PROVINCIAL GOVERNMENT
WESTERN CAPE

PROVINCIAL TREASURY

WESTERN CAPE FISCAL POLICY 2002 – 2005

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Foreword

The Western Cape Fiscal Policy (WCFP) 2002 – 2005 attempts to describe how resources are and should be allocated within the Province. It provides a framework for spending plans and links that to the funding possibilities available to the Province. What is not often appreciated is that the funds available greatly depend on the country's economic performance in a competitive regional and global environment. Expenditure plans are conducted within a three-year medium term fiscal framework, but acknowledging that internal and external factors and practicalities affect the allocations awarded to the different functions.

The overall aims of the Policy are to reduce poverty and unemployment, improve equity through accessibility to quality services, enhance efficiency in delivery (especially education) maintain and improve physical infrastructure, create a safer environment, improve welfare and living conditions, strengthen accountability and long run growth and development.

To achieve government's goals it is not sufficient to only formulate appropriate policies and strategies, but we have to ensure that these are translated into effective spending by all departments. This is the real challenge for the Western Cape Government, achievable only through a collective endeavour by the Province and the stakeholders that we serve or interact with.

I wish to thank my co-writers for their concerted efforts to produce this publication, as well as Professor Servaas van der Berg, Department of Economics, University of Stellenbosch for his valued comments. Their names are listed in the table below, and comments are invited from readers with a view to improve the Western Cape Fiscal Policy further during 2002.

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INTRODUCTION

1

Evolution of the budget system in the Western Cape

Fiscal policy

Fiscal policy deals with the sources of revenue (national and provincial) and how the revenue is spent. According to the classical definition of fiscal policy it is built on three distinct pillars namely allocation, stabilisation and redistribution. Fiscal policy therefore focuses on issues such as how much a government can spend, on which services, and how it affects the level of service delivery of existing services that are to be rendered. Choices and trade–offs are made between objectives and goals as available funds will never suffice, given the plethora of real needs. Provincial resource allocation never occurs in a vacuum and many externalities have an effect on the final allocations awarded to the different departments.

The evolvement of provincial fiscal policy

During several strategic sessions in 1998, the Provincial Cabinet adopted eight main allocation principles as a starting point to inform the medium-term expenditure framework (MTEF) from 1999/2000 to 2001/02 on how Provincial resources should be allocated. These principles in essence incorporated the rule of thumb guideline that expenditure on social services (Education, Health and Welfare) had to be no more than 85 % of total provincial expenditure. The remaining 15 % of the total budget for all other services had to be protected from the possible detrimental crowding out effect of social spending pressures on the remaining Provincial services.

During 1999 the Western Cape Treasury provided a policy base for spending plans in the Western Cape Revenue and Expenditure Policy Framework 2000/01 – 2002/03. The Policy Framework *inter alia* allowed for better prediction of future government expenditure and enhanced public transparency in the budget process. The Western Cape Government formulated ten policy goals, better known as the Western Cape Government's Strategic Objectives (WCGSO's). These are described more fully in Chapter 6.

The Western Cape Fiscal Policy Framework (WCFP) 2001 – 2004

During 2000 the Western Cape Revenue and Expenditure Policy Framework 2000/01 – 2002/03, improved in quality and culminated into the Western Cape Fiscal Policy Framework (WCFP) 2001 – 2004.

The overall objective of the WCFP was to direct departmental budget allocations and planning towards attaining the ten WCGSO's. The WCFP *inter alia* contained a chapter on each of the WCGSO's. Departments were required to link their key measurable objectives (outputs) to an applicable WCGSO. Two other chapters addressed the special needs and contingent liabilities of the departments.

The key measurable objectives, special needs and contingent liabilities ultimately formed the departure point for the development of a sequential priority framework for allocating available revenue. Premised on the assumptions that allocations between votes were basically correct, the Sequential Priority Framework dealt with four other main priorities, contingent liabilities (Group A) as the first, followed by Community Safety (Group B) to enhance crime prevention and Group C. The latter was to receive 70 % of the remaining additional funds to be directed towards general capital infrastructure of which percentages as indicated went to each of the following:

Buildings	21 %	
Information Technology	17 %	(Less fixed amount for Environmental Impact Studies)
Roads	60 %	
Tourism	2 %	

Group D received 30 % of the remaining additional funds and catered for special needs recorded on a priority list.

Although not initially part of the Sequential Priority Framework provision for inflationary pressures, salary and social pension improvements translated into a first adjustment constituting the first claim to additional funding received. The latter had to be catered for to prevent the scaling down of existing services in real terms. The WCFP subsequently informed the Budget Statements 1 and 2 for 2002/03 and the medium-term expenditure period. The process deepened the understanding of resource allocation, fiscal policy and of socio-economic realities. In addition the WCFP incorporated key measurable departmental objectives, more predictable allocations with amendments on the margin and links between planning, policy and the amounts to be budgeted.

Evolution of the budgeting system

The Public Finance Management Act, 1999 (Act 1 of 1999), the Treasury Regulations, 2001, and the Public Service Act, 1994 (Proclamation 103 of 1994), make the tabling of departmental Annual Reports (inclusive of financial statements) and departmental strategic plans in the Western Cape parliament compulsory.

Annual reports had already been introduced in respect of the 2000/01 financial year, whilst the strategic plans will take effect from 2002/03. Thus the total package of fiscal policy, strategic plans, budget statements and annual reporting all ultimately have in common to:

- promote transparencies and political oversight of resource allocation and spending;
- link policy choices with resources;
- deliver services where most needed; and
- strengthened long term planning.

The focus/direction and contents of the Western Cape fiscal policy 2002 – 2005

Formulation of the new WCFP 2002 - 2005

The purpose of the latest fiscal policy is to describe the funding possibilities available to the Province and to give an overview of all the issues that influence the composition of provincial budgets (Chapters 2 and 3). An assessment of fiscal government performance is done in Chapter 4. Capacity building or human resource development and the effective management of contingent liabilities (Chapter 5) are sources of key challenges that lie ahead for the Provincial Treasury. The policy imperatives (Chapter 6) that drive the allocation process (Chapter 7) attempt to explain the suggested future course or direction that the Province should follow.

The new procedure prescribed by the National Treasury on how to compile strategic plans in line with Budget Statements 1 and 2 necessitated many changes in the budget process where responsibility should be vested in future. These changes suggested a different approach to formulating fiscal policy. Therefore, the Planning Component in the Office of the Director-General co-ordinated their planning efforts with those of the Provincial Treasury and uniform templates for the measurable objectives of departmental strategic plans and Budget Statement 2's were compiled. This hopefully not only assisted departments in compiling their strategic plans, but also helped ensure that the latter were seamlessly aligned with the departments' programmes and organisational structures to facilitate accountable execution and monitoring of their stated objectives.

To avoid duplication of information, the measurable objectives of the departmental strategic plans have not been included in the new WCFP 2002 – 2005, but will be reflected in departmental Budget Statement 2's. Greater emphasis is now placed on actual fiscal policy issues and the new document should thus be more reader-friendly with less repetitive information. It should also provide a clearer picture and a sense of the direction the Provincial Treasury intends to follow over the medium term.

The contents and key features of the WCFP 2002 - 2005

The contents of the new Western Cape Fiscal Policy (WCFP) 2002 – 2005 consists of seven chapters, briefly summarised as follows:

Chapter One provides the history, purpose and focus area of the entire document.
Chapter Two provides a very brief economic overview of South Africa.
Chapter Three describes the fiscal envelope, consisting of the division of revenue between the three spheres of government, the provincial equitable share, conditional grants, provincial own revenue and provincial borrowing.
Chapter Four entertains a general overview of expenditure efficacy, financial systems, accounting, training and human resource development and procurement. It thus gives some idea of the current status of fiscal performance and the challenges that lie ahead.
Chapter Five assesses the contingent liabilities and debtor status of the Western Cape Government.
Chapter Six explains the policy imperatives and framework underlying the fiscal policy of the Western Cape Government. This entails per capita growth, poverty reduction, vulnerability and dealing with income disparity. It also presents efforts at trying to obtain inputs from other institutions and the public on fiscal policy. Furthermore, the departments that participated and interacted to determine fiscal policy, Provincial Parliament and the Executive are also referred to.
Chapter Seven concludes the main focus areas and proposal for the 2002 – 2005 MTEF allocation framework, taking into account the issues raised in the previous six chapters.

Focus on the fiscal framework and sequential priority framework

Underlying principles of allocating R13 billion

The underlying principles in allocating a budget of R13 billion could be briefly summarised as follows:

- As a first principle the Provincial Cabinet priorities should be adhered to.

- Secondly, the augmentation and stabilisation of social sector spending should take into account the following factors:
  - Conditional grants;
  - Improved efficiency in resources used and associated financial management; and
  - An assessment of the required socio-economic delivery in relation to available skilled personnel.

- As a third principle, although growth in economic services spending is chiefly dependent on:
  - Improved macro-economic conditions;
  - Growth in own revenue; and
  - Improved efficiency, effectivity and financial management overall in the Province, the derived thrust of additional resources becoming available for redistribution should necessarily be prioritised in this direction. This would also be in synch with the statements impressed in the Medium Term Budget Policy Statement, 2001, of the National Treasury.

- Growth in the transversal sectors will be dependent on the contribution made towards general productivity and management.

The financial constraints on the allocation process and sources available for allocation

National transfers (equitable share and conditional grants) contributes on average 94 % of the total provincial revenue with provincial own revenue making up the balance of 6 %. In the previous MTEF the total provincial revenue of R13,191 billion were foreseen for 2002/03, R13,838 billion for 2003/04 and R13,838 billion for 2004/05.

Additional funding available for allocation (R625,074 million for 2002/03, R477,327 million for 2003/04 and R1,248,085 million for 2004/05) is proposed to be prioritised and allocated as outlined in Chapter 7.

Trade-offs/reprioritisation

The current inputs received from departments include many contingent liabilities and special needs for 2002/03, respectively amounting to R1,487 billion and R1,765 billion for the Province. These needs and contingent liabilities should be considered against the background of the main theme of the national and provincial financial community. In essence this implies that additional allocations from the equitable share should be directed towards lessening of inequality, and reducing poverty and vulnerability in South Africa, primarily by supporting those initiatives, whether in the private or public sector, that would contribute to job creation and increased universal prosperity.

Against this backdrop, it can be expected of departments to address their requirement by also making trade-offs between any special needs, contingent liabilities and current budgets. Concerted steps over the 2002 – 2005 MTEF period should be instituted, *inter alia* to:

- Improve performance by setting and delivering on priorities;
- Improving maintenance and upgrading of physical infrastructure;
- Improving the overall economic performance of the Western Cape;
- Improving overall efficacy of spending;
- Stabilising social delivery; (Education, Health and Social Services)
- More efficient use of current infrastructure;
- Revisiting the purpose and scope of existing services;
- Looking for synergy between different services;
- Maintaining fiscal discipline; and
- Exploiting new sources of revenue and optimising existing sources.

2

S A MACROECONOMIC OVERVIEW

Economic review

According to the South African Reserve Bank's latest Quarterly Report[1], the weakening of the international economy negatively affected growth in the South African economy during the first quarter of 2001. However, the domestic economy improved from an annual 2 % per annum in the first quarter of 2001, to 2,5 % in the second quarter.

The recovery of the South African economy in the first half of 2001 may therefore be attributed, *inter alia*, to the flexibility of the exchange rate. The fact that the potential benefits emanating from the recent depreciation of the rand was not eroded by a higher level of inflation, as has happened previously, also had positive effects in that the economy did not slow down further.

The Bureau of Economic Research is of the opinion[2] that the risk scenario due to a weaker world economy and a weaker exchange rate, incorporates the likelihood that South African export and import volumes and prices could be affected, with imported upward pressures on inflation. The real effect, together with a weaker world economy, should impact negatively on confidence levels, both at consumer and at business levels.

In his address to Parliament on 30 October 2001 the Minister of Finance, Mr Manuel, made the following statement[3], "Since the 2001 Budget was tabled during February 2001, a deteriorating international economic trend has been rocked by attacks against the United States and the resulting war in Afghanistan. The slowdown in world growth has deepened and financial markets have experienced a flight from risk to safe havens". However, he emphasised the fact that although the rand weakened considerably against other major currencies, South Africa's economic base has improved. South Africa is thus in a position to avoid the dislocation that many other emerging economies are currently experiencing.

Compared to the 1998 situation, the rand again depreciated by the same margin during 2001. However, key elements of the SA economy which performed well could be listed as follows:

- Growth of 10,4 % in merchandise export volumes in the first half of this year, compared with the same period in 2000;
- Growth in services exports by some 15 % over the same period;
- Steady growth in most sectors of the economy this year, and particularly in wholesale and retail trade, financial services and the transport, storage and communications sectors, have contributed positively to the economy;

- An improvement in domestic investment across a broad range of industries, including real growth in both public and private sector capital formation;
- A modest recovery in domestic saving, accompanied by an encouraging reduction in household debt relative to incomes; and
- Steady declines this year in both producer and consumer price inflation.

In summary, the global economic slowdown should not affect South Africa as much as previous economic slowdowns. The main negative effects for the South African economy in the near future will be:

- Subdued demands for SA exports;
- Currency volatility;
- The fuel price may threaten inflation forecasts; and
- Further cutbacks in interest rates may not be achieved if inflation reverses its current downward trend.

Government performance

Policy and delivery on GEAR

The government's policy is to achieve stable economic growth and to create a sufficient level of employment in the country. GEAR further attempts to address inequalities and promote the redistribution of resources to the poor as well as to create an environment where basic services are available to all people. Solid macroeconomic management to sustain growth and social upliftment was hampered to some extent by labour legislation. This led to a lack of investor confidence, which did not sufficiently promote GEAR, while poverty reduction and employment generation were less successful. Over the last two years a number of investigations into new labour market legislation[4] have unfortunately as yet not really improved the situation.

Service delivery in government

From a provincial and local government perspective, service delivery issues have been extensively addressed by the National Minister of Finance, in his Intergovernmental Fiscal Review tabled in Parliament on 9 October 2001, and will not be repeated here.

The Economy of the Western Cape

The lack of economic indicators currently, makes it difficult to review a provincial or regional economy relative to the SA economy or other provincial economy. However, Statistics South Africa (SSA), is in the process of investigating means to produce data on provincial level which should be available within a year or two.

According to The Western Cape Investment and Trade Promotion Agency (WESGRO)[5], the following aspects of the Western Cape Economy can be highlighted for 2002:

- The tragic events on 11 September 2001 in the United States with the subsequent fears about the safety of travelling should have a further negative effect on the Province's tourist industry as statistics indicated that overseas tourists visiting the Western Cape have already declined by 3 % from 1999 to 2000 prior to the attacks on America. This will also negatively affect hotel occupancy levels;
- The current turbulence in the world economy should also have a negative effect on the demand for exported commodities, such as fruit, wine and steel. If the supply of commodities, such as agricultural products due to excellent winter rains, could improve in quality and the right volumes and prices be supplied, exports should however, continue to grow;
- In summary, the lower than expected growth in the Western Cape Regional Economy could be attributed to *inter alia*:
  - extremely adverse world market conditions for core agricultural products such as fruit;
  - fewer overseas tourists visiting the Province;
  - reduced activity in property markets due to lower in-migration into the province;
  - the negative impact of the change in spending habits of the consumer;
  - the slump in steel prices and its effect on Saldanha Steel.

