latter, entered into with the relevant labour organisations, is aligned to Resolution 7 of 2002 – the framework that is aimed at transforming and restructuring the public service to improve its efficiency and to provide for redeployment, retraining and, where possible, alternative employment for excess employees.

Considerable effort went into developing and implementing a new structure and filling core senior management and professional positions. This process must now be consolidated through further appointments that ensure employment equity and allow excess employees to the new establishment to apply for voluntary severance packages.

Over the next three years, the Department intends to implement improved human resource processes, procedures and systems. Key among these are the implementation of new performance-management and personal development systems, ensuring completion of performance contracts for all senior managers and the provision of further employee training and development at all levels. *Corporate Services* also intends piloting a service delivery programme aimed at improving divisional performance and delivery over the MTEF period.

Driven by its skills requirements over the next few years, the National Treasury has developed its own Education, Training and Development strategy that focuses on enhancing employees' skills at all levels. As part of the strategy, the National Treasury has developed a competency framework and training curriculum. The Department intends implementing a leadership, management and supervisory development programme, an internship programme and a mentorship programme during 2003/04. These programmes will contribute towards the implementation of a career-development system that provides for further employee training and development at all levels.

The finalisation of a skills audit at the macro level contributed towards completion of the Treasury training curriculum. This year the team intends completing a skills audit at the individual level, ensuring continual compliance with the requirements of the Skills Development Act.

The *Financial Management* unit is focused on maximising compliance with all relevant financial statutes and regulations the most important of which is the Public Finance Management Act (PFMA) and providing excellent service to its customers, both internal and external.

The appointment of a new Chief Financial Officer has contributed to improvements in and the streamlining of National Treasury financial management procedures and processes. The unit has made considerable progress with the establishment of an outsourced internal audit function, completion of a risk-management assessment exercise and development of a fraud-prevention plan in line with PFMA and National Treasury Regulation requirements.

The focus going forward will be on enhancing and building on these achievements to ensure continual compliance. Key priorities this year include the finalisation of the Department's financial manual and further progress on National Treasury financial delegations.

National Treasury is one of the pilot departments for the new decentralised procurement system, which aims to improve procedures, transparency and to meet empowerment targets. The Department has made considerable progress in this area. The Accounting Officers Procurement Procedures contains departmental procurement procedures. An established Accredited Procurement unit is now in operation, and further streamlining of procedures will continue with annual targets being set regarding procurement from black economic empowerment and small-, micro- and medium-sized firms. Key vacant positions need to be filled to drive this process forward over the next three years.

A Director for *Security and Facilities Management* was appointed in 2002 to develop this key support service within National Treasury. Further security and facilities policies and procedures will be developed and implemented to ensure the continual safety and security of personnel, information and assets. Key projects in progress include the vetting of all personnel and the development of a security manual.

The *Communications and Information Technology* unit appointed a Director for Information and Technology this year and plans to strengthen the section over the next three years. Presently, the information technology function and support is outsourced to two contract houses, as well as the State Information Technology Agency, which provides basic services such as Wider Area Network (WAN) connectivity and Internet access to National Treasury. The Department has entered into comprehensive service level agreements with all three providers.

Over the past year, state-of-the-art network infrastructure was installed at the 240 Vermeulen Street building, mirroring the information technology infrastructure at the 40 Church Square building. Further plans include installing a fault-tolerant “backbone” and an advanced disaster recovery system (in the case of infrastructure failure), as well as an asset-tracking system, venue and facilities booking systems, a document-tracking application and task-specific applications that are relevant to specific needs.

Over the next 18 months, the unit intends to restructure the information technology function and infrastructure, providing enhanced support to the National Treasury over the 2003 MTEF period. Restructuring plans include a redesign of the current network operating system, which will providing further functionality to the current environment. This will include advanced digital authentication and signatures, and the implementation of an electronic work-flow system, eliminating paper-based approval procedures. The unit intends adding further security, encryption and intruder-detection systems, and will investigate the use of mobile solutions that allow National Treasury personnel to link up to the departmental information technology network on a remote, but safe, basis.

Communication in the National Treasury centres on the provision of a strong media-liaison service for the Ministry and Department. The divisional heads continue to feature strongly in the media, ensuring that the broader National Treasury leadership is introduced to the public. Major media and communication events include the annual Budget tabled in Parliament, the Medium Term Budget Policy Statement, the annual meetings of the International Monetary Fund and the World Bank.

The *Legal Services* component of National Treasury has developed from playing an advisory role to providing a more comprehensive and fundamental support function to the Department and the Ministry. National Treasury intends to strengthen the unit over the next three years to enable it to provide legal services on a wider range of domestic and international finance legislation.

This year the unit will also focus on developing Treasury-specific policy and procedures regarding the Promotion of Access to Information Act (2 of 2000). The Act requires that organisations set out policies and procedures regarding access to their documents and records. National Treasury policy and procedures that set the rules and provide the framework for access to information will be implemented through an appropriately designed document-management system, according to the National Archives Act (43 of 1996). The documentation system will facilitate documentation tracking and recall.

MEASURABLE OBJECTIVES AND MEDIUM-TERM OUTPUT TARGETS

Medium-term output targets: Programme 1 Administration

Measurable objective: To improve the quality of financial reporting by ensuring that appropriate policies and procedures are developed and implemented.

