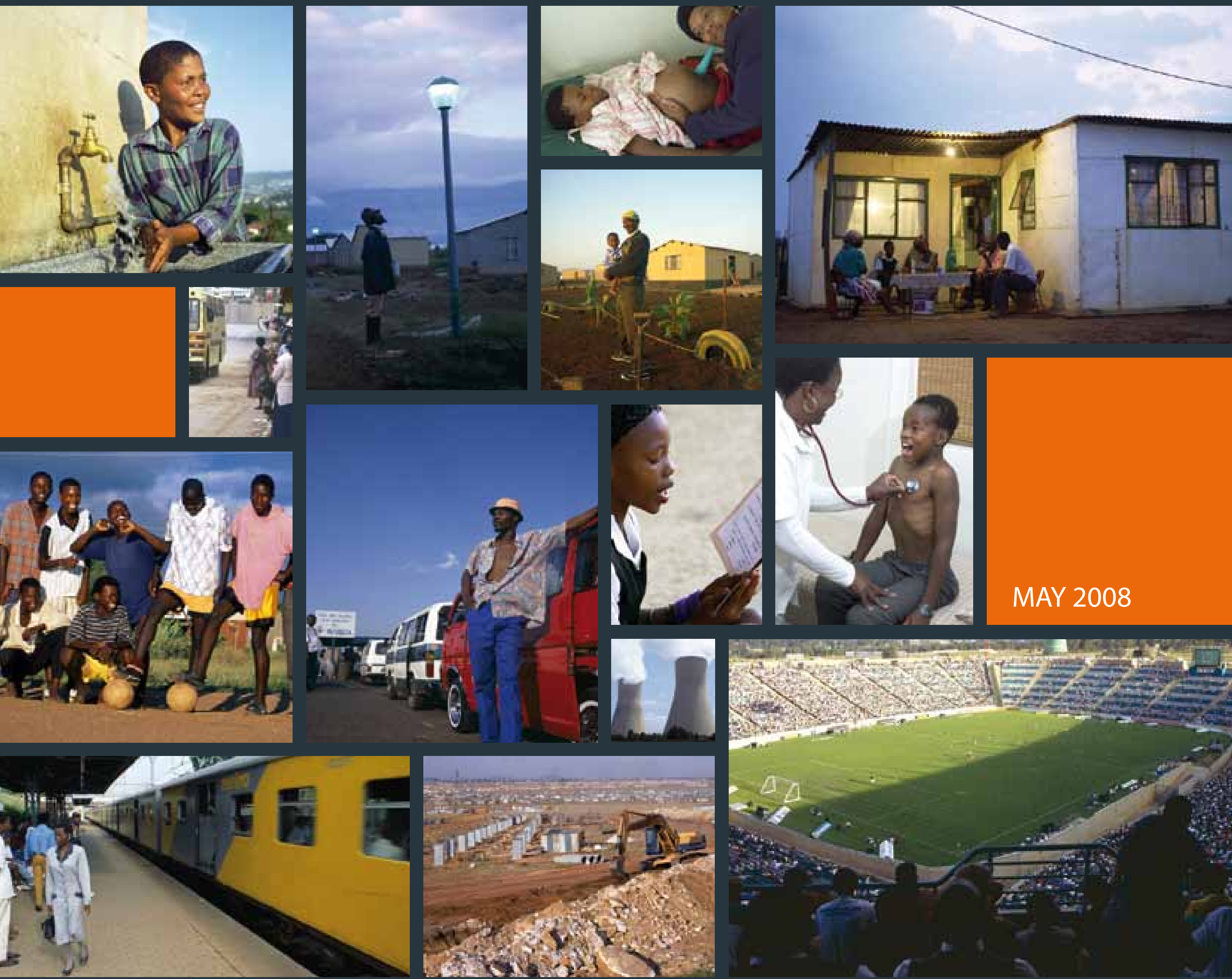
Financial and Fiscal Commission

Submission for the Division of Revenue 2009/10



MAY 2008

FINANCIAL AND FISCAL COMMISSION

For an Equitable Sharing of National Revenue

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ISBN: 978-0-9802666-3-4
RP: 93/2008

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Acronyms

ASGISA	Accelerated and Shared Growth Initiative for South Africa
CD	Cobb-Douglas
CES	Constant Elasticity of Substitution
CGE	Computable General Equilibrium Model
DME	Department of Minerals and Energy
DoRB	Division of Revenue Bill
DOE	Department of Education
DoT	Department of Transport
DPLG	Department of Provincial and Local Government
DPW	Department of Public Works
EPWP	Expanded Public Works Programme
FIFA	Fédération Internationale de Football Association
FFC	Financial and Fiscal Commission
FS	Free State
GDP	Gross Domestic Product
GT	Gauteng
IDP	Integrated Development Plan
IES	Incomes and Expenditure Survey
IHHSD	Integrated Housing and Human Settlement Development Grant
IGP	Infrastructure Grant for Provinces
INEP	Integrated National Electrification Programme
I-O	Input-Output
IPP	Independent Power Producer
kWh	Kilowatt-hours
KZN	KwaZulu-Natal
LES	Local Government Equitable Share
LM	Limpopo
LES	Linear Expenditure System
MIG	Municipal Infrastructure Grant
MimMec	Ministers and Members of Executive Councils
MPU	Mpumalanga
MTEF	Medium Term Expenditure Framework
MTBPS	Medium Term Budget Policy Statement
NC	Northern Cape
NCB	National Coordinating Body
nDoE	National Department of Education

nDoH	National Department of Housing
nDoT	National Department of Transport
nDPW	National Department of Public Works
NERSA	National Energy Regulator of South Africa
NLTA	National Land Transition Act
NLTSF	National Land Transport Strategic Framework
NQ	National Quintile
NW	North West
PBER	Provincial Budgets and Expenditure Review
pDoH	Provincial Department of Housing
pDoT	Provincial Department of Transport
PED	Provincial Education Department
PHC	Primary Health Care
PHP	People's Housing Process
PTIF	Public Transport Infrastructure Grant
RED	Regional Electricity Distributor
RIFSA	Road Infrastructure Strategic Framework for South Africa
RTT	Resource Targeting Table
SAM	Social Accounting Matrix
SANRAL	South African National Road Agency Ltd
SASA	South African Schools Act
SCOF	Select Committee on Finance
StatsSA	Statistics South Africa
TWh	Terrawatt hours
WC	Western Cape

Foreword

This Financial and Fiscal Commission Submission for the Division of Revenue 2009/10 addresses a number of issues arising from the Commission's Submissions of 2005, 2006 and 2007, and raises new concerns regarding local government data collection, electricity supply and pricing. There are also broader matters addressed here that relate to the current reform process in the local government sphere. Local government revenue and the restructuring of the electricity distribution industry are also dealt with in this document.

The issues raised cut across all three spheres of government, although an attempt has been made to divide them according to their commonalities. Thus the submission is divided into three parts: provincial interest issues, local government interest issues and data issues. It must also be noted that there are cross-cutting issues of relevance for all three spheres of government.

The Commission notes that government's response to the submission for the 2008/09 Division of Revenue was very positive, with agreement on over ninety per cent of the recommendations. The response is detailed in Annexure E of the Division of Revenue Act (2008). This Commission also notes that a key issue referred to in the 2008/09 Division of Revenue submission was the review of the provincial equitable share formula. While this work is still in progress and therefore is not part of this submission, the Commission would like to note that it will consult intensively on the review with stakeholders during the course of this year..

This submission is the product of considerable collaborative effort and research. The Commission would like to thank all the departments that contributed through their comments and the provision of information.

In particular the Financial and Fiscal Commission drew on the knowledge and insights of a number of technical advisors, namely Mr Ismael Fofana, Mr David Solomon, Mr Abel Mawela, Ms Marle van Niekerk and Prof Servaas van der Berg. Their contributions are greatly appreciated.

The Commission would also like to thank the staff in the Secretariat of the Financial and Fiscal Commission for their support in the development of the submission.

Finally this submission would not have been completed without the involvement of Commissioners at the various research project review sessions and Research Committee meetings. The Commission also expresses its sincere gratitude to those Commissioners whose term has come to an end. These include the long-serving Deputy Chairperson Mr Jaya Josie, Commissioner Antony Melck, Commissioner Kamalesen Chetty and Commissioner Gugu Moloi.

The Commission also welcomes the new Commissioners, Mr Bongani Khumalo (Deputy Chairperson, National nominee), Mr David Savage (National nominee), Mr Krish Kumar (Local Government nominee), and Mrs Nelisiwe Shezi (Provincial nominee).

As the Commissioners (and Executive) of the Financial and Fiscal Commission, we, the undersigned, are pleased to submit this Annual Submission in accordance with the obligations placed upon us by the Constitution of the Republic of South Africa.

Bethuel Setai

Blake Mosley-Lefatola

Risenga Maluleke

Martin Kuscus

Tania Ajam

Bongani Khumalo

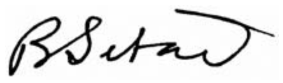
Nelisiwe Shezi

David Savage

Krish Kumar

For and on behalf of the Commission

Chairperson Dr Bethuel P Setai



Deputy Chairperson Bongani Khumalo

Executive Summary

This submission of the Financial and Fiscal Commission for the Division of Revenue 2009/10 is made in terms of Section 214 (2) and Section 229 (5) of the Constitution, and Section 9 of the Intergovernmental Fiscal Relations Act of 1999. These require the Financial and Fiscal Commission to make recommendations on the division of revenue among the three spheres of government, and also recommendations to support government's policy-making on intergovernmental fiscal relations. In doing so, the Financial and Fiscal Commission recognizes that it remains the prerogative of the three spheres of government to determine the fundamental policy objectives and priorities for the nation.

As is customary, the recommendations presented here are a culmination of rigorous consultations with its primary stakeholders. These range from the provincial and national legislatures expressed through the finance committees, to government, primarily via the Budget Council and Budget Forum and local government via the South African Local Government Association. Furthermore the Commission also highlights that it has taken into consideration the formal response to its recommendations for the 2008/09 Division of Revenue as detailed in Annexure E of the Division of Revenue Act (2008).

Some of the issues that are highlighted in this submission require the urgent attention of specific government departments. A good example is the electricity industry that, from both a distribution and a generation perspective, requires speedy decisions given the current crisis in the industry. Then there is the provision of learner transport, impacting on both the right to equitable access to education and the safety of learners. Issues around the finalization of the road classification process receive attention here, as does the accreditation of municipalities with capacity in order to address the issue of access to housing. This submission also raises important concerns about the financial and non-financial data available to the Commission to enable it to carry out its work more effectively and also to enable the general public and other institutions of state, including legislatures, to assess and monitor the efficiency and performance of government programmes funded with taxpayers' money. The Commission has also observed that in certain sectors of government there is a lack of compliance, in terms of reporting requirements, with the provisions of the Division of Revenue Act.

Regarding local government, it is the view of the Commission that there are ever more demands being placed on this sphere, legislative and otherwise. A number of laws affecting local government have been enacted in the last five years. They include the Municipal Finance Management Act, the Municipal Fiscal Powers and Functions Act and the Municipal Property Rates Act. The implementation of all this legislation requires municipalities to dedicate considerable resources, including time. There are indeed reporting requirements with which municipalities should comply, and also much information that municipalities are expected to provide to national departments and other organs of state. All of these requirements however fall on municipalities in an ad hoc manner.

The Commission is therefore making certain recommendations on the need to rationalize requests for data in order to reduce any unnecessary burden on municipalities.

The proposals contained in this submission cover all three spheres of government. The following are the key recommendations of the Commission for the 2009/10 Division of Revenue.

With respect to education

- Government should review the method used to inform the national quintile ranking of schools. Rather than classifying schools according to the ward or neighbourhood in which they are located, the method should take into account the socio-economic circumstances of the learners (with particular reference to inequality and poverty).

- National norms and standards for the provision of learner transport should be established. This will be possible once the location of this function has been clearly demarcated between the national departments of Education and Transport. In this regard, the Commission recommends that the location of the responsibility for the provision of learner transport should be clarified as a matter of urgency.

- In the intervening period, all provinces should implement the statutory provisions that ensure learners are afforded the opportunity of equal access to the right to education irrespective of their province of residence and irrespective of whether they reside in a rural or an urban area. The Commission notes that the problem of learner transport is particularly acute in rural areas.

With respect to health infrastructure and health care

- The requirement of the Division of Revenue Bill for 2008 that indicative allocations to schools and hospitals be gazetted with the tabling of provincial government budgets should be extended to clinics and other primary health care facilities, as and when they fall under provincial control.

- Greater emphasis should be placed on improving the quality of service provided at clinics and funding the maintenance of existing primary health care facilities. There is still a need for the construction of clinics in poorly serviced rural and urban informal settlements, however .

- The health component of the Infrastructure Grant to Provinces (IGP) should be aligned to the roll-out of infrastructure through municipal infrastructure grants.

With respect to road infrastructure

- The process of classifying roads amongst the national, provincial and municipal spheres of government should be accelerated, in line with the classification framework already established.

- Where provincial roads have been earmarked to be incorporated into the national road network, the premiers of the provinces should apply for such roads to be incorporated into the national road network without further delay.

With respect to housing delivery

- The Commission reiterates its previous recommendation that the accreditation of municipalities with adequate capacity should be accelerated in line with the framework provision of the Integrated Housing and Human Settlement Development Grant (IHHSD) contained in the Division of Revenue Bill for 2008 and the Housing Act of 1997.

With respect to local government revenue sources

- In light of the disestablishment of the RSC Levy, which formed a significant source of municipal revenue, the replacement revenue source for municipalities should be a tax that:

  - Enhances the fiscal autonomy and discretion of local governments;
  - Strengthens the accountability of local government regarding the administration and use of the proposed tax base;
  - Yields an adequate and buoyant revenue stream for municipalities in the face of cyclical instability; and
  - Does not negatively impact on the macroeconomic balance.

With respect to electricity

- Government should work with the National Energy Regulator of South Africa to put in place a financing framework that deals effectively with electricity pricing. Such a framework should capture the scarcity of the resource in a pricing environment that reflects costs, efficiency, stability and, eventually, externalities.

- Given that reforms in electricity pricing structure will, in essence, necessitate an increase in electricity prices, such higher electricity prices will adversely impact on poor households with access to electricity as well as raise the cost to government of extending basic access to electricity for poor households. As such, government will need to increase annual funding for the rollout of services under the free basic electricity programme.

