W1

Website annexure to the 2010 Budget Review

Explanatory memorandum to the division of revenue

Background

The allocation of resources to the three spheres of government is a critical step in the budget process, required before national government, nine provinces and 283 municipalities can determine their own budgets. The allocation process takes into account the powers and functions assigned to the three spheres of government. The process for making this decision is at the heart of cooperative governance as envisaged in the Constitution.

To foster transparency and ensure smooth intergovernmental relations, section 214(1) of the Constitution requires that every year a Division of Revenue Act determine the equitable division of nationally raised revenue. The Intergovernmental Fiscal Relations Act (1997) prescribes the process for determining the equitable sharing and allocation of revenue raised nationally. Sections 9 and 10(4) of the Act set out the consultation process to be followed with the Financial and Fiscal Commission (FFC), including the process of considering recommendations made with regard to the equitable division of nationally raised revenue.

This explanatory memorandum to the 2010 Division of Revenue Bill fulfils the requirement set out in section 10(5) of the Intergovernmental Fiscal Relations Act that requires the Division of Revenue Bill to be accompanied by an explanatory memorandum detailing how the bill takes account of the matters listed in sections 214(2)(a) to (j) of the Constitution, government's response to the recommendations of the FFC, and any assumptions and formulas used in arriving at the respective divisions among provinces and municipalities. This explanatory memorandum contains six parts:

- Part 1 lists the factors that inform the division of resources between the three spheres of government.
- Part 2 describes the 2010 division of revenue.
- Part 3 sets out how the FFC's recommendations on the 2010 division of revenue have been taken into account.
- Part 4 explains the formula and criteria for the division of the provincial equitable share and for conditional grants to provinces.
- Part 5 sets out the formula and criteria for the division of the local government equitable share and conditional grants among municipalities.
- Part 6 summarises issues that will form part of subsequent reviews of provincial and local government fiscal frameworks.

The Division of Revenue Bill and its underlying allocations are the culmination of extensive consultation processes between national, provincial and local government. The Budget Council deliberated on the matters discussed in this memorandum at its August 2009 lekgotla and at several other meetings during the year. The approach to local government allocations was discussed with organised local government at technical meetings with the South African Local Government Association (SALGA), culminating in a meeting of the Budget Forum (Budget Council plus SALGA) on 12 October 2009. An extended Cabinet meeting involving ministers, provincial premiers and the chairperson of SALGA on 14 October 2009, agreed on the division of revenue for the next three years.

Part 1: Constitutional considerations

Section 214 of the Constitution requires that the annual Division of Revenue Act be enacted only after account is taken of factors in subsections (2)(a) to (j) of the Constitution. These include national interest, provision for debt, 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, reduction of economic disparities, and promotion of stability and predictability. The constitutional principles taken into account in deciding on the division of revenue are briefly noted below.

National interest and the division of resources

The national interest is encapsulated by those governance goals that benefit the nation as a whole. The spending priorities that inform the medium-term expenditure framework (MTEF) are: expanding employment and safeguarding social security; improving the quality of education and skills development; enhancing the quality of health care; rolling out a comprehensive rural development strategy and creating a built environment to support economic growth. Programmes directed towards these purposes cut across all spheres of government and are largely coordinated by national government.

Provision for debt costs

The resources shared among the three spheres of government include proceeds from national government borrowing used to fund spending by all spheres. National government provides for the resulting debt costs to protect the integrity and credit reputation of the country.

National government's needs and interests

The Constitution assigns exclusive and concurrent powers and functions to each sphere of government. National government is exclusively responsible for functions that serve the national interest and are best centralised. For the division of revenue, national government priorities were taken into account.

Provincial and local government basic services

Provinces and municipalities are assigned key service delivery functions such as school education, health, social development, housing, roads, provision of electricity, water and municipal infrastructure. They have significant autonomy to allocate resources to meet basic needs and respond to provincial and local priorities, while at the same time giving effect to nationally agreed priorities. The division of revenue provides equitable shares to provinces and local government. This year's division of revenue takes explicit account of cost pressures relating to occupation-specific dispensation (OSD) agreements in the health and education sectors, policies on HIV and Aids treatment, and pressures that affect the provision of housing and certain education services. The division of revenue also reinforces government's commitment to free basic services at the municipal level through a substantial increase to the local government equitable share. This increase will help enable municipalities to deal with the increased cost pressures of providing free basic services due to increased electricity charges, as well as the expansion of free basic services to poor households.

Fiscal capacity and efficiency

The Constitution assigns the primary government revenue-raising power to the national sphere. Provinces have limited revenue-raising capacity relative to the resources required to deliver provincial functions that do not lend themselves to self-funding or cost recovery. Local governments finance most of their expenditure through property rates, user charges and fees. It is recognised, however, that rural municipalities raise significantly less revenue than larger urban and metropolitan municipalities. To compensate for this, provinces receive the largest share of nationally raised revenue, and local government a portion that is substantial and which has been revised upwards substantially over the medium term. The provincial equitable share formula will be reviewed during 2010 for implementation during 2011. A review of the local government equitable share is also being undertaken. Both reviews should result in recommendations of substantial changes to the financing of existing functions.

Developmental needs

Developmental needs are encapsulated in the equitable share formulas for provincial and local government, and in specific conditional grants. In particular, the various infrastructure grants and growing capital budgets aim to boost the economic and social development of provinces and municipalities. Developmental needs are accounted for at two levels: firstly, in the determination of the division between the three spheres, which explains the strong growth in the provincial and local government shares of nationally raised revenue, and secondly, in the determination of the division within each sphere, through the formulas used for dividing national transfers among municipalities and provinces.

Economic disparities

Both the equitable share and infrastructure grant formulas are redistributive towards poorer provinces and municipalities. Government continues to invest in economic infrastructure like roads, and social infrastructure like schools, hospitals and clinics to stimulate economic development and job creation, and address economic and social disparities.

Obligations in terms of national legislation

While the Constitution confers autonomy on provincial governments to determine priorities and allocate budgets, national government retains responsibility for policy development, national mandates and the monitoring of implementation for concurrent functions. New national mandates and priorities result in increased allocations to provincial and local government over the 2010 MTEF baseline allocations. In particular, the 2010 MTEF and division of revenue provide funding to cover the cost of OSD agreements in health and education and the implementation of HIV and Aids treatment policies.

Predictability and stability

Provincial and local government equitable share allocations are based on estimates of nationally raised revenues. These allocations are protected. In the event that nationally raised revenue falls short of the estimates, the equitable share will not be adjusted downwards. Allocations are assured (voted, legislated and guaranteed) for the first year and are transferred according to a payment schedule. To contribute to longer-term predictability and stability, forward estimates for a further two years are published alongside the annual proposal for appropriations.

Need for flexibility in responding to emergencies

Government has flexibility to respond to emergencies through a contingency reserve that provides a cushion for emergencies and unforeseeable events. Sections 16 and 25 of the Public Finance Management Act make specific provision in relation to allocation of funds to deal with emergency situations, while section 30(2) deals with adjustment allocations in respect of unforeseeable and unavoidable expenditure. Section 29 of the Municipal Finance Management Act allows a municipal mayor to authorise unforeseeable and unavoidable expenditure in an emergency of extraordinary circumstances.

Part 2: The 2010 division of revenue

The 2010 medium-term expenditure framework (MTEF) takes into account the important developmental role played by provincial and local government, and continues to strengthen their ability to provide social and municipal basic services and perform their constitutional functions. Over the next three years, however, all spheres of government must identify cost savings, eliminate non-essential expenditure and prioritise high-priority programmes over lower-priority ones.

Excluding debt service costs and the contingency reserve, allocated expenditure to be shared between the three spheres amounts to R740.8 billion, R787.9 billion and R836.3 billion over each of the MTEF years. These allocations take into account government's spending priorities, the revenue-raising capacity and functional responsibilities of each sphere, and inputs from various intergovernmental forums and the recommendations of the FFC. Further, the design of the equitable share formulas for both provincial and local governments are such that these spheres have desirable, stable and predictable revenue shares, and economic and fiscal disparities are addressed.

Government's policy priorities for the 2010 MTEF

Government's major budget priorities over the MTEF include:

- Support job creation, moving resources towards labour intensive sectors and the expanded public works programme
- Enhance the quality of education and skills development, focusing on improving foundation phase literacy and numeracy, and on increasing the number of learners passing grade 12 mathematics and science
- Improve the provision of quality health care, with particular emphasis on reducing infant, child and maternal mortality rates, and broadening access to antiretroviral and tuberculosis treatment
- Carry out comprehensive rural development linked to land and agrarian reform
- Intensify the fight against crime and corruption

Government will continue to invest in the built environment and infrastructure over the next three years to promote access to basic services, to expand public transport and to build more schools and hospitals. These investments will support the economy's ability to grow more rapidly in future.

The division of revenue for the 2010 MTEF is supportive of pro-poor policy programmes, and in the light of the prevailing economic climate, all spheres of government are required to seek efficiency gains and shift their funding towards core government priorities. Additional resources are allocated to provinces to ensure better service conditions for teachers, doctors and therapists so as to retain skilled and experienced practitioners in these sectors. Changes are made to baselines allocated to HIV and Aids treatment to ensure the announcements made by the President on World Aids Day during December 2009 are adequately funded. Resources have also been added to the local government equitable share over the medium term to soften the impact on the poor of rising electricity prices.

Sustained economic growth over the past decade and increased migration from rural areas have contributed to significant changes in South Africa's cities. Rapid urbanisation has brought about greatly increased demands for land, housing, water and sanitation, electricity and transport in large towns. Infrastructure and service-delivery functions need to interact effectively to promote efficiency, employment and integrated development.

Table W1.1 shows how the additional allocations are apportioned to the priority areas across the three spheres of government.

Table W1.1 2010 Budget priorities – additional MTEF allocations, 2010/11 – 2012/13

R million	2010/11	2011/12	2012/13	Total
Provincial equitable share	6 400	7 000	7 600	**21 000**
Includes general adjustment and wage increases				
Compensation of employee adjustments	3 600	4 000	4 400	**12 000**
Social grants	1 785	3 598	6 809	**12 192**
Education and skills development				
Workbooks	750	930	1 000	**2 680**
Dinaledi schools	–	70	100	**170**
Higher education subsidies	–	300	700	**1 000**
Further education and training colleges grant	400	430	450	**1 280**
Occupation-specific dispensation for educators	3 000	3 000	3 000	**9 000**
Health care				
Comprehensive HIV and Aids grant	1 700	2 800	3 900	**8 400**
Hospital revitalisation grant	140	–	–	**140**
Occupation-specific dispensation for health professionals	1 281	1 302	1 324	**3 907**
Justice, crime prevention and policing				
Additional policing personnel	200	230	250	**680**
Military skills development system	50	70	100	**220**
New SA National Defence Force remuneration system	600	730	850	**2 180**
Implementation of Children's Act, Child Justice Act and Sexual Offences and Related Matters Act	30	60	90	**180**
Landward defence modernisation	–	100	500	**600**
Occupation-specific dispensation for correctional services workers	300	300	300	**900**
Rural development				
Rural development	260	300	300	**860**
Land Bank recapitalisation	750	750	–	**1 500**
Job creation, infrastructure and environment				
Expanded public works programme incentive	567	800	1 100	**2 467**
Clothing and textile production incentive	400	600	750	**1 750**
Automotive production and development programme	450	600	700	**1 750**
Regional bulk infrastructure	54	200	300	**554**
Municipal infrastructure grant	–	–	2 500	**2 500**
Public transport, roads and rail infrastructure	468	1 052	1 329	**2 849**
Transnet fuel pipeline	1 500	1 500	1 500	**4 500**
Human settlements and local government				
Rural households infrastructure grant	100	350	750	**1 200**
Human settlements development grant	–	–	1 000	**1 000**
Local government equitable share	900	2 050	3 750	**6 700**
Other adjustments	2 145	2 134	3 793	**8 072**
Total	**27 831**	**35 256**	**49 144**	**112 231**

The fiscal framework

Table W1.2 presents medium-term macroeconomic forecasts for the 2010 Budget. It sets out the growth assumptions and fiscal policy targets on which the fiscal framework is based.