Subprogramme	Output	Measure/Indicator	2003/04 Target/ Milestone	2004/05 Target/ Milestone	2005/06 Target Milestone
Parliamentary	A procedurally sound and politically astute Parliamentary Unit	Achieving a proactive relationship with Parliament	Develop Unit's awareness of its role and relationship with Parliament	Unit providing support to new members of Parliament in developing relationship with National Treasury	Proactive support established
	Extensive engagement with the Legislature on the budget reform processes, with specific reference to the Constitutional requirement for a process to deal with money bills	The number of dialogue/meetings held between the National Treasury and Parliament on the budget reform processes, with specific reference to the Constitutional requirement for legislative powers and processes to amend money bills	Facilitate throughout 2003 as the process develops	Legislation that facilitates amendment to money bills promulgated	Monitoring feedback from all role players for evaluation of Act
	Monitoring and facilitating promulgation of financial legislation and policies that are presented to the Legislature	Monitoring the passage of legislation from drafting to enactment	Monitoring and facilitating promulgation of identified financial legislation and policies	Monitoring and facilitating promulgation of the Financial Services Bill (establishing a single financial Regulator) and the Accounting Profession Bill	Monitoring and facilitating promulgation of identified financial legislation and policies
	Providing continued parliamentary service to the Ministry and its Departments	% satisfaction of the Minister, Deputy Minister and the Director General regarding quality of parliamentary services provided	100% satisfaction	100% satisfaction	100% satisfaction

Measurable objective: To improve the quality of financial reporting by ensuring that appropriate policies and procedures are developed and implemented.

Subprogramme	Output	Measure/Indicator	2003 Target/ Milestone	2004 Target/ Milestone	2005 Target Milestone
Corporate Services	Full compliance with PFMA and full implementation of procurement reform	Unqualified audit	31 July 2003	31 July 2004	31 July 2005
		% compliance with new procurement programme	100% with new procurement programme by 30 June 2003		
	Implementation of transformation programme through restructuring and enhanced HR systems	% of policies and procedures finalised	75 % policies and procedures finalised by September 2003	100% of policies and procedures finalised by 31 March 2005	Develop new policies and procedures that arise
	Improve leverage of IT investment	% implementation of new & updated IT systems	Develop new IT strategic plan and technical redesign of IT systems 100% by 31 October 2003	Implementation of technical redesign 100% by 30 June 2004	Implementation of paperless and completely mobile environment 100% by 30 June 2005
	Internal and external communication programme and new corporate image	% increase in visits to the Intranet (staff) and National Treasury website (public)	Redesign of Internet and Intranet sites 100 % by 31 October 2003	Implementation of mobile-device access to Internet and Intranet sites 100% by 30 June 2004	Interactive Internet and Intranet sites 100% by 30 June 2005
	Diverse legal and legislative services	Meet divisional legal services needs in terms of time and quality	Throughout 2003 as required by divisions	Throughout 2004 as required by divisions	Throughout 2005 as required by divisions
		Draft Bills of quality introduced on time	As determined by the relevant divisions	As determined by the relevant divisions	As determined by the relevant divisions

RESOURCE PLAN

Expenditure estimates

Table 2: Administration

Subprogramme		Medium-term expenditure estimate		
	Adjusted appropriation			
R thousand	2002/03	2003/04	2004/05	2005/06
Minister[1]	691	746	791	835
Deputy Minister[2]	511	552	585	617
Management	8 585	8 088	8 484	9 055
Corporate Services	108 492	92 863	88 598	94 843
Sector Education and Training Authority	126	133	140	140
Capital Works	–	–	–	–
Total	**118 405**	**102 382**	**98 598**	**105 490**
Change to 2002 Budget Estimate	40 889	19 704	**10 834**	

[1] Payable as from 1 April 2002. Salary: R552 984. Car allowance: R138 246.

[2] Payable as from 1 April 2002. Salary: R408 600. Car allowance: R102 150.

Economic classification				
Current	93 414	91 888	91 000	95 881
Personnel	36 397	43 362	40 655	42 650
Transfer payments	126	133	140	140
Other current	56 891	48 393	50 205	53 091
Capital	24 991	10 494	7 598	9 609
Transfer payments	–	–	–	–
Acquisition of capital assets	24 991	10 494	7 598	9 609
Total	**118 405**	**102 382**	**98 598**	**105 490**

Standard items of expenditure	36 397	43 362	40 655	42 650
Administrative	12 957	15 937	16 710	17 775
Inventories	2 452	2 522	2 478	2 585
Equipment	25 653	6 444	3 375	5 720
Land and buildings	–	4 800	5 100	4 800
Professional and special services	40 820	29 184	30 140	31 820
Transfer payments	126	133	140	140
Miscellaneous	–	–	–	–
Total	**118 405**	**102 382**	**98 598**	**105 490**

Transfer payments per subprogramme				
Sector Education and Training Authority				
Finance, Accounting, Management, Consulting and Other Financial Services Sector Education and Training Authority	126	133	140	140
Total	**126**	**133**	**140**	**140**

Expenditure trends

Expenditure on the programme falls from a high of R118,4 million in 2002/03 to R98,6 million in 2004/05, before rising to R105,5 million in 2005/06. The trend reflects the rise in spending owing to the merger and restructuring of the National Treasury as well as once-off costs owing to the occupation and renovation of the 40 Church Square building. Renovation of the 240 Vermeulen Street building is expected to be completed this year, after which programme expenditure declines into the outer years of the MTEF.

It is envisaged that, in support of the National Treasury's policy agenda for financial and fiscal reform, funds will be required to assist in passing and implementing significant pieces of legislation. These include the Municipal Finance Management Bill, the Financial and Fiscal Commission Amendment Bill, and the Money Bills Amendment Procedure Bill. Proposed Constitutional amendments to ensure appropriate interventions in municipalities that are faced with financial emergencies will be a major legislative item over the medium term. These needs have resulted in the creation of a legal budget of about R4 million.

The enhanced structure of the Office of the Director General will necessitate increased funding on the *Management* subprogramme. It is expected that these costs will be tabled in the Appropriations Estimate later this year once the revised structure has been costed and approved.

PROGRAMME 2: ECONOMIC PLANNING AND BUDGET MANAGEMENT

Purpose: *Economic Planning and Budget Management* provides for professional advice and support to the Minister of Finance on economic and fiscal policy, international financial relations, financial regulation, tax policy, intergovernmental financial relations, public finance development and management of the annual Budget process.