- For greater efficiency of resource allocation, technological innovation and increased investment in renewable energy sources, government will need to increase funding resources set aside for such purposes, and incentives that establish and implement a framework that:

  – Encourages new forms of electricity generation technologies to enter the market;
  – Expands opportunities to consumers to access such forms of energy;
  – Allows non-utility developers equal market opportunity to compete with established providers; and
  – Incorporates financial incentives to expand production and distribution capacity, and effect savings through improving end-user efficiency.

With respect to the FIFA World Cup 2010 public transport infrastructure

- Spending on public transport infrastructure for 2010 should be linked to broader city development plans. A more resourced Public Transport Infrastructure and Systems Grant must continue after the 2010 FIFA World Cup. Projects that are funded under this arrangement should be selected based on a full appraisal of economic, environmental and social costs/benefits. Funding mechanisms to cover the maintenance costs of constructed 2010 FIFA World Cup facilities should be developed.

With respect to data needs from the sector departments

Education

- In order to assess the pro-poor impact of school funding norms, the Department of Education should make publicly available and accessible the funding norms for no-fee and fee-paying schools, in line with new provisions of the Division of Revenue Bill 2008 requiring indicative allocations by school.

- Provincial Education Departments should be enabled to report on budgets and spending on learner transport, in line with the new economic reporting format (see 2008 MTEF Treasury Guidelines, 22 June 2007, page 24).

Health

- In line with international and national practice, and referring to the 2003 National Health Act in Section 2(c)(iv) which makes specific mention of "…protecting, respecting, promoting and fulfilling…" the rights of "…vulnerable groups such as women, children, older persons and persons with disabilities", health data for vulnerable groups such as the proportion of women with access to antenatal care, the availability, affordability and accessibility of health facilities for tuberculosis, HIV/AIDS, children, older persons and persons with disabilities, should be collected and improved using the South African Statistical Quality Assurance Framework .

Extended public works programme

- In accordance with the requirements of the Extended Public Works Programme , job creation for target groups such as women, youth and people with disabilities, should be included in the reporting requirements for all infrastructure conditional grants to provinces and municipalities.

Housing

- All provincial departments receiving the Integrated Housing and Human Settlement Development Grant should comply with the measurable outputs-related reporting requirements detailed in the Housing Conditional Grant framework and published in the Division of Revenue Act annually.

- To enable measurement of housing delivery, the following should be specified:

  - The number of houses completed should be reported separately from those under construction;
  - The proportion and number of these houses completed that are occupied;
  - The proportion and number of these properties that have been transferred to their occupiers;
  - The value of these houses; and
  - Norms regarding average construction time.

- All provincial departments assigned the housing function should provide financial and non-financial output and impact data to a sub-programme level, such that data can be analyzed for every component of the housing subsidy programme (e.g. project-based, People's Housing Process, social housing, rural housing etc.).

With respect to local government data collection

- National and provincial government departments, agencies and other organs of state should eliminate duplicate data requests submitted to municipalities.

- Uniform definitions should be established between national and provincial organs of state and municipalities, with careful consideration given to the purpose of collecting and producing statistics. The interpretation should reflect the purpose and mandate of the department collecting the data and be concurrent with the legislation which guides those organs of state.

- A national coordinating body should be established to coordinate and rationalize the data collection activities of local governments. The national coordinating body should recommend and implement data collection standards according to the South African Statistical Quality Assessment Framework.

Part A

National-Provincial Fiscal Relations

Chapters 1-4

1

Chapter 1:

The Financing of Basic Education

Introduction

In 2004/05 the Financial and Fiscal Commission (FFC) embarked on a project to investigate and make recommendations on the financing of basic education. The work was triggered in part by the release of a report by the national Department of Education (nDoE) on the costs of resourcing schools with specific focus on non-personnel non-capital costs . A key result of the nDoE study was the revision of the 1998 school funding norms and standards. This report is part of the continuing work in this area, and follows on the first part which addressed the financing of learner support material as published in the FFC Annual Submission 2008/09. This report has two sections, namely the re-ranking of schools using national rather than provincial quintiles, and the provision of learner transport.

1.1 Re-ranking of Schools local

1.1.1 Background

A key difference between the 1998 school funding norms and the 2007 amended school funding norms is that national quintiles (NQ) replace provincial quintiles. The outcome of the amended norms is that schools are ranked into five quintiles (NQ1 to NQ5) with NQ1 being the poorest and NQ5 the least poor. It is envisaged that the use of national quintiles will bring about equal levels of funding among poorer schools in the country. This is so, because the School Funding Norms (1998) required Provincial Education Departments (PEDs) to rank the schools according to the resource targeting table (RTT) and to target 60% of financial resources to the poorest 40% of the learners. The list contained all schools in each province ranked on the basis of the physical or poverty conditions of the schools and the relative poverty of the communities around the schools.

This submission evaluates the distributional implications of applying the new national quintile ranking as opposed to the old provincial ranking system. Comparative assessment was done in order to determine the redistribution of both schools and learners between the five quintiles for the two ranking systems. The analysis is based on data from nine provinces which provided complete resource targeting datasets.

Further the report addresses the following questions:

- The financial implications (if any) of the shift from provincial to national ranking;
- Whether or not the national ranking reduces provincial disparities in terms of equitable access to schooling by learners from poor communities;
- Whether or not all provinces are conforming to the use of national ranking and its implementation.

1.1.2 Key Findings

In poorer provinces, many schools and learners that had previously been assigned to provincial quintiles 2 and 3 have been reassigned to national quintiles 1 and 2 and should, by implication, receive greater funding allocations than previously. By contrast in richer provinces, many schools that were previously located in provincial quintiles 1 and 2 have been reassigned to national quintile 3 and are therefore re-ranked as fee-paying schools with reduced funding allocations from government. In principle where schools are moved to lower quintiles, this implies less resource dedication even though, in practical terms, schools should not be disadvantaged as a result of reclassification. An increase in the share of the poorest quintiles in schools and learners thus indicates that the re-ranking would indeed have an impact on the school funding system.

The ranking of schools using the new approach requires that schools in a ward are allocated the same poverty score irrespective of the community they serve. The use of wards in allocating poverty scores to schools does not solve or reflect the poverty distribution of the school and the actual reflection or needs of the school. The index that is currently used to rank schools into the different quintiles should be reviewed as it has resulted in unintended consequences where certain schools have been re-classified into different quintiles by virtue of the wards under which they fall irrespective of the profile of the community that they serve.

Another observation is that a nationally driven re-ranking process does not necessarily translate into the same outcome as when the ranking was province-specific. For example, a poor person in a rural province may not be of the same income level as a poor person in a relatively urbanized province. However the new approach treats them as the same. The redistribution has resulted in the re–assignment of quintile classifications for schools in each province and the degree of the impact differs per province. For example, for the majority of provinces there has been a significant increase in the percentage shares of schools in quintile 1 and 2, especially in the rural provinces. Further, for the majority of provinces there has been a significant decrease in the percentage shares of quintile 5 schools.

1.1.3 Conclusion

The application of the national re-ranking in provinces has resulted in a redistribution of learners and schools among the five quintiles which will have implications for funding allocations for schools as the school allocation is largely driven by the quintile position of the school and the number of learners enrolled. The ranking applies a uniform classification of schools and learners across all the provinces and ignores the fact that in practice provinces are not homogenous.

1.1.4 Recommendations

- Government should review the method used to inform the national quintile ranking of schools. Rather than classifying schools according to the ward or neighbourhood in which they are located, the method should take into account the socio-economic circumstances of the learners (with particular reference to inequality and poverty).

1.2 Learner Transport

1.2.1 Background

During the third quarter conditional grants public hearing in the National Council of Provinces in May 2007, the Select Committee on Finance (SCoF) requested the FFC to investigate some of the challenges associated with the provision of learner transport, especially in rural areas. The request stemmed from the growing concerns over the institutional fragmentation associated with the provision of learner transport. For instance, in provinces where there is provision, it is either rendered by the provincial DoE (for example Eastern Cape and Western Cape) or in other provinces it is conducted by the provincial Department of Transport (for example Mpumalanga, and North West). In KwaZulu Natal (KZN), it was established that the provincial DoE does not have a policy on learner transport, while the strategic framework of the provincial Department of Transport (pDoT) does not make reference to learner transport.

[1] Review of the Financing, Resourcing and Costs of Education in Public Schools (2003)

Where learner transport is being provided, there have been positive outcomes in terms of timeliness and regularity of learner attendance. However, the lack of coordination between departments (Education and Transport) and the lack of transport provision has resulted in the service being rendered on an ad hoc basis. This has, in a number of cases, resulted in learners having to walk long distances to get to school. In responding to the request of the Committee this report assesses the status quo through a review of the legislative framework and an investigation into the current practices in provinces.

1.2.2 Key Findings

Chapter 2 of the Constitution (1996) recognises access to basic education as a basic right of all South Africans. It requires that the state, through reasonable measures, should make this right progressively available and accessible. Schedules 4 and 5 of the Constitution consider public transport to be a concurrent function between the national and provincial governments.

The South African Schools Act (SASA) requires that education Members of the Executive Councils in each province should ensure availability and accessibility of schools to learners. Section 21(d) of this Act details the allocated functions of school governing bodies and among them is the responsibility to 'pay for services to the school'. This can be interpreted as including learner transport. Section 34 states that it is the responsibility of the State 'to fund public schools from public revenue in order to ensure the proper exercise of the rights of learners to education and redress of past inequities in education provision'. This could also be read to imply that the State has an obligation to provide learner transport in order that the right to education is realised.

The School Funding Norms of 1998 require the building of hostels if the travelling time to the school exceeds one and a half hours (1.5). Further the Amended School Funding Norms 2006 indicate the school allocation amount that may be used for non-personnel non-capital expenditure including 'public or scholar transport'. This is consistent with South African Schools Act 1996 assigned functions as set out in Section 21 (d).

One of the important goals in the White Paper on National Transport Policy which is of relevance to learner transport is that of meeting customer needs. These include 'the users of passenger transport services, for commuting, educational, business, tourism and private purposes, in the urban, rural, regional and international environment by all modes'.

Furthermore, Section 44 of the National Land Transition Act (NLTA) 2000 considers the conveyance of learners, students, teachers or lecturers to and from school on a daily basis as a public transport service. In addition, Section 21 of the NLTA 2000 makes it the duty of the Minister of Transport in consultation with MECs to prepare a National Land Transport Strategic Framework (NLTSF) for the country for a five-year period. The NLTSF for 2002 to 2005 requires the nDoT to coordinate the issuing of clear guidelines to assist the relevant authorities to regulate the transportation of learners, and for sedan taxis, private hires and tourist transport. The NLTA Act also requires provinces to have a five year land transport framework and that the needs of learners be incorporated in the Provincial Land Transport Framework.

The Rural Transport Strategy for South Africa developed by the nDoT in 2003 also refers to learner transport by requiring that the delivery of rural transport infrastructure and services should include special needs transportation services in order to address the needs of learners, people with disabilities, the elderly and tourists.

In general there is no single specific national policy dealing with the provision of learner transport services. While there are references to this in a number of pieces of legislation, these cut across the departments of education and of transport. Thus there is no clear definition and division of responsibilities between the departments of education or transport at both national and provincial level.

Instead the policies and practices applied by the provinces differ depending on the respective departments providing the service. A lack of national service delivery norms and standards resulted in provinces adopting their own strategies which are sometimes difficult to understand and implement. In most provinces the formalization and legislation or regulation around the provision of the service has been a challenge, and in some instances financial support has not been forthcoming for the provision of learner transport services.

The criteria used to determine eligible learners for transport provision is mostly done through (a) determination by household income level; (b) distances travelled greater than 5km and in some cases 3km; or (c) learner identification is undertaken by principals and district officials. The modes of transport used also differs (buses, taxis) and in some instances especially in rural areas, bakkies and donkey carts are used.

The nDoT is developing a draft policy on learner transport. This has been necessitated by the fragmentation of policies operating currently in different provinces. The nDoE conducted a status quo report in 2006 because learners were having difficulty in accessing schools.

International practices and polices differ. In developed countries, learner transport is often the responsibility of local authorities. In several developing countries, free school transport has been provided in order to promote greater access to education.

1.2.3 Conclusion

The results so far indicate that as much as access to basic education is a constitutional right, it is still far from being fully realised in practice. Indications are that for many learners, especially in rural areas, access to school is still hampered by long travelling distances and a lack of basic infrastructure such as safe roads and pedestrian bridges.

Broad policies in support of learner transport are in place, but they have not been fully implemented or adhered to because a specific national learner transport policy has been lacking. The legislative framework for the provision of transport exists in different formats for different departments. The location of the function is not very clear, as both the Departments of Education and of Transport claim some responsibility in law. There is therefore a need to improve the integration and coordination of the processes between the two departments at both national and provincial level.

1.2.4 Recommendations

- National norms and standards for the provision of learner transport should be established. This will be possible once the location of this function has been clearly demarcated between the national departments of Education and of Transport. This responsibility should be clarified as a matter of urgency.

- In the interim, all provinces should implement the statutory provisions that ensure learners are afforded the opportunity of equal access to the right to education, irrespective of their province of residence and irrespective of whether they reside in a rural or urban area. The Commission notes that the problem of learner transport is particularly acute in rural areas.

2

Chapter 2:

The Financing of Health Care

Introduction

In preparing the health report for the Financial and Fiscal Commission's (FFC) 2009/10 submission, emphasis was placed on primary health care and its delivery facilities, primarily the clinics. The report is in two parts. The first part deals with the performance of community health clinics and was assessed through a detailed analysis of budgets. The second part of the report deals with the role of infrastructure and its effect on health outcomes. This is the second output from the broader work that the FFC has been conducting on the impact of infrastructure on outcomes in the social sector. In the 2008 Division of Revenue (DoR) Submission the Commission reported and made recommendations on the impact of infrastructure on education outcomes.

2.1 Fiscal Performance of Community Health Clinics Sub- Programme

2.1.1 Background

The methodology adopted in the report for the budget analysis component is based on seven years of data (2003 to 2009) which was sourced from National Treasury's Provincial Budgets and Expenditure Review (PBER) of 2007. This entailed an analysis of the budget, spending and policy performance of the Community Health Clinics sub-programme, a sub-programme within the District Health Services Programme.

2.1.2 Key Findings

Primary health care (PHC) refers to a set of basic services that are commonly thought of as a minimum consumable input to achieve the eradication of widely spread ailments. The District Health Services is the largest programme within provincial health budgets and is the cornerstone of South Africa's PHC approach and the transformatory drive to ensure that the delivery of health-care is all inclusive and more equitable. The logic behind the adoption of the PHC approach was the need to transform the health-care sector from a curative approach that serviced a minority of the population to a preventative one that is all inclusive. The shift to this approach prompted the introduction of free PHC services and a large clinic building programme[2].