References

[1] SA Reserve Bank quarterly bulletin: September 2001
[2] Bureau for Economic Research: Economic Prospects third quarter 2001
[3] Address to the National Assembly on the introduction of the Adjustments Appropriation Bill and hte 2001 Medium-Term Budget Policy Statement: 30 October 2001
[4] H. Bhorat, et al, Fighting Poverty, Labour Markets and Inequality in South Africa, 2001
[5] Business Prospects 2002, Western Cape, WESGRO, November 2001

3

FISCAL ENVELOPE

3.1 Division of revenue between the three spheres of government

Division of Revenue

Section 214 of the Constitution of South Africa, 1996 (Act 108 of 1996) ("the Constitution") provides for the sharing of nationally raised revenue between, the three spheres of government. It also provides for the determination of each province's equitable share of the provincial share of revenue. Section 227(1) of the Constitution, 1996 entitles each province to an equitable share to enable them to provide and perform basic services that are constitutionally entrusted to them. Each year a Division of Revenue Act is enacted that sets out the equitable share for each sphere of government, the horizontal division between the nine provinces, and provides detailed schedules of all other allocations (conditional grants) from national departments to the respective provinces and local governments.

The "vertical division" refers to the allocation of nationally-raised revenue between the three spheres of government. Before the "vertical division" of revenue can be effected between the different spheres of government. National Treasury provides for debt service cost and contingency reserves. The latter two items are always regarded as the first liability against the National Revenue Fund.

Adjustments to the fiscal envelope will affect the vertical division as more or less funds will then be available for distribution between the three spheres of government. Changes in economic growth of the Country have a direct influence on the "vertical division" as inflation or fiscal deficit targets may change which could affect total national revenue, borrowing and taxes. This may also lead to trade-off decisions between whether government expenditure as a percentage of GDP should change and what the socio-economic consequences for the Country could be.

Adjustments to baseline allocations are fundamentally the outcome of government's policy priorities. The medium-term expenditure planning process and recent reforms to the budget programme reinforced the linkages between policy, strategic planning and budgeting. While this clearly needs the co-operation of all three spheres of government to do the planning[1], the executive responsibility for policy choices in this regard rests with Cabinet at national level. The "vertical division" is therefore

[1] Division of Revenue Protocol Memorandum, Budget council Lekgotla 4-7 July 2001.

essentially a political judgement for which national Cabinet takes responsibility in preparing the budget framework each year. The national Cabinet also considers the concurrent nature of many government functions. The "vertical division" of revenue is considered each year at an extended Cabinet meeting, where the provincial premiers and their members responsible for financial matters attend the proceedings.

Transfers from national to provincial and local governments can usually be categorised as either equitable shares or conditional grants. Equitable shares are unconditional transfers to the other two spheres of government, but conditional grants, on the other hand, were introduced to expand oversight by national departments by ensuring the attainment of certain national policy objectives by provinces and municipalities.

The provincial share of the "vertical" division of revenue[2] that is divided (horizontal division) between the different provinces is referred to as the equitable share. The provincial equitable share on average, comprises 86 % of the total revenue of provinces and is calculated by means of a formula.

It is thus evident that the equitable share allocation is used to fund the bulk of public services rendered by provinces.

The evolution of the equitable share formula

The history of how the formula evolved can be briefly summarised as follows:

- The formula was introduced for the 1998/99 Budget and relied primarily on data from the preliminary 1996 Census;
- For the 1999/00 Budget, the formula was updated to reflect the final 1996 Census results and the basic component was split into a basic share and backlog component. The formula was implemented with a five-year phase-in plan to be completed in the 2003/04 Budget year;
- For the 2000/01 Budget, remuneration data (from the Stats SA quarterly report on remuneration based on the Regional Services Council payroll levy) replaced gross geographic product (GGP) data in the economic activity component of the formula;
- For the 2001/02 Budget, no changes were made to either the structure of the formula or the data; and
- For the 2002/03 Budget, certain weightings were changed as reviewed later in this document.

[2] National Treasury Budget Review, 2001.

The seven components of the equitable share

The equitable share formula for 2002/03 comprises seven components that attempt to capture the relative demand for services between provinces and to adjust for particular provincial circumstances:

- An education component (41 % weighting) based on the average school-age population (ages 6-17), and the number of learners in schools enrolled in the public ordinary schools for the past 3 years;
- A health component (19 % weighting) based on the proportion of the population without access to medical aid funding;
- A social security component (18 % weighting) based on the estimated number of people entitled to social security grants – the elderly, disabled and children – weighted using a poverty index derived from the Income and Expenditure survey;
- A basic component derived from each province's share of the total population of the country (7 % weighting);
- An institutional component divided equally among the provinces to reflect the costs of running a provincial government (5 % weighting);
- A backlog component based on the distribution of capital needs as captured in the Schools Register of Needs, the audit of hospital facilities and the share of the rural population (3 % weighting); and
- An economic output component (7 % weighting) based on the distribution of total remuneration in the country.

The different sets of data that are used for the compilation of each component clearly illustrates how the weightings differ per component between provinces. The basic share that is weighted on the 1996 Census population could be taken as benchmark to see how all the other components deviate where other data influences the weights of each component.

Table 1 shows the pre–2002/03 structure and distribution of the shares by component and the target shares to be reached by 2003/04 for the nine provinces.

Table 1

Components	**Education**	**Health**	**Social welfare**	**Basic Share**	**Economic Activity**	**Institutional**	**Backlog**	**Target 2003/04**
Weighting	41,0	19,0	17,0	7,0	8,0	5,0	3,0	100,0
Eastern Cape	18,5	17,0	19,6	15,5	6,5	11,1	20,6	16,9
Free State	6,3	6,5	7,1	6,5	5,3	11,1	5,7	6,6
Gauteng	12,3	14,7	13,9	18,1	41,6	11,1	5,1	15,5
Kwazulu-Natal	22,1	21,7	19,6	20,7	17,0	11,1	22,9	20,6
Mpumalanga	7,3	7,2	6,5	6,9	4,9	11,1	8,5	7,2
Northern Cape	1,9	2,0	2,2	2,1	1,7	11,1	1,3	2,4
Northern Province	15,7	13,3	13,7	12,1	3,0	11,1	22,9	13,6
North West	8,0	8,6	8,7	8,3	5,7	11,1	9,4	8,3
Western Cape	7,9	8,9	8,8	9,7	14,4	11,1	3,7	8,9
Total	**100,0**	**100,0**	**100,0**	**100,0**	**100,0**	**100,0**	**100,0**	**100,0**

Note that Table 1 does not show adjustments in the weightings discussed below.

Status of the Western Cape Budget in respect of the equitable share

Table 2 below shows how the revision of the formula affected the Western Cape Province in monetary terms, after also making allowances for revised inflation projections and the latest agreement on improvement of conditions of employment for public servants.

Table 2: Net Changes to Equitable shares and Conditional grants on a year-to-year basis

	2002/03 R '000	2003/04 R '000	2004/05 R '000
Equitable Share	312,945	393,072	[3]1,125,996
Conditional Grant	11,436	(1,800)	82,635
Net difference	**324,381**	**391,272**	**1,208,631**

Revision of the equitable share formula

The structure of the equitable share formula has been retained for the 2002/03 Budget. The formula, however, has been adjusted to reflect the increased spending on social services in provinces and new data to make provision for new and more accurate data that have become available.

Firstly, the weighting of the social services components in table 1 reflect expenditure on these services over a three year period. Based on expenditure data reported in the Intergovernmental Fiscal Review 2001, the average share of welfare in 2001/02 had risen to 19 %. This resulted in the welfare weighting component being increased by one percentage point. A balancing reduction of 1 % in the weight of the economic component was also effected, advantaging poorer provinces.

Secondly, the formula has been updated with the latest enrolment data in education. The data used in the education update is the average of the past three years (1998, 1999 and 2000) obtained from the Department of Education.

Conditional grants

Conditional grants are proportionally a small but significant portion of provincial revenue. These grants were introduced in 1998/99 to support national priorities, particularly in the social services sector. Conditional grants are used for the following reasons:

- Enable national priorities to be provided for in the budgets of other spheres of government;
- Promote national norms and standards in a specific sphere of government;
- Compensate provinces for cross border flows and inter-provincial benefits;

[3] The higher than proportional growth includes provisions for inflation and salary increases that have already been provided for in 2002/03 and 2003/04.

- Support capacity-building and structural adjustments to effect transition; and
- Address backlogs and regional disparities in social infrastructure.

The administration and functioning of conditional grants has generated numerous problems since their introduction. The various annual Division of Revenue Acts have also progressively introduced measures aimed at addressing some of these problems, but the administrative burden has increased significantly for provinces as new measures are introduced each year while others are changed, which implies that provincial treasuries and departments are compelled continuously to introduce new control and reporting measures. It is hoped that the 2002/03 Division of Revenue Bill will finally complete this process of reform. The reforms were aimed at promoting early planning and enhancing transparency and accountability by clarifying the responsibilities of national and provincial departments.

Table 3: Percentage growth in conditional grants in comparison with Budget 200/01

Percentage growth	2002/03	2003/04	2004/05 *
Health: Tertiary and professional training	-2,92	-5,94	-4,36
Housing fund	8,72	16,27	22,16
Provincial infrastructure	0,00	0,00	23,42
Supplementary grant	-0,12	-0,17	0,34
Other	24,60	26,66	32,73
Total	**0,60**	**-0,08**	**3,69**

* The base year used for calculations was the allocation of conditional grants for 2003/04 as allocated in the 2000 budget.

The **health conditional grants** [National tertiary services (NTS) and Health professional training development grants (HPTD)] comprises an average of 63 % of the total conditional grants received by the Province. During the current financial year the health sector has developed a new framework for the tertiary services and training grants, which provides for a major reconfiguration of the three tertiary services and training grants, with a view to make them more equitable and available to all provinces. This redistribution of funds from the Western Cape and Gauteng to other provinces will effect a change to the structure of health conditional grants (NTS and HPTD) as an average decrease of 4,4 % over the period 2002/03 to 2004/05 for the Western Cape as shown in table 3. According to National Treasury the said provinces are expected to fund any resulting shortfalls from their equitable shares or own revenue resources. This change to the structure will be phased in over the next five years.

The purpose of the NTS and HPTD is as follows:
- To fund national tertiary services, as identified and costed by the Department of Health (DOH);
- To ensure equitable access by all South Africans to basic tertiary health level care;
- To ensure collective planning for tertiary services;
- To support the training of health professionals;
- To support provinces to fund service costs associated with undergraduate and post-graduate students training;
- To development and recruit of medical specialists in under-served provinces; and
- Enable shifting of teaching activities from central hospitals to regional and district facilities.

The purposes of the **housing fund and provincial infrastructure grants** are:
- To help accelerate construction, maintenance and rehabilitation of new and existing infrastructure, and to fund the reconstruction and rehabilitation of infrastructure damaged during the 1999/2000 floods; and
- To finance subsidies under the national housing programme.

The **supplementary grant** was used as a mechanism for consolidating small grants in the 2001 Budget, as part of the rationalisation process. The main component of this grant is the finance supplementary grant. Other smaller components of this grant is the Housing capacity building grant, National Land Transport Transition Act (NLTTA) grant, Health financial management grant and Financial management (implementation of PFMA) grant.

The purpose of the supplementary grant can be summarised as follows:
- Supplementing provincial budgets in order to ensure that provinces budget adequately for health, welfare, education, and other priorities as agreed between provinces and national government;
- Ensuring that provinces make progress in implementing the PFMA, 1999 and improving financial management; and
- Enabling provinces to provide for functions for which grants have been consolidated into the supplementary allocation.

The Financial and Fiscal Commission (FFC) report

In terms of sections 214 and 220 of the Constitution, 1996, the Financial and Fiscal Commission (FFC) must make recommendations that inform the intergovernmental policy process, including recommendations on the equitable division of revenue in the annual division of Revenue Bill. The FFC made a submission in June 2001 that made recommendations to inform the intergovernmental-policy making process.

Government did not accept the FFC's new recommendations and the reasons can be summarised as follows:

The aspects of the 2001 FFC recommendations are broadly consistent with the current approach to the division of revenue. Nevertheless, to the extent that the FFC proposals still have embedded in them an approach which seeks to translate constitutional provisions on basic services into a "formula based approach" to the division of revenue, they still suffer some of the deficiencies of the "costs norms" approach proposed last year. These include:

- Lack of concise definitions of constitutionally mandated basic services associated with each sphere;
- Non-existence of objectively determined norms and standards pertaining to all other constitutional functions; and
- Unavailability of data.

Unless it can be demonstrated that current divisions of nationally raised revenue, both vertical and horizontal, are inequitable in a way that allocates disproportionately more resources to one or two of the spheres and/or some of the provinces or local governments, there is no sound basis for jettisoning the current approach and the provincial and local government equitable formulae. The benefits of changing the formulae must always be weighed up against the disruptions, instability and uncertainty that would arise from those changes. However, the process of regularly reviewing the formulae with a view of effecting changes at the margin should be maintained.

3.2 Own revenue overview and trends

This Province, like all the other, is heavily reliant on transfers from National Government, as provincial own revenue represented only 6,67 % of the total provincial revenue in 2000/01. Although own revenue sources are fairly limited and consist in the main of motor vehicle licences, hospital fees and gambling and betting taxes, they remain an important source of provincial funding at the margin. Growing demands on the fiscus to meet the required level of service delivery necessitated the Provincial Treasury to institute measures to ensure the maintenance and stability of own revenue sources to maintain fiscal stability in the Province. Although own revenue for 2001/02 is projected to decline, if compared to the previous year's actual, it is projected that own revenue as a percentage of gross provincial revenue will vary between 5,55 % in 2001/02 and 5,89 %, 5,93 % and 5,56 % in the years 2002/03, 2003/04 and 2004/05 respectively. Total transfers from National Government over the same period are also projected to increase at a rate of 8,63 %, 4,63 % and 6,12 % respectively. In respect of the years 1999/00 and 2000/01 own revenue collected represented 8,63 % and 8,77 % of the total equitable shares respectively, being considerably more than the national average of between 4 % and 5 %. Table 1 below captures the changes as described above in some more detail.

Table 1

Provincial Revenue Envelope															
Revenue resources		ACTUAL						BUDGET							
		1998/99		1999/00		2000/01		2001/02		2002/03		2003/04		2004/05	
		R'000	%	R'000	%	R'000	%	R'000	%	R'000	%	R'000	%	R'000	%
OWN REVENUE SOURCES	Motor vehicle licenses	251,497	48	299,072	41	344,127	43	427,741	62	491,519	62	564,839	67	564,839	68
	Hospital fees	66,098	13	61,679	8	70,451	9	67,955	10	70,721	9	74,726	9	78,900	9
	Betting	32,008	6	29,773	5	27,733	3	21,038	3	15,500	2	15,500	2	15,500	2
	Gambling		0		0	21,654	3	85,667	12	84,000	11	84,000	10	84,000	10
	Casino Bid Fees		0	135,000	18	11,400	1		0		0		0		0
	Other	178,067	33	207,805	28	319,342	40	88,474	13	136,212	17	104,003	12	92,404	11
	Grand total	527,670	100	733,329	100	794,707	100	690,875	100	797,952	100	843,068	100	835,643	
NATIONAL TRANSFERS	Equitable share	8,199,006		8,499,192		9,059,151		9,761,840		10,614,985		11,129,346		11,862,270	
	Conditional grants	1,627,200		1,696,310		2,084,533		1,997,881		2,129,397		2,236,720		2,321,155	
	Total National payments	9,826,206		10,195,502		11,143,684		11,759,721		12,744,382		13,366,066		14,183,425	
	Total Provincial revenue	10,353,876		10,928,831		11,908,061		12,450,596		13,542,334		14,209,134		15,019,068	

The consistent growth in provincial own revenue in this Province can be contributed to some concerted efforts by the Provincial Treasury and Departments in the implementation of new initiatives coupled with the annual revision of user charges and fees in terms of the Treasury Regulations, 2001.