Table W1.2 Medium-term macroeconomic assumptions, 2009/10 – 2012/13

	2009/10		2010/11		2011/12		2012/13
R billion	**2009 Budget**	**2010 Budget**	**2009 Budget**	**2010 Budget**	**2009 Budget**	**2010 Budget**	**2010 Budget**
Gross domestic product	2 474.2	2 449.9	2 686.3	2 699.9	2 953.0	2 967.6	3 295.7
Real GDP growth	*1.4%*	*-1.5%*	*3.4%*	*2.9%*	*4.1%*	*3.4%*	*3.6%*
GDP inflation	*5.9%*	*7.2%*	*5.0%*	*7.1%*	*5.6%*	*6.3%*	*7.2%*
National budget framework							
Revenue	643.0	571.5	709.1	643.2	781.2	721.7	807.9
Percentage of GDP	*26.0%*	*23.3%*	*26.4%*	*23.8%*	*26.5%*	*24.3%*	*24.5%*
Expenditure	738.6	748.8	792.4	818.1	849.0	888.3	964.3
Percentage of GDP	*29.9%*	*30.6%*	*29.5%*	*30.3%*	*28.7%*	*29.9%*	*29.3%*
Main budget balance[1]	-95.6	-177.3	-83.3	-174.9	-67.7	-166.6	-156.4
Percentage of GDP	*-3.9%*	*-7.2%*	*-3.1%*	*-6.5%*	*-2.3%*	*-5.6%*	*-4.7%*

1. A positive number reflects a surplus and a negative number a deficit.

Table W1.3 sets out the division of revenue for the 2010 MTEF after taking into account new policy priorities.

Table W1.3 Division of revenue between spheres of government, 2006/07 – 2012/13

R million	**2006/07**	**2007/08**	**2008/09**	**2009/10**	**2010/11**	**2011/12**	**2012/13**
		Outcome		**Revised estimate**		**Medium-term estimates**	
State debt cost	52 192	52 877	54 394	57 600	71 358	88 463	104 022
Non-interest expenditure	418 000	488 619	581 670	691 217	746 785	799 875	860 292
Percentage increase	*14.3%*	*16.9%*	*19.0%*	*18.8%*	*8.0%*	*7.1%*	*7.6%*
Total expenditure	**470 192**	**541 496**	**636 063**	**748 816**	**818 143**	**888 338**	**964 314**
Percentage increase	*12.8%*	*15.2%*	*17.5%*	*17.7%*	*9.3%*	*8.6%*	*8.6%*
Contingency reserve	–	–	–	–	6 000	12 000	24 000
Division of revenue between spheres							
National departments	210 172	242 632	289 346	346 103	359 106	370 688	393 757
Provinces	181 328	208 666	248 286	294 968	322 858	350 547	369 348
Equitable share	*149 246*	*171 054*	*201 796*	*236 878*	*260 974*	*280 689*	*294 780*
Conditional grants	*32 082*	*37 612*	*46 491*	*53 890*	*61 884*	*69 858*	*74 568*
Gautrain loan	–	–	–	*4 200*	–	–	–
Local government	26 501	37 321	44 037	50 146	58 821	66 640	73 187
Equitable share[1]	*18 058*	*20 676*	*25 560*	*24 356*	*30 168*	*33 940*	*37 234*
General fuel levy sharing with metropolitan municipalities	–	–	–	*6 800*	*7 542*	*8 531*	*8 958*
Conditional grants	*8 443*	*16 645*	*18 477*	*18 990*	*21 111*	*24 169*	*26 995*
Total	**418 000**	**488 619**	**581 670**	**691 217**	**740 785**	**787 875**	**836 292**
Percentage shares							
National departments	*50.3%*	*49.7%*	*49.7%*	*50.1%*	*48.5%*	*47.0%*	*47.1%*
Provinces	*43.4%*	*42.7%*	*42.7%*	*42.7%*	*43.6%*	*44.5%*	*44.2%*
Local government	*6.3%*	*7.6%*	*7.6%*	*7.3%*	*7.9%*	*8.5%*	*8.8%*

1. With effect from 2006/07, the local government equitable share includes compensation for the termination of Regional Services Council (RSC) and Joint Services Board (JSB) levies for metros and district municipalities. From 2009/10 the RSC levies replacement grant will only be allocated to district municipalities.

Table W1.4 shows how additional resources are divided among the three spheres of government. The new priorities and additional allocations are accommodated through shifting of savings towards priorities.

Table W1.4 Changes over baseline, 2010/11 – 2012/13[1]

R million	2010/11	2011/12	2012/13
National departments	6 592	9 689	16 923
Provinces	13 209	14 607	17 756
Local government	938	1 676	5 269
Allocated expenditure	**20 739**	**25 972**	**39 948**

1. Excludes shifting of savings towards priorities to the amount of R25.6 billion over the MTEF.

Table W1.5 sets out Schedule 1 of the Division of Revenue Bill, which reflects the legal division of revenue between the three spheres. In this division, the national share includes all conditional grants to the other two spheres in line with section 214(1) of the Constitution, and the provincial and local government allocations reflect their equitable shares only.

Table W1.5 Schedule 1 of the Division of Revenue Bill, 2010/11 – 2012/13

	2010/11	2011/12	2012/13
	Column A	Column B	
R million	Allocation	Forward estimates	
National[1, 2]	527 001	573 709	632 299
Provincial	260 974	280 689	294 780
Local	30 168	33 940	37 234
Total	**818 143**	**888 338**	**964 314**

1. National share includes conditional grants to provinces and local government, general fuel levy sharing with metropolitan municipalities, debt service cost and the contingency reserve.

2. The direct charges for the provincial equitable share are netted out.

The 2010 *Budget Review* sets out in detail how the constitutional issues and government's priorities are taken into account in the 2010 division of revenue. It focuses on the economic and fiscal policy considerations, revenue issues, debt and financing considerations, and expenditure plans of government. Aspects of national, provincial and local government financing are discussed in some detail in Chapters 8 and 9. For this reason, this memorandum should be read with the 2010 *Budget Review*.

Part 3: Response to the recommendations of the FFC

Section 214 of the Constitution and section 9 of the Intergovernmental Fiscal Relations Act (1997) require the FFC to make recommendations in April every year, or soon thereafter, on the division of revenue for the coming budget. The FFC complied with this obligation by tabling its *Submission for the Division of Revenue 2010/11* to Parliament in May 2009. This part of the explanatory memorandum complies with the Constitution and section 10 of the Intergovernmental Fiscal Relations Act by setting out how government has taken into account the FFC's recommendations when determining the division of revenue for the 2010 MTEF.

The 2010/11 recommendations are divided into eight chapters covering a wide range of issues across the three spheres.

Chapter 1: Review of the provincial equitable share (PES) formula

The FFC's recommendations on the provincial equitable share formula deal with principles, as well as short- and medium-term solutions to the reform of the formula.

Principles

The FFC recommends that there should be clarity on expenditure assignments between provinces and national government, especially distinguishing between delegated and own or devolved responsibilities of the provincial governments. More emphasis should also be placed on exclusive assignments, as opposed to concurrent assignments, to increase accountability. There should be a clear separation of instruments in the transfer system. The following principles should be observed: (a) the equalisation grant should equalise on the basis of expenditure need; (b) there is a need to establish a performance-based conditional grant system; and (c) there is a need for other transfers for regional development. Provinces should be encouraged to exercise their legislative revenue powers. Further, provincial borrowing should be carefully facilitated and linked to their revenue-raising capacity to close the infrastructure gap.

Option 1: The short-term solution

The FFC recommends that the reform of the provincial equitable share formula stays within the confines of the current constitutional dispensation. The provincial equitable share formula should retain for the most part its current structure, and only be reformed to bring it closer to a conventional equalisation grant, which equalises both expenditure and revenue. The provincial equitable share formula should be divided into a number of components in pursuit of clear and separate objectives as follows:

- The economic activity component should be removed to become a straightforward conventional form of revenue sharing, allocated either on a derivation basis or some other criterion such as share of gross domestic product.
- A component dealing with a system of conditional capital grants, mainly targeting backlogs in capital infrastructure and capital investment needs of provinces, especially for those that are not expected to be financed through borrowing, and which should build on current infrastructure grants for provinces.
- A component dedicated to implementing a system of unconditional equalisation grants, taking into account differences in expenditure needs and fiscal capacity. The latter assumes that none of the expenditure assignments to the provincial governments (and in particular, education, health, and social welfare) are delegated. This would allow provinces complete autonomy to set priorities within the parameters of the Constitution, i.e. respecting the role of national government. An incentive system of matching grants should be developed to support the implementation of national priorities.

Institutional weakness in the budget process should be addressed as a matter of urgency to enhance cooperation between the national and provincial spheres, improve the enforcement of norms and standards and increase the capacity of national departments to monitor and build capacity of provincial counterparts. The role of the FFC, as defined in the Constitution, should be strengthened within the institutions dealing with division of revenue matters.

Option 2: The medium- to long-term solution

The FFC recommends that the reform should depart from the realisation that fixing the provincial equitable share as a pool requires the fixing of other aspects of the current fiscal decentralisation system. The reform of the provincial equitable share will require the reform of current expenditure and revenue assignment between the national and provincial governments. The implementation of this option will require significant changes in the current legislation and amendments to Schedules 4 and 5 of the Constitution to enable the conversion of several functions into delegated functions. This option should be considered with utmost caution owing to the inherent risks related to transition costs and the potential to compromise service delivery. It will be necessary to have a dedicated intergovernmental committee that will oversee and manage the transition process as well as identify potential risks.

The FFC recommends that the education and health services should be taken out of the provincial equitable share, and that those components be converted into separate block: conditional grants from the national government to provinces. Under a block grant, the provincial governments will have the obligation to spend the grant in the particular expenditure area (for example, primary education) but they will also be free to determine how the funds are used within that area. Education and health will remain concurrent responsibilities of the national government and the provinces. In the reformed expenditure assignment system, these services will be explicitly recognised as "delegated" responsibilities from the national government to provinces. Under this redefinition, the national government will have explicit responsibility for securing adequate funding on behalf of the provinces for the provision of these services. Provincial governments will use their discretion to add their own funds for improved financing and speeding up service delivery. The national government will also have responsibility for establishing performance standards for the delegated services. The necessary level of funding for the delegated responsibilities in education and health will be determined in the annual budget of the national government, by using financial per client norms or any other expenditure quantification criteria. The quantification of expenditure needs can be improved by adjusting the norms for differences in the costs of provision across jurisdictions.

The FFC also recommends that the "economic activity" component be removed from the provincial equitable share formula and be converted into a revenue-sharing pool. Also, the revenue autonomy of provincial governments should be increased by fully implementing the provisions of section 228 of the Constitution and the Provincial Tax Regulation Process Act (2003).

Lastly, an equalisation grant with the following features should be introduced: (a) a predetermined fixed funding rule, which allows beneficiary provinces to anticipate and plan, based on funding that will be available from this grant from year to year; and (b) a distribution formula for the available funds, proportionate to the fiscal gap computed for each province, on the basis of the difference between allowable expenditure needs and fiscal capacity. Unlike the first option, expenditure will be a derivative of all expenditure responsibilities for provinces other than the delegated responsibilities (education and health) which are already minimally financed by the block grants.

Government response

In 2007, government endorsed a comprehensive review of the provincial equitable share formula. A task team consisting of the FFC, National Treasury, provincial treasuries and relevant sector departments is conducting this review and should complete its work in time for the 2011 MTEF. The recommendations of the FFC will be considered as part of this review.

Chapter 2: Public infrastructure investment

The FFC recommends that increased funding be directed to infrastructure programmes that are linked to basic services including water, health, electricity, roads, transport and communication. For funds already in the system, government should improve the quality of targeted outcomes of infrastructure investment towards employment creation and poverty reduction. Leveraging from efficiency gains throughout all baselines of departments should be made an ongoing exercise, as it strengthens the link between planning and spending, especially within the provincial sphere of government.

The FFC also recommends that government should implement a fully comprehensive national infrastructure maintenance strategy, especially for those infrastructure classes with a high impact on unemployment and poverty, with dedicated maintenance objectives. To achieve sustainable outcomes, the government must improve management of infrastructure investment by building in/safeguarding adequate future lifecycle replacement and maintenance provision for the infrastructure. Government should develop appropriate funding mechanisms through intergovernmental coordination to facilitate, integrate and sequence infrastructure planning and delivery.

Government response

Government agrees that investment should be targeted towards infrastructure that supports basic needs. Informed by the medium-term strategic framework (MTSF), which covers the period 2009-2014, government will continue with the infrastructure investment programme aimed at expanding and improving social and economic infrastructure to increase access, quality and reliability of public services. This will boost economic activity and create jobs.

Infrastructure expenditure continues to be one of the fastest-growing items in provincial and municipal expenditure. Provinces will spend R146.4 billion on education, health, roads and agriculture infrastructure over the next three years. Municipalities will spend R147.8 billion on infrastructure that supports basic services, roads and housing over the next three years.

Government is also taking active steps to ensure that these large investments result in increased access to quality services. Through the Siyenza Manje and IDIP programmes, government aims to improve infrastructure management. This includes ensuring that budgeting for infrastructure includes full lifecycle costing.