[2] National Treasury, 2001:41

Within provincial health budgets, the Community Health Clinics sub-programme (which falls under the District Health Services programme) is responsible for public clinics. The table below provides a break-down of the province-level performance of this item. Looking at projected per annum growth over the MTEF period, it is apparent that strong growth within one province is driving growth within this sub-programme. Very marginal growth and below average growth projected in certain provinces (particularly the Eastern Cape and North West provinces) are of concern if one considers the poverty profile and the large proportion of people without medical aid in these provinces.

Using the 2007 PBER it is possible to determine spending performance (under/over-spending) during 2006. With the exceptions of the Free State and KZN, under-spending is recorded across the majority of provinces. Most of the cases of under-spending exceed the 5% cautionary range as set by the Auditor-General.

Table 2.1: Performance of the Community Health Clinics Sub-programme by Province

Community Health Clinics	Real 3 yr Growth Rate - Spending FY 2003 to FY 2006	Adjusted Appropr. 2006/07	Under/ Over-spending 2006	Medium Term Estimates			Real 3 yr Growth Rate - Budget 2006 MTEF
				2007/08	2008/09	2009/10	
EC	4.87%	784,405	6.17%	798,259	836,896	824,166	1.66%
FS	9.17%	182,349	(5.10%)	195,682	219,511	220,334	6.51%
GAU	13.11%	629,019	13.17%	749,114	722,735	726,994	4.94%
KZN	1.51%	986,604	(4.13%)	1,274,711	1,303,377	1,331,735	10.52%
LIM	-0.53%	689,788	20.16%	959,749	1,285,905	1,605,516	32.53%
MPU	6.80%	269,224	9.46%	320,949	367,716	383,395	12.51%
NC	9.86%	103,151	14.77%	126,148	133,481	139,702	10.64%
NW	10.95%	309,719	3.37%	315,881	319,632	321,641	1.27%
WC	6.59%	379,028	1.61%	380,878	494,018	495,889	9.37%
AVG	5.05%	4,333,287	6.41%	5,121,372	5,683,272	6,049,373	11.76%

Source: National Treasury, 2007, Own calculations.

Further province-specific information (such as the performance of particular clinics, whether growth is being driven by increased allocations to rural or urban clinics and whether excessive or marginal growth is as a result of over or under-spending) is, at present, not available in the PBER or the Division of Revenue Bill (DoRB). As a result one is only able to get a sense of aggregate province-level performance.

The 2008 DoRB requires that indicative allocations to individual hospitals be published with the tabling of provincial government budgets. The rationale is that this will improve the managerial efficiency of the health care systems through greater decentralization and transparency. This approach transfers greater responsibility to the head of the particular institution (i.e. the school or hospital). It ensures greater transparency as clients (patients) are aware of resource allocations to particular facilities and are, based on performance, able to hold decision-makers accountable. This approach is equally important in respect of PHC institutions and as such should be extended accordingly. However, there may be difficulties to do this across the board as there is still a process underway to fully shift the function of PHC to provinces. This shifting of the function will constitute further work from the Commission's perspective.

2.1.3 Conclusion

Clinics are an integral component of the health sector's package of pro-poor interventions. Current financial information only allows for aggregate, province-level analysis of the performance of clinics, thus limiting the extent to which institutional performance can be measured. Evidence shows that, by adopting the cost-centre approach, accountability and transparency is improved, thereby facilitating greater managerial efficiency.

2.1.4 Recommendations

- Just as the DoRB 2008 requires that indicative allocations to schools and hospitals be gazetted with the tabling of provincial government budgets, this practice should be extended to clinics and other PHC facilities, as and when they fall under provincial control.

2.2 Infrastructure for Primary Health Care and Health Outcomes

2.2.1 Background

As already indicated, this part of the report deals with primary health infrastructure, specifically trying to ascertain its impact on health outcomes. This is undertaken against the background that PHC is universally acknowledged to be a far more cost effective and appropriate way of improving health care for the poor than secondary and tertiary health services.

However, the focus here is on PHC infrastructure. An important issue is the extent to which infrastructure interacts with other facets of PHC. In particular, primary health infrastructure, clinics in particular, can only potentially be effective if they are well equipped, staffed, managed and maintained. The question of infrastructure is thus here largely focused on access to public primary health services. It should not be forgotten that many primary health services are also provided by the private sector, in particular by general practitioners, whose services often substitute for public clinics. There is evidence that the demand for health services in South Africa, even amongst the poor, reflect a strong bias towards private health care because of quality concerns with public health services. Providing more clinics if they are not currently being used will accomplish little in the absence of a greater focus on quality of health service provision in clinics and improved perceptions of public service delivery quality.

Two different methods were used to determine the likely impact of primary health infrastructure on health outcomes. The first was an assessment of the international literature drawing mostly from the much publicised Grossman's health production model. This literature is substantial, but its focus is less often on health infrastructure per se but rather more on the whole package of primary health care. Furthermore, the literature focuses on developing countries since access to primary health care is primarily a developing country deficit, whilst such care is already well established in developed countries.

The second method used in the study was the empirical estimation, using statistical and other regression models, of the impact of distance from public health facilities on predetermined outcomes.

2.2.2 Key Findings

The findings from the literature are fairly convincing. There is substantial evidence that health outcomes throughout the world are only moderately responsive to public health spending. The reason for this lies in the fact that there are so many other determinants of health outcomes (nutrition, clean water, sanitation, housing, hygiene, education, personal incomes and lifestyles, access, energy) so that public health spending can only play a subsidiary role. Moreover, inefficiencies in health care services often further weaken the impact of such spending.

In the poorer countries, there is some evidence that expanding access by the provision of more public clinics improves the likelihood of treatment; however there is little evidence that having more public clinics necessarily improves health outcomes. In such countries, though, it appears that investing more in the quality of health care brings higher returns in terms of health outcomes. In more developed countries, where the public clinic network is already more advanced, there is not even evidence that providing more clinics improves treatment.

The application of the empirical methodology referred to above to a very recent South African dataset (the General Household Survey of 2006) shows no evidence that distance from public clinics acts as a major constraint on treatment for ailments. Even in the Eastern Cape, where the public clinic network is least developed, distance does not determine treatment-seeking; getting-treatment patterns hardly differ between those close to and those far removed from clinics, even though the latter are often poorer and less likely to have medical aid. If treatment does not differ, this dataset indicates that distance is not a major factor in the quality of care received and thus on health outcomes.

Admittedly, this dataset used for the statistical and regression exercises is relatively poor in variables measuring health outcomes; the richer dataset provided by the Demographic and Health Survey of 2003 was still not available when this study was undertaken and future work would utilize it. However, earlier studies in South Africa confirm that the demand for health services (treatment) since the expansion of the clinic network after the transition to democracy has been much less influenced by distance, whilst the only study using data from an earlier period (1993) showed that distance did play a role in treatment during that earlier time. The change in the effect of distance may be related to the expansion of the clinic network as one of the major health initiatives of the new dispensation. Moreover, the findings are in line with the international evidence that distance does not seem to play a role in health outcomes once the public clinic network is largely in place.

2.2.3 Conclusion

The results of the study indicate that health outcomes are no longer influenced by the availability of public clinics in South Africa. Far more important is the quality of health services provided, which depends on the complementary infrastructure (such as electricity, roads, sanitation), quality of clinical care, maintenance, staffing and equipment of clinics, how well staff do their jobs and how well they in turn are managed. Capacity constraints and other shortcomings in some provinces lead to situations where the quality of clinics is very poorly rated by clients. In other cases it is simply poor management that leads to lack of cleanliness and long waiting times. An improvement in these areas is currently more important than a further expansion of the clinic network. However, evidence from the literature does confirm that where the clinic network is under-developed, outcomes are improved with its expansion.

2.2.4 Recommendations

- Greater emphasis should be placed on improving the quality of service provided at clinics and funding the maintenance of existing primary health care facilities. A need for the construction of clinics in poorly serviced rural and urban informal settlements still remains however.

- The health component of the Infrastructure Grant to Provinces (IGP) should be aligned to the roll-out of infrastructure through municipal infrastructure grants.

3

Chapter 3:

Transport

Introduction

The Financial and Fiscal Commission (FFC) noted in its 2005 Annual Submission for the 2006/07 Division of Revenue (DoR) that the delivery and funding of roads and transport infrastructure occurred in a very fragmented manner. This has expressed itself through the lack of clarity among the spheres of government and other organs of state about their responsibilities for roads and transport infrastructure. The FFC therefore recommended, among other things, that government should ensure as matter of urgency, the development of criteria and processes for classifying all roads and assigning each class of road to the respective sphere of government or category of local government. This recommendation was accepted by Government.

This submission of the FFC focuses on:

- The progress made in the process of the classification of roads;
- The extent to which provincial roads identified and earmarked to be incorporated into the national road network have, in fact, been incorporated and the problems encountered by South African National Road Agency Ltd (SANRAL) in the process; and
- The analysis of budgets, expenditure and performance on the maintenance of roads.

3.1 Road Classification Framework

3.1.3 Key Findings

A road classification framework hierarchically categorises different types of roads in terms of their network design and management. A classification system therefore assigns roads and streets into different groups according to the type of service each group is intended to provide and, by so doing, improve transport planning, road infrastructure design, maintenance and traffic and road operations[3]. According to the Road Infrastructure Strategic Framework for South Africa (RIFSA) of 2006, 221 000 km of roads (approximately 29% of South Africa's road network) remains unclassified. Most of them are community access roads which historically have been neglected.

[3] See road classification system – a consolidated report available online www.toronto.ca/transportation/roads_class.htm {Accessed 04 February 2008}

In South Africa, the Department of Transport has proposed a functional road classification with six classes as indicated in Table 3.1.

Table 3.1: Classification of Roads in South Africa

Class	Strategic Function	Nature of roads
1. Primary distributor	High mobility roads with limited access for rapid movement of large volumes of people, raw materials, manufactured goods, and agricultural produce of national importance.	Public road: • Between, through and within regions of national importance; within provincial capitals and key cities; major city nodes, which have significant economic or social traffic; • Between SA and adjoining countries which have significant national economic or social transport interaction. • Providing access to major freight and passenger terminals including major ports and airports.
2. Regional distributor	Relatively high mobility roads with lower levels of access for the movement of large volumes of people, raw materials, manufactured goods, and agricultural produce of regional importance in rural and urban areas.	Public roads: • Between, through and within centres of provincial importance provincial capitals, large towns and municipal administration centres. • Between class 1 roads and key centres which have a significant economic, social, tourism or recreational role. • Between SA and adjoining countries which carry limited economic or social road traffic. • Providing access to economic and transport hubs of regional importance.

Class	Strategic Function	Nature of roads
3. District distributor	Moderate mobility with controlled higher levels of access for the movement of people, raw materials, manufactured goods, agricultural produce in rural and urban areas of regional importance.	Public road: • Through and within centres and towns and linking with rural residential areas and villages, industrial/farming areas. • Between residential areas and local industrial/commercial areas, large residential areas. • That provides linkages between Class 2 and or Class 1 routes. • That provides linkages between centres, towns, rural residential, industrial/farming areas, and Class 2 or Class 1 routes.
4. District Collector	High levels of access and low levels of mobility for lower traffic volumes of people, raw materials, manufactured goods, agricultural produce in rural and urban areas of regional importance.	Public roads: • Between, through and within villages, farming areas and scattered rural settlements, which provide access to social services and markets. • Within commercial, residential and industrial areas. • Linking Class 3 roads. • With limited direct access to property in urban context.
5. Access roads	High access and very low mobility routes for the movement of people and goods within urban and rural areas.	Public roads: • Within residential areas. • Between Class 3 and 4 type roads and residential areas. • That provides direct access to industries and businesses. • That provides access to specific destinations such as heritage sites, national parks, mines, forests, etc. • That accommodates safe mobility of pedestrians and other non-motorised transport systems.
6. Non-motorized access ways motorized access ways	Public rights of way for non-motorized transport providing basic and dedicated movement.	Public right of way: • That provides safe dedicated access and mobility for pedestrians, cyclists and animal drawn transport. • That provides dedicated access to social, recreational and economic areas.

Source: Road Infrastructure Strategic Framework for South Africa (2006)

Consultations with the DoT indicate that the process of classification and re-classification is underway in line with the FFC's proposals of 2006/07. Guidelines for classifying and re-classifying roads are currently being developed. These guidelines will ensure that common criteria are followed in the process of classification/reclassification and enable uniformity in classification across the country. According to the DoT, the process of developing guidelines is expected to be completed by the end of March 2008, while the process of road c lassification/reclassification and assignment to the relevant sphere of government is expected to be completed in the 2008/09 financial year.

3.2 Shifting of Provincial Roads to SANRAL

3.2.1 Key Findings

Over the past few years, SANRAL has taken over a number of provincial roads that have been earmarked for incorporation into the national road network. This increases the responsibilities of SANRAL in respect of the management, planning, operation and maintenance of national roads. The expansion of the national road network is shown in Table 1.3.6 below.

3

Table 3.2: Length of Road (in km) incorporated or to be incorporated into the National Road Network

Province	Total length proclaimed	Total length incl. planned	2001/02	2003/04	2004/05	2005/06	2006/07
Western Cape	551	1 062		150		401	
Eastern Cape	740	740		740			
Free State	760	1 228		760			
Gauteng	175.5	314		130			45.5
KwaZulu-Natal	273	961		273			
Limpopo	1430	1 430			1 430		
Mpumalanga	1 669	1 727	172		130	788	579
Northern Cape	2 617	2 617				2 617	
North West	1 032	1 267				1 032	
Total	9 247.5	11 346	172	2 053	1 560	4 838	624.5

Source: SANRAL's 2007 Annual Report

Based on Table 3.2 above and the report it can be seen that the target that SANRAL has for 2010 is 11 346 kilometres. As at the end of 2006/07 financial year, 9 247.5 kilometres had already been incorporated. In some of the provinces (for example Limpopo and the Northern Cape) all earmarked roads have been incorporated into the national road network, whereas in other provinces this is not the case.

According to SANRAL, the delay in the transfer of roads earmarked for incorporation into the national network is due to failure by some provinces to forward the relevant applications.

With respect to budgets and spending on provincial road infrastructure maintenance, Table 3.3 below shows the real budget and expenditure performance for 2003/04-2009/10.