Major own revenue sources

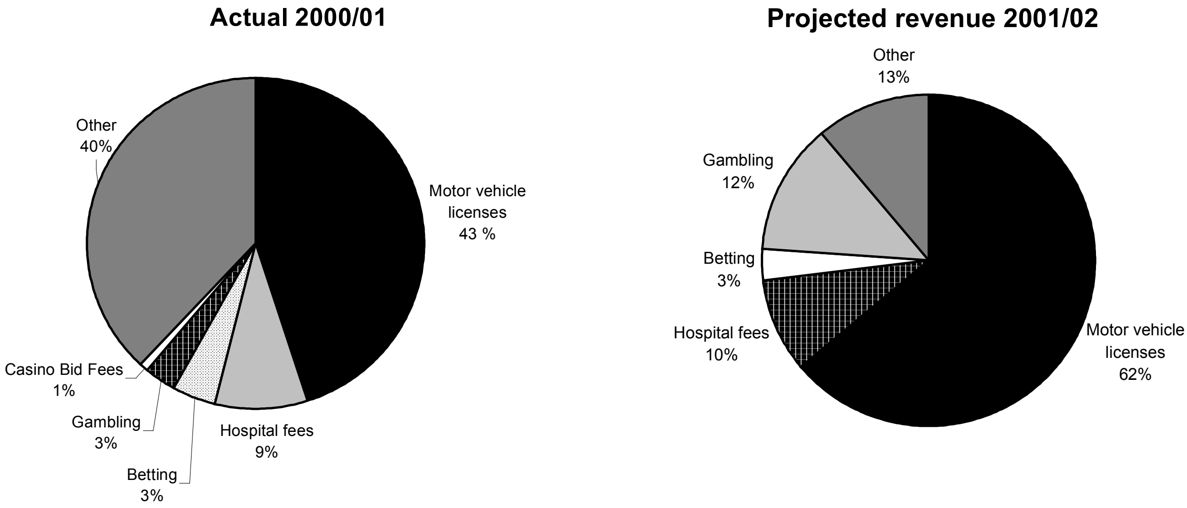
Motor vehicle licences

The Western Cape Province has exclusive responsibility under the Constitution, 1996 for provincial roads and traffic. Although the Constitution provides for concurrent national and provincial responsibility for public transport, traffic registration and vehicle licensing, motor vehicle registration and licensing, roadworthy testing, the issuing of learners' and drivers' licences and other traffic-related activities are carried out in terms of the Road Traffic Act, 1989 (Act 29 of 1989) and associated regulations. In the interim this Act has been repealed and replaced with the National Road Traffic Act, 1996 (Act 93 of 1996) and the National Road Traffic Regulations that have been promulgated in terms thereof. Section 92 of the National Road Traffic Act, 1996 determines that "fees payable shall be as provided by the laws of the province concerned". The Western Cape Road Traffic Act, 1998 (Act 12 1998), which became effective on 18 December 2000, is a Provincial act in terms of which this Province, through the Provincial Minister for Transport, may issue regulations determining its own taxes / fees and rate structures.

This source of revenue currently represents the biggest single source of provincial own revenue in the Province. In line with national norms for the years 1998/99 to 2000/01, these fees represented approximately 45 % of total provincial own revenue. However, after an extensive investigation during the year 2000/01 into the fee structure of motor vehicle licences in the Province, a once off average increase of approximately 25 %, effective 1 April 2001, was implemented with further increases of 15 % over the remaining medium term expenditure framework ("MTEF") period. These increases have now resulted in motor vehicle licence income representing in excess of 60 % of total provincial own revenue with projections for the year 2004/05 growing to an estimated 68 % of total provincial own revenue. The rationale behind this major increase was in the main to supplement the current funding that is voted for the maintenance of the provincial road infrastructure. The underlying principle behind these new taxes was the setting of higher rates for heavier vehicle weights, which implies that road damage, and therefore maintenance costs, are directly related to vehicle size.

Figure 1 below shows the make-up of total own revenue and most importantly the shift in motor vehicle licence fees as a major source.

Figure 1



Comparing whether a correlation exists between the increase in motor vehicle licences versus spending levels on maintenance of provincial road infrastructure, it can be mentioned that funding towards the maintenance of the provincial road infrastructure shows a degree of fluctuation and does not increase in the same margin as that of motor vehicle licences. It does, however, show a 21 % increase in budgeted spending with regard to road infrastructure for the years 2001/02 to 2002/03. What the Department of Economic Affairs, Agriculture and Tourism has opted to do was to utilise some of the additional funding for roads to fund initiatives under the transport programmes to address the problems identified by the Department surrounding the ever-growing taxi industry. It is acknowledged that significant year-on-year increases in motor vehicle licences can pose a fiscal risk to the credibility of the revenue budget, as road users might decide to migrate the registration of their vehicles to other provinces with a cheaper motor vehicle licence rate structure, thus putting further pressure on law enforcement resources to control this. However, one should acknowledge that although the motor licence rates in this Province are amongst the highest in the country, the Province can be complimented for its fiscal efforts applied, referring to the degree to which this Province is using its revenue-raising potential effectively, to the ultimate benefit of the same road users.

Hospital patient fees

In terms of section 226(1) and (2) of the Constitution, 1996, revenue collected by the Department of Health is required to be deposited into the Provincial Revenue Fund. Hospital patient fees are generated in the main from sales of services to private patients in a competitive market and it is therefore not regarded as a compulsory fee or tax. Given the public nature and substantial state funding relating to the Health sector one can argue that public health services are not rendered in a true open market system. The demands of this type of public service clearly dictate the supply. In most cases, although it is linked to prices and tariffs, the provision of Health services in the public sector is a constitutional requirement and is provided to patients who might only pay a portion of the tariff or alternatively receive services free of charge. In the spirit of Batho Pele, this Province maintains that if the standard of service delivery is to be improved, this perception could change to a culture of payment for services rendered. In line with national trends, revenue collections within the Department of Health have shown a persistent decline between the years 1996/97 and 1999/2000 which in this Province in particular, even faster than the national average.

According to national evidence the main reason for the decline in hospital revenue was the reduction in the number of paying patients using public sector facilities. The loss of medical aid patients to the private sector, coupled with free services to certain citizens as a result of national policy amendments and an increasing culture of entitlement and non-payment reduced the capacity for revenue at public hospitals.

The Department of Health has managed to reverse the downward trend in hospital fees since 2000/01 and has made good progress in increasing revenue collection from patient fees, which in the main can be attributed to improved administration in the collection of outstanding accounts, increased tariffs and the collection of overdue accounts by a contracted debt collector. This is evident in the fact that revenue collection during 2000/01, compared to 1999/2000, increased by 14 %, which is substantially higher than the average patient fee increase of 8 % during the same period.

A major critical challenge currently facing the Department of Health is to attract larger numbers of paying patients to make use of the public sector facilities. In this Province, as per the hospital and private patients per patient classification, private patients as a percentage of total hospital patients has shown a consistent decline in all major categories, except for the category of in-patients, from an average of 5 % to as low as 2 % from 1998/99 to 2000/01. Initiatives from the Department of Health currently being implemented to grasp this window of opportunity, is the introduction of a Uniform Patient Fee System ("UPFS") in the Province and the concluding of preferred provider agreements with medical aid societies whereby private patients make use of public facilities by way of shared services. The current billing system, which is fraught with inefficiency, has paved the way for the UPFS, which will provide for more effective billing based on a professional fee and a facility fee. With regard to the preferred provider agreements, one should realise that this challenging initiative of attracting payment of private patients back to the public hospitals is a longer-term initiative which will require capital investment to address the quality of care issues such as old equipment and the aesthetic or quality of services provided by public hospitals. Politically and socially, the challenge that the Department of Health is facing, is to ensure that this policy does not lead to the "impression" that different classes of health care exists within public facilities. One should agree, given the constraints, that these initiatives will be to the benefit of both the public and private sectors.

Gambling and Betting

The Western Cape Gambling and Racing Law, 1996 (Law 4 of 1996) is the regulatory framework that regulates gambling and racing activities and incidental thereto in the Province and or enforced by the Western Cape Gambling and Racing Board, a provincial Public entity. In this Province two important distinctions must be drawn, namely between horse racing and casino gambling. In South Africa, gambling on horseracing has been legally permissible for more than a century, as opposed to legal casino gambling, which up to fairly recently was only legal in the former homelands. Horse racing in the Western Cape is an important contributor towards tourism, provincial taxes and in the socio-economic context towards employment. Casino gambling on the other hand is still in its infancy stage with the first licensed casino having opened its doors during October 2000. A further two casino licences were allocated in the West Coast and the Metropole during the latter half of 2000.

Betting revenue comprises taxes generated from the totalisator and bookmakers. For the past three years (1998/99 – 2000/01) bookmakers contributed on average R18,4 million (± 63 %) annually to total betting revenue consisting mainly of betting on horse racing, as opposed to betting on other sporting events. Totalisator taxes on the other hand for the same period contributed on average R10,7 million (±37 %) annually to total betting revenue. Revenue from betting is dependent on various factors, some of which are the weather, the quality of thoroughbred racehorses and the amount of stakes, to name but only a few. However, the horse racing industry in general is facing difficulties due to the advent of and competition from other forms of gambling like casino gambling, the national lottery and the possible implementation of a limited gambling machines industry. As for the future, betting revenue could decrease mainly as a result of the aforementioned alternative forms of legalised gambling.

Revenue from casino gambling is a fairly new revenue source in the Province. Total gambling revenue from the opening day of the first legal casino in October 2000 to 31 March 2001 amounted to R21,65 million which was well above projections for the 2000/01 financial year. Slot machines proved to be the most popular and were the main contributor to gambling taxes, which was R16,8 million (77,6 %), over the same period. Once-off revenue in respect of casino bid fees to the amounts of R135 million and R11,4 million were received in the years 1999/2000 and 2000/01 respectively.

Own revenue from both the horse racing and casino industries has recently shown dwindling turnovers, which poses a risk to own revenue streams and a challenge to prepare fiscally credible and achievable revenue budgets. In this regard, the Provincial treasury has chosen to budget conservatively with projected figures that correlate with industry expectations. The aforementioned, coupled with the uncertainty whether the limited gambling machine industry will come into operation within the next two years, are clear indicators that revenue from horse racing will decrease over the MTEF, whilst revenue from the casino industry is expected to remain consistent over the same period, in the amount of approximately R84 million annually.

Other revenue

The residual category of revenue, namely other revenue, represented 40 % of provincial own revenue in 2000/01 of which R150 million consisted of interest received as a result of improved cash management in the Province. For the financial years 2003/04 and 2004/05 falling investment interest in the amounts of R32,634 million and R19,701 million are projected mainly due to the systematic lowering in liquidity of the Provincial Revenue Fund. The remainder represented in the main user charges and fees which include abnormal load permits, commission fees paid by insurance companies, examination fees, sale of provincial property (which include buildings and livestock), liquor licences, etc. Also included, are payments from the three local universities that use the academic hospitals as part of their medical training. In general, user charges and fees are regarded as payments charged for a specific marketable goods or services for which a direct benefit accrues to the person making the payment. The fee structure, which is revised at least annually by the accounting officers of departments in terms of the Treasury Regulations, is based strictly on the cost-recovery principle. User fees are therefore regarded as an efficient way of recovering the cost of publicly provided goods and services and provide incentives for improving the quality of service delivery. A further advantage to regular revision is that user fees can relieve some pressure on budgets without compromising national economic policies and can therefore be expanded as required by departments.

Another portion of other revenue is so-called miscellaneous revenue, which is very small in nature, and accordingly does not receive the necessary attention. However, the sum of these totals can be significant, although they rise and fall in no discernible pattern, implying that they might be one-off or may not flow according to a regular pattern. One should realise that the unpredictable nature of these revenues make projection very difficult and complicates the budgeting and planning process which remains a challenge to the Provincial Treasury.

Initiatives from the Provincial Treasury

In terms of the Public Finance and Management Act, 1999 (Act 1 of 1999) ("the PFMA"), it is incumbent upon a provincial treasury to promote and enforce transparent and effective management of revenue. To comply with this requirement, the Treasury, with regard to own revenue, will pursue the following objectives:

- Tabling of sustainable and credible revenue estimates;
- Management oversight roles in collection of provincial own revenue;
- Promote and enforce regular revision of tariffs and tariff structures;
- Assist in the management of revenue generation incentives which makes economic sense and which will ensure fiscal prudence; and
- Assist in the improvement of the management/administration of existing sources and the introduction of new taxes.

Tabling of sustainable revenue estimates will provide stable revenue streams for the funding of services. Revenue targets set by departments and evaluated by the Treasury form the basis for estimates over the MTEF period. The implementation of the revenue budget is monitored, as required by the PFMA, and accounting officers have to table remedial steps to address any deviations from budget estimates.

The Treasury will provide advice and support to accounting officers on the implementation of processes that provide for the identification, collection, safeguarding, recording and reconciliation of information regarding revenue. The annual revision of tariffs by the accounting officers, representing one of these processes, will be monitored to ensure that tariffs remain fair and where applicable market-related. This will enable accounting officers to report more transparently on aspects that have a material influence on their revenue yield.

The Provincial Treasury has put in place an incentive scheme whereby departments may retain additional revenues collected, or a portion thereof which is in excess of the revenue target for a specific financial year. This revenue incentive was approved by the Provincial Cabinet during 1998 and re-affirmed in 2000. In line with the revenue incentive scheme, the increased revenue collected above estimates by the Departments of Health and Economic Affairs, Agriculture and Tourism during 2000/01, will result in expenditure levels to be increased appropriately. Additional funding, as a result of increased revenue collection, will contribute to improved service delivery, which in turn could also lead to further increases in revenue generated over the MTEF period and beyond.

Treasury is continuously requested by departments to revisit the current revenue retention policy in order that departments may retain 100 % of revenue collected above revenue targets. However, Treasury remains reluctant to accede to this request until proper systems/databases are in place to identify real own revenue flows versus realistic own revenue budgets whereby Treasury can identify concerted efforts made by departments to exceed targets. Monies such as refunds from previous years, which are common to all departments, should as an example of the aforementioned, be excluded from this calculation.

Challenges facing the Treasury

It is reasonable to deduce that the Province has applied considerable fiscal effort to increase own revenue, for example by means of motor vehicle licences, and as a result have managed to reverse the national downward trend in provincial own revenue collection. However, the challenge is the ability to continuously improve in areas which remain a concern and which include, but are not limited to, improving the management/administration of existing taxes and fees and the introduction of new taxes.

With regard to improving the management/administration of existing taxes, the Treasury needs to build its capacity to determine benchmarks and implement best practices in revenue collection and administration. Initiatives implemented thus far include a detailed electronic Excel-based tariff register of all tariffs in departments, by means of which due dates and comparative tariffs within the Province are checked manually. It is a challenge though to implement and maintain an electronic register with comparable rates within and outside the Province and which has an early warning system to indicate when tariffs are due for revision. This will result in cost savings through increased efficiency in administration capacity and in increased compliance and accountability.

