



# Explanatory memorandum to the Division of Revenue Amendment Bill

## ■ Background

The Division of Revenue Amendment Bill (2020) (the amendment bill) is tabled as part of the special adjustments budget in response to the COVID-19 pandemic. This bill fulfils the requirement in section 12(4) of the Money Bills and Related Matters Act (2009) that the Minister of Finance must table an amendment bill with the revised fiscal framework if the adjustments budget changes the Division of Revenue Act for a given year.

By law, the bill must be accompanied by an explanatory memorandum detailing how the legislation takes account of the matters listed in section 214(2)(a) to (j) of the Constitution; government's response to the recommendations of the Financial and Fiscal Commission (FFC); and any assumptions and formulas used in arriving at the respective divisions among provinces and municipalities. Because the FFC's recommendations are specific to the main budget, and none of the formulas used in the Division of Revenue Act (2020) have been changed, this explanatory memorandum does not address these two issues. The memorandum contains two parts:

- The constitutional considerations that inform the division of resources between the three spheres of government.
- A summary of the proposed amendments to the Division of Revenue Act (2020) and their impact on national, provincial and local government.

The amendment bill and its underlying allocations are the culmination of extensive consultation processes between national, provincial and local government. The adjusted allocations have been discussed in online meetings that have been held with officials from affected national departments, provincial treasuries, provincial health departments, metropolitan municipalities, the South African Local Government Association and the FFC. The Minister of Finance has also consulted the provincial Members of the Executive Council for Finance through online meetings of the Budget Council.

## ■ Constitutional considerations

Section 214 of the Constitution requires that the annual Division of Revenue Act be enacted only after taking account of factors in sub-sections (2)(a) to (j). These include the national interest; provision for debt; the needs of national government and emergencies; the allocation of resources to provide basic services and meet developmental needs; fiscal capacity and efficiency of the provincial and local spheres;

the reduction of economic disparities; and the promotion of stability and predictability. Annexure W1 to the 2020 *Budget Review* detailed how these considerations were taken into account in the 2020 Division of Revenue Bill. None of the adjustments in the amendment bill alter the constitutional considerations that informed the 2020 division of revenue. The reprioritisation and addition of funds to respond to COVID-19 are allocated between spheres based on their respective functions and funding needs.

## ■ Summary of changes in the Division of Revenue Amendment Bill

Changes to provincial and municipal allocations made through the 2020 special adjustments budget include additions, in-year suspensions in planned expenditure and reprioritisations within existing allocations. Additional funds are allocated to the health sector in provinces and to local government to support their response to the COVID-19 pandemic. Suspensions of some conditional grant allocations in 2020/21 are necessary to release funding for the pandemic response. Grant funds that are less likely to be spent due to construction and other delays caused by the lockdown have been revised down first. Further suspensions are made where grant spending can be delayed and projects can be postponed for a year. Some suspensions will also result in the cancellation or scaling back of projects in 2020/21.

The largest adjustments are achieved through the repurposing of conditional grants already allocated to provinces and municipalities. To enable this, the conditions in the grant frameworks that were tabled as annexures to the Division of Revenue Bill (2020) in February 2020 have been amended to allow funds to be reprioritised within grants. These amendments were made with the approval of Parliament and after consultations with the national departments that are the transferring officers for each affected grant, provincial treasuries and the South African Local Government Association. The amendments are reflected in the frameworks gazetted by the Minister of Finance in terms of section 16(1) of the Division of Revenue Act (2020). The reprioritisations within direct conditional grants, which total over R7 billion for provincial grants and R9 billion for local government grants, will complement the R20 billion that provinces will reprioritise within their own budgets, funded from the provincial equitable share.

Government recognises the need to retain flexibility in its pandemic response as new hotspots emerge, and as scientific advice and regulations are updated. The conditions added to conditional grant frameworks have therefore been constructed to be enabling rather than restrictive in the spending and activities allowed. A greater degree of flexibility is also expected in how transferring national departments will consider and approve applications for revised business plans from provinces and municipalities. The reprioritised amounts within each conditional grant are estimates of the funds expected to be used for COVID-19 response activities; the actual amounts spent may differ. Provinces and municipalities are required to report on the amounts spent from each conditional grant on the COVID-19 response in the reports they submit to the National Treasury and transferring officers.

The timely release of funding is crucial in responding to a disaster. To enable this, adjustments in the amendment bill only add and reprioritise funding within existing funding instruments. This means payments can be advanced against the existing baselines of these transfers, even before the amendment bill is passed through the parliamentary process.