Table 3.3: Real Budget and Expenditure, (R'000) Performance in Maintenance, 2003/04 – 2009/10

Province	2003/04	2004/05	2006/06	2006/07	3 YR Annual Growth Rate	2006/07	2007/08	2008/09	2009/10	3 YR Real Annual Growth Rate
	Outcome			Preliminary Outcome		Adjusted appropriation	Medium-term estimates			
EC	441,880	448,834	502,335	627,311	12.39%	617,805	627,708	666,618	660,756	2.27%
FS	190,343	219,147	200,713	347,008	22.16%	249,576	265,414	326,592	329,633	9.72%
GP	160,466	296,208	379,808	169,838	1.91%	298,573	394,544	551,317	547,443	22.39%
KZN	804,275	607,197	686,530	824,337	0.82%	807,986	944,492	1,106,436	1,272,049	16.33%
LIM	336,767	333,236	336,434	327,840	-0.89%	319,363	364,037	354,619	333,263	1.43%
MPU	219,115	211,131	205,979	245,711	3.89%	243,519	422,607	418,690	417,458	19.68%
NC	64,752	95,192	83,388	82,676	8.49%	83,819	105,374	130,658	140,471	18.78%
NW	217,546	231,643	265,137	267,309	7.11%	314,778	196,065	372,346	456,896	13.22%
WC	338,967	448,384	601,264	658,182	24.76%	664,883	555,600	506,651	498,784	-9.14%
Total	2,774,110	2,890,972	3,261,589	3,550,215	8.57%	3,600,302	3,875,841	4,433,927	4,656,753	8.96%

Source: Derived from PBER 2003/04 to 2009/10, Annexure A

Table 3.3 indicates that, in aggregate, real annual growth rates for expenditure and indicative budget allocations in maintenance are 8.57% and 8.96% respectively. The Free State and Western Cape provinces contributed to this healthy growth in spending, with real expenditure rising from R190 million to R347 million for Free State and from R338 million to R658 million in the Western Cape.

Future allocations indicate that maintenance would be prioritized at a real growth of 8.96% over the 2007 period of the Medium-Term Expenditure Framework (MTEF). This is evident in Gauteng, KwaZulu Natal, Mpumalanga, Northern Cape and North West provinces, with the exception of the Western Cape where a declining growth rate is anticipated. The manner in which certain provinces spend and project for future maintenance budgets requires attention. For example in the Western Cape, expenditure stood at R658 million in 2006/07 and yet real budget allocations are estimated to decline to R499 million in 2009/10. In this instance there is a budget cut. On a different note, Gauteng budgets are greatly expanded from R170 million, in 2006/07 to R547 million in 2009/10, raising concerns about absorption capacity.

The situations highlighted above would seem to indicate under-budgeting (through the deferral of maintenance expenditure to later periods) or possibly inadequate planning. Maintenance costs are also escalating as result of increases in the fuel prices, labour and plant cost and the price of bitumen[4]. There is a need for provinces to produce adequate non-financial data on the conditions

[4] Bitumen is a by-product of crude oil which is used in the construction of waterproof surface layers and for 2005/06 financial its price increased by 13.7 % compared to the consumer price index which increased by 3.6% in the same period.

of roads (e.g. physical condition, age, physical integrity, functionality, utilization, etc) in order to inform maintenance budgets as part of a broader asset management strategy.

This analysis reinforces the fact that most provincial roads taken over by SANRAL during the past few years had not been properly maintained by provinces. Provincial asset management strategies for road networks should emphasize not only reactive maintenance, but also planned maintenance over the lifecycle of the infrastructural asset. SANRAL has also indicated that further delays in the incorporation of these earmarked provincial roads into the national road network could exacerbate the deterioration of roads at high future cost to the economy.

3.3 Conclusion

Due to the importance of roads in the economy it is imperative that the road infrastructure be kept in a good condition by performing the required periodical maintenance. This will help to prevent premature deterioration of road infrastructure by undertaking periodical planned maintenance and to avoid the exponentially higher future costs associated with maintenance which has been overdue. It is also important that all roads be classified and assigned to the relevant sphere of government so that there is clear ownership and accountability. The progress thus far with the process of the classification of roads is noted by the Commission. However, the Commission also notes that the actual process of classifying roads has not yet started.

Even though SANRAL has successfully incorporated some of the earmarked provincial roads, one of the challenges which remains is that provinces delay the process by failing to submit the appropriate applications to SANRAL. This may exacerbate the deterioration of the provincial road network.

3.4 Recommendations

- The process of classifying roads amongst the national, provincial and municipal spheres of government should be accelerated in line with the classification framework already established.
- The premiers for the provinces with provincial roads earmarked to be incorporated into the national road network should apply for such roads to be incorporated into the national road network without further delay.

4

Chapter 4:

Bottlenecks Hampering Housing Service Delivery

Introduction

The Financial and Fiscal Commission (FFC) in its submission for the 2006/07 Division of Revenue (DoR) made a number of recommendations for housing delivery. These included a proposal that the government should address housing delivery bottlenecks to reduce under-spending in the provinces and that, in cases where municipalities have the capacity, they be accredited to administer housing programmes. This report examines the progress with the accreditation process. The report also investigates the institutional bottlenecks affecting the speed and efficiency in housing delivery.

4.1 Integrated Housing and Human Settlement Development Conditional Grant

4.1.1 Key Findings

Local government is responsible for overall planning at the municipal level. This includes decisions on infrastructure and housing planning and development. The Integrated Housing and Human Settlement Development Conditional Grant (IHHSDG) is the most important source of funding for housing delivery and currently flows from the national to the provincial Department of Housing and then to municipalities and/or private developers.

Analysis of the current housing funding reveals that the process of transferring funds for housing is bureaucratic and inefficient. The problems primarily arise due to the fact that allocations are determined in the provincial sphere while planning is done at the municipal level. There are often delays in the announcement of decisions on maximum subsidies that municipalities should receive that make it difficult for municipalities to plan and budget. This problem is further complicated by delays in transfers which cause cash flow problems for municipalities.

The IHHSDG grant represents the dominant source of housing revenue at the provincial level (in most instances this conditional grant composes over 80% of total provincial housing budgets). This grant flows predominantly to the Housing Development Implementation Programme and from there on to municipalities in the form of transfers. Analysis shows substantial under-spending of both the IHHSDG grant and the Housing Development Implementation Programme over the period under review. This under-spending partly confirms the existence of the bottlenecks raised in the section above. This is particularly true with respect to the slow disbursement of funds to municipalities.

Tables 4.1 and 4.2 below provide a detailed, disaggregated view of the performance of the IHHSDG grant and the Housing Development Implementation Programme by province. In both instances, most provinces demonstrate a level of under-spending that falls within the Auditor General's cautionary range (under-spending that exceeds 5%). The trends indicate that municipalities either do not get funding timeously, or they receive large amounts close to the end of the financial year and are then unable to spend such large amounts (fiscal dumping).

However, despite the trends of past under-spending the 2006/09 MTEF projections for both the IHHSDG grant and the Housing Development Implementation Programme show a strong increase of under 12% per annum. Given inefficient levels of past spending, it is questionable whether departments will be able to effectively use the increased funding or whether under-spending will persist.

Table 4.1. Integrated Housing and Human Settlement Development Grant: Real Allocations to Provincial Housing Departments, 2003 - 2009

IHHSD Grant (R'000)	2003/04	2004/05	2005/06	Under/ Over spending (FY2003-FY2005)	2006/07	2007/08	2008/09	2009/10	Real Annual Growth Rate (FY2007-FY2009)
EC	1,136,650	674,402	636,020	7.2%	761,994	1,003,388	1,135,792	1,273,775	12.7%
FS	400,872	605,791	515,292	15.1%	528,629	622,777	701,267	767,556	11.0%
GAU	1,163,791	1,267,835	1,048,191	1.3%	1,757,666	2,094,588	2,342,343	2,544,415	10.2%
KZN	1,114,717	901,014	837,271	(0.1%)	1,048,376	1,249,337	1,430,465	1,593,901	13.0%
LIM	508,202	435,243	500,667	12.1%	521,331	621,263	711,105	792,083	12.9%
MPU	338,404	356,297	345,797	8.2%	421,002	501,703	571,256	632,794	12.3%
NC	127,946	107,446	87,005	2.7%	104,774	124,858	146,454	167,283	15.7%
NW	414,886	586,112	489,887	51.5%	697,419	730,988	813,565	879,087	9.7%
WC	492,069	648,878	558,330	15.5%	998,143	904,240	1,093,090	1,262,711	18.2%
TOTAL	5,697,536	5,583,016	5,018,460	11.2%	6,839,334	7,853,142	8,945,338	9,913,605	12.4%

Source: National Treasury Section 35 Reports, Own calculations.

Table 4.2: Housing Development Implementation (Subsidy Programme): Performance by Province, FY2003 to FY2009

Housing Development Implementation	Real 3 yr Growth Rate - Spending FY 2003 to FY 2005	Adjusted Appropr. 2006/07	Under/Overspending 2006	Medium Term Estimates 2007/08	Medium Term Estimates 2008/09	Medium Term Estimates 2009/10	Real 3 yr Growth Rate - Budget 2006 MTEF
EC	-13.16%	793,008	15.60%	1,014,780	1,162,299	1,299,914	17.91%
FS	7.64%	578,178	2.57%	653,616	732,784	800,106	11.44%
GAU	17.34%	2,010,785	1.58%	2,268,287	2,495,686	2,693,912	10.24%
KZN	1.76%	985,672	(2.61%)	1,136,456	1,326,081	1,510,101	15.28%
LIM	222.10%	676,360	1.02%	665,996	756,522	837,243	7.37%
MPU	-0.49%	359,014	5.03%	537,248	606,799	668,134	23.00%
NC	-3.16%	113,192	1.67%	142,046	163,332	186,572	18.13%
NW	32.25%	729,915	0.45%	746,270	822,163	888,708	6.78%
WC	31.09%	1,029,479	22.38%	949,627	1,108,425	1,278,648	7.49%
AVG	12.57%	7,275,603	5.57%	8,114,325	9,174,091	10,163,338	11.79%

Source: National Treasury, 2007, Own calculations.

Based on the poor spending performance of provincial housing departments with respect to the IHHSDG grant and the Housing Development Implementation Programme, it is evident that there are inefficiencies in the system. The result is a negative impact on the delivery of houses.

Lack of capacity has also been cited as one of the key reasons for poor spending performance. Table 4.3 provides information regarding the number of staff positions available across the various provincial housing departments. Information was found for all provinces except the Eastern Cape. It is clear from the figures that a number of provinces are facing severe capacity shortages. This challenge impacts negatively on the ability of provincial housing departments to carry out their mandates

Table 4.3: Number of Positions and Vacancy Rate by Province.

	2003		2004		2005		2006	
Province	No of Positions	Vacancy Rate	No of Positions	Vacancy Rate	No of Positions	Vacancy Rate	No of Positions	Vacancy Rate
GT	708	15.68%	953	31.27%	1179	22.56%	1264	39.64%
KZN	1961	40.80%	1426	23.49%	1342	26.60%	1321	30.89%
NC	460	35.65%	472	44.92%	497	48.29%	820	42.56%
FS	575	47.83%	545	42.57%	656	50.46%	681	53.89%
LIM	2884	41.82%	4758	40.69%	1390	16.04%	2449	52.84%
MPU	496	53.83%	1186	77.15%	885	51.30%	765	38.82%
NW	1295	61.78%	863	45.65%	603	29.52%	945	58.41%
WC	368	23.37%	345	22.90%	565	27.26%	798	20.18%

Source: PERSAL Database

Municipalities are responsible for all decisions pertaining to "housing infrastructure" and housing planning and development. In principle the appropriate location of the housing function would seem to be the local government sphere. Given that municipalities are already responsible for planning, the use of provinces to act as a transferring agent between the national and local spheres seems to add an unnecessary bureaucratic layer. If the housing function were located at the local level, it would allow for better coordination and integration with other municipal infrastructure plans/Integrated Development Plans (IDPs). This would also have the potential to improve the overall municipal planning for infrastructure and the provision of other housing-related services, for example, water and sanitation.

The Housing Act of 1997 and the Division of Revenue Act of 2005-2007 require provincial housing departments, through the MEC, to accredit municipalities with capacity. Furthermore, the Minister of Housing's Cabinet-endorsed plan to expand the responsibilities of municipalities to take up the housing function in 2005 (via the process of accreditation), was aimed at leveraging the potential advantages of decentralization – that is, increasing the efficiency of delivery by devolving the responsibility to the lowest possible level (National Treasury, 2007b:3). Legislation also provides for the devolution of a function to local government if it would be more effectively administered locally, if the municipality has the capacity to administer it. The accreditation process is very important as one of the ways of decentralizing the housing function. Accreditation has three levels as described in Table 4.4.

Table 4.4: Levels of Accreditation

Level	Description
1	Deals with beneficiary management, subsidy budget planning and allocation and priority programme management and administration.
2	Relates to full programme management and administration of all housing programmes.
3	Allows municipality to undertake financial administration.

Source: National Department of Housing

A fully accredited municipality would be able to administer any national housing programme within its jurisdiction including receiving, evaluating and approving or disapproving applications for subsidies[5]. Accredited municipalities would also be able to receive their transfers directly from the national government. Full accreditation effectively removes the provincial sphere from the equation. The process of accreditation consists of nine different stages which are described in Table 4.5.

[5] **National Treasury, Provincial Budgets and Expenditure Review: 2002/03 - 2008/09.**

Table 4.5: Various Stages in the Accreditation Process

Step	Description
Step 1	Identification of municipalities to be accredited in the province by MECs and municipalities.
Step 2	Municipalities apply for a particular level of accreditation. Municipalities should also identify their pre-accreditation capacity needs in order to formulate an accreditation business plan.
Step 3	The nDoH therefore provides capacitation funding for pre-accreditation phase through the pDoH to provide technical assistance.
Step 4	The municipality prepares the accreditation business plan with the technical support provided by nDoH, if necessary and submits the business plan to the province for review.
Step 5	The pDoH reviews the business plan and endorse it if it complies.
Step 6	On thee basis of the conditional accreditation approval, the nDoH provides capacity funding through the pDoH to assist municipality to implement the capacity requirements of the business plan.
Step 7	The municipality implements the business plan and provides monthly progress reports to pDoH.
Step 8	If municipality complies with capacity requirements in terms of the business plan auditors confirm by issuing of ìcompliance certificateî for the level applied for.
Step 9a	By issuing the compliance certificate (level 1 and 2), the MEC delegates the functions relevant to the level of accreditation applied for.
Step 9b	By issuing the compliance certificate (level 3), the MEC approves the level 3 of accreditation of the municipality.