The current debt level, which in the main consists of arrear motor vehicle licences and hospital fees, is of a grave concern to the Province. A substantial portion of this debt is made up of administrative errors, and although current initiatives, which include the appointment of debt collectors, have proved to be reasonably successful, the challenge remains to identify the actual debt due and then both to make concerted efforts to collect it and to maintain current income levels. Initiatives to increase hospital fee income through the uniform patient fee system and preferred providers agreements with medical aid funds will be overseen by the Treasury by playing mainly a facilitating and monitoring role.

With motor vehicle licence fees in this Province being amongst the highest in the country, Treasury realises that a saturation point will be reached and users might be reluctant to comply voluntarily, which implies that compliance will have to be more rigorously enforced. The risks relating to "migration" of motor vehicle owners to cheaper provinces cannot be disregarded and a proper database will have to be developed and maintained, coupled with academic research on trends and movements to minimise risks relating to revenue collection which might undermine the integrity of the revenue budget. A further challenge that remains is to begin dialogue with other Provinces possibly to revisit their motor vehicle licence structures, which will in turn also promote the spirit of co-operative governance. One should realise that a significant improvement in provincial own revenue collections can only come through an improvement in current revenue administration procedures. In addition to improving the administration of existing taxes, this Province also intends introducing new provincial taxes, which are the vehicle created by the Constitution, to increase current provincial own revenue.

New provincial taxes

Section 228 of the Constitution prescribes that provincial taxes should be regulated at national level and authorises limited taxing powers to the Provinces. The power to impose provincial taxes is therefore subject to regulation by national legislation. Section 228 of the Constitution provides that a provincial legislature may impose certain taxes, levies and duties. Subsection 2 of this section, however, contains certain qualifications in that "the power of a provincial legislature to impose taxes, levies, duties and surcharges may not be exercised in a way that materially and unreasonably prejudices national economic policies, economic activities across provincial boundaries, or the national mobility of goods, services, capital and labour"[4]

[4] Section 229(2)(a) of the Constitution of South Africa, 1996 (Act 108 of 1996)

and this power of a provincial legislature to impose such taxes "must be regulated in terms of an Act of Parliament, which may be enacted only after any recommendations of the FFC have been considered"[5].

Section 228(2)(a) of the Constitution assigns co-ordinating and monitoring roles to the National Government in respect of provincial taxes while section 228(2)(b) requires that an Act of Parliament regulate the process whereby provincial governments may implement taxing powers granted to them in terms of the Constitution.

The Provincial Tax Regulation Process Bill ("PTRPB"/"the Bill") purports to give effect to the constitutional requirements of section 228 of the Constitution. It regulates provinces in exercising their powers to impose certain taxes. However the Bill does not set out specific taxes that provinces may enact and the responsibility for initiating a provincial tax proposal therefore rests with provinces, so that they may propose any tax not prohibited by the Constitution. Rather, the Bill regulates the process by which provincial taxes are to be imposed.

Against this backdrop the Western Cape Province on 19 January 2001 submitted a list of twelve preliminary tax proposals to the National Treasury for consideration of their feasibility and subsequently for the inclusion on the so-called "allowed list". However, due to the infant stage of the PTRPB it was considered expedient not to incur any substantial research expense before proper planning has been finalised in respect of the process that needs to be followed. Such research will enable the Province to submit to the national Minister of Finance proposals in line with the process as stipulated in section 3 of the Bill.

Some of the provincial taxes, which have been recommended by the Province for inclusion on the allowed list include environmental taxes, fuel taxes, tourism taxes, development taxes, etc. It is realised that some of the taxes might not be cost-effective to introduce or might have limited applicability to this Province and are therefore unlikely to produce significant revenue sources. If one looks at the economic activity of this Province, the most viable options at this stage appear to be the introduction of fuel and tourism taxes. In-depth research will therefore need to be conducted on the revenue, economic activity and equity implications of these taxes.

The Provincial Treasury realises that it will be premature to introduce new provincial taxes as a short-term challenge if the administration with regard to the current taxes is not increased significantly. As a pilot co-operation project, the Treasury and the

[5]Section 228(2)(b) of the Constitution of South Africa, 1996 (Act 108 of 1996)

Department of Economic Affairs, Agriculture and Tourism will embark on an entire assessment of processes and systems relating to the current liquor licence taxes and will specifically target its research on the basis of the requirements of the PTRPB. A proper database and reference system needs to be developed which will provide the necessary benchmarks for future taxes. Specific efforts to improve provincial tax administration in respect of the liquor licence tax and a review of the entire tax system which will include sector, legal and institutional frameworks is unavoidable. One should also realise that such an exercise requires the necessary capacity and expertise that will promote fiscal accountability. Human resource development and employing the appropriate skills are therefore imperative.

Although the current revenue-raising powers may be a contributor to fiscal governance, this Treasury's vision is to have both the required incentives and capacity to levy the appropriate taxes, which will further enhance fiscal accountability.

Public-Private Partnerships (PPPs)

As a means of government to promote efficient, effective and economical service delivery, the concept of PPPs was introduced. Although not covered in the PFMA itself, PPPs are governed by Chapter 16 of the National Treasury Regulations, 2001 which have been issued in terms of the PFMA.

Currently National Treasury has the regulatory responsibility attached to the different authorisation levels of PPPs and although the said Treasury Regulations provide for delegated powers to provincial treasuries, National Treasury has been reluctant in delegating its responsibility. The rationale behind this reluctance is the current lack of capacity, in all provincial treasuries, to execute major capital investment projects and of the ability to oversee the entire PPP process in provincial departments, coupled with the skills to ascertain whether a PPP project provides value for money for both bodies, in other words that it is affordable to the institution and if appropriate technical, operational and financial risk is transferred to the private partner.

It is noticeable that provincial departments of the Western Cape are eager to explore the possibilities of PPPs, as there are currently three departments exploring these avenues in which the Provincial Treasury is actively involved. These projects include the Chapman's Peak Project, three Department of Health projects and fifteen Western Cape Nature Conservation Board projects.

However, the lack of knowledge and skills poises a challenge to this Province to acquire the necessary skills, but the Treasury views capacity building as a high priority.

The Provincial Treasury has been actively involved in these projects, ably assisted by the close collaboration with National Treasury's PPP unit and with this Province.

3.3 Borrowing

Legal framework

- Borrowing Powers of Provincial Governments Act, 1996 (BPPG)
- Public Finance Management Act, 1999 – Chapter 8 (PFMA)
- Treasury Regulations – Chapter 13
- The Constitution, 1996 – Section 230
- The Constitution of the Western Cape, 1997 – Section 63

The parts of the Constitution, 1996, that are relevant to provincial borrowing are:

- **Distinctive Provincial Government (Section 40):** This implies that the provinces should exercise their borrowing powers as autonomous legal entities.
- **Principles of Intergovernmental Relations (Section 41):** This implies that the provinces in their borrowing activities should be effective, transparent, accountable and coherent, and that they should co-operate with the National Government in respect of those activities.
- **National Economic Policy (Section 146):** This implies that national legislation affecting provincial borrowing should prevail over provincial legislation where this is necessary for effective national economic policy.
- **Basic Principles of Public Administration (Section 195):** This implies that provincial borrowing must promote the efficient, economic and effective use of resources, it must be development-orientated, it must respond to the people's needs, and it must be accountable and transparent.
- **Equitable Share (Section 214):** This implies that the provinces should receive an equitable, stable and predictable share of revenue raised nationally.
- **Provincial Budgets (Section 215):** This implies that the provinces should estimate in their budgets their capital expenditure, and indicate their intentions with respect to borrowing.
- **Borrowing Rights (Section 230):** This implies that provinces may borrow for capital or current expenditure.

Provincial borrowing constraints: under section 230 of the Constitution, 1996

A province may raise loans for capital or current expenditure in accordance with reasonable conditions determined by national legislation, but loans for current expenditure:

- may be raised only when necessary for bridging purposes during a fiscal year, and
- must be repaid within twelve months (will be repealed in due course)

Notwithstanding this provision, the Treasury Regulations states that all bridging finance raised during a financial year must be repaid within 30 days after the end of the financial year.

Borrowing Powers of Provincial Governments Act, 1996: sets out the borrowing powers of the Provinces in detail, including:

- Only the Provincial Minister of Finance may borrow money on behalf of the Province, and only on written approval from this Minister may a department or body established by the Province accept financial assistance, other than from the National Government;
- A provincial government shall not commit itself to any financial product, other than bridging finance, loans or other such products as may be prescribed, which creates an interest or any other exposure of a financial or equivalent kind;
- Bridging finance shall not be raised by a provincial government as a continuous and unlimited revolving credit;
- A provincial government shall not borrow foreign currency loans by the issue of marketable financial instruments or incur a liability or risk payable in a foreign currency;
- A provincial government may raise loans to finance an expected loan requirement, provided that the aggregate amount of loans to be raised by each provincial government during that financial year has been considered, and consensus reached, by the Loan Co-ordinating Committee, and the Financial and Fiscal Commission has been informed by the National Minister of Finance; and
- A provincial government may raise loans to finance an expected loan requirement provided that loans raised in the Republic, denominated in rand and obtained through loan agreements with the National Government, require the concurrence of the National Minister of Finance. The latter Minister may also advise a provincial government to raise a loan through an institution established by an Act of Parliament or an institution approved by the National Minister to make loans to sub-national governments, or advise a provincial government to enter into loan agreements with banks or financial institutions, issue public stocks and bonds, or enter into loan agreements through the issue of financial instruments. Subject to the BPPG, a provincial government may also choose the above options, is responsible for negotiating the related terms and conditions, and may provide any security required.

The National Minister of Finance shall determine annually the maximum ratio of the total expected amount of interest incurred during a financial year by a provincial government on its expected outstanding debt at the end of that financial year over the province's total budgeted current revenue. The Minister may request a recommendation from the Financial and Fiscal Commission in this respect, and must publish the reasons for the determination.

Any money borrowed by a provincial government and the interest owed shall be the financial obligation of the provincial government and shall be chargeable to, and payable from, the revenues and assets of that provincial government.

Definition of bridging finance

Under the BPPG, bridging finance is defined as funds raised during a financial year denominated in rand to finance current expenditure in anticipation of the receipt of current revenue during that year and includes overdrafts.

Public Finance Management Act, 1999

Provincial borrowing restrictions: A provincial government may not borrow money or issue a guarantee, indemnity or security, or enter into any other transaction that binds or may bind that institution or the provincial revenue fund to any future financial commitment, unless such borrowing, guarantee, indemnity, security or other transaction is authorised by the PFMA and is within the limits of the BPPG (Section 66).

In this respect, the Provincial Minister of Finance is the only authorised person to enter into such agreements, must act in accordance with the BPPG and may not delegate a power under the PFMA without the written approval of the National Minister of Finance. Any lending, guarantee, indemnity or security or other transaction which purports to bind a provincial government or entity to any future financial commitment without this authorisation will not bind the national or provincial governments or entity concerned (Section 68).

Provincial public entities, excluding provincial government business enterprises, may not borrow money, nor issue a guarantee, indemnity or security, nor enter into any other transaction that binds or may bind the entity to any future financial commitment. (Section 66(4)).

A provincial government, including any provincial public entity, may not borrow money or issue a guarantee, indemnity or security or enter into any other transaction which binds it to any future financial commitment denominated in a foreign currency or concluded on a foreign financial market (Section 67).

Current legal situation

Section 230(1) of the Constitution provides for provinces to borrow capital and bridging finance, subject to regulation. It intends that borrowing may be used to finance capital investment, but that such borrowing be "in accordance with reasonable conditions determined by national legislation".

The current legal framework for provincial borrowing includes the Constitution, the Borrowing Powers of Provincial Government's Act, 1996 and the Public Finance Management Act of 1999. This framework has overlapping provisions that have led to inconsistency, ambiguity and uncertainty as to what debt-related transactions are permissible, what procedures should be followed and how obligations should be enforced.

The Borrowing Powers of Provincial Governments Act, 1996 (BPPG), which was intended to regulate provincial borrowing, was based on the Interim Constitution. It provided for bridging finance and loans for capital investment, with oversight and co-ordination by consensus decision of a Loan Co-ordinating Committee (LCC).

The Loan Co-ordinating Committee limited provincial borrowing to short-term bridging financing in 1997, until a comprehensive framework could be put in place. This was intended to prohibit borrowing for either operating or capital expenditure, except for short-term bridging loans in anticipation of revenues.

To ensure uniformity, it has been agreed (by resolution) at the 2001 Budget Council Lekgotla meeting held in July 2001 that the National Technical Committee on Finance should compile such a borrowing framework, and that the framework should include substantial consultation, collaboration and consideration of the full range of borrowing options.

In addition to the above, the following resolutions were taken regarding the Provincial Borrowing Framework:

- The substantial risks involved in borrowing were noted which are further aggravated by the lack of provincial expertise in debt management;

- It is agreed that whilst further work was being done to complete the framework, it would be premature for provinces to start borrowing in the 2002/03 financial year; and
- To build provincial expertise in borrowing. National Treasury will assist in this area with training and technical assistance, and provinces are invited to send staff members to learn about borrowing and debt management from the Asset and Liability Branch in the National Treasury.

Preparation

Requirements

In order to enable the Western Cape Government to enter into the highly specialised field of "provincial borrowing" to finance approved capital projects within the Province, an integrated framework and environment for monitoring, managing and reporting such loans must be created.

Prior to undertaking a feasibility survey of such loans, the question of affordability must be the uppermost consideration, given the fact that the utilisation of cash from available revenue as a financing instrument is definitely the first option because the overall cost implications for any capital project through borrowings, after factoring in the costs of loan redemption, will be substantially higher.

To ensure efficient overall debt management, suitably qualified personnel are imperative to effectively co-ordinate, manage and monitor the funds procured. At present, no competent personnel are readily available, a situation which will render it virtually impossible to access private sector funding at this stage. Personnel will have to be trained in this specialised field and as a result, the required competency levels will take time to develop.

Financial institutions require a credit rating from potential clients, which represent a risk assessment analysis of short- and long-term capacity for timely repayment of outstanding commitments. Similarly, the Western Cape Government will have to approach a reputable credit rating agency for such a rating. The state of the Western Cape Government's books is currently of such a nature that it does not bode well for obtaining a good credit rating. Furthermore, much effort has been expended over the last couple of years in reducing the quantum of amounts owed to the Province, even to the extent of requesting the assistance of National Treasury to facilitate repayment by other government spheres. Considerable progress with several authorities has, however, been made and the current outstanding debt owing to this Province is in the region of R500 million which could impact negatively on the allocation of a good credit rating. The weaker the credit rating obtained, the more costly the financing will be as the Western Cape Government may well be perceived as a potential high-risk client with a diminished capacity for repayment, which will result in higher interest rates being quoted if the requested finance is granted.

As mentioned above, the financial institution granting the loan will only do so if the Western Cape Government has a good credit rating and an impeccable track record with regard to the handling of its finances. Financial institutions will probably insist on fixed revenue streams such as motor vehicle licences being utilised to repay at least the interest portion of the loan. This means that such revenue will be committed to a specific creditor for a period of up to 20 to 30 years. With such revenue streams non-existent, funds for other capital expenditure will not be readily available, thereby hampering the initiation of other projects.

If one were to weigh up the advantages and disadvantages of borrowing in real monetary terms, the utilisation of own revenue will definitely be to the advantage of the Western Cape Government. Funds which are held as a temporary investment currently yield an interest rate of approximately 9 %. On the other hand a loan of, for example R150 million, will attract interest payments of R359 million at a rate of 11,97 % over a 20 year period. The capital and interest payable will therefore amount to R509 million, a staggering figure in comparison with utilising the Western Cape Governments own resources and taking into account current day value of such a loan repayment figure. The calculations have been structured on the basis of interest payments on a semi-annual basis and a capital repayment in full at the end of the period.