Measurable objective: The programme aims to promote growth, social development and poverty reduction through sound economic, fiscal and financial policies, efficient revenue measures and effective, efficient and appropriate allocation of public funds.

Organised into four divisions, the programme spans considerable responsibilities. At the hub of Government business, divisional teams are output driven and committed to hard work, tight deadlines and high professional standards.

- *Public Finance* manages the National Treasury's relations with other national departments, provides support to departments in a range of areas and advises the Minister and the rest of the National Treasury on departmental and sectoral matters. The key focus areas are departmental and sectoral financing and budgeting; monitoring of financial management, expenditure and service delivery; policy analysis and policy development support; and through the Technical Assistance unit, support for reconstruction and development programmes and projects.
- *Budget Office* provides fiscal policy advice, oversees the national Budget process, leads the national budget reform programme, coordinates international technical assistance and donor finance, supports public-private partnerships and compiles the public finance statistics.
- *Intergovernmental Relations* coordinates fiscal relations between national, provincial and local government and promotes sound provincial and municipal financial management.
- *Economic Policy and International Relations* is responsible for macroeconomic analysis and policy advice, managing international financial relations, tax policy formulating and development of tax legislation, and coordinates with the South African Reserve Bank and the Financial Services Board on banking and financial services regulation.

Policy Developments

Budget Office

The main output of the *Budget Office* is the annual Budget that the Minister of Finance tables in Parliament in February each year.

A key element of the budget-reform programme is increased political oversight over the annual budget process. The increased focus by the Minister's Committee on the Budget facilitates a more detailed discussion of budget priorities by Cabinet at its mid-year Lekgotla.

Last year, Parliament created a new committee – the Joint Budget Committee – tasked exclusively with dealing with the Budget. The Committee will hold hearings after the tabling of the Medium Term Budget Policy Statement in October and the tabling of the main Budget in February each year. These hearings will provide a key participatory forum for non-governmental organisations, government departments, trade unions, academics and subject experts to make an enhanced impact on eventual Budget allocations.

The National Treasury will continue to work in partnership with national departments, enhancing and strengthening the measurable objectives, output measures and service delivery target information as set out in the annual *Estimates of National Expenditure*. The publication of measurable objectives for each programme, in line with the Public Finance Management Act (1 of 1999) (PFMA), reflects a commitment to improved service delivery, greater transparency and increased accountability.

On the fiscal front, the expansionary fiscal stance first signalled in the 2001 Budget is maintained for the 2003 MTEF, with the deficit widening to 2,4 per cent of GDP next year, declining to 2,3 per cent in 2005/06.

This provides for real annual growth of 4,5 per cent in national and provincial non-interest expenditure to meet Government's expenditure priorities. It also provides for further cuts in taxes to lower- and middle-income earners, and for significant additions to infrastructure development.

While the channels through which fiscal policy contributes towards enhanced growth and development are often well understood, the scale of and interaction between their effects remain the subject of empirical analysis. Recognising this, the *Budget Office* will strengthen its fiscal analysis capacity, deepening understanding of fiscal trends in the economy and their effect on long-term growth and investment.

A key focus in this respect is the integration of databases that draw on fiscal policy information. This will allow the National Treasury to align its fiscal and macroeconomic models, strengthening analysis and understanding of the linkages between the fiscal framework and key economic aggregates and improving macroeconomic forecasts.

Strengthening fiscal analysis capacity is in line with international trends and requirements for prudent public financial management. Following the Asian financial crisis in 1998, multilateral institutions and governments around the world agreed to implemement a system of reviews of performance (Reports on Standard Codes or ROSCs) by governments on a broad range of policy issues related to economic management (fiscal and monetary policy, governance (banking, supervision, corporate governance) and transparency (data dissemination and fiscal transparency). South Africa is one of a few countries to have completed all 11 of the ROSCs instituted by the International Monetary Fund and the World Bank.

Increased spending on infrastructure investment has a significant impact on economic growth and the expansion of service delivery. Over the 2003 MTEF period, capital spending averages 5,7 per cent of GDP, with large investments in the non-financial public enterprises and extra-budgetary institutions and strong growth in public-private partnership expenditure supporting the step up in national, provincial and municipal investment.

The new infrastructure finance focus will facilitate the development of criteria to assess infrastructure investments, supporting departments and provinces in accelerating the pace of delivery and providing a framework for the monitoring and evaluation of infrastructure projects.

The focus supports the increasing workload of the *Public Private Partnership* (PPP) unit. PPP facilitated infrastructure expenditure is projected to rise substantially over the 2003 MTEF period. Key projects include the Gauteng Rapid Rail Link, the Dube Trade Port (including the relocation of Durban International Airport), the Department of Trade and Industry-serviced accommodation project, the Department of Education-serviced accommodation project, Chapman's Peak Toll Road, hospital co-location projects in the Eastern Cape and Western Cape, tourism projects, fleet-management projects, the Home Affairs National Identification System, and the social-pension administration system. The PPP unit has about 50 projects in the pipeline at any given time.

The National Treasury also emphasises improving the link between policy, budgeting and personnel management, given the extent of public resources directed towards personnel expenditure. Over the next year, the *Budget Office* will complete the implementation of a framework for the remuneration of public entities. The team will work closely with the Department of Public Service and Administration and others, to develop appropriate pay progression, career pathing and performance-based incentives for various sectors; notably health, education and policing.

In the public finance statistics arena, priority will be given to developing and implementing a new economic classification for the Budget and a corresponding new Chart of Accounts for the financial systems of government. At present, the economic classification is based on the old "standard-item" approach, which retains outdated classifications such as that for "stores and livestock". The move towards a new Chart of Accounts, prepared on the basis of internationally accepted Government Finance Statistics (GFS) classification principles, advances South Africa towards compliance with the International Monetary Fund's Special Data Dissemination Standards. This is a first step in the process of preparing for a move to accrual accounting.