Source: National Department of Housing

Through consultations with the nDoH and some municipalities, the FFC established that the Housing MinMec has approved a list[6] of 18 municipalities for accreditation including all the metropolitan municipalities. The 18 municipalities are at various stages within the accreditation process, with 11 at step 8 and the rest at step 7. Effectively then, no municipality has received either level 1, 2 or 3 accreditation as yet. This indicates that the pace at which the accreditation process is unfolding is exceedingly slow. This has negatively affected certain municipalities which, in anticipation of receiving accreditation, had started preparing to take over the housing function by establishing dedicated units and staffing to perform this function[7].

4.2 Conclusion

The analysis shows that there are bottlenecks with respect to the flow of funding between the spheres of government and these bottlenecks affect the speed as well as efficiency of housing delivery. The analysis of the budgets and spending trends of provincial housing departments confirms the existence of these bottlenecks. There is significant under-spending although the budgets are growing fast. In most instances the under-spending is attributed to the bureaucratic processes and the high vacancy rates in the provincial housing departments.

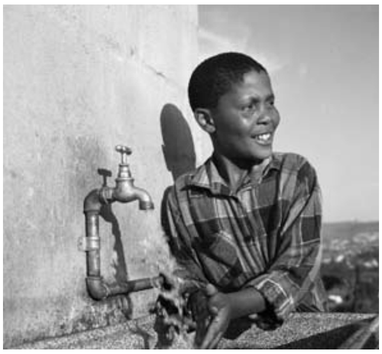
To date, no municipality has been awarded full accreditation although the Housing MinMec identified 18 municipalities for accreditation purposes. Of these, only 11 have progressed beyond the first of eight steps in the process.

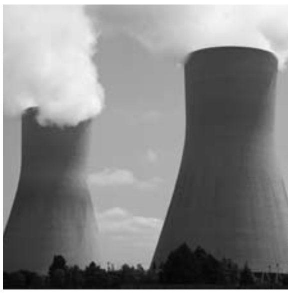
4.3 Recommendation

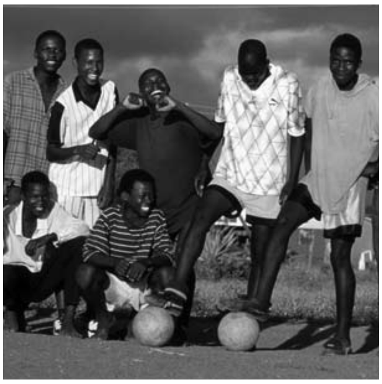
- The FFC reiterates its previous recommendation that the accreditation of municipalities with adequate capacity should be accelerated in line with the framework provision of the Integrated Housing and Human Settlement Development Grant (IHHSDG) contained in the Division of Revenue Bill for 2008 and the Housing Act of 1997.

[6] The list consists of the City of Cape Town, City of Joburg, Ekurhuleni metro, Tshwane metro, Ethekwini metro, Nelson Mandela metro, Buffalo City, Mangaung, Emalahleni, Polokwane, Rustenburg, Sol Plaatjie, Emthanjeni, Khara Huis, Namakwa District municipality, Pixley Ka Seme District municipality, Kgalagadi District municipality and Frances Baard District municipality.

[7] Tshwane Metro is one of those municipalities.







Part B

National-Local Fiscal Relations

Chapters 5-7

5

Chapter 5:

Augmenting Local Government Revenue

5.1 Background

The local government sphere has undergone significant changes since its inception in terms of both the structures and the systems of the fiscal framework and its component institutions. The most recent changes include the abolition of Regional Service Council / Joint Services Board (RSC/JSB) levies and the subsequent enactment of the Municipal Fiscal Powers and Functions Act (Act No. 12 of 2007), which is expected to bring about changes to the local government fiscal framework through the regulation of the introduction of municipal taxes and surcharges.

As an interim measure for the replacement of the loss of RSC/JSB levies' revenue, a levy replacement grant was introduced by the National Treasury. In addition, the property tax has been zero-rated for VAT purposes. Previously, the VAT paid by municipalities on inputs to services provided by municipalities, but financed by property tax, was exempt from VAT. Zero-rating property tax allows municipalities to reclaim the tax, although ratepayers do not pay VAT on property tax. In response to this, the FFC undertook in 2007 to conduct a broad assessment of the local government fiscal system, including making recommendations on local government revenue sources. This section reports the first output of this work.

In order to identify potential revenue sources for municipalities, a literature review of internationally-used options was undertaken. A survey of district municipalities was also undertaken whereby the municipalities were interviewed in order to establish their potential revenue bases as well as their capacity to collect their own taxes. The main issues addressed in the survey were:

- Powers and functions;
- Existing and potential revenue bases;

- Alternative revenue sources;
- Assessment of collection and enforcement capability; and
- Reactions to a list of proposals.

5.2 Key Findings

5.2.1 Powers and Functions

Local government respondents stressed the importance of the principle that revenue assignment should follow the assignment of functions. Municipalities are also of the view that revenue being made available to them for the performance of functions allocated to them should be adequate to cover their expenditure needs. However, there were situations where municipalities were allocated certain functions and no corresponding revenue was made available. These municipalities were compelled to finance those unbudgeted functions. It was concluded that the current alignment between functions and revenue sources is unsatisfactory in respect of both the amounts of revenue and the suitability of the revenue source in terms of local linkages. This lack of alignment is particularly problematic in the cases of the smaller districts with poor revenue bases.

5.2.2 Revenue Sources

In discussions with municipalities regarding the criteria to assess local government taxes, all municipalities expressed support for the principle that whatever revenue source is available to them should enhance local independence. The literature reveals the following as general criteria for a good local revenue source:

- Local autonomy: Tax or surcharge rates should be set and administered locally.
- Yield: A tax should be considered only if it makes a significant contribution to the municipal revenue.
- Collectability: If the tax cannot be administered or can only be administered at very high cost, the tax should not be considered, regardless of any theoretical advantages it might have.
- Economic efficiency: Any economic damage caused by raising revenue should be minimised.

- Immobility of base. Local taxes are best based upon assets or activities that cannot easily move to another jurisdiction.

- Base stability in economic cycles: Minimise vulnerability of local finances to fluctuations in macroeconomic conditions.

The FFC concludes that the following criteria should guide the choice of revenue instruments at the local government sphere:

- Potential to strengthen local independence.

- Fairness (Equity): Fairness relates to the equitable distribution of the tax burden vertically and horizontally.

- Efficiency: Suggesting that municipalities should levy taxes on immobile factors in order to preserve the local tax base in the face of the movement of economic resources between municipal jurisdictions.

- Revenue Adequacy: i.e. The tax should be able to match expenditure responsibilities of municipalities.

- Political acceptability

- Ability of local municipality to control the key variables: i.e. Municipalities should have some discretion to adjust the tax rate.

- Suitable for local collection.

5.2.3 Existing and Potential Revenue Bases

The following existing and potential revenue sources which could be further enhanced were identified by municipalities: user charges; residential property; commercial and industrial property; property transactions; business turnover; agricultural property; public service infrastructure and tribal land. It was concluded that the best potential revenue bases are the existing ones, in particular the value of local business property and of the businesses themselves.

Respondents favoured a tax based on local businesses. It was pointed out that the local business tax should accrue to the district local authority and not where the head-office is situated. The previous dispensation in respect of RSC levies was distorting in effect as the levies generally accrued to metros at the expense of districts. The essence of the local business tax lies in the advantage of it being a local form of revenue earned through business and enterprise within a local authority area of jurisdiction, and ploughed back for the betterment of that region by the local authority.

5.2.4 Tax Administration

Municipalities confirmed that existing RSC infrastructure is already in place, and remains available. With suitable training it could be enhanced, to administer the collection of any local business tax. However, municipalities raised concerns that the powers of inspection in the RSC Act had been inadequate, and that stronger powers would be needed in any new legislation, combined with more cooperation from South Africa Revenue Services (SARS). Municipalities considered their involvement in local administration to be important and believed themselves to have the structures and capacity to be suitably involved.

5.2.5 Reaction to a List of Proposals on Alternative Revenue Sources

Municipalities were given a list of proposed revenue instruments and asked to respond to each. The list was selected from a range of instruments under current discussion, with some more controversial additions in order to extend the potential range of responses. It included the following revenue instruments:

- Special Rate on Property tax for District Councils (controversial);
- Arrangements for both District and Local Councils to impose rates on properties within their jurisdictions (controversial);
- Capital Gains Tax on Non-primary residence (controversial);
- Local Business Tax collected locally (under discussion);
- Local Business Tax collected by SARS (under discussion);
- Tax on local sales (Business turnover) (under discussion);
- Tax on local payrolls (under discussion); and
- Motor vehicle Tax (under discussion).

Officials interviewed were given an opportunity to reflect on these revenue instruments and suggest what would be most appropriate for their municipality, given the economic circumstance, the tax base and the capacity they currently have. Municipalities were also given the opportunity to suggest any other revenue instrument(s) that had not been included in the list mentioned above. One proposal put forward by municipal officials was a surcharge on the national fuel levy, part of which should be allocated to local government as an intergovernmental transfer. This is perceived to be a productive and apparently trouble free revenue source, despite the fact that it fails to meet the main criterion of supporting local independent decision making. In general the best sources of revenue for local government are property taxes (rates) and user charges for local utilities. Municipalities are already levying property taxes and user charges and there was agreement that these should be used to their maximum before other sources are contemplated.

5.3 Conclusion and Recommendations

It is important that reforms to the fiscal framework of local government ensure that the fiscal autonomy of municipalities is not compromised but enhanced.

- The FFC recommends that, in light of the disestablishment of the RSC Levy, which formed a significant source of municipal revenue, the replacement revenue source for municipalities should be a tax that:
  - Enhances the fiscal autonomy and discretion of local governments;
  - Strengthens the accountability of local government regarding the administration and use of the proposed tax base;
  - Yields an adequate and buoyant revenue stream for municipalities in the face of cyclical instability; and
  - Does not disturb macroeconomic balance.

6

Chapter 6:

Electricity Pricing, Generation and Distribution

6.1 Background

Following years of being endowed with surplus electricity generation, South Africa is currently at a critical juncture where it needs to make new investments in its power sector geared towards overcoming supply constraints that are currently being addressed through load shedding. A significant proportion of these new investments are intended to meet anticipated electricity demand necessitated by government's higher growth target of 6% between 2010 and 2014 under the Accelerated and Shared Growth Initiative for South Africa (AsgiSA) growth plan.

Since 1998, Government has initiated a number of far-reaching processes to deal with the restructuring of the electricity distribution industry. They commenced with the establishment of Eskom as a public company in 2001. Due to the large number of distributors, both large and small, restructuring has been geared towards rationalizing the electricity distribution industry. This involves proposals to transfer assets from Eskom and local governments to six Regional Electricity Distributors (REDs)[8].

Huge investments of the nature proposed[9], distribution reforms and new pricing structures for electricity will have substantial impacts not only on welfare, but also on broader resource allocation and the rest of the economy. From the point of view of the process of the division of revenue (DoR), an understanding of the implied tradeoffs and opportunity costs of such huge changes in institutions and pricing structure are important as they will entail a re-assessment of the revenue allocation process.

In order to address these questions and draw consequences for the DoR process, the Commission has used two complementary economy-wide modelling approaches to estimate the impact of the shocks. The first approach uses a behavioural accounting model which combines input/output tables and household expenditure. The second approach employs structural computable general equilibrium (CGE) models that are designed specifically for the South African economy to analyse expansions in electricity

[8] This is being done taking into account that the constitutional responsibility for electricity reticulation lies with municipalities.

[9] Eskom plans to invest about R343 billion in the next five years.

infrastructure. The models build in price-responsive behaviour to measure pass-through effects and account for the effects of higher energy prices on households, consumer price indices, government balances, investment, the balance of payments and unemployment.

6.2 Electricity Policy

The 1998 White Paper on Energy Policy set out government's energy policy as being to 'increase access to affordable energy services, improve energy governance, stimulate economic development, manage energy-related environmental impacts and secure energy supplies through diversity' (Department of Mineral and Energy, 2005).

In 2005, Government gazetted the National Electricity Basic Services Support Tariff Policy which aims to bring relief to poor households through allowing 50 kilowatt-hours (KWh) of free electricity a month. Users pay the normal tariff for any consumption exceeding that. Free basic electricity is funded through the Local Government Equitable Share.

The electrification programme is funded through infrastructure transfers from the Department of Minerals and Energy Affairs to Eskom and local government. Eskom's involvement in the electrification programme reflects insufficient capacity at local government level.

6.3 Restructuring the Electricity Industry

There are three major players in the electricity supply and distribution industry: Eskom, the 187 amalgamated local municipalities (hereafter referred to as municipalities) and private producers. The electricity supply industry is dominated by Eskom Holdings (Pty) Ltd. Gross electricity generation was about 230 TWh in 2004. Of this, Eskom contributed 96% while private generators contributed 3.2% and municipalities generated 0.8% (National Energy Regulator of South Africa (NERSA), 2004). With the exception of the Motraco line that is jointly owned with utilities from Mozambique and Swaziland, Eskom owns all remaining transmission lines around the country. With regard to distribution, Eskom is responsible for close to 60% of all direct sales while the 177 local authorities are responsible for the remaining 40%. Eskom distributed 60.3% of the 214 TWh available for distribution in 2004. The remaining 39.7% was attributed to municipal and other distributors (NERSA, 2004).

Since 1998, Government has initiated a number of processes to deal with the restructuring of the electricity supply industry and generation. With regard to electricity generation, restructuring will establish an Eskom Holdings-owned subsidiary that will retain 70% market share for electricity generation. The remaining 30% will be shared between private independent power producers

(IPPs) (20%) and Black Economic Empowerment groups (10%). Electricity generating enterprises will not be allowed to carry out business in the transmission or distribution industry.

Changes to the regulations governing the electricity distribution industry are far-reaching. In 1997 Cabinet approved the Electricity Industry Committee (ERIC) report, which recommended the restructuring of the Electricity Distribution Industry (EDI) into a number of Regional Electricity Distributors (REDs). Prior to 1994, municipalities distributed electricity in historically white areas, while ESKOM covered historically black townships and some homelands. The electricity distribution industry was thus characterised by inequality stemming from different tariffs charged by municipalities and poor service delivery due to lack of capacity in poor municipalities.