### Changes to provincial allocations

Provincial governments are responsible for key social services at the frontline of the pandemic response. These include the public health system, schools and social welfare services. Provinces will fund their COVID-19 response primarily through reprioritisations. They have committed to reprioritise at least R20 billion within their own budgets for this purpose. The details will be included in provincial adjustments budgets, but it is expected that at least R15 billion will be reprioritised to increase capacity in the public health system. The remaining R5 billion will be used to augment the education catch-up plan, provide social welfare support for communities, and fund responses in other sectors, including the provision of quarantine facilities by public works departments.

**Table A.1 Transfers to provinces, 2020/21**

R million	Budget 2020	Revision	Adjusted allocation	Amount repurposed within
<b>Equitable share</b>	<b>538 472</b>	–	<b>538 472</b>	<b>20 000</b>
<b>Direct conditional grants</b>	<b>110 785</b>	<b>-3 961</b>	<b>106 823</b>	<b>7 379</b>
<b>Agriculture, Land Reform and Rural Development</b>	<b>2 153</b>	<b>-438</b>	<b>1 716</b>	–
Comprehensive agricultural support programme	1 522	-317	1 205	–
Ilima/Letsema projects	549	-121	428	–
Land care programme: poverty relief and infrastructure development	82	–	82	–
<b>Basic Education</b>	<b>19 564</b>	<b>-2 349</b>	<b>17 216</b>	<b>4 540</b>
Education infrastructure	11 008	-2 221	8 787	4 400
HIV and AIDS (life skills education)	247	-60	187	40
Learners with profound intellectual disabilities	243	–	243	20
Maths, science and technology	401	-68	333	30
National school nutrition programme	7 666	–	7 666	50
<b>Cooperative Governance</b>	<b>138</b>	–	<b>138</b>	–
Provincial disaster relief	138	–	138	–
<b>Health</b>	<b>49 267</b>	<b>2 846</b>	<b>52 113</b>	<b>1 991</b>
HIV, TB, malaria and community outreach	24 387	2 846	27 233	605
Health facility revitalisation	6 368	–	6 368	1 066
National tertiary services	14 069	–	14 069	298
National health insurance grant: health professionals	289	–	289	23
Statutory human resource, training and development	4 155	–	4 155	–
<b>Human Settlements</b>	<b>17 493</b>	<b>-1 728</b>	<b>15 765</b>	<b>378</b>
Human settlements development	16 621	-1 728	14 892	–
Title deeds restoration	578	-378	200	–
Provincial emergency housing	295	378	673	378
<b>Public Works and Infrastructure</b>	<b>834</b>	–	<b>834</b>	–
Expanded public works programme integrated grant for provinces	421	–	421	–
Social sector expanded public works programme incentive for provinces	414	–	414	–
<b>Social Development</b>	<b>915</b>	–	<b>915</b>	<b>65</b>
Early childhood development	915	–	915	65
<b>Sports, Arts and Culture</b>	<b>2 076</b>	<b>-536</b>	<b>1 539</b>	<b>68</b>
Community library services	1 479	-312	1 167	10
Mass participation and sport development	597	-224	373	58
<b>Transport</b>	<b>18 343</b>	<b>-1 756</b>	<b>16 587</b>	<b>337</b>
Provincial roads maintenance	11 593	-1 756	9 837	–
Public transport operations	6 750	–	6 750	337
<b>Indirect conditional grants</b>	<b>4 060</b>	<b>202</b>	<b>4 262</b>	<b>200</b>
<b>Agriculture, Land Reform and Rural Development</b>	<b>36</b>	–	<b>36</b>	–
Ilima/Letsema indirect	36	–	36	–
<b>Basic Education</b>	<b>1 736</b>	<b>540</b>	<b>2 276</b>	–
School infrastructure backlogs	1 736	540	2 276	–
<b>Health</b>	<b>2 288</b>	<b>-338</b>	<b>1 949</b>	<b>200</b>
National health insurance indirect	2 288	-338	1 949	200

Source: National Treasury

An amount of R2.8 billion has been added to the new COVID-19 component that was created within the *HIV, TB, malaria and community outreach grant* when the frameworks were gazetted. This component complements provincial spending for the purchase of personal protective equipment and ventilators, and the hiring of additional staff, including Cuban medical personnel, to assist in responding to the additional

caseload resulting from the pandemic. The initial gazetted allocation for this component was R605 million, funded through the reprioritisation of funds from other components of the grant. This adjustment brings the total available in this component to R3.4 billion.

Suspensions of spending in provincial conditional grants total R6.8 billion in 2020/21, as shown in Table A.1. These suspensions will enable the funding of the COVID-19 response in other sectors and spheres. For the affected conditional grants, these adjustments will result in the delay of planned projects this year (some of which were already delayed due to restrictions during the lockdown).

Screening and contact tracing for COVID-19 will be supported through the community outreach services component of the *HIV, TB, malaria and community outreach grant*. About 10 000 community healthcare workers have already been trained to do this work. Provisions for this spending have already been added to the gazetted grant framework.