Budgeting is not only about managing domestic resources – it also involves coordination of donor assistance programmes. Since 1994, South Africa has benefited from an increasing flow of foreign grants and technical cooperation. This now includes some 30 international framework co-operation agreemnts, which, since 2001/02, have contributed approximately R1,6 billion (or 0,5 per cent of consolidated revenue) annually.

Over the next three years, development cooperation will focus on strengthening the alignment of official development assistance with government spending. Key considerations are the optimal utilisation of limited resources in support of South Africa's development priorities; ensuring long-term sustainability beyond the phase of foreign support and strengthened South African ownership of foreign assistance programmes and projects.

South Africa receives almost R800 million a year in international development assistance through the Reconstruction and Development Programme Fund. A further R800 million a year is managed directly by our donor partners. Over the past year, the *International Development Cooperation* unit within the *Budget Office* facilitated the negotiation of new development cooperation strategies with the European Union, the United Nations Development Programme, Germany, France, Ireland, Belgium, Denmark and Flanders. The cooperation strategy with Canada was extended for a further five years. These strategies were concluded in line with South Africa's development priorities and strategies. During the year, the team also finalised development of systems to monitor donor-assisted projects, improving National Treasury oversight and management of overseas development assistance to South Africa.

Public Finance

The *Public Finance* teams are the key link in the detailed interactions with the policy and budget teams of all national departments and other government entities. Better budgeting at the national level depends largely on these teams developing good, cooperative relationships with their line departments, enhancing policy and expenditure management and oversight at the national level.

The responsibilities of the division are divided among four teams, which span the range of Government services and functions:

- *Social Services* liaises with the Departments of Health; Education; Social Development; Labour; Arts and Culture; Science and Technology and Sports and Recreation.
- *Economic Services* works with the Departments of Agriculture; Land Affairs; Environmental Affairs and Tourism; Communications; Minerals and Energy; Housing; Transport; Trade and Industry and Water Affairs and Forestry.
- *Protection Services* deals with the Departments of Defence, Safety and Security; Justice and Constitutional Development; Correctional Services; the Independent Complaints Directorate and the Secret Services.
- *Administrative Services* includes Parliament, the Presidency and the Departments of Home Affairs; Foreign Affairs; Provincial and Local Government; Public Works; Government Communication and Information System; National Treasury; Public Enterprises; Public Service and Administration; the Public Service Commission; the South African Management and Development Institute and Statistics South Africa.

Transforming public sector financial management is a key objective of National Treasury. The *Public Finance* teams facilitate implementation of the PFMA and Treasury Regulations within national departments, public entities and constitutional institutions, providing and overseeing appropriate systems for monitoring and managing expenditure.

Reforms introduced under the PFMA place the National Treasury spending teams at the centre of policy and budgetary debate across Government. Expenditure monitoring remains a key activity. However, teams will increasingly shift their focus towards monitoring service delivery and engaging and analysing key sectoral policies that drive spending and service delivery in support of sustainable growth and development.

Over the next three years, a key focus of the *Social Services* team will remain the development of appropriate budgets and financing mechanisms for the social services, with significant attention given to those sectors where national and provincial governments have concurrent responsibilities – health, education and social development. This will entail deepening assessments of sectoral trends and needs and enhanced interaction with national departments in the budget process.

The team will also support intergovernmental processes and committees (particularly the sectoral joint technical committee processes better known as "4x4s") to facilitate deliberations on the division of revenue between the spheres of government and to guide and assess provincial budget allocations. A key element of the latter is assistance to the *Intergovernmental Relations* section in reviewing the provincial equitable share formula in the light of changing conditions and new information, in particular the release of the 2001 Census results.

Financing and budgets for a range of service delivery areas will receive priority attention. In the health sector, the team will assist in developing the funding framework for the Enhanced Response to HIV/Aids and will examine the fiscal implications of the division of responsibilities for primary care between provincial and local government. Refining strategies and financing for the recruitment, retention and appropriate distribution of scarce health professionals is a further focus.

The *Social Services* team plays a key policy role in respect of the reconfiguration of health grants aimed at equity in tertiary health services. The tertiary services grant amounts to R4 billion in 2003/04, increasing to R4,5 billion in 2005/06. The training and development grant, which increases to R1,5 billion over the next three years, has a new component for employing more registrars and medical specialist trainers in those provinces with the most severe shortage of medical specialists.

Eighteen hospitals are earmarked for major upgrading of infrastructure under the Hospital Revitalisation Grant. Funding for the grant will rise to R1 billion in 2005/06. A new component of the grant, introduced this year, is aimed at improving systems for the upgrading and management of medical equipment.

Funding for the integrated nutrition programme almost doubles over the next three years. In addition to extending the coverage of the programme to Grade R pupils, the increase will also ensure provision of standard menus across a larger number of schools. The transfer of the Primary School Nutrition Programme from the health to the education department will require adjustments in budgets and financing mechanisms.

In higher education, the *Social Services* section will cooperate with the national department in implementing budgets for restructuring the sector. R800 million was allocated for this purpose over the next three years and will be directed towards recapitalisation of undercapitalised institutions, personnel retrenchment costs, harmonising systems, facilitating the process and for physical infrastructure. Refining and introducing a new funding formula for higher education will also be supported.

In provincial and school education the implications of the national department's *Review of the Financing, Resourcing and Costs of Education in Public Schools* for budgets and funding mechanisms require elaboration. Financing implications of the restructuring of the further education and training sector, the extension of access to early childhood development and the development of policy for learners with special needs will be developed further.