The cost of borrowing, versus the returns over the life of the investment must be carefully weighed against each other to ensure a best return to the Province. Nevertheless, the expertise to make effective and appropriate decisions of this nature has to be developed urgently over the next year for the Province to be able to effectively utilise the lifting of embargos on provincial borrowing with the advent of the 2003/04 financial year.

3.4 **Total revenue and expenditure for the Province**

To conclude this chapter on the fiscal envelope for the Province, Table 4 illustrates the different components making up the total Revenue and Expenditure Budget of the Province available for distribution over the MTEF period 2002/03 – 2004/05 as in mid November 2001 before allocation to departments were made.

Table 4: Fiscal envelope in perspective

	2002/03 R'000	2003/04 R'000	2004/05 R'000
REVENUE			
Equitable share	10,614,985	11,129,346	11,862,270
Conditional grants	2,129,397	2,236,720	2,321,155
Own revenue	797,952	843,068	835,643
Provincial Revenue (before contingent liabilities and contingencies)	**13,542,334**	**14,209,134**	**15,019,068**
Contingent liabilities	(52,750)	(55,335)	(58,267)
Unforeseen and unavoidable contingencies	(52,750)	(55,335)	(57,825)
Total Provincial Revenue (excluding cash financing)	**13,436,834**	**14,098,464**	**14,902,976**
Cash financing	299,543	166,659	132,905
Total Provincial Revenue	**13,736,377**	**14,265,123**	**15,035,881**
EXPENDITURE (Budget 2001)			
Departmental allocations	**13,111,303**	**13,787,796**	**13,787,796**
TOTAL FOR DISTRIBUTION	**625,074**	**477,327**	**1,248,085**

4 PROVINCIAL OVERVIEW

4.1 General Overview: Expenditure quality and quantity

Introduction

The purpose of this section is to give an overview of actual Provincial expenditure from 1997/98 to 2000/01, budgeted expenditure in 2001/2002 and current MTEF allocations for 2002/03 and 2003/04.

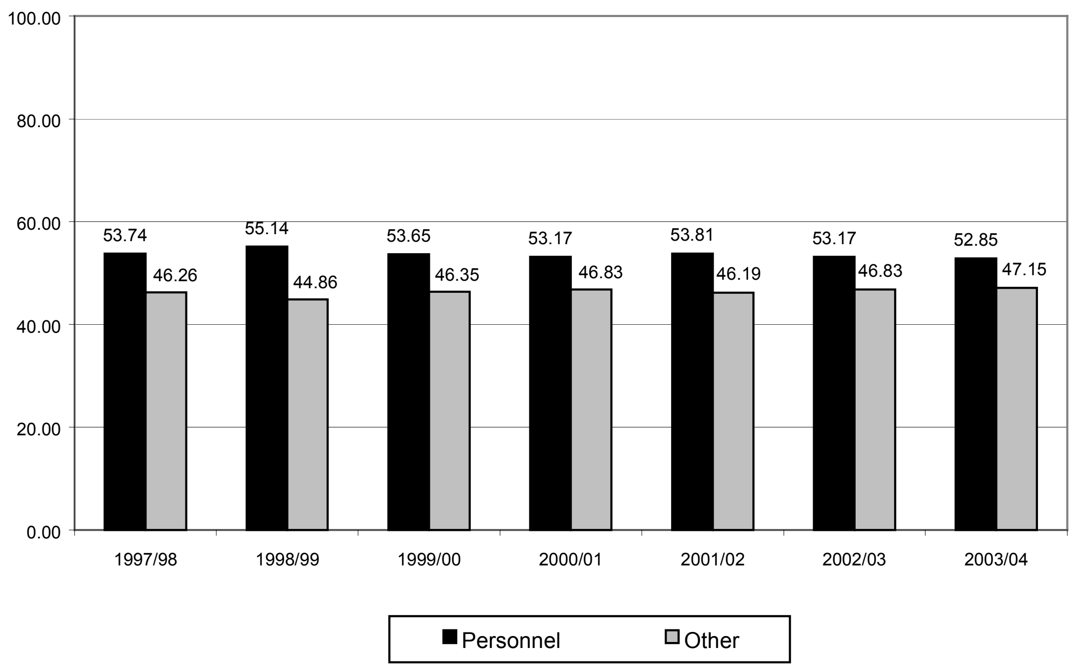
The focus is on certain spending trends/allocations, i.e. expenditure on social sector (education, health and welfare) vs other expenditure, personnel vs other expenditure and infrastructure vs other expenditure. In addition, certain other issues are also addressed. These include overspending vs underspending, classroom shortages and other non-financial information regarding the delivery of services to serve as an indication of outputs and outcomes.

Overall trends

Personnel vs other (all other expenditure excluding personnel expenditure)

(Figure 1)

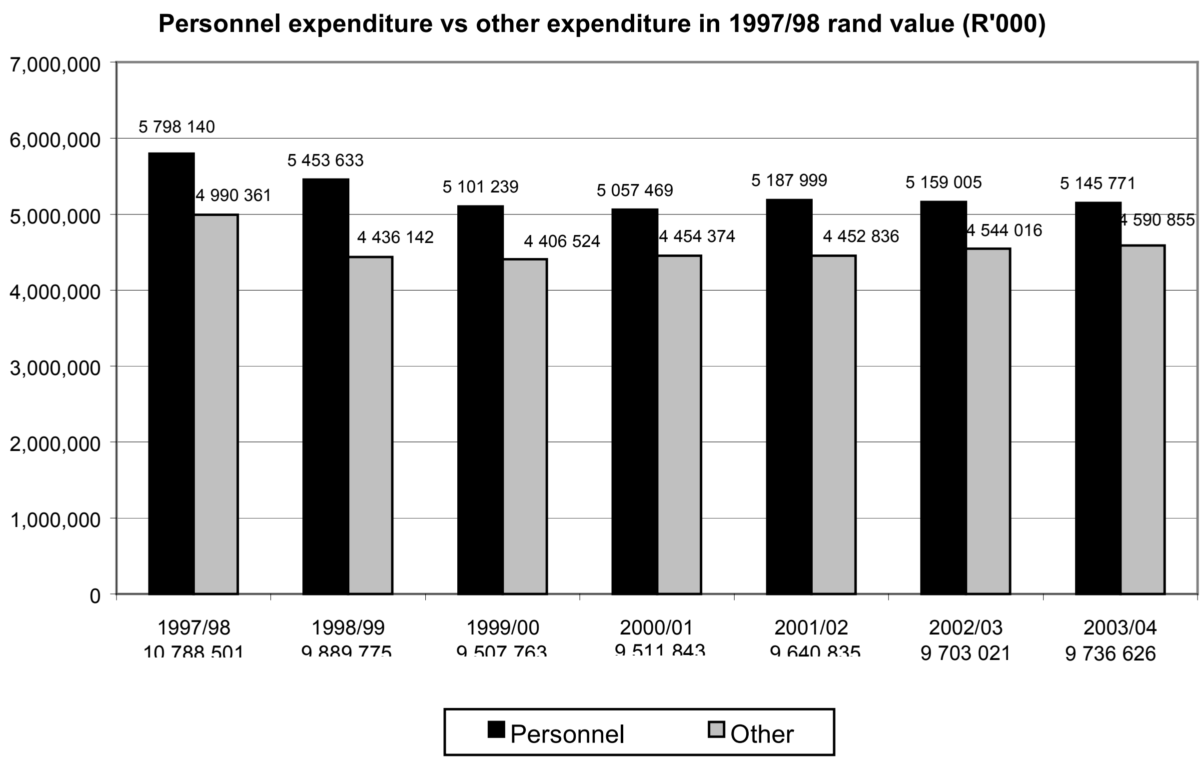
Percentage of personnel expenditure vs other expenditure



Many of the key services delivered by the Provincial Government are labour intensive such as education and health. Personnel expenditure on health consumes 60 percent (2000/01) of the health budget, while in the case of Education it is ± 88 percent (2000/01). For the Province as a whole personnel expenditure consumed 53,17 percent of the total budget during 2000/01 financial year. This compares favourably with the 55,14 percent spent in 1998/99 on personnel.

From a Provincial perspective it is fairly difficult to manage down personnel expenditure, due to the fact that improvement in conditions of service (salary increases) are negotiated nationally, as well as the lack of a discretionary retrenchment tool. The 1996/97 salary agreement created tremendous upward cost pressures on personnel spending.

(Figure 2)



In real terms (1997/98 rand value) the Province spent ± R5,798 billion on personnel in 1997/98 vs ± R5,057 billion in 2000/01. This reduced spending on personnel was achieved by reducing the number of personnel employed from 74 173 in April 1998 to 67 499 in April 2001. The average cost in real terms per incumbent as measured in terms of total personnel expenditure decreased from R78 170 to R74 927 over the same period. In nominal terms, however, it increased from R78 170 to R90 694 per incumbent. From the aforementioned it is clear that, if the

Province had not reduced its number of employees drastically (by 9 % or 6 674 persons) during the period (97/98 to 2000/01), there would have been no room for spending on other categories of expenditure, excluding social security grants, which are a statutory requirement.

It is also important to note that the major reduction in personnel numbers over this period occurred in Health, Education, the administrative/financial components of departments as well as professionals (engineers/technicians, etc.). Most of the employees who left the service were probably highly experienced and took with them a lot of know-how, which impacted negatively on the capacity of the Provincial Government to deliver. The challenge to the Provincial Government is thus to rebuild capacity to ensure effective service delivery. The emphasis should be a combination of employing personnel with the required skills and competence and building the required skills and competence of the existing staff to enable the Provincial Government to cater for the challenges facing the public sector in the 21^{st} century.

According to the Inter Governmental Fiscal Review 2001 there are 15,6 provincial public servants per 1 000 of the population in the Western Cape Province. Some research might be required to assess what this ratio should ideally be, in other words what the composition of such a figure must be to ensure optimal service delivery within available means.

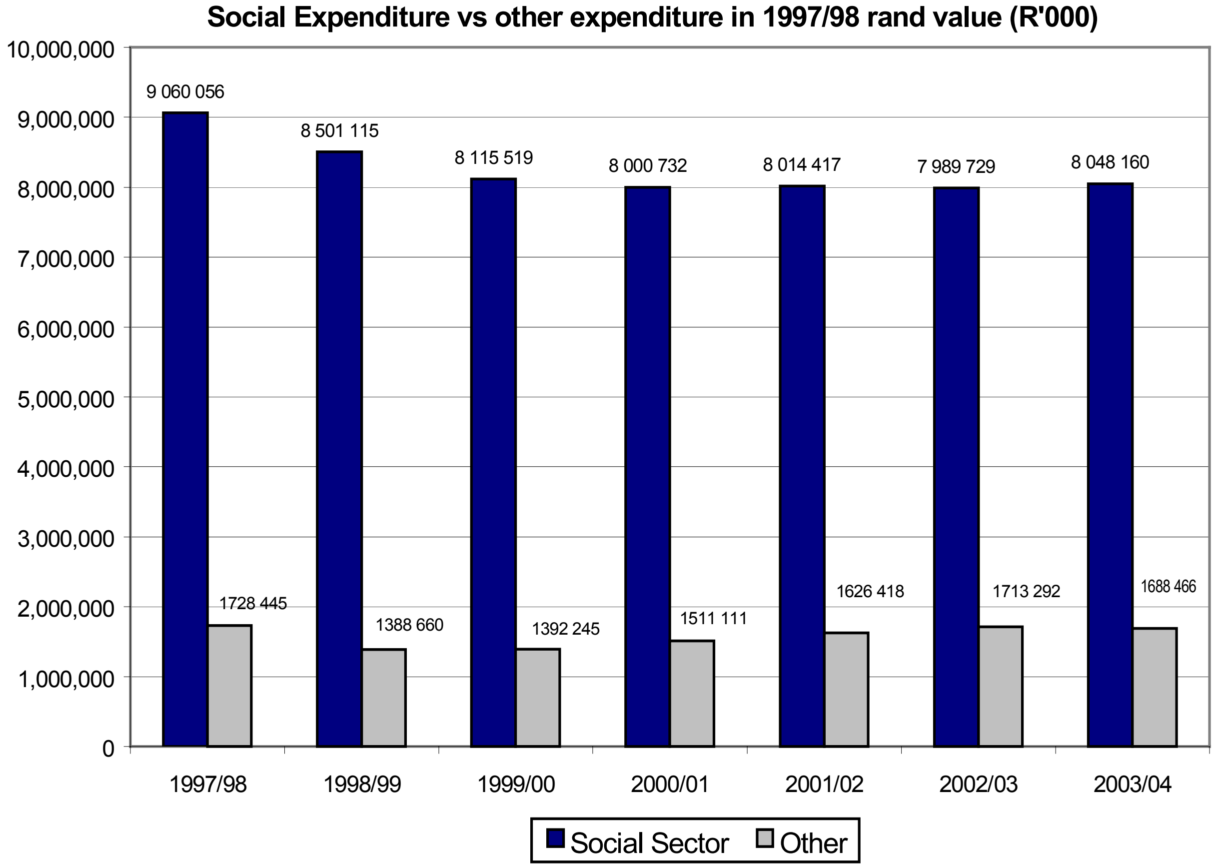
A further challenge facing the Provincial Government will be to deal effectively with the impact of HIV/Aids on its employees. Little information on the prevalence of the disease is available, which suggests that further research will be required to manage the possible impact thereof.

Another challenge would be to keep the expenditure on personnel within reasonable limits to allow room for other spending categories (learner support material, roads, etc.). The challenge is also to define such a balance, as some provincial services can only be delivered in a labour-intensive manner, as mentioned earlier.

Social sector vs other

Social sector (Education, Health and Social Services) trends

(Figure 3)



In nominal terms social sector expenditure grew over the period 1997/98 to 2003/04 from R9,060 billion to R11,418 billion, which relates to a growth of 26 % or an average of 4,34 % year on year. However, in real terms the picture looks totally differently as expenditure declined from R9,060 billion to R8,048 billion over the same period. This relates to a decline of 11,17 % over the same period in real terms.

The social sector's budget, as a portion of the Provincial budget, declined from 83,98 percent in 1997/98 to a projected 82,66 percent in 2003/04. Consequently the expenditure on the remainder of the Provincial budget increased from 16,02 % to 17,34 % over the same period. Social spending reached a high of 85,96 % percentage of the total Provincial budget in 1998/99, initially crowding out other expenditure, infrastructure in particular being the main victim.