Chapter 3: Efficiency and equity effects of social grants

The FFC recommends that government should increase the rollout of social grants to cushion poor people from the effects of the economic downturn. There is, however, a trade-off between coverage and grant amounts given limited resources. Past experience at provincial level has illustrated that increases in social grants may crowd out other forms of social expenditure. Social assistance should be managed in such a way as to eventually reduce dependency on the social grants. Fiscal sustainability of scaling up conditional cash transfers needs to be carefully managed. As a starting point, social grants on the demand-side appear to be working well and can be scaled up in the short term, but those on the supply side are not working well and will need to be scaled down. Government should use infrastructure expansion to provide opportunities for workfare programmes, and consider an immediate pilot of workfare in the expanded public works programme.

Government response

Government agrees that the social grants system should be managed in a manner that does not compromise fiscal sustainability. Social grants are an important mechanism to cushion the most vulnerable in times of economic contraction. Government has succeeded in containing the cost of the social grant system without compromising coverage and crowding out other areas of spending.

In addition through its large capital investments and expanded public works programme, government is taking active steps to increase employment.

Chapter 4: Performance of public hospitals

The FFC recommends that while recognising the provisions of the National Health Act (2004) and current norms guiding the primary health care system, there is a policy gap in respect of legislative provisions and norms and standards for a well-functioning public hospital system. To close the gap, government must develop norms and standards that should address the following issues in relation to the public hospital system: (a) specification of minimum service requirements; (b) establishment of minimum input norms; (c) establishment of a workable quality assurance framework; (d) establishment of a transparent reporting system focusing on inputs, processes, outputs, and outcomes; (e) identification of governance requirements; (f) establishment of governance norms and standards; (g) establishment of a strategic planning framework which outlines the medium/long-term vision of the hospital system, expressed in terms that are implementable and auditable; and (h) development of hard (codified by legislation) and soft (guidelines to aid departments) norms and standards. Provinces should be allowed to contextualise soft norms and standards which suit their needs/socio-economic circumstances. Government needs to standardise and institutionalise budget format processes across all hospitals. Consistent with hard norms and standards, allocations should be determined by differentiating by hospital type: central, regional and district hospitals; acute psychiatric and chronic hospitals; and infectious disease hospitals.

Government response

The recommendations are in line with Government's vision to improve the country's entire health system. The Department of Health's 2009/10 strategic plan offers a comprehensive set of programmes intended to overhaul the health system, with public hospitals a key area of focus. Factors such as norms and standards, enhanced management and training, delegation of authority, appropriate levels of autonomy, human resources for health, quality assurance, quality improvement and monitoring will be looked at. Although the Department of Health recognises that norms and standards are an important tool in reforming the health system, it is important that these norms and standards be informed by the available resource envelope.

Chapter 5: Rental Housing

Relaxation and flexibility

The FFC recommends relaxation of and flexibility towards the (a) eligibility criteria for accessing the *social housing capital restructuring grant* to allow projects falling outside the designated restructuring zones (DRZs) to access funding; (b) number of DRZs to respond to excess demand for rental housing; and (c) minimum unit size for redevelopments of existing buildings. The process of disbursing funds for rental housing within the housing sector should be made shorter to minimise time lags following the submission of approved project plans.

Government response

The social housing programme is a targeted programme – rather than a mass housing delivery programme – with specific restructuring objectives. The restructuring aims to facilitate the further provision of rental accommodation by the private sector in areas where no or minimal investment in rental housing is occurring, but it is required.

The Social Housing Regulatory Authority and inter-sectoral coordination

The FFC recommends that the Social Housing Regulatory Authority (SHRA) should improve the inter-sectoral coordination between departments responsible for integrated human settlement.

Government response

The SHRA was established to focus on the regulation of the social housing sector to protect government's investment in rental housing. In terms of the Social Housing Act and the Rental Housing Act, national government should ensure that national departments and all spheres of government are aligned to enable and support the development of rental/social housing.

Qualifying income bands

The FFC recommends that the qualifying income bands should be reviewed to ensure that individuals are not unfairly excluded from benefiting from the subsidy (due, for example, to increases in the cost of living).

Government response

Government acknowledges that there is great demand and need for affordable rental housing. It is important to note that the institutional subsidy qualifying criteria does not apply when the SHRCG is used in the social housing programme. There are, however requirements to ensure that government's investment does benefit targeted income groups (those below R3 500-R1 500) through cross-subsidisation with middle- and higher-income groups.

Chapter 6: Management and financing of road infrastructure

The FFC recommends that there should be an increased and stable flow of funds for maintenance, rehabilitation and addressing road infrastructure backlogs in the long-term. Potential policy proposals to ensure that this is achieved can include explicitly providing for a road infrastructure component within the provincial equitable share formula.

There should be greater coordination of road management functions across the three spheres of government. In this regard, the revision and modification of the inter-road authority coordinating model by the national Department of Transport, which proposed a roads coordinating body comprised of metropolitan municipalities, district municipalities, local municipalities and SALGA should be carried out with a view to possible future implementation. Priority should be given to addressing the lack of technical skills in the road management sector of sub-national governments. Attaining this objective can be done via the introduction of a separate conditional grant specifically targeted at building technical capacity within the road management sector of sub-national governments.

Government response

This proposal will be dealt with as part of the review of the provincial equitable share formula.

The proposal to expand the existing Roads Coordinating Body (RCB) may have merit as it could improve intergovernmental coordination and resolve issues such as Roads Infrastructure Framework of South Africa (RIFSA). Including metros and SALGA seems realistic, but including all municipalities may not be viable logistically. Funding through a separate grant should not be necessary as capacity building and staff development should be part of the department's budget already. Government, through its IDIP and Siyenza Manje programmes, is stepping up efforts to build infrastructure capacity in provinces and municipalities.

Chapter 7: Assessment of universal access to water and sanitation services

Free basic water and sanitation subsidy

The FFC recommends a review of free basic water and sanitation subsidy and water tariff structures, to ensure that the shortcomings of the current subsidy system do not outweigh the benefits. At present, there is no coherent oversight framework for how water service authorities manage trade-offs in the design and determination of their water tariffs. The tariff structures, which vary across municipalities, have a substantial impact on the pricing of water. Principles and practices guiding both tariff and subsidy structures and price levels should be made clear and routinely monitored.

Government response

Government agrees with the proposal for a review of the water tariff structures. Specific legislation, regulations, policies and guidelines have been developed on water tariffs. At present municipalities set tariffs and the National Treasury and Department of Water Affairs only oversee and comment on such tariff setting. Therefore, government supports the need for strengthened regulation on water tariffs and monitoring.

Expanding access to sanitation services and improving sanitary outcomes

The FFC recommends that the sanitation strategy should target behavioural change in relation to sanitation practices by households, rather than the provision of infrastructure alone, premised on attaining certain health outcomes. Greater consideration should also be given to household affordability constraints that may affect the long-term sustainability of sanitation investments.

Government response

Government agrees and already implements a holistic sanitation strategy that includes behavioural change. In determining appropriate sanitation investments, affordability and safety are considered.

Establishment of a National Water Regulator

The FFC recommends that government should consider establishing an independent National Water Regulator that would report to Parliament. Its functions would include regulating the entire water supply industry; issuing licences, regulating tariffs and monitoring integrated resource plans for infrastructure investments; regulating compliance with industry norms and standards; regulating the supply of water and sanitation services and their compliance with quality standards; regulating water efficiency and demand-side management; developing regulatory frameworks for public-private partnerships and alternative service delivery models in the water sector; and ensuring regulatory instruments support the achievement of universal access to water and sanitation services.

Government response

Government agrees to the FFC's recommendation on the establishment of an independent National Water Regulator subject to its cost and affordability. Any lessons learnt from the regulation of both bulk and retail electricity should be taken into account.

Chapter 8: Assessment of the institutional and fiscal capacity support mechanisms of local government

The FFC recommends that local government should be central to setting the agenda for capacity-building programmes in recognition of the fact that municipalities remain accountable for their own performance until such time as section 139 of the Constitution is invoked. Capacity programmes should be informed by a local government performance management system which is driven by key performance indicators. Prior to capacity programmes being developed and implemented at a local government level, a comprehensive assessment and design process should be undertaken. Capacity-development programmes should be aligned to each stage of the developmental transition of municipalities. There should be differentiated approaches in building capacity. Capacity-development programmes should be comprehensive and not only focus on training of personnel and deployment of experts within municipalities. They must also focus on other organisational, fiscal and institutional constraints that impact on the overall performance of municipalities.

The FFC also recommends that government must establish an intergovernmental framework for understanding what constitutes a lack of capacity within the context of local government. The replication of poorly defined roles and responsibilities between national and provincial government and district municipalities in the policy framework should be eliminated. This is necessary to create clear lines of responsibility and accountability for spheres of government or sector departments over their capacity-building roles for local government. Each capacity building programme must have a clear outline of measurable objectives, targets and timelines. These must detail conditions under which a programme can be withdrawn from a respective municipality and, following a detailed monitoring and evaluation of success factors and failures, suggestions for sustaining the programme. The method of implementing capacity programmes should be changed from a standard stop-gap package to an incremental solution focusing on the identified problems within the municipality, and identifying key leverage points where capacity programmes can make a difference.

A variety of grant instruments should be used to address different capacity challenges within different functional areas. Such grants should only be devolved to sector departments once they have demonstrated capacity to manage effectively such grants and capacity programmes in an IGR system. The Commission further recommends that appropriations for Siyenza Manje should be allocated through the Division of Revenue like other capacity grants. This will promote order, transparency and accountability.

Government response

Government agrees that local government capacity should be streamlined to enhance its performance. Through various initiatives, such as the local government turnaround strategy and implementation of municipal budgeting and reporting reforms, government is looking at measures to improve service delivery at local level.

The current local government capacity grant frameworks have clear outlines of measurable objectives, targets, conditions and timelines.

Government does not agree with the recommendation that Siyenza Manje be allocated through the division of revenue. This is because the funds are allocated to the Development Bank of Southern Africa (DBSA) to perform local government capacity-building on behalf of national government, and one-third of the funding comes from DBSA's own revenues. In addition, the DBSA has the capability to source this expertise much faster than government. It needs to be noted that given the need for in-year intervention, it is not possible to allocate these funds to specific municipalities from the start of the financial year. Government agrees however, that more transparent reporting of where funds have been used is required.

Part 4: Provincial allocations

Over R45.5 billion is added to the provincial baselines over the next three years. The provincial equitable share baselines are revised upwards by R33.9 billion and conditional grants are increased by R11.7 billion. National transfers to provinces increase from R295.3 billion in 2009/10 to R322.9 billion in 2010/11. Over the three-year period provincial transfers will grow at an average annual rate of 7.7 per cent to R369.3 billion in 2012/13.

Table W1.6 below sets out the total transfers to provinces for the 2010/11 financial year, which amount to R322.9 billion, with R261.0 billion allocated to the provincial equitable share and R61.9 billion to conditional grants.

Table W1.6 Total transfers to provinces, 2010/11

R million	Equitable share	Conditional grants	Total transfers
Eastern Cape	40 134	7 453	**47 587**
Free State	15 959	4 788	**20 747**
Gauteng	45 134	13 768	**58 902**
KwaZulu-Natal	56 743	11 742	**68 485**
Limpopo	33 238	5 861	**39 099**
Mpumalanga	21 323	4 222	**25 545**
Northern Cape	7 102	2 177	**9 279**
North West	17 314	4 203	**21 517**
Western Cape	24 026	7 670	**31 696**
Total	**260 974**	**61 884**	**322 858**

Provincial equitable share

At 78.6 per cent of total provincial revenue and 80.9 per cent of national transfers in 2010/11, the equitable share constitutes the main source of revenue for meeting provincial expenditure responsibilities. The proposed revisions of R10.7 billion, R11.3 billion, and R11.9 billion bring the equitable share allocations to R261.0 billion in 2010/11, R280.7 billion in 2011/12, and R294.8 billion in 2012/13. These revisions result in the provincial equitable shares increasing 10.2 per cent between 2009/10 and 2010/11, and 7.6 per cent over the MTEF in nominal terms.

Policy priorities underpinning equitable share revisions

The revisions to baseline equitable share allocations provide for personnel and policy adjustments as well as functional shifts.

Functional shifts provide for the shift of functions that were previously the responsibility of the provincial sphere to another sphere of government, such as preparing for the eventual shift of Further Education and Training (FET) colleges to national government (Department of Higher Education and Training) and the amalgamation of the Qwa-Qwa nature reserve into the Golden Gate Highlands National Park.

Personnel and policy adjustments seek to improve access to and quality of services, particularly in education, health and social development, and to implement strategies to retain and attract skills to this cluster. The additions to baseline equitable share allocations are set aside to deal with the higher-than-anticipated wage settlement and to stabilise the OSDs for health professionals and educators. A general provincial equitable share adjustment is also made to boost spending in frontline services such as education and health, and assist provinces in strengthening support to municipalities.