The Electricity Distribution Industry Blueprint report of 2001 (the Blueprint) contained five key objectives of the restructuring process as follows:

- To provide low cost electricity to all consumers, with equitable tariffs for each customer segment;
- To provide a reliable and high quality supply and service to all customers, in support of the government's economic and social development plans;
- To meet the country's electrification targets in the most cost-effective manner and ensure that electrification is contributing to social and economic development;
- To meet the legitimate employment, economic and social interests of all employees in the sector, and ensure their safety; and
- To operate in a financially sound and efficient manner, in order to provide a reliable and sustainable future for both consumers and employees.

6.3.1 Municipalities and Eskom

In its submission for the fiscal year 2002/03 to the Division of Revenue Act (DORA), the FFC recommended, inter alia, that no stakeholder should experience deterioration in its circumstances owing to the restructuring process and that the revenue accruing to REDs should remain within local government. The following were some of the proposals relating to the restructuring that were contained in the said submission:

- Municipalities should be compensated for all losses related to the transfer of electricity distribution to REDs.
- A detailed study of both the costs and benefits of the transfer should be carried out to ascertain whether a net loss will result.

- The advantages and disadvantages of retaining consolidated billing systems with municipalities should be carefully weighed, and measures should be implemented to retain the advantages conveyed to municipalities by electricity distribution.

- RED boundaries should be co-terminus with municipal boundaries to ensure that residents of a given municipality do not fall within different REDS and hence under different tariff structures[10].

[10] FFC Submission to the DOR 2002/03

Government did not respond in any comprehensive manner to the FFC's recommendations on the restructuring of the electricity distribution industry.

Of particular relevance to the FFC is that municipalities have traditionally generated significant financial surpluses from their electricity undertakings, which have been used to cross-subsidise other services. There are other costs which have been cited, such as compensation for the assets taken to the REDs, employees cost of migration to REDs, loss of assets resulting in lower credit ratings and therefore higher capital costs, all of which will need to be addressed.

A Cabinet Decision of September 2005 approved the formation of six REDs plus one national electricity distributor. This decision was reversed in October 2006 when Cabinet approved a proposal to create six REDs which would be established as public entities under the auspices of the Electricity Distribution Industry (EDI) Holdings (Ltd). No details have been provided on how the public entity is to be managed. The change of the REDs from a municipal entity to a public entity is likely to have a negative financial impact on municipalities. In the case of a municipal entity, the latter operates within a jurisdiction of the respective municipalities – the funds flowing to the municipal entity are controlled and managed by the municipalities. However, with regard to the REDs being a public entity, municipalities run the risk of losing control over the entity and the finances thereof.

Similar to municipalities, the proposed restructuring process is likely to have a financial impact on Eskom's business as well. At the time of writing this chapter, information on the exact financial impact was not yet established as Eskom is still in the process of conducting an assessment of the extent of the potential loss of revenue resulting from the restructuring process. However, Eskom has since confirmed that the loss of Eskom's assets to the REDs will mean a weaker balance sheet and this will have a bearing on ESKOM's credit rating[11].

[11] Meeting between FFC research team and Eskom Distribution on 28 February 2008

6.3.2 Constitutional and Legislative Issues

Local government is authorized in terms of Part B of Schedule 4 of the Constitution to undertake electricity reticulation. In terms of the current restructuring, the Constitution is seen as an obstacle to the successful implementation of the process. It is envisaged that REDs will be registered as public entities in which both national and local government have a shared participation. Such an entity or governance arrangement may be in conflict with Constitutional provisions as electricity reticulation is a sole competence area of municipalities.

The electricity restructuring process has been unfolding at a very slow pace because of the incompleteness of the necessary legislation as well as misalignment of existing legislation. These include amongst others, the RED Establishment Bill, Asset Transfer Framework, the National Cross Subsidy Framework, the Municipal Finance Management Act and the Municipal Systems Act.

The delay in finalising legislation has led to uncertainty among stakeholders involved in the electricity distribution industry. The uncertainties are likely to culminate in challenges such as lack of maintenance of electricity infrastructure by both municipalities and ESKOM. EDI Holdings has estimated the maintenance backlogs to be at R5 billion in 2007. Thus, all the stakeholders need to set workable timeframes and deadlines by which all the necessary legislations is finalised.

6.4 The Impact of Tariff Increases and Electricity Capacity Expansion

The impact on sectors of an increase in electricity prices is through changes in costs of production which are split into changes in input cost, basic cost and purchase cost for all the 95 industries in the modelled economy. The economy-wide average increase in purchase cost is 1.1% for a 100% electricity tariff increase and 0.2% for a 20% electricity tariff rise. Most of the industries that experience purchase cost increases above the economy-wide average are highly electricity-intensive sectors. The greatest impact of the tariff increase is on non-ferrous metals, whose purchase cost increases by 9.4% and 1.9% respectively for the 100% and 20% tariff increases. Gold is also severely impacted, experiencing increases of 7.3% and 1.5% following the two simulations. Outside the electricity industry itself, the other sectors that experience significant pressure on their purchase costs are treated metals, water and trade.

For households the focus is on the impact on household well-being/welfare as measured by equivalent variation[12]. Overall, a 100% (20%) increase in electricity tariff will lead to a 2.6% (0.7%) decrease in household welfare for South Africans as a whole. Welfare declines the least for the poorest households across the country. Fourth quintile households experience higher than average declines in their welfare following the hike of electricity prices.

[12] Equivalent variation is the change in income that would be required without electricity tariff reform to make people as well-off economically as they would be with the electricity tariff reform.

An increase in capital infrastructure in the electricity sector of 5% leads to an increase in GDP of 0.19%. Private consumption rises as incomes have gone up. With a given current account balance, the increase in output induces a real exchange rate depreciation which leads to an increase in exports and consequently imports. The increase in investment, consumption and exports all contribute to the increase in GDP.

The main mechanism behind the mesoeconomic results of the policy simulation comes from the investment closure. As demand for investment products increases in line with increased infrastructure demand, industries whose products are used intensively in investment experience substantial increases in their demand, and consequently, their output. Coal is heavily utilised in electricity production and experiences the highest increase in output. Heavy manufacturing, light manufacturing and mining have among the highest shares of their product in total investment demand and hence experience higher than the economy-wide average increase.

With respect to employment and earnings, employment and the wage rates of high skilled workers increase while the wage rates of low skilled workers and return to capital decrease.

Consumption prices in real terms decrease for all households. The price reductions in real terms are more important so that the welfare effect as measured by the equivalent variation is positive for all households.

6.5 Conclusion and Recommendations

The slow pace at which the restructuring process is unfolding poses great concerns for stakeholders affected by the process, especially municipalities that are currently distributing electricity. The impact of the potential loss of a crucial revenue source from electricity distribution for municipalities will need to be adequately addressed. To ensure the commitment and full buy-in from all stakeholders involved in the restructuring process, further guidelines on the participation of municipalities and Eskom in the REDs need to be worked out. In that respect the FFC recommends that:

- Government should address the potential loss of a crucial revenue source for local government as a result of the establishment of Regional Electricity Distributors (REDs).
- The proposed restructuring process needs to factor in current reforms to the fiscal framework and the greater developmental role envisaged for the local sphere of government.
- There is a need to review legislation in respect of (i) the transfer of assets, (ii) the national pricing framework and (iii) the establishment of the REDs.

The chapter has also analysed the impacts of huge investments in electricity as well as increases in electricity pricing. In this respect, the FFC makes the following recommendations:

- Government should work with the National Energy Regulator of South Africa to put in place a financing framework that deals effectively with electricity pricing. Such a framework should capture the scarcity of the resource in a pricing environment that reflects costs, efficiency, stability and, eventually, externalities.

- Given that reforms in the electricity pricing structure will, in essence, necessitate an increase in electricity prices, such higher electricity prices will adversely impact on poor households with access to electricity as well as raise the cost to government of extending basic access to electricity for poor households. As such, government will need to increase annual funding for the rollout of services under the free basic electricity programme.

- For greater efficiency of resource allocation, technological innovation and increased investment in renewable energy sources, government will need to increase funding resources set aside for such purposes and enhance incentives with a view to establishing and implementing a framework that:

  - Encourages new forms of electricity generation technologies to enter the market;

  - Expands opportunities to consumers to access such forms of energy;

  - Allows non-utility developers equal market opportunity to compete with established providers; and

  - Incorporates financial incentives to expand production and distribution capacity, and effect savings through improving end-user efficiency.

7

Chapter 7:

World Cup 2010 Transport Infrastucture

7.1 World Cup 2010 Transport Infrastructure

This chapter follows up on work initiated by the Financial and Fiscal Commission (FFC) in 2007 to explore the macroeconomic impacts of government financing of the 2010 Fédération Internationale de Football Association (FIFA) World Cup, and has a specific focus on transport infrastructure financing[13].

[13] See FFC Submission on the DoR 2008/09

Government has decided to use the World Cup not only to support the success of the event itself but also to fast track implementation of transport infrastructure and create a lasting transport legacy. A Transport Action Plan that has as a strategic focus the acceleration of public transport by using the 2010 World Cup mechanism as leverage has been put in place. Its main idea is to create a legacy for public mobility through investments in public transport systems and infrastructure, services and non-motorised transport infrastructure investment.

There are opportunity costs that must be considered when evaluating government expenditure on infrastructure for the 2010 FIFA World Cup. To address squarely the issue of opportunity cost of public funds, a one-unit expansion in transport infrastructure spend is run through a specially designed macroeconomic model to assess the contribution this makes to economic growth, poverty reduction and equity. The model enables an evaluation of the government's overall transport infrastructure strategy, including that portion not necessarily geared for the 2010 FIFA World Cup, in terms of equity and efficiency.

7.2 Modelling Specification and Data

A transport-focused Social Accounting Matrix (SAM) is used for the analysis (Financial and Fiscal Commission, 2006). The SAM disaggregates the transport sector into finer sub-categories of rail, road, air, water, pipeline and transport support services. Demand injection in one industry will affect others indirectly. The indirect channels operate through changes in intermediate demand, factor demand, household demand and government demand.

The SAM used has 48 activities and commodities, 14 representative households disaggregated by income[14], one enterprise institution, a government institution subdivided into various taxes and subsidies and expenditure, a rest of the world institution and a savings and investment entry divided into changes in stock and gross domestic fixed investment.

Analysis carried out to ascertain the magnitude of forward linkages associated with the transport sector suggests that most of the output from the transport sector is used as marginal or intermediate inputs by other sectors. The only exception is road transport which delivers 48% of its output to households as final consumption. Most of the forward linkages of transport are with primary sectors such as agriculture, forestry and fishing, coal and other mining. Sectors involved with mineral refining are also among the sectors demanding higher than average intermediate goods and services from the transport sectors. The tertiary sectors are also strongly linked to the transport sectors, the main ones being wholesale and retail trade, communication, business services and government. The main backward linkages from the transport sectors are demands for inputs from business services, coke and refined petroleum products, motor vehicle parts and accessories and other transport equipment.

Analysis reveals that most of the factor remuneration goes to capital, then skilled labour, followed by highly skilled labour, with the least amount of resources going to semi-skilled and unskilled workers. This further confirms the capital intensity of the sector. Semi-skilled and unskilled workers form the majority of people employed in most transport sectors. In the road transport sector, which mainly employs skilled and highly skilled workers, the opposite applies.

For households, it is observed that the richest households or 10% of the households receive 43.5% of the available income while the poorest 10% receive only 1.28%. The richest group also pays more than 50% of the direct taxes and transfers to the government. This group also contributes substantially to total expenditure and total household savings. The high saving propensity for this group suggests that leakages will be higher for this group when it comes to multiplier[15] analysis.

[14] For equity analysis, households are grouped into poor, middle income and rich categories. Poor households are defined as the bottom 40% of income earning households while the richest households are defined as the top 10% income earning households. The residual make up the middle income households. Higher transport expenditures impact on household welfare through direct and indirect effects. These are estimated using the Leontief Inverse matrix.

[15] A Multiplier is the cumulative sum of the endogenous effects following an exogenous intervention. It is inversely related to the exogenous portion of economic activity.

7.3 Simulations and Results

Combining the model constructed and the data just described, this section reports on the results of an exogenous increase in transport demand. The findings suggest that this investment is not without opportunity costs. The aggregated transport SAM multipliers are, on average, below the national average when it comes to production, supply and household income. This suggests that an extra rand will have a higher return if invested elsewhere. Furthermore, a unit expansion in transport will create less additional household income compared to the economy-wide average.

In terms of equity, the results suggest that household income increases, following a unit expansion in transport demand, disproportionately benefits middle income households. Finally, the underlying growth rate in the modelled economy is premised on a given stock of capital stocks which is maintained by replacing the capital stock through using economy-wide depreciation rates.

7.4 Conclusion and Recommendations

This chapter investigates how much impact a unit increase in exogenous transport commodity demand will have on production, supply, value added and household income. Based upon the empirical research, the study demonstrates a compelling link between transport and economic growth and productivity, and supports a strong case for continued investment in transport. However, there are opportunity costs associated with such investments as well as equity considerations that policymakers would need to take into consideration.

The FCC recommends that:

- Spending on public transport infrastructure for 2010 should be linked to broader city development plans.
- A more resourced Public Transport Infrastructure and Systems Grant must continue after the 2010 FIFA World Cup.
- Projects that are funded under this arrangement should be selected based on full appraisal of economic, environmental and social costs/benefits.
- Funding mechanisms to cover maintenance costs of constructed 2010 FIFA World Cup facilities should be developed.

Part C

Intergovernmental Data Issues

Chapters 8-9

8

Chapter 8:

Performance Monitoring Framework

8.1 Background

This chapter reviews the data requirements for assessing the performance of various grants and programmes that are financed through these grants. The FFC's budget analysis perspective reveals that there are still significant gaps in both financial and non-financial data for evaluating the effectiveness and efficiency of government programmes. The incompleteness of the data is even more glaring when one needs to assess the efficiency of government programmes, including progress towards achieving the millennium development goals (MDGs). Such efficiency evaluation is a key requirement for the Commission's consideration in making recommendations for the division of revenue (DoR) in terms of Section 214 (a-j) of the Constitution. There are also equity considerations that the Commission must take into account in making its recommendations that can only be assessed if certain information is obtained from the administrative databases of government departments.

Starting from 2006, the Commission has introduced in its work programme the assessment of the performance of government departments with a view to informing its recommendations on the DoR. This assessment is currently limited to the provincial sphere but will be extended to the local sphere in the near future, with an initial focus on the metropolitan councils and the bigger local municipalities.

The approach used in measuring performance of provincial departments is based on the criteria listed in Section 214 (2) a-j of Chapter 13 of the Constitution. The quantitative aspects of this methodology entails comparing budgeting and spending trends over the previous three years (i.e. FY 2003 to FY 2005), current financial year (FY 2006) with projected budgets for the forthcoming Medium-Term Expenditure Framework (i.e. FY 2007 to FY 2009). Financial and non-financial information was extracted from the 2007 Provincial Budget and Expenditure Review (PBER), as collated by National Treasury.