The fiscal management of the rapid expansion in access to social grants, and the extension of the child support grant to older children, will be a high priority. At the same time the management and funding of improved service delivery, and addressing the fiscal implications of the envisaged shift of responsibility for administration and delivery of grants to the national sphere will be dealt with. Conditional grant funding of food relief (a new mechanism in 2003), financial implications of key legislation (such as the Child Justice Bill) and the review of the special poverty-relief allocation will also be on the agenda.

One of Government's biggest challenges is to accelerate employment creation in the economy. Together with the *Macroeconomics Policy* unit, the *Social Services* team supports the Department of Labour in the development of an integrated employment strategy and in the planning and preparation for the Growth and Development Summit later this year. Further development of the National Skills Development Strategy is being supported. The team will also focus on assisting the Department of Science and Technology to implement the National Research and Development Strategy, backed by significant increases in allocations over the MTEF. Implementation of the National Language Policy as approved by Cabinet will also receive attention.

Government recognises the importance of accelerating land reform delivery for reducing rural poverty and ensuring broad-based economic participation, particularly of black farmers. The 2003 Budget adds a further R1,9 billion in support of land restitution and land reform, specifically the Land Redistribution for Agricultural Development (LRAD) programme. Over the next three years, the *Economic Services* team will work closely with the Departments of Land Affairs and Agriculture to evaluate the LRAD programme, probing its fiscal impact and future budgetary implications, particularly at the provincial level.

Economic Services plans to step up its engagement with the Department of Minerals and Energy on the establishment of regional electricity distributors. The Electricity Distribution Industry Holdings Company is allocated R150 million over the 2003 MTEF period to transform the Eskom and municipal electricity distribution systems into six regional electricity distributors. Of key concern, however, is the impact of the restructuring on local government finances and the proposed ownership and corporate governance arrangements of the new regional distributors.

The team also intends to strengthen its interaction with the Transport Department. In particular, research and analysis on public transport infrastructure will assess the costs of implementing and maintaining infrastructure investment as well as rates of return and long-term economic and environmental impact. This work will complement continued engagement on the appropriate targeting and level of commuter subsidies for the rail and bus systems, which place continued pressure on the fiscus.

Water Affairs and Forestry receives a further R1 billion over the 2003 MTEF period for the community water and sanitation programme and for the refurbishment of water schemes, ahead of their transfer to local authorities. Operated by the former homelands administration, these schemes are in disrepair and show poor revenue collection from water users. Local authorities are reluctant to assume responsibility for the schemes unless they are refurbished and recapitalised.

The Department of Environmental Affairs and Tourism is also concerned about infrastructure institutional arrangements. During the next year, the National Treasury and this department will collaborate to analyse the institutional arrangements of fishing harbours regarding their state of infrastructure, level of usage and user fee structure, and their possible transfer to local authorities.

Over the next three years, the *Economic Services* team intends to establish a regulation and tariff unit to development a common approach to structural regulation issues, in particular tariff approvals that impact on regulated and administered prices. The team will work closely with the *Macroeconomic Policy* unit in this regard.

The *Protection Services* team is instrumental in the policy and funding debates and activities of the integrated justice sector cluster review team. The team – comprising the Departments of Safety and Security, Justice and Constitutional Development, Correctional Services and the National Treasury – is focused on balancing and coordinating spending, and ensuring quality service delivery in the integrated justice system.

Improved synergy within the criminal justice sector remains a key priority in preparing medium-term expenditure plans. The 2003 Budget gives priority to improving case management through information systems and cooperation between the criminal justice system departments. Substantial additional funding goes to the management of courts, system improvements in the Department of Justice and Constitutional Development and further expansion of police personnel, focusing on sector policing. Personnel of the South African Police Service will increase from 118 818 in 2000 to a projected 155 260 by 2006.

Re-engineering court and case management remains a key priority for the Department of Justice and Constitutional Development and the sector over the next three years. The Automated Fingerprint Identification System has been successfully introduced and has significantly reduced search times in managing the records of criminals. Notable progress has also been made in reducing the outstanding cases on magistrates' court rolls through the introduction of Saturday and additional courts, and the Durban Court Processes Project has successfully demonstrated the potential for reducing the incidence of lost and late dockets. Key projects over the remainder of the MTEF period will include improved expenditure management, a public-private partnership for the administration of monies held in trust by the Department of Justice, further investment in court security and improvements to court buildings.

The National Treasury is working closely with the Department of Justice on issues related to constitutional bodies. At present, funds are voted to constitutional bodies on the Justice and Constitutional Development vote. Given the Constitutional independence of these bodies, analysis and consultation is needed to address the appropriate location of their budget allocations and the level of funding.

The Safety and Security budget is a significant component of national expenditure, rising to R22 billion this financial year. The 2003 Budget provides additional funds to expand personnel. The employment of civilian personnel will alleviate the administrative burden and enable functional police members to focus on crime prevention. This contributes to the effectiveness of the sector policing strategy, which entails policing in manageable areas to increase police visibility, especially in priority crime areas.

The *Protection Services* team is actively engaging the Department of Correctional Services on the construction of four new prisons in 2003, scheduled for completion in 2005/06. Substantive work is also in progress on a lower-cost prison design, new approaches to prison management and a reorientation of Correctional Services towards effective rehabilitation and restorative justice, alongside this department's responsibility for secure custody of offenders. Together with other justice, crime prevention and security-cluster departments, efforts to reduce the numbers of awaiting-trial and juvenile prisoners have been prioritised.

The strategic defence procurement programme, aimed at modernising critical equipment of the South African National Defence Force, enters its fourth year in 2003/04 and will shortly see the delivery of the first tranches of light utility helicopters and trainer aircraft and the first of four corvettes. Over the next three years, the Department of Defence and the National Treasury will monitor the expenditure trends of the procurement programme, manage the funding needs for peace-keeping operations and assess the short-, medium- and long-term human resource, capital and maintenance expenditure needs.