The equitable share formula

An objective redistributive formula is used to divide the equitable share among provinces. The formula is reviewed and updated with new data annually. For the 2010 MTEF, the equitable share formula has been updated with the data from the 2009 School Realities published by the Department of Education in September 2009, the 2008 General Household Survey published by StatsSA on 2 September 2009, the 2009 Mid-year Population Estimates published by StatsSA on 27 July 2009, and the Gross Domestic Product (2007 GDP-R) published by StatsSA on 24 February 2009. The 2009 School Realities data is used to update the education component, the 2008 General Household Survey is used to update the health component, the 2009 Mid-Year population estimates are used to update the basic and poverty components, and the 2007 GDP-R data is used to update the economic component.

The impact of these updates on the provincial equitable shares is to be phased-in over the MTEF, which will result in shifts in the equitable shares of provinces.

Impact of re-demarcation on provincial equitable shares

Newly demarcated provincial boundaries between North West and Gauteng took effect on 26 March 2009, but by agreement, implementation for provinces was deferred until 1 April 2010. The demarcation impacts on the equitable shares and requires them to be realigned to adjust for changes in total provincial populations. Table W1.7 shows the impact of the realignment of the provincial equitable shares to account for the revised provincial allocations. The GDP-R component will not be affected by the redrawing of provincial boundaries mainly because StatsSA sampling does not cover the area affected by the demarcation. The institutional component is independent of data and therefore also not affected.

Table W1.7 Impact of the realignment of the equitable shares by province before data updates

	Education	Health	Basic share	Poverty	Economic activity	Institu-tional	Weighted average after re-alignment	Weighted average before re-alignment	Difference in weighted average
	51%	**26%**	**14%**	**3%**	**1%**	**5%**	**100%**	**100%**	
Eastern Cape	16.8%	13.8%	13.5%	16.7%	7.8%	11.1%	15.2%	15.2%	0.00%
Free State	5.7%	5.8%	5.9%	6.1%	5.4%	11.1%	6.0%	6.0%	0.00%
Gauteng	15.4%	21.0%	21.9%	15.3%	33.6%	11.1%	17.7%	17.4%	0.35%
KwaZulu-Natal	23.0%	21.2%	20.8%	22.2%	16.3%	11.1%	21.5%	21.5%	0.00%
Limpopo	14.2%	11.4%	10.8%	14.2%	6.8%	11.1%	12.8%	12.8%	0.00%
Mpumalanga	8.5%	7.5%	7.4%	8.7%	6.8%	11.1%	8.2%	8.2%	0.00%
Northern Cape	2.2%	2.3%	2.3%	2.6%	2.2%	11.1%	2.7%	2.7%	0.00%
North West	6.2%	6.8%	6.6%	7.9%	6.4%	11.1%	6.7%	7.1%	-0.35%
Western Cape	8.2%	10.2%	10.8%	6.2%	14.6%	11.1%	9.2%	9.2%	0.00%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**–**

Because the formula is largely population driven, the allocations it generates are sensitive to and capture shifts in population across provinces. Shifts in population in turn lead to changes in the relative demand for public services across the provinces. The weighted average for Gauteng increases and the average for North West decreases in line with the change in the populations of the respective provinces.

Phasing-in of the formula

To mitigate the impact of the new data updates on provincial equitable shares, the new shares are phased in over the 2010 MTEF. Table W1.8 shows the revised weighted provincial equitable shares for the period 2009/10 to 2012/13. The realignment to the new boundaries for Gauteng and North West takes effect with no phasing in over the MTEF.

Table W1.8 Implementation of the equitable share weights, 2009/10 – 2012/13[1]

	2009/10	2010/11	2011/12	2012/13
	weighted shares	2010 MTEF weighted shares 3-year phasing		
Percentage				
Eastern Cape	15.6%	15.5%	15.4%	15.2%
Free State	6.2%	6.1%	6.1%	6.0%
Gauteng	16.9%	17.3%	17.4%	17.4%
KwaZulu-Natal	21.6%	21.7%	21.8%	22.0%
Limpopo	12.9%	12.8%	12.7%	12.6%
Mpumalanga	8.2%	8.2%	8.2%	8.1%
Northern Cape	2.7%	2.7%	2.7%	2.7%
North West	7.0%	6.6%	6.7%	6.7%
Western Cape	9.0%	9.1%	9.1%	9.2%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**

1. *The realignment to the new boundaries for Gauteng and North West takes effect with no phasing in over the 2010 MTEF.*

Summary of the structure of the formula

The formula, shown in Table W1.9 below, consists of six components that capture the relative demand for services between provinces and take into account specific provincial circumstances. The components of the formula are neither indicative budgets nor guidelines as to how much should be spent on those functions in each province or by provinces collectively. Rather, the education and health components are weighted broadly in line with historical expenditure patterns to provide an indication of relative need. Provincial executive councils have discretion regarding the determination of departmental allocations for each function, taking into account the priorities that underpin the division of revenue.

Table W1.9 Distributing the equitable shares by province[1]

	Education	Health	Basic share	Poverty	Economic activity	Institu-tional	Weighted average
	51%	**26%**	**14%**	**3%**	**1%**	**5%**	**100%**
Eastern Cape	16.8%	14.0%	13.5%	16.7%	7.8%	11.1%	15.2%
Free State	5.6%	5.9%	5.9%	6.1%	5.4%	11.1%	6.0%
Gauteng	15.4%	19.9%	21.8%	15.3%	33.5%	11.1%	17.4%
KwaZulu-Natal	23.2%	22.2%	21.2%	22.8%	16.2%	11.1%	22.0%
Limpopo	13.9%	11.3%	10.6%	13.9%	6.9%	11.1%	12.6%
Mpumalanga	8.4%	7.5%	7.3%	8.7%	6.9%	11.1%	8.1%
Northern Cape	2.2%	2.4%	2.3%	2.6%	2.2%	11.1%	2.7%
North West	6.2%	6.7%	6.5%	7.6%	6.5%	11.1%	6.7%
Western Cape	8.2%	10.1%	10.9%	6.2%	14.5%	11.1%	9.2%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

1. *The weighted shares include the realignment to the new boundaries for Gauteng and North West.*

For the 2010 Budget, the distribution of the weights by component remains unchanged as set out below:

- An *education share* (51 per cent) based on the size of the school-age population (ages 5-17) and the number of learners (Grade R to 12) enrolled in public ordinary schools
- A *health share* (26 per cent) based on the proportion of the population with and without access to medical aid
- A *basic share* (14 per cent) derived from each province's share of the national population
- An *institutional component* (5 per cent) divided equally between the provinces
- A *poverty component* (3 per cent) reinforcing the redistributive bias of the formula
- An *economic output component* (1 per cent) based on GDP by region (GDP-R) data.

The weights assigned to the education (51 per cent) and health components (26 per cent) are derived from average provincial spending on education and health in total provincial spending for the past three years, excluding conditional grants.

Education component

The education component is intended to enable provinces to fund school education, which amounts to about 90 per cent of provincial education spending. The formula uses school-age population (ages 5-17), based on Census 2001, and actual enrolment drawn from the 2009 School Realities data to reflect relative demand for education, with each element assigned a weight of 50 per cent. Table W1.10 shows the impact of the realignment and the data updates on the education component. Enrolment declined in the Eastern Cape, Free State, Limpopo, Mpumalanga and North West and increased in the other provinces. The relatively large increases in Gauteng and the decreases in North West are attributable to the realignment.

Table W1.10 Impact of the realignment and the data updates on the education component

	Realignment		Data updates		New		Difference (new vs. old)	
Learner numbers	Changes in school enrolment	Changes in school age cohort 5 - 17	Changes in school enrolment	Changes in school age cohort 5 - 17	School enrolment	School age cohort 5 - 17	Changes in school enrolment	Changes in school age cohort 5 - 17
Eastern Cape	–	–	-3 594	–	2 076 400	2 151 992	-3 594	–
Free State	–	–	-13 834	–	656 754	760 486	-13 834	–
Gauteng	35 393	38 521	9 811	–	1 939 231	1 931 719	45 204	38 521
KwaZulu-Natal	–	–	45 554	–	2 816 974	3 013 243	45 554	–
Limpopo	–	–	-57 389	–	1 707 280	1 798 862	-57 389	–
Mpumalanga	–	–	-16 062	–	1 035 469	1 074 972	-16 062	–
Northern Cape	–	–	1 843	–	267 709	280 975	1 843	–
North West	-35 393	-38 521	-1 975	–	741 892	826 218	-37 368	-38 521
Western Cape	–	–	11 128	–	973 136	1 094 565	11 128	–
Total	**–**	**–**	**-24 518**	**–**	**12 214 845**	**12 933 032**	**-24 518**	**–**

Table W1.11 shows the full impact of the realignment and data updates on the education component shares. Although the most significant changes occur in North West and Gauteng, the data updates also have a significant impact on the relative weights, indicating how sensitive the formula is to changes in enrolment.

Table W1.11 Impact of the realignment and the data updates on the education component shares

	Revised education component				Difference in weighted average
Percentage	**Old weighted**	**Realignment**	**Data updates**	**New weighted**	
Eastern Cape	16.8%	16.8%	16.8%	16.8%	0.00%
Free State	5.7%	5.7%	5.6%	5.6%	-0.05%
Gauteng	15.1%	15.4%	15.1%	15.4%	0.35%
KwaZulu-Natal	23.0%	23.0%	23.2%	23.2%	0.21%
Limpopo	14.2%	14.2%	13.9%	13.9%	-0.22%
Mpumalanga	8.5%	8.5%	8.4%	8.4%	-0.06%
Northern Cape	2.2%	2.2%	2.2%	2.2%	0.01%
North West	6.5%	6.2%	6.5%	6.2%	-0.30%
Western Cape	8.2%	8.2%	8.2%	8.2%	0.05%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**–**

Health component

The health component addresses the need for provinces to deliver health care. As all citizens are eligible for health services, the provincial shares of the total population form the basis for the health share. Within the health component, people without medical aid are assigned a weight four times that of those with medical aid, on the grounds that the former group is likely to use public health care more. The health component (table W1.12) is updated for population with medical aid using the 2008 General Household Survey. The 2009 mid-year population estimates are used to update the subcomponent "people without medical aid".

Table W1.12 Impact of the realignment and the data updates on the health component[1]

	Old		New		Difference (new vs. old)	
Population (thousand)	**Population with medical aid**	**Population without medical aid**	**Population with medical aid**	**Population without medical aid**	**Changes: Population with medical aid**	**Changes: Population without medical aid**
Eastern Cape	752	5 827	729	5 920	-23	92
Free State	468	2 410	432	2 470	-36	61
Gauteng	2 021	8 426	2 789	7 968	768	-458
KwaZulu-Natal	1 178	8 928	1 064	9 385	-114	458
Limpopo	385	4 890	422	4 805	37	-85
Mpumalanga	420	3 170	441	3 166	21	-4
Northern Cape	164	962	155	993	-9	31
North West	359	3 066	422	2 802	63	-264
Western Cape	1 087	4 175	1 277	4 080	190	-95
Total	**6 834**	**41 853**	**7 731**	**41 590**	**897**	**-264**

1. *The changes in population with and without medical aid include the realignment to the new boundaries for Gauteng and North West.*

Table W1.13 shows the full impact of the realignment and data updates on the health component shares.

Table W1.13 Impact of the realignment and the data updates on the health component shares

Percentage	Revised health component: Old weighted	Realignment	Data updates	New weighted	Difference in weighted average
Eastern Cape	13.8%	13.8%	14.0%	14.0%	0.21%
Free State	5.8%	5.8%	5.9%	5.9%	0.12%
Gauteng	20.5%	21.0%	19.4%	19.9%	-0.59%
KwaZulu-Natal	21.2%	21.2%	22.2%	22.2%	1.01%
Limpopo	11.4%	11.4%	11.3%	11.3%	-0.16%
Mpumalanga	7.5%	7.5%	7.5%	7.5%	0.01%
Northern Cape	2.3%	2.3%	2.4%	2.4%	0.07%
North West	7.2%	6.8%	7.2%	6.7%	-0.56%
Western Cape	10.2%	10.2%	10.1%	10.1%	-0.10%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**–**

Poverty component

The poverty component introduces a redistributive element within the formula and is assigned a weight of 3 per cent. The poor population comprises persons who fall in quintiles 1 and 2 based on the 2005 Income and Expenditure Survey. Each province's share is then expressed as the percentage of the "poor" population residing in that province, where the population figure is drawn from the 2009 Mid-year Population Estimates. The proportion of poor population per province is not adjusted to the new provincial boundaries as the sampling method used by StatsSA does not cover the affected areas. However the poverty component will be adjusted, partially to reflect changes in basic component value or population changes per province. Table W1.14 shows the poverty quintiles of the IES survey, basic component value and the weighted share of the poverty component per province.