An amount of R4.4 billion has been reprioritised within the *education infrastructure grant*. This amount will cover the trucking of water to refill water tanks at schools, and the purchase of sanitisation materials and equipment. It will also fund salaries for temporary (2020/21 only) assistants at Expanded Public Works Programme (EPWP) rates to screen learners, and clean and sanitise school facilities. An amount of R600 million has been reprioritised from the direct *education infrastructure grant* to the indirect *school infrastructure backlogs grant*, to urgently provide potable water and safe sanitation for all schools that lack such access. After accounting for a R60 million spending suspension in this indirect grant, the net increase to the *school infrastructure backlogs grant* is R540 million. Funds from both grants can also be used to fund temporary water trucking to ensure that schools have water. Water trucking is an expensive way to supply water and so the grants also allow funds to be spent on local source development (such as drilling boreholes) and installing bulk connections to ensure a more sustainable water supply for schools.

To support catch-up activities, R30 million in the *maths, science and technology grant* and R40 million in the *HIV and AIDS (life skills education) grant* has been reprioritised. Reprioritisation in the *HIV and AIDS (life skills education) grant* can be used to provide education on measures to respond to the pandemic. Within the *learners with profound intellectual disabilities grant*, R20 million has been reprioritised for sanitisation and provision of personal protective equipment to support the provision of education to children with severe to profound intellectual disabilities. Provisions for this spending have already been added to the *education infrastructure grant*; *maths, science and technology grant*; *HIV and AIDS (life skills education) grant*; and *learners with profound intellectual disabilities grant* frameworks.

An amount of R50 million has been reprioritised within the *national school nutrition programme grant* for additional sanitisation in food preparation and distribution areas, and the provision of personal protective equipment for food handlers. If schools are closed due to a declared state of disaster, funds from the grant that would have been spent on providing school meals may be used to provide meals to learners through alternative means. Provisions for this spending have already been added to the grant framework.

The full R89 million available within the infrastructure component of the *early childhood development grant* can be used to prepare early childhood development (ECD) sites for reopening. This primarily involves providing a standard support package that includes basic health and hygiene products. Where other infrastructure projects have already been contractually committed to, the grant can be used to meet these commitments, but provinces should try to maximise the amount available to make ECD sites safe for reopening. The National Treasury estimates that at least R65 million will be used for the COVID-19 response. Provisions for this spending have already been added to the grant framework.

An amount of R10 million has been reprioritised within the *community library services grant* to sanitise libraries, provide hand sanitiser for library users and issue personal protective equipment for staff. Libraries will be deep-cleaned prior to reopening. Provisions for this spending have already been added to the gazetted grant framework.

In the *public transport operations grant*, R337 million has been reprioritised to sanitise buses and public transport facilities. This includes providing personal protective equipment for public transport workers, establishing hand-washing facilities and implementing physical distancing measures.

An amount of R378 million has been added to the *provincial emergency housing grant* to swiftly provide emergency housing solutions in areas where existing housing arrangements do not allow people to socially distance or self-isolate where required.

Some grant frameworks, where business plans could be modified to respond to activities that fall within the pandemic response, did not require amendment. These include reprioritisations of R1.1 billion within the *health facility revitalisation grant*, R298 million within the *national tertiary services grant* and R58 million within the *mass participation and sport development grant*. The *health facility revitalisation grant* will be used to provide additional capacity such as more bed space for COVID-19 patients through upgrading and refurbishing health facilities. The *national tertiary services grant* will be used to strengthen intensive-care unit capacity – for example, by procuring more specialists to respond to COVID-19 in accordance with nationally approved business plans. The *mass participation and sport development grant* will be used to provide additional support to sportspeople and support staff while sporting events are suspended. Provinces are revising the projects in their business plans for these grants to prioritise COVID-19-related projects.

The *human settlements development grant* continues to provide access to water and sanitation through the delivery of housing and upgrading informal settlements (including in mining towns).

### **Changes to local government allocations**

In his 21 April 2020 speech, the President said that additional funding of R20 billion would be made available to municipalities to provide emergency water supply, increase sanitisation of public transport and facilities, and provide food and shelter for the homeless. This amount will consist of R11 billion in additions through the local government equitable share, and over R9 billion in repurposed spending within conditional grants already allocated to municipalities.

To assist the municipal pandemic response, R11 billion has been added to the local government equitable share. These funds will allow municipalities to maintain existing services despite a temporary decline in revenue collections. They will also cover some additional expenses incurred in responding to the pandemic, including providing temporary shelter for homeless people during the lockdown. These additions have been factored into the basic services component by increasing the number of poor households by 13.9 per cent and increasing the community services component by 41.5 per cent. The increase in the basic services component amounts to R7.5 billion. As a result, an additional 1.4 million poor households can be provided with free basic services, up from 10.4 million households in the 2020 Budget, if they become indigent as a result of a loss of income during the pandemic.