The *Administrative Services* team engages actively with the Departments of Home Affairs and Foreign Affairs, in particular. Recognising the need to raise its medium-term baseline allocation to more sustainable levels, the 2003 Budget allocates a further R669 million to the Department of Home Affairs over the next three years. These funds are directed towards expanding its personnel establishment, improving equipment and information systems, and stepping up maintenance and rehabilitation of offices. Funds are set aside for an Automatic Fingerprint Identification System and work is in progress on a public-private partnership for the HANIS "smart identity card" project.

This year, the National Treasury and Home Affairs are engaging in a joint research project to address the issue of illegal immigration. The emphasis of the research will be the associated social concerns, xenophobia, increased crime, poverty and the cost burden to the country, particularly from the fiscal perspective. The venture will examine various issues of illegal immigration such as a determination of the number of illegal foreigners, whether they are employed or unemployed, and distinguishing between different types of illegal foreigners. This will assist in informing immigration policy as well as labour market policy. It will be a useful planning tool, providing insight into what measures should be adopted with regard to removal and prevention of illegal immigrants.

The Department of Foreign Affairs is a key player and driver of the New Partnership for Africa's Development (Nepad). The Presidential initiative is focused on peace and security in Africa, good governance, human rights and sound economic management as conditions for sustainable development. It is at the centre of South Africa's engagement with African countries and the wider international community.

The 2003 Budget accommodates the phased establishment of 16 new missions in African countries, contributions to the funding of the African Union and the Nepad Secretariat and increased contributions to regional development through the African Renaissance Fund, which is administered by the Department of Foreign Affairs. The National Treasury has worked closely with that department regarding the affordability and sustainability of expenditure trends on the Foreign Affairs vote. A more stable budget trend is anticipated, following the recent strengthening of the rand.

The National Treasury team is working closely with the Department of Provincial and Local Government to finalise the Property Rates Bill this year. The Bill will have a significant impact on the expenditure of the Department of Public Works. In anticipation of this increased expenditure on leases and rates and taxes, the 2003 Budget increased the allocation to Public Works by R200 million for 2003/04.

The team will also become more directly involved in the establishment of the State Property Management Agency. The Agency will be used to manage the Department of Public Works's property portfolio and will be set up as a public entity, once proven viable.

There is a growing acceptance of a programme and project management approach to enhance the capacity of Government to address reconstruction and transformation. In reaching our developmental objective, technical assistance will focus on strengthening management capacity in priority programmes in government to deliver on basic needs and services.

Co-funded by the European Union, the *Technical Assistance* unit supports the work of the *Public Finance* teams. Over the past year, the unit has addressed blockages in key projects such as the funding of community projects, social housing, partnerships in the public health sector and reviewing infrastructure delivery. Over the next three years, the unit will focus on facilitating the implementation of programmes especially in the Social Services Cluster and the Crime Prevention and Justice Cluster, promoting effective management and good governance.

Intergovernmental Relations

The *Intergovernmental relations* division coordinates fiscal relations between the national, provincial and local government spheres – a key role in South Africa's evolving intergovernmental fiscal system.

Approximately 60 per cent of expenditure on the main Budget takes the form of transfers to provincial and local governments, placing them at the forefront of social and basic service delivery.

The *Intergovernmental relations* team plays a pivotal role in this respect, managing the intergovernmental fiscal framework; analysing and ensuring oversight of provincial and local government budgets and intergovernmental grants; and implementing financial management reforms at the provincial and local level.

The 2003 Budget reflects the continuing evolution of our intergovernmental system. Over the past few years, the national and provincial treasuries have co-operated to introduce and implement financial management and budgeting reforms underpinned by the PFMA. These efforts are now bearing fruit. Provincial finances are stabilising. Greater transparency and improved accountability is expected to contribute towards improved service delivery at the provincial level.

The Municipal Finance Management Bill, which is close to being adopted by the National Assembly, is a key pillar in the overall public finance architecture of Government. The legislation facilitates the extension and deepening of financial management and budget reforms at the local government level, similar to reforms implemented at the national and provincial level under the PFMA. Implementation of the Act, to be completed by mid-2007, will take cognisance of the uneven capacities of municipalities to implement financial reforms.

Much of the team's time is taken up in developing good, constructive working relationships with the nine provincial treasuries that guide the interactions of Team Finance – the Minister of Finance and his provincial colleagues. Ensuring constructive debate at the technical level in the Technical Committee for Finance and the sectoral technical committees ("4x4s" and "10x10s") facilitates more robust interaction at political forums such as the Budget Council, Budget Forum and the sectoral MinMECs in the health, education, social development, local government and housing sectors. Over the next three years, the provincial team will engage with the agriculture and transport sectors to establish intergovernmental fora and technical committees in these sectors.

The division is responsible for overseeing the equitable share and conditional grants to provinces and municipalities. It also implements Programme 6 – *Provincial and Local Government transfers*. The team will ensure the accurate and timely transfer of the R142 billion equitable share to provincial government over the 2003 MTEF period. It is also responsible for developing policy on fiscal transfers to local government, although the Department of Provincial and Local Government is responsible for the administration of the transfers. An important focus of the team is to monitor compliance with the provisions of the PFMA and the Division of Revenue Act that relate to fiscal transfers, specifically to conditional grants administered by the National Treasury.

The 2003 division of revenue reinforces the shift in the division of nationally raised revenue towards provinces and local government. Over the next three years, national transfers to provinces will increase by 6,1 per cent in real terms and those to local government will rise by 12,2 per cent.

Changes to the provincial share provide for increases in social grants and the extension of the child support grant, improvements to schooling and health services and further investments in roads and other infrastructure. Increases to the local government share provide further support for free basic services and the extension of infrastructure to formerly unserviced neighbourhoods.

More specifically, the 2003 MTEF allocations provide for R69,3 billion more to provinces over the 2002 Budget baseline. This raises the provincial share from 56 per cent to 57,6 per cent over the next three years.