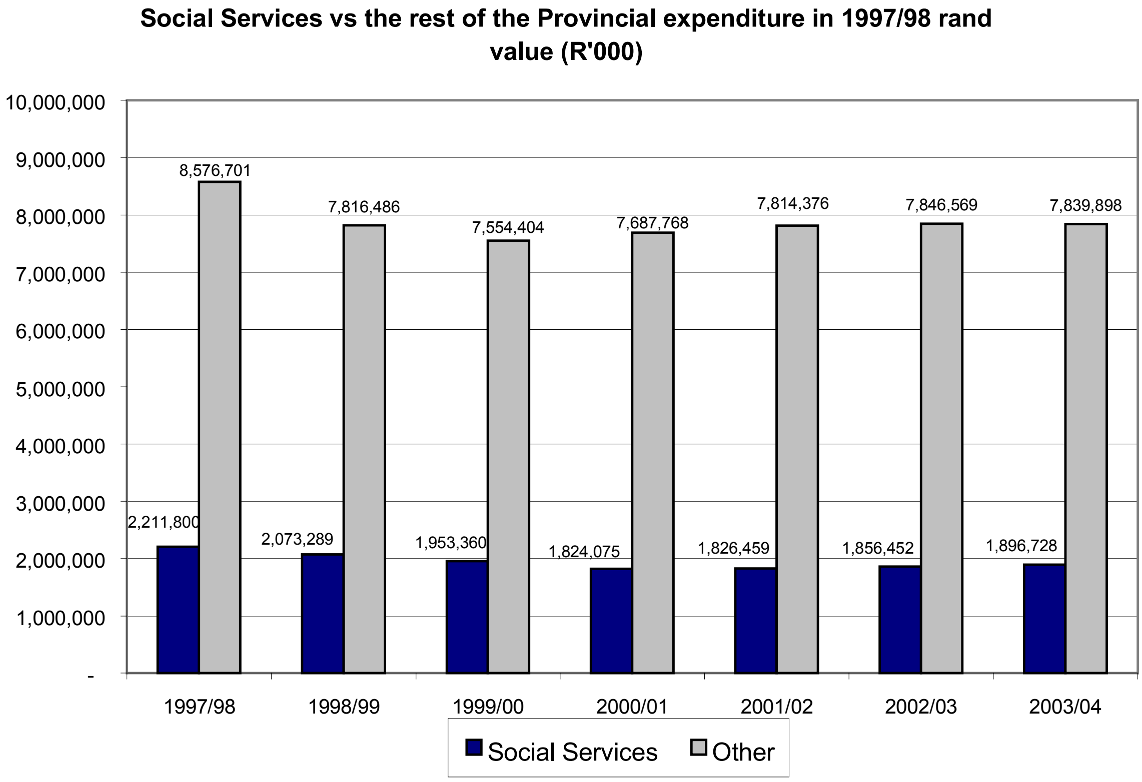
Trends in other expenditure

Other expenditure (excluding the social sector) increased in nominal terms from R1,728 billion in 1997/98 to R2,395 billion in 2003/04, which relates to a nominal growth of 38,59 percent or an average of 6,43 % year on year. In real terms, however, the picture looks slightly different as the expenditure will decline from R1,728 billion in 1997/98 to R1,688 billion in 2003/04.

This relates to a real decline of 2,31 % over this period. It is important to note that "other" spending reached an all-time low of R1,388 billion in 1998/99, with a steady year on year recovery since then. This recovery was achieved by a dedicated effort to reduce the expenditure on personnel as well as by the phasing out of the State Maintenance Grant and the implementation of the Child Support Grant. As can be seen from the above graph, expenditure on other spending categories is still below the level it used to be or what it should be. From the overall reduction of R1,052 billion (R10,785 billion in 97/98 to R9,737 billion in 2003/04), in real terms, the social sector took the brunt (R1,012 billion) of it.

Social services

(Figure 4)



In line with the social sector, Social Services expenditure/budget/MTEF allocations also decreased sharply over the period 1997/98 to 2003/04 from R2,212 billion to R1,897 billion in real terms, which relates to a 14,25 % decline over this period.

This is mainly due to the decline in transfer payments (social security grants) from R2,057 billion in 1997/98 to R1,689 billion in 2003/04, or 17,87 % in real terms, while personnel expenditure increased from R86,079 million to R113,489 million in real terms over the same period.

Transfer payments consist mainly of social security grants to individuals, supplementing the income of poor households. These comprised more or less 90 % of the total expenditure of the Department in 2000/01. Other transfers include subsidies and other payments to NGOs for services like probation and adoption, family counselling and homes for children and the aged.

State Maintenance Grant (SMG) vs Child Support Grant (CSG)

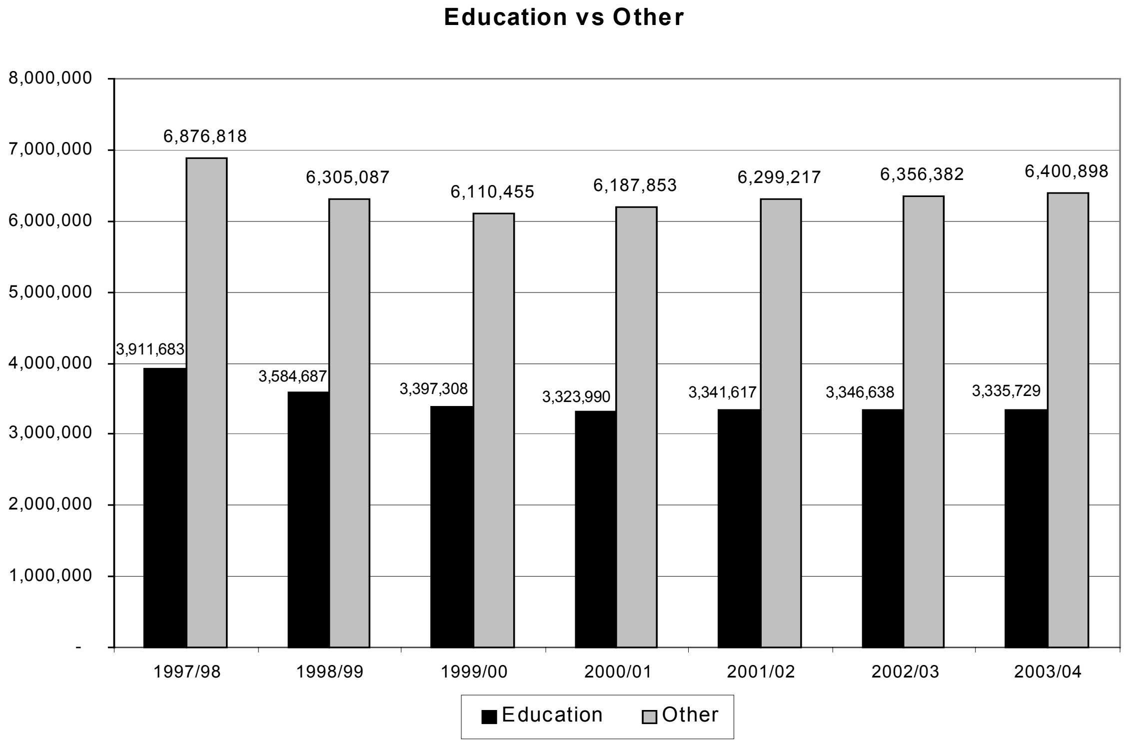
In 1997 a National Cabinet decision was taken to phase out the SMG over a period of three years, starting in April 1998 and terminating at the end of March 2001. Over this 3-year period, the phasing out affected approximately 72 000 women and the children up to the age of 18 years in the Western Cape. The SMG was reduced on an annual basis from R430 (parental allowance) and R135 per child (child allowance) to zero in April 2001. The SMG was replaced by the CSG for children under 7 years of age. The phasing out of SMG and replacing it with the CSG were dramatic for certain former beneficiaries of the SMG, as research conducted by the Social Services Department revealed that for 50% of them the SMG was their primary source of income and that 70 % of the children in these households are over the age of 7 years and therefore do not qualify for the CSG. From the aforementioned it would thus appear that, generally speaking, a large portion of this Department's clients are worse off in 2001/02 than they were in 1997/98.

The aforementioned policy decision also explains the decrease in transfer payments (social security) as the CSG was introduced at R100 per month per child. This R100 per child was increased to R110 from April 2001. Furthermore, due to the fact that the SMG was more beneficial to the applicant, the take-up rate for the CSG was very slow. However, since April 2000 the take-up rate increased dramatically and the number of children receiving the CSG as at November 2001 was already at 103,537. The aforementioned number far exceeded the nationally set target of 90,000 children by March 2003. According to the Social Services Department the potential number of children could be more than 180 000 for the Province. This viewpoint is based on the 1996 Census as well as on the deteriorating economic environment in certain sectors, such as agriculture and the textile industry.

Needless to say, the aforementioned will create upward pressure on the budget of the Social Services Department as well as the Province. As this is a statutory obligation, there is little other choice than to provide for it.

Education

(Figure 5)



Spending trend

In line with the decline in the social sector, the Education expenditure/budget/MTEF also decreases sharply from 1997/98 to 2003/04 from R3,912 billion to R3,336 billion in real terms, which relates to a 14,72 % decline over this period. This is mainly due to the decline in personnel expenditure from R3,412 billion in 1997/98 to R2,877 in 2003/04 or 15,67 % in real terms. In nominal terms, however, the expenditure for the Department increases from R3,912 billion in 1997/98 to R4,732 billion in 2003/04, which relates to an increase of 20,98 percent in nominal terms. Similarly, personnel expenditure increased from R3,412 billion to R4,082 billion or 19,64 % in nominal terms. As mentioned before, the Department had little other choice than to cut back on personnel expenditure.

Educator: learner ratios

The educator numbers in institutions have decreased from a total of over 34,000 during 1997/98 to a current figure of approximately 27,600 educators. The reasons for this decrease is due to the decrease, in real terms, in funds available to the Western Cape Education Department (WCED) as well as to an attempt to correct the educator: learner ratios, in line with the nationally determined affordable ratios. A measure used to reduce the number of educators was to offer them voluntary severance packages.

In 1997 there was a total of 905,976 learners and this decreased to 881,020 learners in 2000. Consequently, the educator: learner ratio for primary schools moved up from 1:36 in 1997 to 1:39 in 2000. The ratio for secondary schools currently stands at 1:33. The decrease in the number of learners in 2000 compared to 1996 is mainly due to the higher entry age set for grade 1 learners. This will have a carrythrough effect in the subsequent years as these learners progress through and eventually exit the system. The net impact in grade 1 was that approximately 30 000 fewer learners entered the system.

Shortage of class rooms

Despite the decrease in the number of learners, the number of schools indicating they have a shortage of classrooms increased from 16 % in 1996 to 17 % in 2000. This could be ascribed to the migration of people/communities, which has the effect that certain areas are overprovided with classrooms while others areas, especially new developments, are underprovided or not provided at all. The challenge facing the WCED and the Provincial Government is thus to turn this trend around with the limited funds available.

Facilitation/infrastructure/backlogs

The education infrastructure backlog totals R1,123,662 million and can be summarized as follows:

1 250 instruction rooms in existing schools	R367,0 million
1 250 instruction rooms in new developed areas	R367,0 million
Toilets/water/electricity and other necessities inside public schools on private land	R30,0 million
Accessibility of existing education buildings to the disabled	R10,0 million
700 forums	R300,0 million
80 new computer centres	R7,2 million
199 media centres	R27,462 million
Changes to 500 existing rooms for computer and media	R15,0 million

The current budget (2001/02) allocation is R39,205 million (provincial budget allocation) and R10,745 million (Provincial Infrastructure Grant (National Conditional Grant)). The provision for the remainder of the MTEF reflects provision of R39,205 million (provincial budget allocation) and R24,053 million (Provincial Infrastructure Grant) for 2002/03 and R39,205 million (provincial budget allocation) and R28,624 million (Provincial Infrastructure Grant) for 2003/04. Based on the provincial budget allocation, it is estimated that without any increases in backlogs or escalation, it will take approximately 25 years to address all the identified backlogs. According to the WCED statistics, the number of schools built from various financing sources are as follows:

- 1997/98 – 20 new and 9 extensions
- 1998/99 – 9 new and 3 extensions
- 1999/2000 – 9 new and 1 extension
- 2000/01 – 7 new and 35 extensions

An amount of R20,0 million was spent on unscheduled maintenance by schools during 2000/01. The MTEF allocations in this regard are R22,0 million for 2001/02, R24,2 million for 2002/03 and R26,620 million for 2003/04. According to the prescribed norms and standards for the funding of schools, day-to-day maintenance is part of the allocations the schools receive in this regard every year. It is expected of each school governing body to allow at least R20,00 per learner for this day-to-day maintenance and repair of other apparatus and machines used at the schools.

Initiatives are being taken by the WCED in conjunction with the Branch Property Management to redress the shortage much faster by using the core school system where the core facilities can be constructed in the conventional manner, but instruction rooms can then be provided relatively faster by means of good quality prefabricated classrooms and by making use of standard plans. The building of standard facilities can then follow later. By means of this method, schools can become available within 6 months instead of 31 months (planning and construction). This policy will assist in catering for the migration of learners, which on average amounts to 36 learners migrating from one school to another year on year. In practical terms this means that an average of one classroom per school needs to be moved due to migration. Furthermore, it is estimated that up to 2 % inward migration of the learner population to the Province takes place annually, while some outward migration/relocation also takes place. Of the 67 new schools built in the past 7 years not one was in the former white areas.

Section 21 schools

On 1 April 2000 the WCED started to empower schools with section 21 status (SA Schools Act, 1996 (84 of 1996)). The aim is that 100 schools a year should receive section 21 status in order for all schools to become section 21 schools over an 8 year period. Currently 560 out of 1 461 schools are run as section 21 schools and the staff of the Education Management and Development Centres (EMDCs) monitor these schools. The number of section 21 schools increased from 560 in 2001 to a projected total of 663 in 2002, as included in the budget inputs of WCED. This represents 45 % of all schools in the Western Cape.

Material [learner support material – (LSM)]

Actual expenditure during 2000/01 on LSM amounted to R100,543 million, with the spending per learner being R114,82. The budget for 2001/02 is R114,480 million (R130.74 per capita), for 2002/03 R124,787 million (R142,51 per learner) and 2003/04 R155,43 million. There was no problem with the delivery of LSM to schools in 2000/01, except in a few cases, where books were out of print or not available.

Norms and standards

The allocations to schools in terms of the prescribed norms and standards for the funding of schools increased from R112 million in 2000 to R129 million in 2001 and to R200 million in 2002.

Ratio of personnel vs other expenditure

The aim of the Western Cape Education Department (WCED) is to reach the 85:15 ratio of spending on personnel to non-personnel in 2005. Inclusive of the spending on education buildings and IT facilities, the ratio stands at 82:18 in 2001/02 moving down to 83:17 in 2002/03 and 83:17 in 2003/04. This ratio is broadly moving in the right direction to reach the target of 85:15 in 2005. As this shift takes place, it allows scope for the WCED to address other high priority spending pressures, such as learner support material.

Redeployment of personnel/CS educators

As can be deduced from the figures mentioned in the first paragraph of this section, the WCED went through major rationalisation and restructuring in recent years and lost a large number of personnel/CS educators with considerable experience, skills and competencies. It would appear that everything is fairly stable in the current financial year, in comparison with the previous years. However, at the beginning of the financial year the Department had more than 1 200 supernumeraries in the system. As at the end of October 2001 the Department had managed to reduce this to approximately 400.

The challenge facing the Department is to stabilize matters even further and to rebuild the lost capacity by means of training and employing people with the required skills. There appears to be a critical need for capacity building in the administrative and financial disciplines of the Department.

It can thus be argued that it is absolutely critical to address the aforementioned gaps by allocating additional resources to those areas. It is also important that the negotiations surrounding improvement in conditions of service (salary increases) be taken very seriously and it is the responsibility of all parties involved to ensure that further disruptions, due to unaffordability of salary increases do not occur.