Table W1.14 Comparison of new and old poverty component weighted shares[1]

	Old				New				Difference in weighted shares
	IES Survey 2005 (Q1+Q2)	Basic compo-nent value	Poor population	Weighted shares	IES Survey 2005 (Q1+Q2)	Basic compo-nent value	Poor population	Weighted shares	
Eastern Cape	49.8%	6 579	3 279	16.7%	49.8%	6 649	3 314	16.7%	0.00%
Free State	41.7%	2 878	1 200	6.1%	41.7%	2 902	1 211	6.1%	-0.01%
Gauteng	28.1%	10 447	2 938	15.0%	28.1%	10 757	3 025	15.3%	0.29%
KwaZulu-Natal	43.2%	10 106	4 363	22.2%	43.2%	10 449	4 511	22.8%	0.52%
Limpopo	52.9%	5 275	2 788	14.2%	52.9%	5 227	2 763	13.9%	-0.27%
Mpumalanga	47.7%	3 590	1 712	8.7%	47.7%	3 607	1 720	8.7%	-0.05%
Northern Cape	44.9%	1 126	506	2.6%	44.9%	1 148	515	2.6%	0.02%
North West	46.9%	3 425	1 608	8.2%	46.9%	3 224	1 513	7.6%	-0.56%
Western Cape	23.1%	5 262	1 215	6.2%	23.1%	5 357	1 237	6.2%	0.05%
Total		**48 687**	**19 608**	**100.0%**		**49 321**	**19 809**	**100.0%**	**–**

1. The new weighted shares include the realignment to the new boundaries for Gauteng and North West.

Economic activity component

The economic activity component is a proxy for provincial tax capacity and is assigned a weight of 1 per cent. For the 2010 MTEF, 2007 GDP-R data is used. The GDP-R is not adjusted to the new provincial boundaries mainly because the sampling of StatsSA did not cover any of the areas affected by the demarcation. Table W1.15 shows the impact of the revised weighted shares of the economic activity component. The right-hand column shows changes as a result of relative growth of provincial contributions to GDP.

Table W1.15 Comparison of new and old economic activity component weighted shares

	Old		New		Difference in weighted shares
	GDP-R, 2006 (R million)	Weighted shares	GDP-R, 2007 (R million)	Weighted shares	
Eastern Cape	136 668	7.8%	155 520	7.8%	-0.07%
Free State	94 269	5.4%	108 892	5.4%	0.03%
Gauteng	585 114	33.6%	668 926	33.5%	-0.15%
KwaZulu-Natal	283 655	16.3%	324 216	16.2%	-0.07%
Limpopo	118 865	6.8%	138 163	6.9%	0.08%
Mpumalanga	118 825	6.8%	138 732	6.9%	0.11%
Northern Cape	37 613	2.2%	44 159	2.2%	0.05%
North West	112 234	6.4%	129 872	6.5%	0.05%
Western Cape	253 815	14.6%	290 607	14.5%	-0.04%
Total	**1 741 058**	**100.0%**	**1 999 087**	**100.0%**	**–**

Institutional component

The institutional component recognises that some costs associated with running a provincial government, and providing services, are not directly related to population. This component is distributed equally between provinces and constitutes 5 per cent of the total equitable share, of which each province receives 11.1 per cent.

Basic component

The basic component is derived from the proportion of each province's share of the national population and is assigned a weight of 14 per cent. For the 2010 MTEF, population data are drawn from the 2009 mid-year population estimates.

Table W1.16 shows the impact of the revised weighted shares of the basic component.

Table W1.16 Comparison of new and old basic component weighted shares[1]

	Old		New		Difference in weighted shares
	2008 Mid-year population estimates	Weighted shares	2009 Mid-year population estimates	Weighted shares	
Eastern Cape	6 579	13.5%	6 649	13.5%	-0.03%
Free State	2 878	5.9%	2 902	5.9%	-0.03%
Gauteng	10 673	21.9%	10 757	21.8%	-0.11%
KwaZulu-Natal	10 106	20.8%	10 449	21.2%	0.43%
Limpopo	5 275	10.8%	5 227	10.6%	-0.24%
Mpumalanga	3 590	7.4%	3 607	7.3%	-0.06%
Northern Cape	1 126	2.3%	1 148	2.3%	0.01%
North West	3 199	6.6%	3 224	6.5%	-0.03%
Western Cape	5 262	10.8%	5 357	10.9%	0.05%
Total	**48 687**	**100.0%**	**49 321**	**100.0%**	**–**

1. *The mid-year population estimates for 2008 and 2009 are adjusted to the new boundaries for Gauteng and North West.*

Conditional grants to provinces

There are three types of provincial conditional grants. Schedule 4 sets out general grants that supplement various programmes partly funded by provinces, such as infrastructure and central hospitals. Transfer and spending accountability arrangements differ, as more than one national or provincial department may be responsible for different outputs expected from the grant. Schedule 5 grants fund specific responsibilities for both the transferring and receiving provincial accounting officers. A Schedule 8 grant, introduced in 2009/10, is intended to provide provinces (and municipalities) with an incentive to meet or exceed prescribed targets.

Changes to conditional grant framework

The 2010 MTEF introduces three new conditional grants. The *expanded public works programme grant for the social sector* will subsidise non-profit organisations so they can pay salaries to care workers currently working voluntarily on social development and health related matters in the home community based care sector. The *technical secondary schools recapitalisation grant* will modernise technical schools. The *Dinaledi schools grant* provides support to Dinaledi schools to enhance the quality of maths and science grade 12 passes in these schools starting in 2011/12. Provision is also made for the funding of further education and training colleges, which previously took place under the equitable share.

Table W1.17 shows the additions to provincial conditional grants which provide for policy and inflation adjustments. Technical adjustments between spheres total R3.3 billion, R3.6 billion and R3.7 billion over the MTEF. Conditional grant baselines have been revised upwards by R2.5 billion, R3.3 billion and R5.8 billion over the MTEF and bring the new conditional grant baselines to R61.9 billion in 2010/11, R69.9 billion in 2011/12 and R74.6 billion in 2012/13.

Table W1.17 Revisions to conditional grant baseline allocations, 2010/11 – 2012/13

R million	2010/11	2011/12	2012/13	2010 MTEF Total revisions
Technical adjustments to baselines				
Arts and Culture	**19**	**20**	**21**	**60**
Community library services	19	20	21	60
Higher Education and Training	**3 373**	**3 542**	**3 719**	**10 634**
Further education and training colleges	3 373	3 542	3 719	10 634
Public Works	**-69**	**–**	**–**	**-69**
Expanded public works programme incentive grant to provinces for the infrastructure sector	-69	–	–	-69
Total technical adjustments to baselines	**3 322**	**3 562**	**3 740**	**10 624**
Additions to baselines				
Basic Education	**–**	**70**	**220**	**290**
Dinaledi schools	–	70	100	170
National school nutrition programme	–	–	120	120
Health	**1 840**	**2 800**	**3 900**	**8 540**
Comprehensive HIV and Aids	1 700	2 800	3 900	8 400
Hospital revitalisation	140	–	–	140
Higher Education and Training	**400**	**430**	**450**	**1 280**
Further education and training colleges	400	430	450	1 280
Human Settlements	**134**	**–**	**1 000**	**1 134**
Housing disaster relief	134	–	–	134
Human settlements development	–	–	1 000	1 000
National Treasury	**–**	**–**	**262**	**262**
Infrastructure grant to provinces	–	–	262	262
Public Works	**57**	**–**	**–**	**57**
Expanded public works programme grant for the social sector	57	–	–	57
Transport	**98**	**5**	**–**	**103**
Gautrain rapid rail link	98	5	–	103
Total additions to baselines	**2 528**	**3 305**	**5 832**	**11 666**

Table W1.18 provides a summary of conditional grants by sector for the 2010 MTEF. More detailed information, including the framework and formula for each grant, is provided in Appendix W2 of the 2010 Division of Revenue Bill. The frameworks provide the conditions for each grant, the outputs expected, the allocation criteria used for dividing each grant between provinces, a summary of the audit outcome in 2008/09 and any other material issues to be addressed.

Table W1.18 Conditional grants to provinces, 2009/10 – 2012/13

R million	2009/10	2010/11	2011/12	2012/13
Agriculture, Forestry and Fisheries	**974**	**1 117**	**1 437**	**1 509**
Agricultural disaster management	157	–	–	–
Comprehensive agricultural support programme	715	862	979	1 028
Ilima/Letsema projects	50	200	400	420
Land care programme grant: poverty relief and infrastructure development	51	55	58	61
Arts and Culture	**441**	**513**	**543**	**571**
Community library services	441	513	543	571
Basic Education	**2 575**	**3 931**	**5 048**	**5 447**
Dinaledi schools	–	–	70	100
HIV and Aids (life skills education)	181	188	199	209
National school nutrition programme	2 395	3 663	4 579	4 928
Technical secondary schools recapitalisation	–	80	200	210
Higher Education and Training	**3 168**	**3 773**	**3 972**	**4 169**
Further education and training colleges	3 168	3 773	3 972	4 169
Health	**16 417**	**19 853**	**21 972**	**24 030**
Comprehensive HIV and Aids	4 376	6 012	7 433	8 765
Forensic pathology services	502	557	590	620
Health disaster response (cholera)	50	–	–	–
Health professions training and development	1 760	1 865	1 977	2 076
Hospital revitalisation	3 085	4 021	4 172	4 381
National tertiary services	6 614	7 398	7 799	8 189
2010 World Cup health preparation strategy	30	–	–	–
Human Settlements	**12 592**	**15 161**	**17 222**	**17 939**
Housing disaster relief	150	134	–	–
Human settlements development	12 442	15 027	17 222	17 939
National Treasury	**9 249**	**11 315**	**13 091**	**14 008**
Infrastructure grant to provinces	9 249	11 315	13 091	14 008
Public Works	**1 401**	**1 484**	**1 962**	**2 060**
Devolution of property rate funds	1 350	1 096	1 162	1 220
Expanded public works programme incentive grant to provinces for the infrastructure sector	51	331	800	840
Expanded public works programme grant for the social sector	–	57	–	–
Sport and Recreation South Africa	**402**	**426**	**452**	**475**
Mass sport and recreation participation programme	402	426	452	475
Transport	**6 670**	**4 312**	**4 159**	**4 361**
Gautrain rapid rail link	2 977	438	5	–
Overload control	10	11	–	–
Public transport operations	3 532	3 863	4 153	4 361
Sani Pass roads	34	–	–	–
Transport disaster management	117	–	–	–
Total	**53 890**	**61 884**	**69 858**	**74 568**

Agriculture grants

The *comprehensive agricultural support programme* aims to provide support for newly established and emerging farmers. Included in this grant is the extension recovery programme, which focuses on improving extension services through training programmes and providing equipment for extension officers. The grant also targets farm infrastructure and provides support for dipping, fencing, and rehabilitation of irrigation schemes where these could be viable. An amount of R2.9 billion is allocated to this grant over the MTEF.

The *land care programme grant: poverty relief and infrastructure development* aims to optimise productivity and sustainable use of natural resources. Provinces may use this grant to create jobs through the expanded public works programme. R173 million is allocated over the medium term.

The *Ilima/Letsema projects grant* is intended to boost food production. The grant is aimed at assisting previously disadvantaged South African farming communities to achieve an increase in agricultural production and receives R1 billion over the MTEF.

Arts and Culture grant

The *community library services grant* is administered by the Department of Arts and Culture. The purpose of the grant is to enable South Africans to gain access to knowledge and information that will improve their socioeconomic situation. The grant is allocated to the relevant provincial department and either administered by that department or through a service level agreement with municipalities.

Over the MTEF, R60 million is added to the grant to provide for the building of new libraries in the Eastern Cape and the operation costs of a donor funded library in the Western Cape. This grant is allocated R1.6 billion over the next three years.

Basic Education grants

The Department of Basic Education administers the *national school nutrition programme grant, the Dinaledi schools grant* and *the technical secondary schools recapitalisation grant* and the *HIV and Aids (life skills education) grant*.

The *national school nutrition programme* seeks to improve nutrition of poor school children, enhance active learning capacity and improve attendance in schools. An amount of R120 million is added to this grant in 2012/13 to protect its real value and respond to higher food prices.

The technical secondary schools recapitalisation grant comes into effect during the 2010 MTEF. This grant, amounting to R80 million in 2010/11, R200 million in 2011/12 and R210 million in 2012/13 provides for equipment and facilities in technical high schools.