The equitable share comprises 89,5 per cent of national transfers to provinces and rises by 5 per cent in real terms over the MTEF. Unlike the case for conditional grants – in which spending is determined by national government and prescribed through the Division of Revenue Act – provinces have discretion over how they allocate the equitable share among the functions they perform. Increased equitable share allocations give provinces greater flexibility in determining budgets and give effect to national and provincial priorities.

The equitable share is divided among provinces by means of an objective redistributive formula, the data and weights of which are reviewed annually, taking into account recommendations of the Financial and Fiscal Commission (FFC). The present structure of the formula, a product of collaboration between National Treasury and the FFC, was adopted in 1998/99. For demographic data, the formula currently uses the 1996 Census data. The publication this year of the 2001 Census allows the *Intergovernmental* team to undertake a comprehensive review of the equitable share. The structure of the formula, component weights and veracity of data will be investigated through a process that includes extensive consultation with sector departments at provincial and national level. The availability of the Census 2001 demographic data will be central to this process, and the revised equitable share will inform the 2004 Budget.

In addition to the equitable share, conditional grants remain an important part of the intergovernmental transfer system, providing for national priorities in provincial budgets, compensating provinces for cross-boundary flows, for specialised services and to support transition and capacity building.

Conditional grants make up 10 per cent of total national transfers. The current conditional grant system has been shaped by reforms introduced through the Division of Revenue Act since 2000. These reforms, which have aligned the management of conditional grants with PFMA, have contributed to clarifying accountability between spheres, resulting in improved use of the grants to enhance service delivery. The new amendment of PFMA will include the key requirements for the management of conditional grants. Further reforms over the next few years will see a consolidation of grants to the provincial sphere in particular.

For the first time this year a breakdown of national transfers to local government, by municipality, was published in the Division of Revenue Bill on Budget day, four months ahead of the municipal financial year. Early publication of municipal allocations from national government will enable municipalities to incorporate these allocations into their budgets, to improve planning and budgeting and enhancing delivery. Further reforms to the Division of Revenue Act include enhancement of the reporting requirements in respect of non-financial as well as financial information on conditional grants.

In this year's Budget, the most significant change to the conditional grant allocations to provinces is the introduction of the Child Support Extension Grant, which provides funding to extend the child support grant to children until they are 14 years old. Currently, the grant is accessible to children until they are seven years old. Extension of the grant will be phased in over the next three years.

While social assistance currently is a provincial responsibility, Cabinet has agreed, in principle, to a consolidation of this function into a new agency, to be overseen by the national Department of Social Development. The *Intergovernmental* team is a critical player in the detailed planning and preparation for this change, ensuring successful implementation over the next few years. In particular, the team will advise on how the Division of Revenue Bill and the equitable share should be adapted to take account of the shift.

The Provincial Infrastructure Grant, introduced in the 2000 Budget to assist provinces to step up their spending on infrastructure, rises to R3,1 billion in 2005/06. After a period of sluggish performance, provinces are increasing their capital spending rapidly. Over the next three years, the *Intergovernmental* team intends enhancing its capacity to monitor and track provincial infrastructure spending and deliverables in collaboration with the *Budget Office*.

The *2003 Intergovernmental Fiscal Review*, published in April this year, is an accessible resource on provincial and municipal budgets and service delivery issues. It provides a consolidated review of how the nine provinces and 284 municipalities fund the delivery of social and basic services to our communities.

The *2003 Review* provides information on the 2003 provincial budgets tabled by MECs of Finance between 4 and 18 March this year and the 2002/03 municipal budgets. It accounts for public expenditure for the past three years, that is 1999/00 to 2001/02. It also spells out in more detail provincial and local government spending plans, taking the focus on service delivery one step forward and enabling users to compare provincial and municipal service delivery standards and achievements. The wealth of information is aimed at promoting better accountability by providing valuable information to the public, elected officials, public servants and policy researchers in order to improve the quality and delivery of public services.

The provincial section of the division works closely with the *Budget Office* and the *PFMA* unit in the National Treasury to facilitate implementation of the PFMA and budget reforms in the provinces.

An exciting development is the provincial tabling of departmental strategic plans during March and April this year. These strategic and performance plans are based on uniform budget formats for each of the social services sectors. They will attempt to set uniform measurable objectives, performance indicators and targets for each budget programme and subprogramme. Key to this reform is ensuring that there is a close relationship between strategic plans and budget allocations, so that, in reporting, departments can reflect what they have delivered with the resources allocated to them.

Over the next three years, reforms aim to strengthen alignment between departmental strategic plans, budgets, financial statements and annual reports. Further, the team will review the provincial equitable share formula and all provincial conditional grants.

In local government, substantial resources are made available in the 2003 Budget to provide for poverty relief, to extend infrastructure delivery and further strengthen the local government system through skills development and capacity building. National transfers to local government increase from R8,8 billion in 2002/03 to R14,6 billion in 2005/06. This increases the local government share of nationally-raised revenue from 3,6 per cent in 2002/03 to 4,4 per cent by 2005/06.

The bulk of the additional resources will be targeted at the provision of free basic services, the extension of services to areas not presently serviced and further infrastructure investment. In total, R4,1 billion over the 2003 MTEF will be made available for water, electricity, refuse removal and sanitation as part of Government's commitment to provide free basic services to households that cannot afford them.

Infrastructure grants to municipalities remain a key instrument in urban renewal and rural development. An additional R1,8 billion over the next three years is allocated for infrastructure delivery, of which R1 billion will be earmarked for labour-based infrastructure investments to boost employment creation at a local level.