Matric/grade 12 pass rates in "context"

Figure 5a

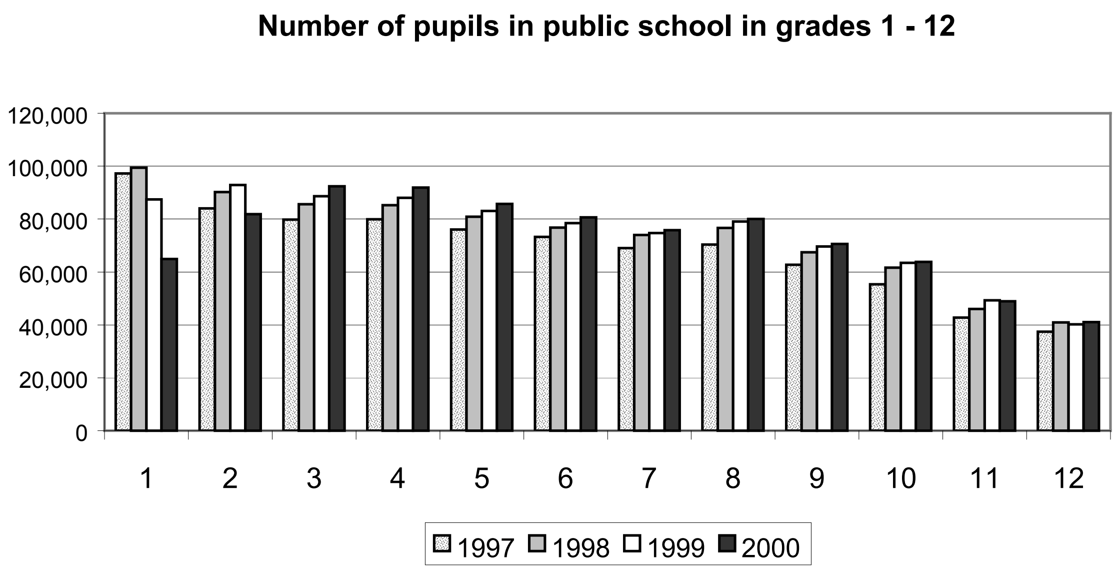
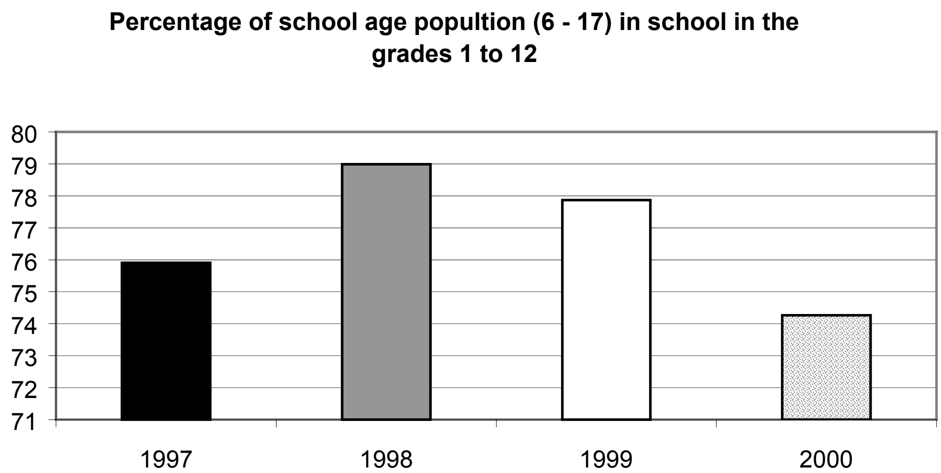


Figure 5b



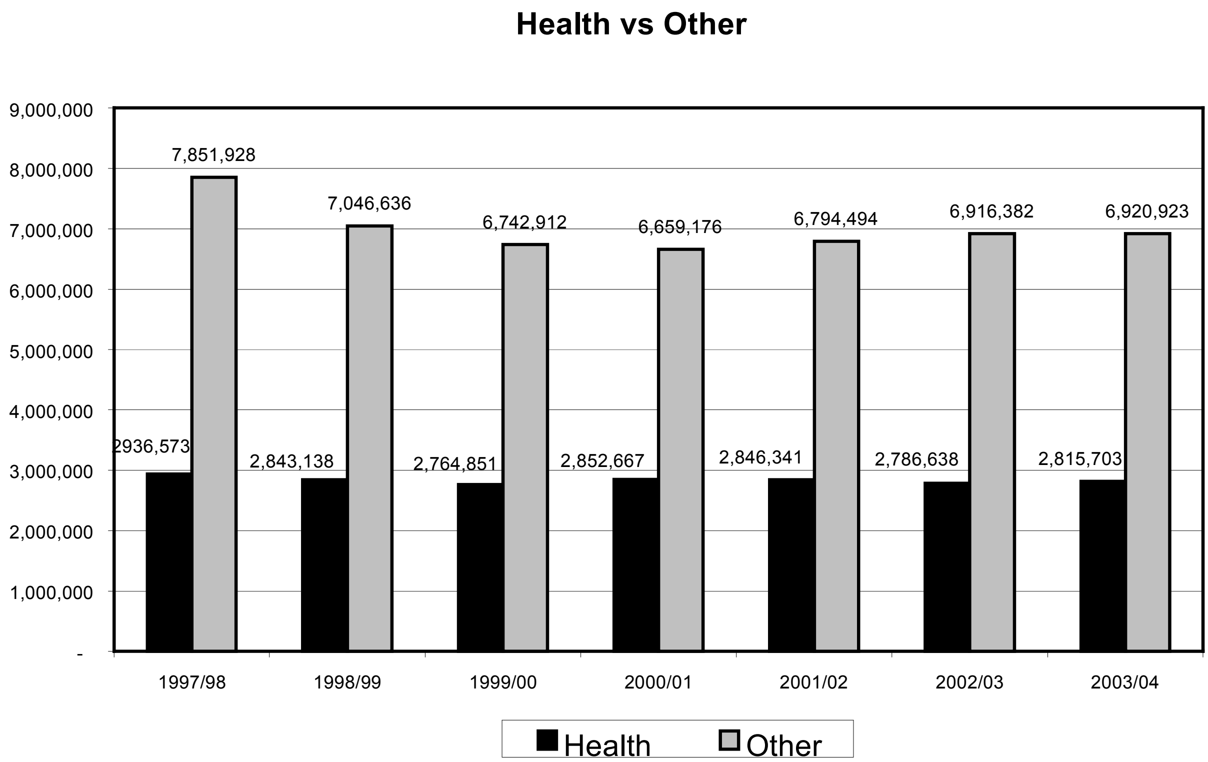
As can be seen from the above figure (5a), the number of pupils in grade 12 is less than half those in grade one with the exception of 2000, when only 64,844 pupils were in grade 1. However, the reduction of the grade 1 number in 2000, is due to the new policy that all pupils should be 7 years of age before they are allowed to enter the public school system. What is also important to note from the above figure, is the steady decline in the number in the various grades, from grade 1 to grade 8, but that from grade 8 to grade 12 there is a sharp decline in the pupil numbers. This might indicate that despite compulsory education up to grade 9, primary school might be too easy. The above figure also indicates that only ± 40 % of those who should be in grade 12 are in fact in grade 12. If one then considers that approximately 80 % pass grade 12, the picture looks bleak as 40 % x 80 % = 32 %. This means that only approximately 32 % of those who should be in grade 12, actually passes grade 12, versus the well publicised figure of 80 %. Figure 2 indicates that only approximately 75 % of the school age population are in fact in the school system, with a whole 25 % possibly lost to schooling.

It can thus be argued that if this Province really wants to take part in the knowledge economy, than something drastic needs to be done to ensure, firstly that greater numbers of children are captured in the school system and, secondly, that the quality of education is improved vastly, by ensuring that a greater number of pupils succeed in passing grade 12. Good education is regarded by many as the cornerstone of economic growth. The institutional framework needs to be developed in such a manner that as many as possible of the Province's children can be taken up in the economy and not the opposite, as is currently the case. As proved in many countries, higher levels of education also lead to lower population growth and improved health, which lightens the burden on other public services such as health and social welfare.

Health

Spending trend

(Figure 6)



In line with the decline in the social sector, the Health expenditure/budget/MTEF also decreased from 1997/98 to 2003/04 from R2,937 billion to R2,816 billion in real terms, which relates to a 4,12 % decline over this period. This is mainly due to the decline in personnel expenditure from R1,976 billion in 1997/98 to R1,754 billion in 2003/04, or an 11,23 % decline in real terms. In nominal terms, however, the expenditure for the Department increases from R2,937 billion in 1997/98 to R3,995 billion in 2003/04, which relates to an increase of 36,63 %. Similarly, personnel expenditure increases from R2,888 billion in 1997/98 to R3,881 billion in 2003/04 or 34,37 % in nominal terms. As mentioned before, this department had little other choice than to cut back on personnel expenditure in order to remain within budget.

Personnel vs other expenditure (in Health)

The aim of the Western Cape Health Department (WCHD) is to reach an optimum ratio between personnel expenditure and non-personnel expenditure within the Department. However, this appears to be a difficult exercise, especially after the

1996 wage agreement and the increased personnel costs arising from the leg and rank promotions. As a result of the aforementioned, personnel expenditure rose to a high of 67,29 % of WCHD's total expenditure in 1997/98. As part of the 1996 wage agreement the voluntary severance package (VSP) was introduced. The WCHD managed to, with the VSP tool, to reduce their personnel numbers from 28 363 in 1997/98 to 23 658 in 2000/01 (a reduction of 4 705, or 16,7 %), with the result that personnel expenditure was reduced to 60,33 % of the total expenditure in 2000/01, compared to 67,29 % in 1997/98. As this shift takes place, it allows the WCHD some room to address other high priority spending pressures such as pharmaceuticals and equipment.

HIV/AIDS

One of the core functions of the WCHD is to ensure that appropriate interventions reduce morbidity. However, it appears that the opposite is taking place. The following figures serve as an example. There has been a massive increase in the number of new cases of TB from 28 000 new cases in 1998 to 31 000 and 38 000 new cases in 1999 and 2000 respectively. This increase is most likely due to the increase in HIV infections.

A separate directorate was set up to focus on TB, HIV/Aids and sexually transmitted infection programmes. As the prevalence of HIV/Aids is still on the increase, a decision was taken to establish a branch within the WCHD to focus on HIV/Aids, Programme Development and Transversal Projects. Furthermore, a Provincial Interdepartmental Committee was also established to galvanise support for an inter-sectoral approach to HIV. The challenge for the Province and in particular the WCHD is to put strategies in place that will ensure that there is change in the sexual behaviour of the community, so as to prevent Aids infection, as it will be difficult for the Province, within available means, to cater for HIV/Aids infections otherwise. Additional resources amounting to R11,325 million in 2001/02, R34,378 million in 2002/03 and R28,974 in 2003/04 were/are being made available for this purpose to the WCHD.

Facilities/infrastructure/backlogs

According to the Building Audit Program (prepared by the Works Branch – August 2000) the average general condition of WCHD facilities is poor. It is further indicated in the report that R543 million (August 2000 rand value) needs to be spent over the next 5 years to address the current state of affairs. This excludes the need for new facilities such as clinics and a new hospital in Phillipi. Current and previous special allocations for upgrading and maintenance from both the National Health Department (approximately R25 million annually) and the Provincial Government (R44 million in 2000/01 and R68 million in 2001/02) appear to be insufficient.

The challenge to the Provincial Government thus remains to address the state of our health facilities, as the poor state thereof also impacts negatively on the morale of the personnel as well as on the quality of services delivered.

Mortality

Although little information is available on mortality figures, it is essential that with the prevalence of HIV/Aids, a concerted effort should be made to get accurate figures on this issue for future reporting and decision-making purposes.

Access to primary health care

Access to primary health care services continues to show an improvement, with attendance showing a steady increase from 10,3 million patient visits in 1999/00 to 10,5 million patient visits in 2000/01. It is expected that this trend will increase further in future years. It is thus apparent that the shift of resources away from academic health services towards preventative and primary health care might continue, while the focus also needs to be on reshaping the service and increasing operational efficiencies to remain within available means/resources.

Challenges for the Western Cape Health Department (WCHD)

Improving service delivery

Improving service delivery and the quality of care are being achieved by developing a Quality of Care Improvement Plan, which focuses on patient satisfaction, improved clinical quality, caring for the ill, control of HIV/Aids and its impact, control of the TB epidemic, and reshaping the health service by developing and implementing a strategic plan. The focus should be on treatment at the lowest possible level of care that ensures quality, prioritisation of primary and secondary services, rationalisation of tertiary and quaternary services and the reassessment of the skills mix to address equity, quality and affordability.

New National Tertiary Services Grant

Proposals are close to finalisation to integrate the Central Hospitals Grant and the Health Professional Training and Research Grant into a new National Tertiary Services Grant. The current grants make up approximately 37,18 % of the Health Budget in 2002/03. The aim of the national Department of Health is more equitably to fund tertiary services of the Provinces and to improve access to tertiary services.

The Western Cape supports the need to reduce structural crowding out of basic health care and to release funds for basic health care services, as well as the need for improved equity of access to specialised services. The current proposals from the National Department of Health indicate that the Western Cape will receive a reduced cumulative grant of close to R230 million by 2006/07. The Western Cape Provincial Government will thus have to implement measures to deal with this issue effectively.

Improvement of financial management at hospitals

An allocation of R16 million was made to the WCHD from the National Treasury in 2001/02 for the improvement of financial and other management reforms in the central (academic) hospitals. This includes the decentralisation of management and the appointment of a Chief Executive Officer for each hospital with responsibilities delegated to him/her by the Accounting Officer. The allocation for this grant is R14 million in 2002/03 and R12 million in 2003/04. In 2001/02 little progress has been made and a large portion of this is expected to be rolled over to 2002/03 due to the failure of the National Department to make these funds available to date. The appointment of new managers, financial consultants (Groote Schuur Hospital) and two directors (Finance) at each of the academic health complexes has lead to a significant improvement in financial management. However, the challenge remains to further improve management at institutional level throughout the Province in the near future.

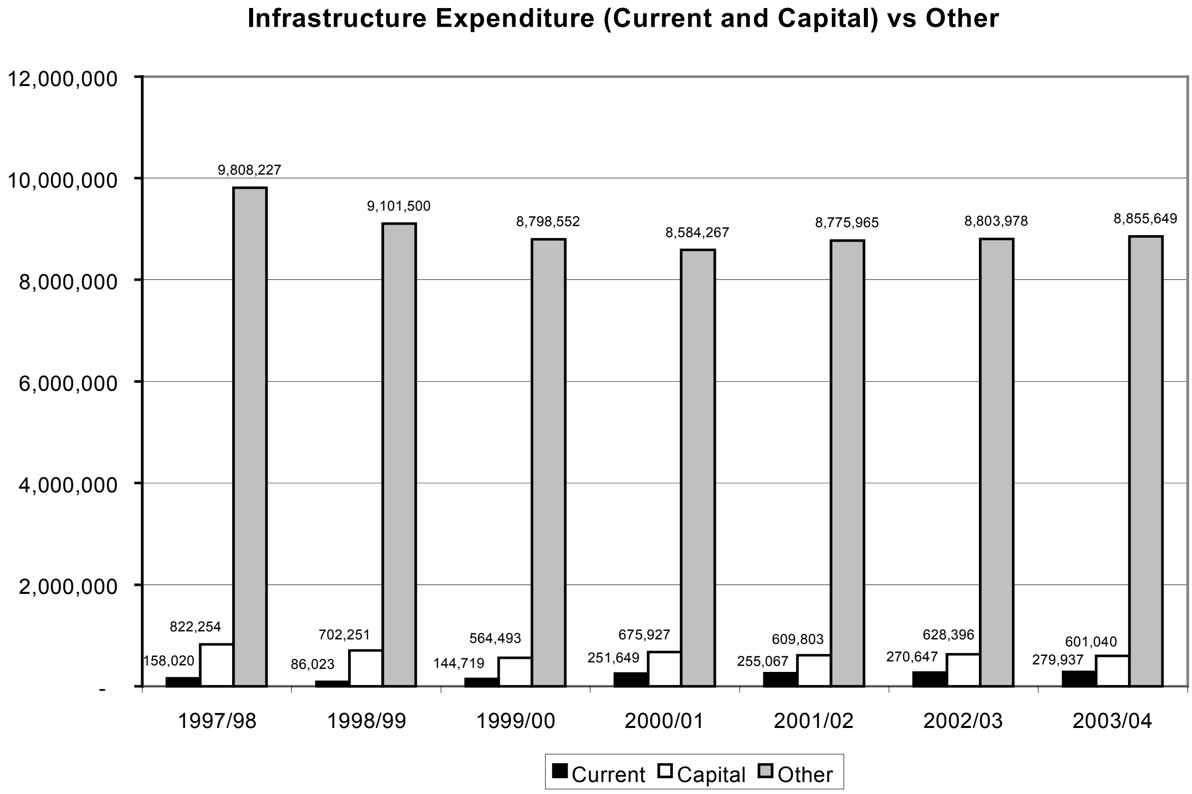
Increased number of patients (clients)

Indications are that, due to the growth in the population migration, a higher percentage of the population not belonging to medical aids (even public servants), increasing trauma cases, an increasing incidence of and linked HIV/Aids and TB epidemics, the demand on health services is set to increase. This will pose quite a challenge for the WCHD in dealing with the increase in patient load effectively and efficiently.