The *Dinaledi schools grant* provides support to Dinaledi schools to enhance the quality of maths and science grade 12 passes in these schools by providing additional resources, including laboratories, lab equipment, textbooks and additional teacher training. This grant is allocated R170 million over the MTEF and will start in 2011/12.

The *HIV and Aids (life skills) programme grant* provides for life skills training, sexuality and HIV and Aids education in primary and secondary schools and is fully integrated into the school system, with learner and teacher support material provided for grades 1 to 9. This grant is allocated R597 million over the MTEF.

Health grants

The health sector accounts for five conditional grants with total allocations of over R19.8 billion in 2010/11, R22 billion in 2011/12 and R24 billion in 2012/13.

The *national tertiary services grant* aims to provide strategic funding to enable provinces to plan, modernise and transform the tertiary hospital service delivery platform in line with national policy objectives. Following a review of hospitals receiving the grant, the grant now operates in 22 hospitals across the nine provinces, concentrated in urban Gauteng and the Western Cape. Consequently, the Western Cape and Gauteng receive the largest shares of the grant as they provide the largest proportion of these high-level, sophisticated services for the benefit of the health sector countrywide. The grant is allocated R23.4 billion over the MTEF.

The *hospital revitalisation programme* plays a key role in transforming and modernising infrastructure and equipment in hospitals. The grant also includes a component aimed at improving systems for medical equipment, and to support management development initiatives, including personnel, procurement delegations and financial management capacity. An amount of R140 million is added to this conditional grant in 2010/11 for the Mitchells Plain hospital. The grant is allocated R12.6 billion over the next three years.

The *health professions training and development grant* funds the costs associated with the training of health professionals, and the development and recruitment of medical specialists. It enables the shifting of teaching activities from central to regional and district hospitals. This grant is allocated R5.9 billion over the medium term.

The *comprehensive HIV and Aids grant* enables the health sector to develop a specific response to HIV and Aids. In addition to HIV and Aids prevention programmes, the grant supports specific interventions that include voluntary counselling and testing, prevention of mother-to-child transmission, post-exposure prophylaxis and home-based care. Over the next three years R8.4 billion is added to this grant to fund the new Aids treatment policies announced on World Aids Day in December 2009. This includes starting Aids treatment at an earlier stage for patients with TB and pregnant women and giving triple therapy for all infected infants. The grant is allocated R22.2 billion over the next three years.

The *forensic pathology services grant* assists with the transfer of medico-legal mortuaries from the South African Police Service to the health sector and to provide comprehensive forensic pathology services for the criminal justice system. This grant will be reviewed during 2011/12 and is allocated R557 million in 2010/11, R590 million in 2011/12 and R620 million in 2012/13.

Higher Education and Training grant

As result of the split in the education ministry and the formation of the new Department of Higher Education and Training, the *further education and training colleges grant* is introduced to protect current spending on these colleges by provinces while the legislative processes required to shift this function to national government are completed.

Total expenditure on further education and training colleges was taken out of the equitable share and shifted into this conditional grant. The value of the conditional grant to each province is based on historical spending on this grant. The grant amounts to R11.9 billion over the MTEF.

Human Settlements grants

The *human settlements development grant* facilitates the establishment of habitable, stable and sustainable human settlements in which all citizens have access to social and economic amenities. The programme targets eradication or formalisation of informal settlements on a phased basis by 2014. Despite progress made thus far, there are still about 1.8 million families living in informal dwellings. This grant is allocated an additional R1 billion in 2012/13 to ensure accelerated housing delivery.

R133.8 million is added to the *housing disaster relief grant* in 2010/11 to address storm water damage on subsidised houses in KwaZulu-Natal caused by heavy rains.

National Treasury grants

The *infrastructure grant to provinces* augments provincial funding to accelerate construction, maintenance and rehabilitation of new and existing infrastructure in education, roads, health and agriculture, and also contributes to rural development. The grant also focuses on the application of labour-intensive methods in delivery to maximise job creation and skills development.

Within the infrastructure grant for provinces, provision is made for specific earmarking for education related infrastructure and R262 million is added to this grant in 2012/13 specifically for the improvement of school infrastructure.

Public Works grants

The *devolution of property rate funds grant* was introduced in 2008/09 to ensure that provinces take over the responsibility of paying property rates and municipal charges on properties that were administered by national government on their behalf. This grant is allocated R3.5 billion over the MTEF.

The *expanded public works programme incentive grant to provinces for the infrastructure sector* provides incentives to provinces and municipalities to increase spending on labour-intensive programmes. It is awarded to provinces on a performance basis measured on the number of work opportunities they create through specific programmes. An amount of R2 billion is set aside for this grant over the MTEF.

The 2010 Budget introduces a new grant on the Public Works vote: the *expanded public works programme grant for the social sector*. This grant receives R57 million in 2010/11 to subsidise non-profit organisations working in the home- and community-based care sector. This grant will be paid to non-profit organisations that have been using the services of unpaid volunteers so that these volunteers can receive some form of remuneration. During 2010, a comprehensive funding model for a programme that will incentivise labour-intensive employment in this sector and inform grant allocations for 2011/12 and 2012/13 will be developed.

Sport and Recreation grant

The *mass sport and recreation participation programme grant* promotes mass participation by historically disadvantaged communities in a selected number of developmental sporting activities. This grant is allocated R1.4 billion over the medium term.

Transport grants

The Department of Transport is allocated R438 million in 2010/11 as a final contribution to the construction of the Gautrain Rapid Rail Link. An additional R5.3 million is available in 2011/12 to cover the cost of any foreign exchange losses.

The o*verload control grant* funds initiatives to ensure the preservation of road infrastructure through the reduction of overloading practices and receives R11 million in 2010/11.

The *public transport operations grant* subsidises commuter bus services. The payment of bus subsidies to operators was previously funded on an agency arrangement between national and provincial government and this grant enables government to take greater responsibility in ensuring contractual obligations are met. This grant will amount to R12.4 billion over the MTEF.

Part 5: Local government fiscal framework and allocations

Municipalities play a critical role in furthering government's objective of providing services to all while facilitating local economic development. Over the next three years, national transfers to local government grow to accelerate the delivery basic services to households that cannot afford them.

Table W1.19 Revisions to direct and indirect transfers to local government, 2010/11 – 2012/13

R million	2010/11	2011/12	2012/13	2010 MTEF Total revisions
Technical adjustments	**-375**	**-724**	**-1 281**	**-2 381**
Direct transfers	**-521**	**-724**	**-1 281**	**-2 527**
Public transport infrastructure and systems grant	-590	-724	-1 281	-2 596
EPWP phase 2 incentive grant	69	–	–	69
Indirect transfers	**146**	**–**	**–**	**146**
Water services operating subsidy grant	146	–	–	146
Additions to baselines	**1 682**	**2 950**	**7 600**	**12 232**
Direct transfers	**1 528**	**2 400**	**6 550**	**10 478**
Equitable share	900	2 050	3 750	6 700
Neighbourhood development partnership grant	400	350	300	1 050
Municipal infrastructure grant	–	–	2 500	2 500
Municipal drought relief grant	228	–	–	228
Indirect transfers	**154**	**550**	**1 050**	**1 754**
Regional bulk infrastructure grant	54	200	300	554
Rural households infrastructure grant	100	350	750	1 200

The 2010 MTEF provides for an additional R10.5 billion in the local government budget framework (direct transfers), R6.7 billion for the local government equitable share and R3.8 billion for infrastructure transfers. The growth in the equitable share allocation will ensure that municipalities are able to extend basic services to the growing number of poor households and to alleviate the pressure that the increase in the cost of purchasing bulk electricity had on municipal budgets. The remaining R228.4 million is allocated to the *municipal drought relief grant* in 2010/11 to provide drought relief in Eastern Cape and Western Cape. A saving of R2.6 billion on the *public transport infrastructure and systems grant* over the MTEF has also been identified due to the need to review the policy on public transport in non-metropolitan municipal areas.

Table W1.20 Transfers to local government, 2006/07 – 2012/13

	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
R million		Outcome		Revised estimate		Medium-term estimates	
Direct transfers	**26 501**	**37 321**	**44 037**	**50 146**	**58 821**	**66 640**	**73 187**
Equitable share	**18 058**	**20 676**	**25 560**	**24 356**	**30 168**	**33 940**	**37 234**
General fuel levy sharing with metros	**–**	**–**	**–**	**6 800**	**7 542**	**8 531**	**8 958**
Conditional grants	**8 443**	**16 645**	**18 477**	**18 990**	**21 111**	**24 169**	**26 995**
Infrastructure	7 447	15 128	17 095	16 910	19 039	22 072	24 793
Capacity building and other	996	1 517	1 382	2 081	2 072	2 097	2 202
Indirect transfers	**1 436**	**1 884**	**2 307**	**3 017**	**3 125**	**4 014**	**4 618**
Infrastructure	943	1 334	1 928	2 774	2 979	4 014	4 618
Capacity building and other	493	550	379	243	146	–	–
Total	**27 938**	**39 205**	**46 344**	**53 163**	**61 946**	**70 654**	**77 805**

Indirect transfers to local government are allocated an additional R1.9 billion over the MTEF. Direct infrastructure transfers are allocated an additional R3.8 billion in the 2010 MTEF, of which R2.5 billion is for the *municipal infrastructure grant* to enable municipalities to extend much needed infrastructure to support economic growth and eradicate backlogs. R1.1 billion is for the *neighbourhood development partnership grant* to ensure that township development is fast tracked to create an environment that will attract private sector investment in selected townships.

An additional R554 million is allocated to *regional bulk infrastructure grant* to ensure that bulk water projects are accelerated in order to provide bulk water to households in a sustainable manner as well as provide drought relief in Limpopo. A *rural households infrastructure grant* has been introduced, amounting to R100 million in 2010/11, R350 million in 2011/12 and R750 million in 2012/13. This grant will cater for the rollout of on-site water and sanitation services to very poor households where conventional connector services are not viable or appropriate. The *water services operating subsidy grant* is allocated an additional R91.7 million in 2010/11 to deal with costs related to the transfer of water schemes from the Department of Water Affairs to municipalities.

Government aims to accelerate the delivery of water and sanitation services in rural homesteads over the next three years. Of the total 3.3 million households' national backlog in sanitation, 85 per cent (2.8 million) is in rural communities. In 2010/11, a new conditional grant (R1.2 billion over the next three years) to be administered by the national department of human settlements is introduced to roll out appropriate on-site solutions to address rural household sanitation and water needs. It is expected that through locally based methods of implementation, job opportunities through EPWP will be created.

The local government equitable share

The local government equitable share is the main fiscal instrument that is used to redistribute local government's share of nationally raised revenue. It supplements municipal own revenues for the provision of basic services to each poor household.

Government is accelerating efforts to better assist municipalities to improve planning and financial capacity, achieve greater efficiency in delivery, and expand service access to households residing in predominantly rural and/or lower-capacity areas. In the context of these efforts, the equitable share (excluding RSC levy replacement and special support for councillor remuneration) grows by an annual average of 12 per cent over the next three years to R26.4 billion in 2010/11, R29.9 billion in 2011/12 and R33.0 billion in 2012/13, compared to R20.3 billion in 2009/10.

Equitable share formula

The structure and components of the formula are summarised in the text box below:

Structure of the local government equitable share formula

Grant = BS + D + I – R ± C

where

BS is the basic services component

D is the development component

I is the institutional support component

R is the revenue-raising capacity correction and

C is a correction and stabilisation factor.

Basic services component

The purpose of the *basic services component* is to assist municipalities in providing basic services to poor households and with meeting municipal health service needs for all. For each subsidised basic service there are two levels of support: a full subsidy for poor households that are connected to municipal services, and a partial subsidy for households that are not yet connected to the municipal networks, currently set at a third of the cost of the subsidy to serviced households.

The characteristics of the basic services component are:

- Supporting poor households earning less than R800 per month in 2001 prices.
- Distinguishing between poor households connected to services and those that are not connected to services and may be provided with alternatives.
- Recognising water reticulation, sanitation, refuse removal and electricity reticulation as the core services.
- Providing for municipal health services to all households.

The basic services component

BS=[Water Subsidy 1*Poor with Water + Water Subsidy 2*Poor without Water] +

[Sanitation Subsidy 1*Poor with Sanitation + Sanitation Subsidy 2*Poor without Sanitation] +

[Refuse Subsidy 1*Poor with Refuse + Refuse Subsidy 2*Poor without Refuse] +

[Electricity Subsidy 1*Poor with Electricity + Electricity Subsidy 2*Poor without Electricity] +

[Municipal Health Services*Total number of households]

Institutional support component

The *institutional support component* of the equitable share formula provides assistance in meeting some of the administrative and governance costs of municipalities. It is a supplement, designed to augment, but not fully cover, institutional costs.