8.2 Key Findings

8.2.1 Education

Although data on the number of schools by household income quintile are available through the Government Gazettes, etc, budget allocations are still not reflected across the nine provinces. The 2008 Division of Revenue Act (DoRA) requires that this information be gazetted per school with the tabling of the budget. It does not, however, specify that this information should be gazetted for fee-paying and no-fee schools. It will be necessary that such information is made readily available and the clause in the DoRA should promote this. At present this information is recorded under transfers and subsidies to non-profit institutions in line with the new economic classification format. It is currently quite difficult to extract financial information relating only to no-fee schools.

For learner transport a challenge exists regarding the availability of financial and non-financial data on the programme across the nine provinces. Furthermore, it is not possible to obtain an indication of the number of learners who are currently benefiting from the programme, or to obtain the associated cost of transporting beneficiaries. This missing information impacts negatively on planning, assessment and evaluation of the efficiency and effectiveness of learner transport provision.

While budget guidelines state that budgets and expenditure information on learner transport should be recorded under the goods and services component, it has been ascertained that this information is not readily available in the provincial budget and expenditure databases. Only two out of nine provinces record budget allocations and actual expenditure, namely Mpumalanga and the Western Cape. The above is a clear indication of non-compliance by the departments.

With respect to measuring the costs of Basic Education, the Commission recommends that:

- In order to assess the pro-poor impact of school funding norms, the Department of Education should make publicly available and accessible the funding norms for no-fee and fee-paying schools, in line with new provisions of the Division of Revenue Bill 2008 requiring indicative allocations by school.

- Provincial Education Departments should be enabled to report on budgets and spending on learner transport, in line with the new economic reporting format (see 2008 MTEF Treasury Guidelines, 22 June 2007, page 24).

8.2.2 Health

Current service delivery information does not disaggregate statistics according to care provided to specific vulnerable groups (women, children, the disabled). This occurs despite the fact that the National Health Act of 2003 (Department of Health, 2004) specifically makes reference, in Section 2(c) (iv), to "…protecting, respecting, promoting and fulfilling…" the rights of "…vulnerable groups such as women, children, older persons and persons with disabilities". DoRA 2008 mentions the availability, affordability and accessibility of health facilities for TB, HIV/AIDS (Conditional HIV/AIDS Grant) as outcome data that should be collected. Data for vulnerable groups such as the proportion of women with access to antenatal care, children, older persons and persons with disabilities are not mentioned. Therefore it is proposed that the latter should be included in the next DoRA.

The above indicators have been identified internationally and nationally as necessary for evaluating service delivery in health and the quality of health care.

In line with international and national practice and the specific reference in the 2003 National Health Act, Section 2(c)(iv) on the rights of vulnerable groups (as outlined above), the FFC recommends that:

- Health data for vulnerable groups such as the proportion of women with access to antenatal care, the availability, affordability and accessibility of health facilities for TB, HIV/AIDS, children, older persons and persons with disabilities, should be collected and improved using the South African Statistical Quality Assurance Framework.

8.2.3 Public Works and Transport

Guidelines[16] for the Expanded Public Works Programme (EPWP) include: (a) Enhancing the ability of workers to earn an income, either through labour market or entrepreneurial activity; (b) Utilising public sector budgets to reduce and alleviate unemployment; and (c) Each public body must formulate plans for utilizing its budget to draw significant numbers of the unemployed into productive work and provide them with training. Important prerequisites of the EPWP are that: (a) all projects should have exit plans, as required by the national Department of Public Works (nDPW), and (b) all recipients or beneficiaries would through the employment, acquire the necessary capacity to continue working elsewhere once finished with the project.

[16] National Department of Public Works, Guidelines of the Expanded Public Works Programme

In light of the upcoming 2010 World Cup and national initiatives such as the Accelerated and Shared Growth Initiative for South Africa (ASGISA), much emphasis has been placed on infrastructure development. As stated previously the EPWP is growing fast. This prioritization is in line with the sentiments expressed by the President and the Minister of Finance in the 2007 State of the Nation Address and the Budget Speech respectively.

The infrastructure sector publishes limited data on delivery and impact. In order to measure progress towards the achievements of the programme objectives, it is vital to measure (for example) job creation as, at the inception of the programme, government set itself a target of 1 million job opportunities to the unemployed and marginalised (i.e. at least 40% women, 30% youth and 2% disabled persons) by 2009. It would thus be vital to assess performance per target group, especially now that more financial resources are being channelled towards the programme. In essence this programme has become one of the fastest growing components in the infrastructure sector. Also, the impact made on the level of unemployment would be of paramount importance.

The FFC recommends that:

- In accordance with the prescripts of the EPWP, job creation for target groups such as women, youth and people with disabilities, should be included in the reporting requirements for all infrastructure conditional grants to provinces and municipalities.

8.2.4 Housing

Efficient and effective delivery of housing requires intergovernmental coordination to ensure that revenue flows smoothly from the national sphere (in the form of the Integrated Housing and Human Settlement Development (IHHSD) grant) to the provinces and on to municipalities, who ultimately deliver houses. In terms of monitoring the progress of housing delivery in South Africa, two issues currently hamper the ease with which performance can be tracked and assessed:

- The Division of Revenue Bill (DoRB) contains a list of performance measures that all departments who receive the IHHSD grant need to report on. The challenge is that not all provincial housing departments are complying.

- The IHHSD grant is the main source of revenue used to fund the delivery of houses. It is transferred to provinces and from there on to municipalities via the various subsidy instruments. All provincial departments receiving this form of funding have to adhere to certain conditions stipulated in the framework of the IHHSD grant - these conditions are published annually in the Division of Revenue Act (DORA)[17].

[17] See DoRA 2008 for the latest reporting requirements

It is worth noting that within the current reporting system, houses under construction are not separated from those that are completed by all provinces. It is thus not possible to distinguish between the two although it is required by the Act. It is clear that not all provinces are complying with the reporting requirements as detailed in the framework for the grant. This prevents both an effective analysis of the impact of current housing interventions and evaluating the efficiency with which the grant is spent.

Even though one of the framework requirements is to report on the number of subsidies allocated to women-headed households, an assessment of provincial housing budget publications shows that very few provinces report on, or even make mention of, this type of information as part of their service delivery measures. Currently the national Department of Housing needs to conduct (at considerable cost) a post-hoc survey to be able to report on this requirement. The same applies to other vulnerable groups such as child-headed households and those living with disabilities, which could be included in the list of reporting requirements.

Another reporting requirement is the number of job opportunities created. The EPWP was established with the aim of increasing employment through the use of labour-intensive methods. The potential for fulfilling this aim is particularly strong within the housing sector. Consequently, data is required for the number of employment opportunities created in accordance with the prescripts of EPWP for all provinces.

One of the key aims of the Breaking New Ground policy is to strengthen the role that the housing sector can play in reducing asset poverty. Information regarding the transferral of properties will aid an assessment of this. Norms regarding average construction time will assist in identifying potential 'problem' projects. It will also aid assessments of the efficiency of housing delivery. Reporting on this type of information will assist in providing an indication of the appropriateness, efficiency and effectiveness of housing delivery.

Currently not all provincial housing departments provide budget, output and outcomes data at sub-programme level. The latter makes it impossible to analyse housing programme implementation and performance. This presents difficulties when integrating any data that is reported at the sub-programme level.

In light of the above, the FFC recommends that:

- All provincial departments receiving the IHHSD grant should comply with the measurable outputs-related reporting requirements detailed in the housing conditional grant framework and published in the DoRA annually.

- To enable measurement of housing delivery the following should be reported:
  - The number of houses completed separate from those under construction;
  - The proportion and number of these houses completed that are occupied;
  - The proportion and number of these properties that have been transferred to their occupiers; and
  - The value of these houses and norms regarding average construction time.
- All provincial departments assigned the housing function should provide financial and non-financial output and impact data to a sub-programme level, so that data can be analyzed for every component of the housing subsidy programme (e.g. project-based, People's Housing Process, social housing, rural housing etc.).

9

Chapter 9:

Data Required for Local Government

9.1 Background

The uncoordinated approach to data collection from local government has resulted in the poor quality of the data returned. Local government data is not comparable, and is unreliable and often inaccurate as a result of duplicate data requests from various institutions. The lack of coordination has allowed at least 225 questionnaires from national organs of state to be distributed to municipalities within the course of a year. Many of these questionnaires duplicate amongst themselves similar data requests from national stakeholders. The problem is further exacerbated by numerous provincial requests.

These problems have led to a situation where municipalities are unable to complete all questionnaires that are received. There is a need for data request duplication to be reduced, if not eliminated completely amongst national stakeholders. Long term solutions are required to transform the current data collection process to a system that can produce 'quality statistics.'

A National Treasury 2006 Report (National Treasury, 2006) provided some preliminary analysis regarding the scope of the data request duplication problem. The report included a list of questionnaire content submitted to municipalities. This dataset was analysed and forms the basis for the quantitative assessments that follow. The results of this analysis were regularly work-shopped during meetings of the Local Government Data Collection Forum, where inputs from National Organs of State (i.e. DWAF, NT, DPLG, SALGA, MDB, SARB, DBSA, and Stats SA) were heard and considered.

9.2 Key Findings

It has been established from the analysis of municipal questionnaire content, that a large amount of duplication exists. In the financial set of questions submitted to municipalities, approximately 35% of all content is duplicated. Within the non-financial set, 66% of all questions are duplicated between national organs of state.

Within the financial section the major share of questions belong to National Treasury (78.67%) followed by Statistics South Africa (16.25%). The major share of non-financial questions lie with the Municipal Demarcation Board (53.16%) followed by National Treasury (30.26%) based on the quantity of questions within each classification area. During consultations with national organs of state, the Commission established that stakeholders have realized that there is an urgent need to eliminate data collection duplication and rationalize the data collection process to ensure maximum efficiency, lessen the survey fatigue experienced by municipalities and hence, improve the data quality.

In the process of reducing duplication in the collection of data, disagreements may arise between stakeholders regarding the manner of how the duplication is resolved. Such disagreements might relate to the interpretation of shared terms that are used interchangeably between stakeholders. The study established that different institutions loosely share similar terms. However the strict definition of the terms may differ across institutions. Therefore there is a need for stakeholders in local government data to reach agreement on the terms and definitions that are in use.

Further to the problem of definitions, there have been examples of legislative definitions that are not clear. Consequently national stakeholders as well the municipalities have varying interpretations of such legislative terms. If the legislation is unclear, finding a comparable measurement of that particular service's output would be quite difficult.

In order for data to be inter-changeable between stakeholders and interpreted consistently amongst different municipalities, it must be verifiable against a standard definition and methodology that is used in the collection and collation of the data (Statistics South Africa, 2006a). By producing data that is comparable, outputs across government can be more closely compared due to the common baseline.

There is a definite need for a National Coordinating Body (NCB) to be established. There is a current lack of formalization in the process of data collection and rationalization. The coordinating body can provide the formal means of addressing data duplication issues that exist between national stakeholders. The formalisation of such a body can assist with the various tasks that need to be completed. Agreements need to be reached regarding how a data collection rationalisation process should unfold. Every questionnaire that is submitted to local government must be evaluated based on the legal mandate, policy mandate and underlying function that require the questionnaire. We may currently have a situation where some questionnaires are not based on a legal mandate.

Efforts will be required to ensure that all organs of state are adequately provided with all their necessary data and information. Furthermore, communication between all relevant parties (viz. national organs of state and local government) will be critical in ensuring that all parties are aware of what is required by the rationalisation process. A coordinating body would be able to address such concerns.

9.3 Conclusion

From the findings, it is clear that the rationalisation of local government data collection will be a lengthy process. Efforts need to be made to transform the current data collection process from the current unstructured, uncoordinated arrangement to a structured, manageable process that will ultimately produce official statistics for the consumption of the users of data.

9.4 Recommendations

- National and provincial government departments, agencies and other organs of state should eliminate duplicate data requests submitted to municipalities.

- Uniform definitions should be established between national and provincial organs of state and municipalities with careful consideration given to the purpose of collecting and producing statistics. The interpretation should reflect the purpose and mandate of the department collecting the data and be concurrent with the legislation which guides those organs of state.

- A national coordinating body should be established to coordinate and rationalize the data collection activities of local governments. The national coordinating body should recommend and implement data collection standards according to the South African Statistical Quality Assessment Framework principle.

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Appendix A: Glossary

Backward linkage:
The connection between an industry and its suppliers.

Bitumen:
A by-product of crude oil which is used in the construction of waterproof surface layers.

Computable general equilibrium:
A class of economic model that use economy wide data to estimate the reaction of the economy to changes in policy, technology or other external factors.

End user efficiency:
The savings, usually energy related, achieved at the end of the energy supply chain.

Externality:
A spill over from economic activity, it occurs when a decision result in usually unintended benefits or costs to the third party.

Equivalent variation:
Equivalent variation in the context of this report, is the change in income that would be required without electricity tariff reform to make people as well-off economically as they would be with the electricity tariff reform.

Fiscal autonomy:
The degree to which sub-national governments have complete independence and discretion (with minimum or no central government control) in setting of priorities, determining expenditure and setting the tax rates.

Fiscal dumping:
The transfer of funds by the transferring department at a rate faster than the receiving agency, e.g. a municipality, is able to spend them. It commonly leads to a build-up of unspent money and requests for massive rollovers by receiving municipalities.

Forward linkages:
The distribution chain connecting a producer or supplier with its customers.

Multiplier:
The cumulative sum of the endogenous effects following an exogenous intervention. It is inversely related to the exogenous portion of economic activity.

Opportunity cost:
The cost of an economic activity foregone by the choice of another activity; OR, the cost (sacrifice) incurred by choosing one option over an alternative one that may be equally desired.

RSC levy:
A levy paid by business to metropolitan and district municipalities based on gross remuneration, including fringe benefits as well as gross income generated from sales of products and services.

Quintile:
A proportion of a set of data that has been ranked and divided into five equal groups (or bands), where each group contains an equal number of data items.

Social Accounting Matrix (SAM):
Flows of all economic transactions that take place within an economy (regional or national).

Surcharge:
Charge, fee or amount added on top of another charge, fee or amount.

VAT:
Value-added tax: tax on the final value of certain goods and services.

VAT zero rating:
Tax relief on payment of certain products or services.