The community services component of the equitable share increases by R3.5 billion. The revenue adjustment factor that is applied to this component of the equitable share formula ensures that this increase will benefit poor and rural municipalities with little capacity to raise own revenue. The total allocation for the community services component increased by 32 per cent. This component funds a range of services that are part of the pandemic response, including municipal health services, and services to cemeteries and crematories. Details about the structure of the components of the local government equitable share formula can be found in Annexure W1 of the 2020 *Budget Review*.

Local government conditional grant allocations amounting to R4.6 billion have been suspended in 2020/21, as shown in Table A.2. This includes R3.6 billion from direct conditional grants and R1 billion from indirect grants. These suspensions will enable the funding of the COVID-19 response, including through additions to the local government equitable share. For the affected conditional grants, these adjustments will result in the delay of planned projects this year (some of which were already delayed due to restrictions during the lockdown).

**Table A.2 Transfers to local government, 2020/21**

R million	Budget 2020	Revision	Adjusted allocation	Amount repurposed within
<b>Equitable share</b>	<b>74 683</b>	<b>11 000</b>	<b>85 683</b>	<b>–</b>
<b>Direct conditional grants</b>	<b>43 819</b>	<b>-3 599</b>	<b>40 219</b>	<b>9 034</b>
Municipal infrastructure	14 671	–	14 671	4 401
Integrated urban development	948	–	948	190
Urban settlements development	11 282	-1 100	10 182	2 257
Integrated city development	317	–	317	–
Public transport network	6 446	-1 902	4 544	1 096
Neighbourhood development partnership	559	-68	492	–
Integrated national electrification programme	1 859	-500	1 359	–
Rural roads asset management systems	108	–	108	–
Regional bulk infrastructure	2 006	–	2 006	401
Water services infrastructure	3 445	–	3 445	689
Municipal disaster relief	354	–	354	–
Energy efficiency and demand-side management	218	-22	196	–
Municipal emergency housing	159	–	159	–
Infrastructure skills development	153	-8	146	–
Local government financial management	545	–	545	–
Expanded public works programme integrated grant for municipalities	748	–	748	–
<b>Indirect conditional grants</b>	<b>7 628</b>	<b>-1 008</b>	<b>6 620</b>	<b>409</b>
Integrated national electrification programme	3 001	-1 000	2 001	–
Neighbourhood development partnership	63	–	63	–
Water services infrastructure	579	–	579	–
Regional bulk infrastructure	3 857	–	3 857	409
Municipal systems improvement	128	-8	120	–

Source: National Treasury

Amounts of R190 million and R4.4 billion have been reprioritised within the *integrated urban development grant* and the *municipal infrastructure grant* respectively. These general infrastructure grants are allocated to non-metropolitan municipalities. These funds are to be used for urgent repairs and refurbishment of water and sanitation infrastructure to restore functionality (municipalities may spend up to 10 per cent of their total grant allocation on this). Municipalities may also use these funds to repair municipal-owned infrastructure identified for quarantine sites (limited to repairs to existing facilities, not modifications and operational costs). Municipalities are also expected to prioritise the provision of basic water and sanitation supplies. Each municipality may also use up to 10 per cent of its grant allocation for sanitisation of public transport facilities and other municipal public facilities. This includes provision for temperature scanners, hand-washing facilities, hand sanitiser, personal protective equipment for municipal and public transport workers, and physical distancing measures.

For metropolitan municipalities, R2.3 billion has been reprioritised within the *urban settlements development grant*. This amount will fund the provision of water and sanitation to communities that lack access, and higher frequency and/or standards of services in informal settlements. The funds may be used to provide temporary relocation areas in line with the requirements of the housing code. Local governments may also use the funds to repair municipal-owned infrastructure identified for quarantine sites (limited to repairs to existing facilities, not modifications and operational costs).

For the 10 cities that receive the *public transport network grant*, the sanitisation of public transport facilities is funded through the reprioritisation of R1.1 billion within the grant. Municipalities may use up

to 25 per cent of their allocations to sanitise such facilities, provide personal protective equipment to public transport workers, arrange for hand-washing facilities and implement physical distancing measures.

Reprioritisations of R401 million within the direct *regional bulk infrastructure grant*, R409 million within the indirect *regional bulk infrastructure grant* and R689 million within the *water services infrastructure grant* will fund the purchase and installation of water tanks, and the trucking of water to refill tanks for up to three months. Funds will also be used to implement source development or bulk linkage projects to replace the need for water trucking. Provisions for this reprioritised spending within local government conditional grants have already been added to the gazetted grant frameworks.

Details of the changes to allocations per municipality and changes to gazetted allocations for provincial conditional grants are contained in the annexures and appendices to the amendment bill.

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