The institutional component

There are two elements to the institutional component: administrative capacity and local electoral accountability. The grant is as follows:

I = Base allocation + [Admin support * Population] + [Council support * Number of Seats]

Where the values used in the formula are:

I = R350 000 + [R1*population] + [R36 000* councillors]

The base allocation is an amount that will go to every municipal structure (except for a district management area). The second term of this formula recognises that costs go up with population. The third term is a contribution to the cost of maintaining councillors for the legislative and oversight role. The number of seats that will be recognised for purposes of the formula is the one determined by the Minister of Provincial and Local Government for purposes of elections and composition.

The revenue-raising capacity correction

To account for the varying fiscal capacities of municipalities, the formula must account for each municipality’s ability to raise revenue for the purposes of fulfilling its constitutional mandate. This component therefore takes into account income from property rates, the RSC/Fuel levy for metropolitan municipalities and the RSC/JSB levy replacement grant for district municipalities. In the absence of proper information on property valuation rolls across the spectrum of municipalities and as an interim measure, previous property rate collections have been used as a basis for determining future capacity to collect income from this source. In the case of the RSC/fuel levy and the RSC/JSB replacement grant, allocations were separately determined for each municipality and are used as published for the MTEF.

In order to achieve greater horizontal equity in the allocation system and to accommodate the bigger service level responsibilities of larger municipalities, as well as the greater revenue-raising constraints faced by smaller municipalities, a differentiated "revenue correction" rate on property rates income is applied on the basis of demonstrated revenue-raising capacity. The applicable "revenue correction" rate for a municipality is based on the level of per capita own operating revenue, while own operating revenue is the difference between past actual total operating revenue and income from grants and subsidies (Table W1.21).

Table W1.21 Differentiated "revenue correction" rates

Operating revenue per capita Rand			Revenue correction rate on property rates
0	–	500	1.5%
501	–	1 000	2.5%
1 001	–	1 500	3.5%
1 501	–	1 750	5.5%
1 751	–	2 000	6.5%
2 001	–	2 225	7.5%
2 226	–	2 500	8.5%
2 501	–	5 000	9.5%

Stabilising constraint

With the publication of three-year budget allocations, a guarantee mechanism is applied to the indicative outer-year baseline amounts with the aim of ensuring that municipalities are given what was indicated in the previous MTEF round of allocations, as far as this is possible, given overall budget constraints. An additional constraint is to ensure that allocations are not negative due to the revenue-raising correction. In the case of the 2010 MTEF the applicable guarantees are 100 per cent and 90 per cent on the allocations for the first two years of the MTEF cycle, respectively.

Other considerations in applying the formula

The formula as outlined above has to be rescaled to make allowance for intricacies in the allocation process. In particular, powers and functions must be taken into account, and the overall budget must balance.

Powers and functions

The local government system has a number of asymmetries, not only between different categories of municipalities, but also within the same category of municipalities. Firstly, there is the broad division of the sphere into Category A, B and C municipalities.[1] Secondly, the division of powers and functions between Category B and C municipalities differs – and this is also true between the different Category B municipalities within the same Category C district. In order to deal with these differences the model has to ensure that the allocations made in terms of the "basic services" component have to go to the municipality that actually performs the function.

[1] Category A are metropolitan municipalities, Category B are local municipalities and Category C are districts.

Balancing allocations

The "horizontal division" of allocations made between municipalities depends on the size of the overall allocation that is made to the local government sphere, normally determined through a separate consultative process to determine the equitable share of nationally raised revenue for each of the three spheres of government (i.e. the "vertical division"). Since there is no guarantee that allocations made in terms of the vertical division add up precisely to the amount allocated to the local government equitable share, such allocations need to be adjusted to fit within the constraints outlined above.

Rescaling of the BS, D and I components

The simplest way of making the system balance is to rescale the BS, D and I components to the available budget, hence the formula actually becomes:

Grant = Adjustment Factor*[BS + D + I] – R ± C

This adjustment factor is calculated so as to ensure that the system balances.

To deal with the constraints, municipalities are divided into two groups: those municipalities that require a "top-up" in order to meet the stabilising constraints and those that do not. The total size of the top-up is calculated and this is deducted from those that do not require a top–up amount in proportion to the "surplus".

Measurement issues

The integrity of the data is as important as the set of equations in determining whether the allocations meet the constitutional requirement of equity. During 2009, an assessment was undertaken by the National Treasury, Stats SA and the Department of Cooperative Governance and Traditional Affairs to explore the possibility of updating the 2001 Census data, which is currently used in the formula, with the results of the 2007 Community Survey. As the 2007 Community Survey was a sample (and not a census), it could lead to problems if the various characteristics of individual 283 municipalities are not picked up in the sample areas chosen for the municipality. The following indicators were used as key determinants to assess the usability of the data in the equitable share formula:

- The quality of the information obtained through the survey instrument.
- How "representative" of the municipality the sampled area was as determined by the sampling process.
- The extent to which the sampled municipal area is different from the municipality itself (referred to as the size of the sampling error).

The quality of the poverty data, a key determinant in determining the size of the basic services allocations to individual municipalities, proved to be problematic primarily because the "household income" variable had too many missing values (the formula reads this as a "non-poor household" and not as a "missing value"). The range within which the estimated population and household numbers for a municipality could fall is also relatively large. It cannot be assured that any shift in population numbers within a municipality from the 2001 census to the 2007 Community Survey is accurate, or whether such a change is based on an assumption within the sampling process. The 2007 Community Survey does not provide sufficient reliable data to be used in the *local government equitable share* formula, or in other formulas that are reliant on accurate population and poverty figures.

Given these challenges, the 2001 Census data will be used for determining equitable share allocations for the 2010 MTEF. As part of the review of the local government equitable share formula, further work will be undertaken to explore the possibility of using the results of the community survey in conjunction with the 2001 Census. For the purpose of calculating the local government equitable share allocations for the 2010 MTEF, the 2001 census information will be updated for the shift of Merafong local municipality to Gauteng province.

Cost values attributable to basic services

The subsidies received for providing basic services to poor households are a key ingredient in the current formula. The subsidy amounts in the current formula use a study conducted by the Department of Cooperative Governance and Traditional Affairs (see Table W1.22).

Table W1.22 Service costs

Service costs per month	1998	2008	
	Estimates	Estimates	
Rand		Serviced households	Households not connected to services
Electricity	36.0	45.0	16.0
Water	20.0	30.0	10.0
Sanitation	10.0	30.0	10.0
Refuse	20.0	30.0	10.0
Total	**86.0**	**135.0**	**46.0**

The equitable share formula distinguishes between poor households connected to services, where conventional municipal service delivery mechanisms are generally used, and those that are not connected to services, where such services are generally provided through alternative mechanisms. The number of poor households with access and without access to services is given in Table W1.23.

Table W1.23 Number of poor households

Service	Serviced households	Unserviced households
Electricity	3 079 340	2 456 443
Water	3 322 295	2 213 488
Sanitation	3 260 814	3 274 969
Refuse	2 176 923	3 358 860

Source: 2001 Census

When the *adjustment factor* and other components are applied, the formula calculates actual subsidies per basic service that are much higher than what is illustrated in Table W1.22 as service costs. By converting these total annual actual basic services subsidies into average monthly subsidies per poor household, the actual average monthly basic services subsidies are derived as illustrated in Table W1.24 below.

Table W1.24 Actual average monthly basic services subsidies per poor household

Monthly	Serviced households			Households not connected to services		
Rand	2010/11	2011/12	2012/13	2010/11	2011/12	2012/13
Electricity	177.9	201.8	222.7	65.3	73.9	81.5
Water	117.2	133.0	146.9	41.2	46.6	51.3
Sanitation	114.3	130.0	143.7	41.2	46.6	51.3
Refuse	112.2	127.8	141.3	41.8	47.3	52.1
Total	**521.5**	**592.6**	**654.6**	**189.5**	**214.4**	**236.2**

The actual average monthly subsidy for a basket of the four basic services for poor households with access to the services is R521.5, R592.6 and R654.6 over the next three years. The actual average monthly subsidy for a basket of the four basic services for poor households *without* access to the services is R189.5, R214.4 and R236.2 over the next three years. Compared to the estimated cost in Table W1.22 these subsidies are higher.

Conditional grants to local government

Conditional grants to local government aim to eradicate backlogs by 2014 and build institutional and financial capacity in local government. Two conditional grants to local government have been discontinued from 2010/11 namely, the *backlogs in water and sanitation at clinics and schools grant* and the *backlogs in the electrification of clinics and schools grant* as the grant objectives have largely been met. A new conditional grant to be administered by the national Department of Human Settlements is introduced to accelerate the delivery of sanitation and water to rural households over the next three years.

Local government allocations in the 2010 MTEF grow to R58.8 billion in 2010/11, R60.6 billion in 2011/12 and R73.2 billion in 2012/13.

Infrastructure conditional grants to local government

Infrastructure grants (direct and indirect) to local government are an important source of municipal capital revenues. Infrastructure grants increase to R22.0 billion in 2010/11, R26.1 billion in 2011/12 and R29.4 billion in 2012/13.

Table W1.25 Infrastructure transfers to local government, 2006/07 – 2012/13

	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
R million		Outcome		Revised estimate	Medium-term estimates		
Direct transfers	**7 447**	**15 128**	**17 095**	**16 910**	**19 039**	**22 072**	**24 793**
Municipal infrastructure grant	5 938	8 754	9 091	11 107	12 529	15 069	18 322
National electrification programme	391	462	589	933	1 020	1 097	1 151
Public transport infrastructure and system grant	518	1 174	2 920	2 418	3 699	4 425	4 125
Neighbourhood development partnership grant	–	41	182	551	1 030	1 190	1 182
2010 FIFA World Cup stadiums development grant	600	4 605	4 295	1 661	302	–	–
Rural transport services and infrastructure grant	–	–	9	10	10	11	12
Electricity demand side management	–	–	–	175	220	280	–
Municipal drought relief grant	–	91	9	54	228	–	–
Indirect transfers	**943**	**1 334**	**1 928**	**2 774**	**2 979**	**4 014**	**4 618**
National electrification programme	893	973	1 148	1 478	1 752	1 770	1 914
Neighbourhood development partnership grant	50	61	54	111	125	100	105
Regional bulk infrastructure grant	–	300	450	612	893	1 675	1 849
Backlogs in water and sanitation at clinics and schools	–	–	186	350	–	–	–
Backlogs in the electrification of clinics and schools	–	–	90	149	–	–	–
Electricity demand-side management	–	–	–	75	109	119	–
Rural households infrastructure grant	–	–	–	–	100	350	750
Total	**8 390**	**16 462**	**19 023**	**19 684**	**22 018**	**26 086**	**29 411**

Municipal infrastructure grant

The largest infrastructure transfers are through the *municipal infrastructure grant* (MIG), which supports government's objective of expanding the delivery of services, as well as alleviating poverty. While the allocations and spending patterns have increased over the years, it has become evident that the design and administration processes of the grant are inconsistent with the prevailing municipal capital funding environment resulting in less than optimal results from the grant. The demographic, economic context, infrastructure development and institutional challenges facing these different municipalities vary significantly. A process has been put in place to introduce a more differentiated approach to funding municipal infrastructural needs.

Government introduced the *MIG (cities) grant* in 2009 to cater for significant differences between larger urban municipalities and smaller, more rural municipalities. The introduction of this grant grew out of a need to reconceptualise how municipalities are funded to better leverage the capacity of the state. A phased approach to extending the *MIG (cities) grant* was adopted, with the inclusion of metros in 2009/10, which will be extended to the 21 large cities over the medium term.

Adopting a differentiated funding approach will allow national regulation of funding to respond to the generic challenges of different types of municipalities, as well as the specific issues faced by individual municipalities. The *MIG (Cities) grant* aims to help cities to more effectively manage, support and account for built environment outcomes. Greater discretion over the selection and implementation of capital projects, as part of their own capital investment programmes, will be matched with oversight of their entire programme performance rather than solely project inputs. This means that larger urban municipalities will be required to commit to the achievement of specific, measurable developmental outcomes arising from their entire capital programme. Smaller, more rural municipalities will largely continue to operate under the existing MIG framework, with innovations to improve expenditure outcomes introduced over time to address capacity and resource deficiencies.

A process is currently underway to accredit municipalities to undertake national housing programmes starting with the large metropolitan municipalities from April 2010 onwards. This process is also looking at creating better alignment and coordination between municipal infrastructure, through the MIG Cities grant, and the housing delivery through accredited municipalities.