Appendix B: Financial and Fiscal Commission's Preliminary Comments on the Public Finance Management Bill 2008

Introduction

This submission is made in terms of the Financial and Fiscal Commission Act (1997) as amended which, amongst other things, mandates the Commission to act as a consultative body for, and make recommendations and give advice to, organs of state in the national, provincial and local spheres of government on financial and fiscal matters.

General observations

The Bill seeks to introduce amendments to the Public Finance Management Act (1) of 1999. While not intended to compromise the principles in the existing Act in respect of fiscal prudence and good financial management, the amendments are wide-ranging and may to a certain extent result in unintended consequences. Generally legislation should be aimed at creating an enabling environment for regulations to be put in place to ensure that the law is followed. Such an approach ensures that there is a significant level of flexibility with which fiscally sound management practices and decisions can be made. The fact that the Bill brings in to the legislation a number of regulations that were applicable to the current Act may mean that the decision-making space for managers is being tightened. Caution is required here to ensure that the flexibility of management in decision making is not unduly compromised.

The Bill also introduces a number of principles that have become entrenched in the Division of Revenue Act. While this might appear to be a positive step, there may be unintended consequences, where changes to the Intergovernmental Fiscal Relations (IGFR) system occur that may require changes to the DoRA. It might be difficult to change this particular piece of legislation as it does not have to be amended annually like the DoRA.

A welcome development is the alignment of the legislation with other legislation of a similar nature (such the Municipal Finance Management Act 2003) and the incorporation of the issues around provincial borrowing. The details with respect to the latter are discussed below.

With specific reference to the Financial and Fiscal Commission Act (1997), there is a need to align the PFMA with Section 23 (2) (b) which empowers the Commission at any time during the financial year to submit estimates of the Commission's income and expenditure supplementary to that appropriated annually by Parliament.

Finally, the Bill does not provide clear guidelines on its application to Constitutional Institutions as apposed to state-controlled institutions. This distinction is particularly important as the definitions of executive authority for the former are critical if the constitutional principles underlying their establishment are not to be compromised. It may in fact be necessary to have a separate section dealing with the constitutional bodies, especially in light of the fact that Parliament (to whom all of these institutions report) is not covered under the PFMA.

Specific Comments

Chapter 1: Definitions

The Commission welcomes the new definitions that have been added to the Act. Of particular relevance to the Commission is that executive authorities have been defined to include those of constitutional entities, which was not the case in the PFMA.

The Commission further notes and supports the broadening of the definition of unauthorised expenditure to include DoRA violations. The amendment will help reduce the widespread practice of fiscal dumping, especially in cases where provinces transfer un-appropriated funds to municipalities.

Chapter 1: Objects

The Commission welcomes the amendment in that it goes a step further than the existing Act and entrenches the constitutional requirement for the Minister of Finance to establish uniform norms and standards in order to secure sound and sustainable financial management. The objects of the Act are further expanded to allow for the regulated establishment, dissolution and conversion of state controlled institutions. This should go a long way towards addressing the appetite for government departments to establish agencies for delivering services that should otherwise be delivered by government departments, often at considerably higher cost.

Chapter 1: Application of the Act

The application of the Act is widened to cater specifically for the South African Revenue Service as a national public entity that should be treated as a special case government department. The amendment also empowers the Minister to issue instructions and regulate the collection and handling of state revenue by the South African Revenue Service. This is a particularly important amendment that should allow the Minister to be able to influence how the Revenue Service conducts its business without having to directly intervene in the day-to-day activities of the public entity.

Chapter 1: Amendments to the Act

This section now includes a requirement that any amendments to the Act be introduced to Parliament only after the Minister and the Financial and Fiscal Commission have been consulted on the contents of the draft legislation and have responded in writing. This is welcomed by the Commission as it enables the Commission to carry out its mandate in respect of legislative changes that impact directly on financial and fiscal matters relating to all spheres of government. This is also consistent with the provisions in the MFMA.

Chapter 2: Treasuries

This amendment ensures the continuance of treasuries, both provincial and national. Two important amendments align the powers and functions of Treasuries to Chapter 13 of the Constitution and all the contingent (enabling) legislation flowing from this chapter of the Constitution, namely the MFMA, the DoRA, the IGFRA and any other legislation conferring functions or powers on the Treasury and enabling the Treasury to enforce compliance with the law. It is not clear why the Financial and Fiscal Commission Act (1997) is not directly referred to here, nor is it clear why the legislation flowing from sections 228, 229 and 230 of the Constitution is not directly referred to as it has direct implications for the powers of the Treasury through the Minister of Finance. As an addition to the current legislation, it is proposed that the Treasury can also intervene in a municipality in terms of Section 139 of the Constitution. This again ensures an alignment and consistency with the MFMA and is welcomed by the Commission. Similarly, with respect to provincial treasuries, there is an amendment to align requirements imposed on these treasuries by the MFMA to the PFMA, namely through delegations from the National Treasury. What may need to be done to ensure that provinces are able to perform their functions properly would be to check how this links up with the delegations to local government departments in provinces.

Furthermore, the FFC notes with concern that Section 12 (2) (b) does not put more emphasis on the role of provinces in building the capacity of local governments. Reference is only made to provincial government components and enterprise as well as provincial public entities. In light of the constitutional obligations on provinces to build municipal capacity and the requirements of section 139 (5), more emphasis needs to be given to local government financial management support. This will not only ensure that provinces carry out their mandate but also that provinces budget adequately for this mandate.

Chapter 5: Budgets

The commission welcomes the provisions contained in Chapter 3, especially section 44 (c) on supporting documentation for budgets. The requirements for national expenditure estimates on current year, the budget year and the two financial years following the budget year as well as last three financial years presented as actual, is a welcome improvement to the existing Act. This principle is also noted in section 68 (1) on performance plans. The FFC supports the initiative towards trend-able and quantifiable indicators.

Section 47 (1) which deals with expenditure before the annual DoR Bill is enacted is supported. The provision will help create more certainty about the equitable share as a substitute for own revenue. The FFC welcomes the fact that the risks associated with the delays in passing the Bill are transferred from sub-national to the national government.

Chapter 6: Budget Related Plans, Reports and Publications

While the FFC generally supports the provisions of section 68 (1) (f) on preparation of performance plans including "…life cycle cost of capital assets payments…", it further suggest that reference be made to the Immovable Asset Management Act, which requires a set of asset management plans for fixed assets.

Chapter 7: Intergovernmental Financial Relations

The PFM Bill addresses the promotion of intergovernmental cooperation in intergovernmental funding. The provisions generally deal with the promotion of co-operative governance, including the resolution of intergovernmental disputes, national allocations and responsibilities of receiving and transferring officers and accounting officers. These are largely drawn from the Intergovernmental Fiscal Relations (IGFR) Act and from the DoRA. The Commission supports the incorporation of these provisions into the Bill, especially because they play an important role in the promotion of fiscal prudence and financial management. However, the Commission is of the view that Section 79 (a – c) of the Bill, dealing with promotion of co-operative governance and 93 (1) on intergovernmental financial disputes could better be dealt with in the IGFR Act as they replicate that Act. The IGFR Act has been enacted specifically to fulfil the requirements of Chapter 3 of the constitution. Therefore, the Bill, instead of being overly prescriptive, should make reference to the provisions set out in the constitution and the IGFR Act, rather than repeat them.

Also included in this Chapter is what could be considered an expansion and detailed amendment of the old Section 35 provision in the PFMA (1999) for dealing with unfunded mandates. The amendments incorporate requirements of Section 3 of the FFC Act (1997) and align these with the provisions of Section 9 of the Local Government: Municipal Systems Act (2000), in order to spell out a process that has to be followed in the assignment and reassignment of functions between spheres of governments and organs of states, where such a process has financial and fiscal implications. These requirements as outlined in Section 91 of the PFM Bill are supported by the Commission. The Commission had already readied itself for this eventuality through its preparation of an instrument for the assessment of the financial and fiscal implications of such function movements.

Section 108 deals with borrowing by constitutional institutions. The provisions are new in respect of constitutional institutions and are welcome by the Commission as they will allow for more flexibility in respect of bridging finance within the appropriated funds and during a fiscal year for these Institutions, However this section should be aligned with Section 4 (2) of the Financial and Fiscal

Commission Act (1997), which prohibits the Commission from borrowing or from overdrawing its bank account.

The Commission welcomes the incorporation of key financial management principles that have been hitherto part of the DoRA . These provisions generally cover entrenched principles that have come to be accepted as the norm in the evolution of South Africa's system of fiscal decentralization and therefore can be legislated in an Act like PFMA. However, the Commission cautions that the incorporation of the principles should not be allowed to create rigidities that may stifle the implementation of government programmes at a management level, as legislation such as the PFMA can not be easily amended when problems are identified. The Commission supports the principle that the DoRA should have a primary focus on allocations among the spheres of government rather than on financial management issues.

Chapter 8: Borrowing, Guarantees and Contingent Fiscal Obligations

This chapter addresses borrowings binding national and provincial revenue funds. Of particular interest to the Commission is that the proposed amendment is intended to establish a basis for repealing the Borrowing Powers of Provincial Governments (BPPG) Act 1996, which gives effect to Section 230 of the Constitution. While this aligns the Act with the MFMA, it is not clear what the implications are for the exercising of borrowing powers by provinces. The power of a province to borrow as provided for in Section 230 of the Constitution in principle involves more than just matters of public finance management. The incorporation of the BPPG Act into the PFMA reduces the power of provinces to borrow to a mere financial management issue, rather than a deliberate policy decision that a provincial government may wish to take. While it is understandable that in the current environment, provinces have by mutual consent, decided not to exercise their borrowing powers, the future may well turn out to be different and the flexibility allowed in the BPPG Act will be completely lost. With respect to Constitutional Institutions and state-controlled institutions, the Commission supports the principles enshrined in the Act.

Chapter 9: Executive Authorities - some questions

The Commission notes and welcomes the Bill's attempt to define the Executive Authority of a Constitutional Institution. Of concern however is that the Bill designates the Speaker of the National Assembly as such Executive Authority.

Section 120(d) of the Public Finance Management Bill seeks to establish the Speaker of Parliament as the Executive Authority of Constitutional Institutions, Section 121 (1) of the Bill goes on to provide that the Executive Authority of a state or state-controlled institution must, amongst other things, provide general guidance to assist the institution in achieving the policy objectives of the Executive Authority, and that such general policy guidance must monitor and oversee the exercise of responsibilities assigned to the Accounting Officer in terms of the Bill. Section 121(2) of the Bill goes on to provide that the powers of the Executive Authority of a Constitutional Institution are limited to those that pertain to ensuring that all reporting requirements are complied with, and to assisting the National Assembly in exercising its oversight of those institutions.

The FFC notes that the primary function of an Executive Authority is to determine and monitor adherence to own policy. There is an inherent contradiction of this proposal with, for example Section 220(2) of the Constitution which establishes the FFC as an independent and impartial entity that is subject only to the Constitution and the law. This section is also not aligned to the provisions of Section 2 and Section 3 of the Financial and Fiscal Commission Act.

The Commission is of the view that the Executive Authority of a Constitutional Institution should be consistent with the spirit and letter of the Constitution. For example, the Executive Authority of the Financial and Fiscal Commission should be the Commission itself.

The current issue of concern that was raised even during the Parliamentary Review of Chapter Nine Institutions is the workability of the scenario where the Chairperson of the Commission is also the Accounting Officer. This is obviously a broader governance issue that should be addressed outside of this Act.

Chapter 10: Accounting Officers and other Officials of State Institutions

Section 134 (2) b reads as follows: an accounting officer may not "use the position and the privileges of, or confidential information used as, accounting officer for personal gain or to improperly benefit other persons". The FFC suggests that the word 'persons' should be extended to include other companies, institutions, organisations, etc.

Chapter 15: Annual Reporting

The FFC is of the view that section 243 (2) on the contents of annual reports should include specific items which parliament has requested if the purpose is to improve accountability.

Appendix C: Financial and Fiscal Commission Comments on the Local Government Laws Amendment Bill 2007

General

The Financial and Fiscal Commission, (hereafter referred to as the Commission) welcomes the opportunity to provide comments on the Local Government Laws Amendment Bill (hereafter referred to as the Bill) as required by section 229(5) of the Constitution. The Bill addresses a number of deficiencies and bottlenecks within the current legislative framework of local government.

The Commission welcomes in particular the fact that the amendments address in a very direct way some of the problems that have resulted from the lack of alignment between the municipal financial year and from changes in boundaries resulting from other pieces of legislation such as the Local Government Municipal Demarcation Act, Local Government Municipal Structures Act, etc. The Commission has in the past made recommendations on aligning legislation governing local government to the overall fiscal framework of the local government sphere. This Bill is a step in that direction.

The Commission further notes that the local government sphere has undergone (and still is undergoing) considerable transformation and that the significant amount of legislation that should be implemented places many demands on municipalities. Therefore proper alignment of the various pieces of legislation should help to ease the burden and the costs of compliance and improve service delivery.

Specific comments

Amendment of Section 23 of the Demarcation Act (1998)

1. The Commission agrees with and welcomes the amendment as the implementation of changes will take into account the commencement of a municipal financial year and therefore allow for adequate planning.

2. However, the Commission proposes that this amendment be more specific by, for example, stipulating that the determination of municipal boundaries and the authorisation of powers and functions takes effect on the date of the municipal financial year, following nine months after the publication of notice effecting such changes. The nine month period would allow for sufficient planning and ensure alignment of policy with the budget process (i.e. MTBPS of both municipalities and national government). This would prevent a situation where publication of notices is made in January when the budget process is nearly over and municipalities are two months away from

tabling of their budgets. The notice given to the Minister of Finance must also be extended to nine months in order to concur with the publication of notices

3. Furthermore, it may also be necessary for the Commission to be informed (as is the Minister) of the notice to change the boundaries in order to allow it to perform its duties in terms of the FFC Act as amended in 2003. The relevant section in the Bill is Chapter 3 (2). Changes in boundaries may result in movements of staff, assets and liabilities and may have negative or positive effects on fiscal capacity.

Amendment to the Local Government: Municipal Structures Act (1998)

1. Section 84 (4) should be amended along the same lines as 2 above.

2. Section 85 (9A) should be amended along the same lines as 2 above.

Amendments to the Local Government: Municipal Systems Act 2000

- The Commission agrees with the amendments.

Amendment to the MFMA

- The Commission agrees with the amendments.

Amendments to the Property Rates Act

- The Commission agrees with the amendments.

Copies of FFC Submission for the Division of Revenue Reports can be obtained by visiting the Commission's website at: www.ffc.co.za

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For an Equitable Sharing of National Revenue