An additional R300 million over this MTEF is set aside for capacity building. The *Intergovernmental* team worked hard to ensure the adoption of an interim framework for aligning the capacity-building grant allocations into a single grant by 2005/06. Over the next three years, capacity-building grants to municipalities that flow through provinces will be incorporated into the Municipal Systems Improvement Grant in 2005/06. This translates into an additional R233 million to the local sphere, and accounts for the sharp increase in the value of the grant in 2005/06. Increases will be focused on financial management and reform, and on improving strategic management and service delivery skills.

The process of reforming municipal financial management systems and refocusing municipal budget priorities is well under way. Thus far, reforms that are being undertaken in pilot municipalities continue to demonstrate that the budget process and preparation of functional budgets is instrumental to the reforming of management systems generally. The reforms within pilot municipalities are being supported by a grant – the Finance Management Grant – from national government. To date 39 municipalities receive the grant. Noteworthy successes have been achieved in the pilots with the tabling of three-year budgets and the appointment of municipal managers and chief financial officers.

The most effective tool for reform has been the placement of international advisers working shoulder-to-shoulder with municipal teams. The next important phase of this programme will see up to 30 municipal financial advisers attached to pilots for a period of two years. These advisers will continue to implement the reforms, while refining them through systematic feedback. They will also provide assistance with rolling-out the reforms to other municipalities in their region. The network of pilot municipalities and international advisers will serve as valuable infrastructure and a resource for the roll-out and implementation of the Municipal Finance Management Act as a whole. New pilots are to be added during the 2003/04 financial year, which will take the total to more than 60 pilots.

Unlike provinces, local governments have significant revenue-raising powers. However, the high proportion of poor households in some municipalities presents serious challenges to the efforts of local government to realise their revenue-raising potential.

Over the next three years, the *Intergovernmental* team will work closely with the Department of Provincial and Local Government to broaden the revenue base of local government. Review of the local government fiscal framework, commencing this year, will entail a range of reforms to accommodate shifts in powers, functions and fiscal capacity. The review will include analysis of the equitable-share formula, restructuring of the electricity-distribution industry and other service sectors, and implementation of the Municipal Finance Management Act and other legislative reforms to financial management, such as the borrowing powers of municipalities.

Economic Policy and International Financial Relations

The *Economic Policy and International Financial Relations* division undertakes policy analysis and engages in consultation and collaborative work in the areas of: macroeconomics, international economics, taxation and financial regulation.

The *Macroeconomic Policy* unit engages in research and policy analysis that contribute towards enhancing sustainable growth, job creation, skills development and empowerment. The primary responsibility of the unit is the production of economic forecasts, in particular on growth, external account and inflation. These forecasts form the foundation for the Budget framework.

The unit will continue to strengthen the inflation-targeting regime in collaboration with the South African Reserve Bank. Over the past year, events led to engagement in a number of activities aimed at analysing pricing behaviour in South Africa. The first involved a joint exercise with the Departments of Agriculture and Trade and Industry to identify sources of the recent price hikes in the food and agricultural sectors. The analysis was undertaken in support of possible policy interventions in these sectors that would support price stability and, in particular, inflation targeting. Nedlac engagement on welfare responses to the food price hikes was informed by this work.

Cognisant of the fact that inflation management is not the sole responsibility of monetary policy the team is engaging in more detailed, collaborative analysis on the regulated and administered prices, and utility prices in particular. Regulated and administered prices emanate from sectors, such as utilities (water and electricity), which provide basic services to communities. Over the next three years, the team will analyse, monitor and advise on appropriate policy responses to developments in administered prices in line with the overall inflation-targeting objectives.

Job creation tops the Government's priority agenda for the 2003 MTEF. The *Macroeconomic Policy* team plays a key role in formulating and coordinating appropriate growth-enhancing policies that contribute towards strengthening employment creation. Over the next three years, work will focus on modelling and analysis that assesses the impact of interest rate and exchange rate variability as well as that of microeconomic reform on South Africa's growth prospects.

Further work will be undertaken in the area of policy design to promote savings by both the household and the corporate sectors. The latter complements and builds on the team's engagement in the Financial Sector Summit last year. The Summit between Government, business and labour deliberated on strategies that will improve delivery of financial services, enhancing national savings and direct them to development purposes. The Summit declared that all South Africans should have access to affordable and convenient payments and savings facilities and that the development of institutions that provide micro-credit to the poorest households should be supported. These intentions are tied in with policy initiatives across Government to raise the domestic savings rate, providing a stable source of financing investment into the future.

The team also represents the National Treasury in several domestic and international bodies and standing committees, including Nedlac, the Common Monetary Area Commission, the Statistical Council, the Policy Board and the Financial Markets Advisory Board to the Minister of Finance, the Southern African Development Community Macroeconomic Subcommittee and the inflation-targeting technical committee.

The *Tax Policy* unit is responsible for advising the Minister of Finance on tax policy issues that arise at all three levels of government. In its policy advice function to Government, the unit must design tax instruments that can optimally fulfil their revenue-raising function, achieve economic and allocative functions and strengthen redistributive and social policy functions at the same time. All of this must be done in a manner that creates a basis for general political acceptability of the selected tax instruments.

In formulating tax policy design, there is a need to match the generally accepted principles of a good tax system within the current macroeconomic and fiscal policy objectives of Government. The policy advice must achieve an acceptable trade-off between competing fiscal and economic policy objectives. In designing tax policy, cooperation between the South African Revenue Service and the National Treasury is of utmost importance, as is daily interaction with the corporate sector and the general tax-paying public.

In the 2003 Budget, the Government continues to grant substantial tax relief to individuals. In addition, sound structural changes since 1994 and strong revenue growth create fiscal space for introducing tax-driven stimulus measures that seek to grow the tax base and create employment opportunities.

Through improved revenue estimation modelling and on the back of robust revenue collections, the *Tax Policy* unit has worked on designing ongoing personal income tax relief of R13,3 billion, increasing the minimum tax threshold further and adjusting the tax brackets to benefit mainly low- and middle-income taxpayers for the 2003/04 financial year.