The formula for allocating the *municipal infrastructure grant* has not changed. A constant component is phased in over three years to ensure that a reasonable minimum allocation is made to poor municipalities. This constant was introduced in the 2008 Budget, and will be fully phased in by 2010/11, when all municipalities will receive at least a minimum allocation of R5 million. The MIG formula comprises a vertical and horizontal division. The vertical division allocates resources to sectors or other priority areas; the horizontal division is determined based on a formula that takes account of poverty, backlogs, and municipal powers and functions. There are five main components of the formula, as demonstrated in the box below.

$MIG_{(F)} = C + B + P + E + N + M$

F Formula

C Constant to ensure increased minimum allocation for poor municipalities (This allocation is made to all municipalities)

B Basic residential infrastructure (new and rehabilitation of existing ones)

Proportional allocations for water supply and sanitation, electricity, roads and ‘other’ (Street lighting and solid waste removal)

P Public municipal service infrastructure (new and rehabilitation of existing ones)

E Allocation for social institutions and micro-enterprises infrastructure

N Allocation to all nodal municipalities

The total MIG allocations grow to R12.5 billion, R15.1 billion and R18.3 billion over the 2010 MTEF years, of which R2.6 billion, R3.1 billion and R3.8 billion are allocated to the *MIG (cities) grant*. The remaining allocation will constitute MIG to flow to the rest of municipalities maintaining the current requirements of the grant, amounting to R9.9 billion, R11.9 billion and R14.5 billion over the 2010 MTEF.

Table W1.26 shows the weighted share per sector and the respective amounts that flow through the vertical division of the MIG funds.

Table W1.26 Municipal infrastructure grant allocations per sector, 2009/10 – 2012/13

	2009/10	2010/11	2011/12	2012/13
Weights			**Adjusted weights**	
Municipal infrastructure grant (a)				
Special municipal infrastructure fund and management (b)				
Ring-fenced allocation: Eradication of the bucket sanitation system (c)				
Bulk infrastructure (d)				
Municipal infrastructure grant (formula)	*(a)-(b)*	*(a)-(b)-(c)-(d)*	*(a)-(b)-(c)-(d)*	*(a)-(b)-(c)-(d)*
B Component	**75.0%**	**75.0%**	**75.0%**	**75.0%**
Water and sanitation	72.0%	72.0%	72.0%	72.0%
Electricity	0.0%	0.0%	0.0%	0.0%
Roads	23.0%	23.0%	23.0%	23.0%
Other	5.0%	5.0%	5.0%	5.0%
P Component	**15.0%**	**15.0%**	**15.0%**	**15.0%**
E Component	**5.0%**	**5.0%**	**5.0%**	**5.0%**
N Component	**5.0%**	**5.0%**	**5.0%**	**5.0%**

Integrated national electrification programme

The grant seeks to ensure quality of electricity supply to all clinics, schools and poor households. Government plans to step up expenditure to R3.3 billion for the direct grant and R5.4 billion for the indirect grant over the next three years to reduce infrastructure backlogs by 2014.

Public transport infrastructure and systems grant

This grant aims to provide passenger transport networks in the major cities of South Africa, with a focus on public and non-motorised transport infrastructure and systems including Bus Rapid Transit systems. The grant is allocated R12.2 billion in the next three years.

Neighbourhood development partnership grant

The grant supports local government projects that provide a foundation for sustainable neighbourhoods, while simultaneously attracting private-sector investments in under-served communities. The direct portion of the grant is allocated R3.4 billion while the indirect portion is allocated R330 million over the next three years.

2010 FIFA World Cup stadiums development grant

The grant seeks to fund the construction of new designated stadiums or the upgrading of designated existing stadiums and supporting bulk services in 2010 FIFA World Cup host cities. The grant has an allocation of R302 million and will be phased out at the end of 2010/11. The construction/upgrading of stadiums has been completed.

Rural transport services and infrastructure grant

The grant aims to improve rural transport by upgrading rural access roads, pedestrian bridges and walkways. The grant is allocated R10.4 million in 2010/11, R11.1 million in 2011/12 and R11.7 million in 2012/13.

Electricity demand-side management

To reduce the demand on energy, government has allocated R500 million to municipalities and R228 million to Eskom to roll out electricity demand-side management programmes to reduce the energy consumption on the national grid. The programme will fund the rollout of energy-saving light bulbs.

Regional bulk infrastructure grant

The grant aims to provide regional bulk water and sanitation cutting across several municipal boundaries. In the case of sanitation, it supplements regional bulk connections as well as regional wastewater treatment works. The grant is allocated R893 million in 2010/11, R1.7 billion in 2011/12 and R1.8 billion in 2012/13.

Rural household development grant

Government aims to accelerate the delivery of water and sanitation services in rural homesteads over the next three years. Of the total national backlog in sanitation of 3.3 million households, 85 per cent (2.8 million) are in rural communities. In 2010/11, a new conditional grant (R1.2 billion over the next three years), to be administered by the national Department of Human Settlements, is introduced to roll out appropriate on-site solutions to address rural household sanitation and water needs. It is expected that through locally based methods of implementation, job opportunities through EPWP will be created.

Municipal drought relief grant

The *municipal drought relief grant* of R228.4 million is allocated to municipalities in the Eastern Cape and Western Cape. This grant will be administered by the Department of Water Affairs.

Capacity-building and other current transfers

Developing capacity to assist municipalities to build critical financial and technical capacity for sustained delivery of quality of services remains government priority. These grants give effect to section 154(1) of the Constitution. Although substantial resources have been committed over recent years towards local capacity-building efforts, concerns have been expressed that these have not had a measurable impact on capacity. Total allocations for capacity-building grants amount to R2.2 billion in 2010/11, R2.1 billion in 2011/12 and R2.2 billion in 2012/13 financial years.

Table W1.27 Capacity building and other current transfers to local government, 2006/07 – 2012/13

R million	2006/07	2007/08	2008/09	2009/10 Revised estimate	2010/11	2011/12	2012/13
Direct transfers	**996**	**1 517**	**1 382**	**2 081**	**2 072**	**2 097**	**2 202**
Municipal systems improvement grant	200	200	200	200	212	225	236
Restructuring grant	265	530	–	–	–	–	–
Financial management grant	145	145	180	300	365	385	404
2010 FIFA World Cup host city	–	–	–	508	210	–	–
Water services operating subsidy grant	386	642	1 002	871	662	380	399
Expanded public works programme - Phase 2 incentive grant	–	–	–	202	623	1 108	1 163
Indirect transfers	**493**	**550**	**379**	**243**	**146**	**–**	**–**
Financial management grant: DBSA	53	53	50	–	–	–	–
Water services operating subsidy grant	440	497	329	243	146	–	–
Total	**1 489**	**2 067**	**1 761**	**2 323**	**2 218**	**2 097**	**2 202**

The *municipal systems and improvement grant* aims to assist municipalities in building in-house capacity to perform their functions and stabilise institutional and governance systems. Key aims of this programme are to develop planning capacity and build governance systems. The grant receives R673 million in the 2010 MTEF.

The *financial management grant* aims to support sustainable management of the fiscal and financial affairs of municipalities. The grant promotes multi-year budgeting, linking integrated development plans to budgets and producing quality reports. The grant is allocated R1.2 billion in the 2010 MTEF.

The *2010 FIFA World Cup host city operating grant* helps host cities carry out their World Cup operations. An amount of R210 million is allocated to the grant in 2010/11, after which it is discontinued.

The *water services operating subsidy grant* consist of a direct and indirect grant (Schedule 6 and 7) to fund water schemes that were administered by the Department of Water Affairs and Environment prior to 1994. To date, 58 agreements have been signed, 3 839 staff moved and 1 787 schemes with a total asset value of about R6.4 billion transferred. The grant covers staff-related costs and direct operating and maintenance costs, while provision is also made for the refurbishment of infrastructure. The allocation per municipality is according to the operational budget for each scheme and the funding requirements identified and agreed on in the transfer agreement. The schedule 7 of the grant will continue in the 2010/11 financial year. This is as a result of the delays in the transfers of staff to water schemes. The Schedule 7 grant is allocated R146 million in 2010/11 and the Schedule 6 is allocated R662 million in 2010/11, R380 million in 2011/12 and R399 million in 2012/13.

The expanded public works programme incentive for municipalities grant encourages municipalities to hire more people in public works projects. The grant receives R623 million in 2010/11, R1.1 billion in 2011/12 and R1.2 billion in 2012/13.

Part 6: Future work on provincial and municipal fiscal frameworks

Review of the provincial fiscal framework and equitable share

The Budget Council of 2007 endorsed a comprehensive review of the provincial equitable share formula. The FFC led the first phase of the review, which identified the policy imperatives that should underpin the reform of the formula. The second phase of the review is being led by the National Treasury in consultation with the FFC and the provincial treasuries. In November 2009 it was agreed that the review be conducted according to six categories of provincial expenditure: education, health, social development, provincial infrastructure, economic services, and governance and administration. Task teams have been established to review the sector policy imperatives that should underpin the division of revenue in each of these categories. The review should be completed in time for the 2011 Division of Revenue.

Refinement of the local government fiscal framework

The 283 municipalities differ according to socioeconomic realities and institutional strengths. A one-size-fits-all approach does not recognise these differences. The local government fiscal framework will be reviewed to take account of these differences. Included in the reforms will be a review of the local government equitable share formula.

Introducing the sharing of the general fuel levy with metros as primary replacement for RSC levies

The sharing of the general fuel levy with metropolitan municipalities was introduced in the 2009 Budget as the primary replacement to the former RSC levies. To facilitate a smooth transition from the *RSC levy replacement grant* system to the sharing of the general fuel levy system, implementation has been phased-in over the three year period beginning with the 2009 MTEF, for full implementation in 2012/13. In 2010/11, metropolitan municipalities receive 50 per cent of the former RSC levy replacement grant and 50 per cent of the sharing of the general fuel levy.

As an interim measure the sharing of the general fuel levy is legislated through the annual Taxation Laws Amendment Act. It is intended to amend the Municipal Fiscal Powers and Functions Act (2007) (MFPFA) to make provision for the sharing of a nationally raised tax with municipalities.

Implementation of the Municipal Fiscal Powers and Functions Act

The main purposes of the MFPFA are to provide for the authorisation of taxes, levies and duties that municipalities may impose under section 229(1)(b) of the Constitution, and to regulate the exercise by municipalities of their powers to impose surcharges on fees for municipal services in accordance with section 229(1)(a) of the Constitution. The act regulates all municipal taxes with the exception of property rates, which are regulated by the Municipal Property Rates Act.

In terms of section 12(1) of the MFPFA, a municipality had to apply to the Minister of Finance by 7 September 2009 for the authorisation of an existing tax, other than a regional establishment levy or regional services levy imposed under the Regional Services Council Act (1985) or the KwaZulu and Natal Joint Services Act (1990) imposed by that municipality prior to the commencement of the MFPFA. All municipalities complied with the legislative requirements by 7 September 2009.

From those submissions and applications received by the National Treasury, 55 municipalities have applied for the continuation of 155 potential taxes/charges that were in place prior to the act. Consultation processes are currently underway in terms of section 4(2) the MFPFA, which states that the Minister should consult with the Minister responsible for local government, the FFC and the affected municipalities. Within three months of the consultation process, the FFC must submit its views in writing on the proposed municipal tax to the Minister in terms of section 4(3). This process will be concluded through the issuing of regulations by the Minister of Finance.

In terms of section 8 of the MFPFA, the Minister of Finance may prescribe compulsory national norms and standards for imposing municipal surcharges. These norms and standards may include maximum municipal surcharges that may be imposed by municipalities. These will be developed simultaneously with developments underway to improve the regulation of tariffs for key municipal services, such as electricity reticulation, water and sanitation. The National Treasury will over the next few years work in close consultation with several sector departments and regulatory bodies to develop frameworks that will harmonise the tariff and surcharge structures.

Implementation of the Municipal Property Rates Act

The Municipal Property Rates Act (2004) regulates the power of municipalities to impose rates on properties in accordance with section 229(1)(a) of the Constitution. Income derived from municipal property rates is an important own revenue source.

The original four-year transitional period given to municipalities to implement the Municipal Property Rates Act (up to 1 July 2009) was extended by two years (up to 1 July 2011) through a legislative amendment to the act in 2009 to allow for those municipalities that had failed to implement new valuation rolls to continue to use existing valuation rolls and supplementary valuation rolls until

30 June 2011. The Department of Cooperative Governance and Traditional Affairs intends to introduce further amendments to the act to improve its implementation.

Improved monitoring of performance of provinces and local government

The Presidency is finalising an outcomes-based performance management system to promote accountability in the implementation of the MTSF. This system will focus on targeted strategic outcomes, which will serve as a basis for coordinating the activities of government departments and clusters. Measurable outputs linked to each outcome will be identified and guide agreements on priority areas of work. This framework should help government make the best use of scarce resources, and improve productivity and innovation in all areas of work.