Infrastructure vs non-infrastructure spending (social services, personnel, etc.)

Spending trends

(Figure 7)



In line with the decline in the overall provincial spending pattern, infrastructure spending/MTEF allocations also decreased sharply from 1997/98 to 2003/04 from R822,254 million to R601,040 million in real terms, which relates to a 26.90 % decline over this period. As the Provincial Government was forced to cut back on certain categories of spending, it was also forced to cut back on infrastructure spending. This cut back on infrastructure spending, including current maintenance, is now reflected in the state of the Province's building and roads stock, of which the average general condition is regarded as fair to bad.

If maintenance (current) expenditure is included in real terms the expenditure declined from R980,274 million in 1997/98 to R880,977 million or 10,13 % in 2003/04. All these figures include spending on housing (national conditional grant). Spending on infrastructure (current/capital) reached a low of R709,211 million in 1999/00 in real terms. Owing, amongst others, to the down management of personnel expenditure, it was possible to allocate more financial resources to infrastructure spending, stabilising it at ± R900 million per year from 2000/01.

Needless to say, this amount is far short of what should be spend/allocated to this spending category.

Maintenance of the Province's building stock

A building audit was carried out by the Department of Economic Affairs, Tourism and Agriculture. In its report Building Audit Program (of August 2000 (BAP)) it is indicated that the total value of the Province's building stock amounts to R16,307 million (replacement value – 1999 rand value). It is further indicated in BAP that to bring the current building stock to a sound condition will cost R1,2 billion. It is also indicated in the report that to prevent any further significant deterioration of properties, 40 % of the R1,2 billion should be spent in the first year. The BAP report further indicated that R540 million, R565 million and R95 million should be spent on health, education and general buildings respectively.

A large sum (R4,9 million) was invested in compiling the BAP report; however, it could be regarded as funds well spent if BAP is used as a tool to allocate funds where they are most needed and the further deterioration of the building stock is thus prevented. The BAP should also be used as a benchmark to measure what progress is made to eradicate backlogs in maintenance. Best value for money could thus be achieved if this "tool" is properly used.

Balance between maintenance and demands for new facilities

One of the challenges of the Provincial Government is to strike an optimum balance between allocation for new facilities and maintenance. It might appear that the top priority should be to reduce the backlog before any consideration should be given to new facilities. However, there are also major backlogs in certain communities due to past policies and Government can ill afford not providing them with facilities, and thus with services, in order to achieve equal access to services by all communities.

Bargaining for funding

It seems to be most appropriate that each department should, via the normal budget process, bargain for funding to address all its requirements, inclusive of infrastructure (new construction, maintenance, etc.). However, such bargaining can only take place after proper consultation with the service provider (Works, where applicable). The capacity of the service provider to deliver should also be taken into account. Both the client department and the service provider must ensure that they are able to afford the resulting additional expenditure, such as operational expenditure (water, electricity, maintenance, etc.), from existing allocations.

Vesting of funds (buildings – maintenance and new construction)

At present, almost all the expenditure in respect of physical facilities (buildings) are reflected in Vote 10 – Economic Affairs, Agriculture and Tourism, with the exception of the day to day maintenance of schools and hospitals and clinics, which is reflected in the budgets of Education and Health respectively.

The question that is often posed is where such funds should be reflected – at the service providing department or at the service delivery (line) department. At national level the tendency is increasingly to reflect all expenditure (capital/operational) in respect of physical facilities in the budget of the service delivery department. For the first time in the 2001/02 financial year, new capital projects for government departments are actually included in their respective budgets.

There are certain advantages and disadvantages in respect of both methods. It is for instance not important where the funds are reflected, but rather how it can be ensured that the funds are spent efficiently and optimally, that accountability is vested appropriately and that service delivery is effective. One of the greatest advantages of reflecting these types of expenditure in the service providing department's (Works) vote, is the earlier faster and smoother payment of contractors for services rendered due to less red tape in the process.

Service level agreements

The desirability of service level agreements will not be debated. At national level it has already been effected. These agreements will capture the fundamental responsibilities of each party to the agreement and become operational in the current financial year. They make Public Works (National), amongst others, accountable for the timeous, cost-effective quality delivery of projects and represent an initial step in creating a formalised business relationship between Public Works and the client departments. It is also anticipated that these service level agreements will play an important role in eliminating the long lead times that, too often, have delayed the delivery of capital projects.

At Provincial level two service level agreements with Agriculture and the Nature Conservation Board have been finalised and another three between Health, Social Services and Education are in the final stages of completion. The intention is to review these agreements annually.

Roads

Spending trends

Spending on roads infrastructure is also split into two categories, namely –

- maintenance (resealing, repair), which is regarded as current expenditure and
- construction (new and upgrading), which is regarded as capital expenditure.

In line with the decline in total Provincial Government spending, spending on roads infrastructure also declined sharply from R332,467 million in 1997/98 to R217,384 million in 1999/00 in real terms (1997/98 rand value), which relates to a 34,61 % decline. The Provincial Government realises the importance of maintaining the roads network and providing access to those communities without proper access to the roads network, and it regards infrastructure spending as category C in the sequential priority framework of the Western Cape Fiscal Policy (WCFP) 2001 to 2004. Consequently, in the current MTEF allocations for 2003/04 the roads budget is R311,856 million in 1997/98 rand value, compared with the 1997/98 level of R332,467 million.

Maintenance of roads

The above-mentioned allocations will unfortunately not be enough to address the current backlog in maintenance, which comprises mainly resealing of tar roads and the preserving of the gravel course on gravel roads. It is of the utmost importance to maintain tar roads properly by timeouse resealing, as rehabilitation costs 7 times more than the former, with reconstruction 16 times more expensive. The Annual Report on the Preservation of the Western Cape Road Network (April 2001) indicates that the current backlog to meet the minimum standards is increasing at an accelerating pace and stands at a total of R1,193 billion (regravel/gravel – R357,440 million, pave – R82,89 million, reseal – R143,660 million, rehabilitation – R232,330 million and reconstruction – R378,03 million). The report indicates that –

- current fund allocations are not sufficient to maintain the network to minimum standards;
- the deteriorating condition of the network is outstripping the rate at which maintenance and rehabilitation can be done;
- to maximise the benefits in terms of total transport costs and asset value the required fund allocation must increase by at least 246 %, totalling R102 million annually for the next five years for the Construction and Maintenance Budget;
- the asset value of the roads network is declining;
- traffic density continues to increase, resulting in even further deterioration;
- the inflation rate has resulted in less “buying power” for the allocation received;

- the cost to road users in the Province will be excessively high because of accelerating vehicle operating costs. If the current funding allocations are maintained, the excess (unnecessary) vehicle operating costs due to poor roads will total R4 500 million by the year 2010, compared to R2 000 million should the network be maintained according to the maximum benefits scenario for the same period;
- the Report further indicates that currently 5 % of the surfaced network and 34 % of the unsurfaced network do not meet the minimum standards of performance. This indicates that a drastic increase in funding will be required to restore these roads to the acceptable standards. At the current fund allocation level, the proportion of roads not meeting the minimum standards will continually increase. As a result, pressure on the Provincial Government will increase because of deteriorating services.
- for the current budget split, the surfaced roads in a poor or very poor condition will increase from 1 % to 25 % after 10 years; and
- for current fund allocation levels, the proportion of gravel roads where all gravel has been lost will increase rapidly. In some cases roads will become impassable in the wet season and transport mobility and access will be compromised.

From the above it is quite clear that something drastic needs to be done to ensure that the Province's roads network is preserved properly. It would appear that this is the last opportunity to do something about it, because rehabilitation and reconstruction at a later stage will be too costly.

Balance between maintenance and demands for new roads

As in the case of buildings/facilities the major challenge remains to strike an optimum balance between the allocation for new roads versus that of maintenance of existing ones. Again the answer should be to maintain what you have, but other factors need to be taken into account, such as provision of roads for communities that never had proper access roads, economic development and related considerations, tourism aspects, social development etc. All endeavours should be made to ensure optimal allocation of limited resources to achieve best value for money.

Other issues

Rural development

Another objective was added to the Provincial Government's core objectives, namely Rural Development. Not much information on spending is available, but in future some focus should be on this spending item. Future reporting should thus include information on this topic.

Urban renewal

As in the case of rural development, information on urban renewal is very limited indeed, which makes reporting on this topic almost impossible. However, this is such an important issue for all levels of government that reporting thereon should become a necessity.

Service delivery effects

It would be difficult to define the effect of poor quality facilities on the service delivery by officials. However, if the work environment is not favourable and impacts negatively on the morale of officials, it would be hard to expect of them to give their best to the Province's clients. On the other hand, if the Province's clients must make use of facilities that are not up to standard, it might and would also impact negatively on their mental state, which might also impact negatively on their perception of and experience of the Province's service.

Overspending vs underspending

During the early years of the new Constitutional dispensation this Province was unable to curb spending in line with available revenue. Despite draconian measures which were taken at that time, the Province was overspent by R642 million in 1997/98. However, those measures were not in vain as the overspending has been turned around so that no single department overspent their budget in 2000/01. In fact, underspending to the amount of R409 million occurred in 2000/01, which could also be regarded as problematic, as services which could have been delivered were not delivered. In fact, the taxpayers did not receive the benefit when it was due to them. Provincial Departments are thus encouraged to spend their full allocation effectively, efficiently and economically and in accordance with their approved budgets.

"Swiss Cheese Effect" – Gaps

If one look s at the current underspending, the qualified Auditor-General's Reports, Internal Audit Reports, etc., then it might serve as some indication of the financial and administrative management capacity within the Provincial Government. There would appear to be gaps (swiss cheese effect) in the aforementioned categories of management. This could be ascribed to the implementation of the voluntary severance packages (VSP's) which resulted in substantial experienced personnel in these disciplines leaving the Service. The challenge now is to rebuild that expertise by allocating additional resources, to amongst others, attract personnel with the required skills and competency and to invest in the building of capacity by means of training existing personnel.

Conclusion

In conclusion one can say that the Province did well in managing the overspending down to underspending. This is especially so if the growth in the population of the Western Cape, the additional burden on public services due to HIV/Aids, free medical services for pregnant woman and children under the age of 6, etc. are taken into account. The challenge facing the Province is now to improve the quality of the services it is rendering by investing in the skills and competencies of its personnel and by finding more innovative ways of delivering services.

FOOTNOTES

[1]"Following the agreement, personnel spending in 1996 rose by 11,3 percent above the inflation rate **(IGFR 2001 P97)**. This was negotiated in the same fiscal year that national Government announced its macro-economic framework, which saw an emphasis on a lower deficit. The net result was a decrease in other categories of spending. This negatively affected service delivery."

[2]"As provincial governments face many financial pressures, provinces reduced spending on infrastructure during the past three financial years. In recognition of this trend, National Government identified accelerated infrastructure service delivery as one of its main priorities. To facilitate the aforementioned, a national conditional grant (Provincial Infrastructure Grant – PIG) was introduced with effect of the current financial year. This grant is administrated by the National Treasury and is focussed on Roads, Hospital and Education facilities and rural development. This grant is based on the average of the equitable share and the backlog component of the vertical division of revenue between provinces. The Western Cape's share is R49,524 million of the R800 million in 2001/02, R96,210 million of the R1 550 million in 2002/03 and R114,094 million of the R2 314 million in 2003/04."

4.2 **Systems (Financial)**

Historical

On 1 April 1992 the Financial Management System (FMS) and Personnel and Salary Administration System (PERSAL) were implemented on a centralised basis in the then Cape Provincial Administration (CPA). With the establishment of the Province of the Western Cape on 1 July 1994, the centralised financial functions, including the administration of the systems, continued for all provincial departments, with the exception of the Department of Education, which managed its own financial functions.

As early as 1994 the devolution of financial functions to provincial departments was identified as a priority by the Provincial Treasury, to improve the quality of financial management and to build capacity in provincial departments.

It was however not before amendments to the Public Service Act, 1994 (PSA) and the Public Service Regulations, 1999, were effected on 1 July 1999, devolving considerable powers to Executing Authorities (National and Provincial), and establishing provincial departments as autonomous entities, that the necessary impetus was provided to proceed with the devolution of financial functions. A further factor necessitating the devolution of the financial functions to the departments was that the Provincial Treasury could not be responsible for the day to day operation of the various systems on behalf of provincial departments and at the same time oversee the integrity of the systems (i.e. be both player and referee).

To ensure that provincial departments have ample time to create the necessary structures and capacity to manage their own financial functions, the implementation and decentralisation of FMS and PERSAL commenced during the 1999/2000 financial year, according to the readiness of the individual departments to assume responsibility for the systems.

Current financial administration and management information system

The following table illustrates the current systems in operation, the main functions of the individual systems, the improvements effected since implementation and shortcomings that still exist.

System	Main Functions	Improvements	Shortcomings
Financial Management System (FMS) 1	• Cash based system • Accounting transactions • Payments • Debtors • Bank reconciliation • Detailed miscellaneous and accounting reports.	• Electronic fund transfers. • Enhanced debtors sub-system (includes age analysis). • Fleetman interface. • Electronic downloading of reports.	• Not an on-line system. • Allows for over-spending on budget. • Does not cater for Generally Recognised Accounting Practice (GRAP). • No standard chart of accounts.
Financial Management System (FMS) 2	• Maintenance of code • Files. • Budget capturing tool. • Various management reports available (monthly and up to date).	• User code/password revoke function. • Identification of conditional grant objectives. • Batch/payment enquiries.	• No on-line data capturing facility. • Extensive time intervals between user request and availability of reports. • Not a budget system. • No consolidated financial statements.
Personnel and Salary System (PERSAL)	• Total human resource planning (organisational structure and establishment administration). • Personnel administration: appointments, promotions, terminations, personnel development, service conditions and benefits. • Salary administration: all types of payment of allowances and deductions and correct tax and fringe benefit calculations. • Programmatical adjustment of e.g. salaries and state contributions of medical and housing allowances. • Management information: various reports are available.	• The new leave dispensation • SMS packages • Grievances • Skills development • Interface with the Government Employee Pension Fund. • Access and profile control.	• Ad hoc reports not readily available. • Does not cater for total personnel administration of Educators. • Does not optimally cater for certain control measurements. • Scanning facilities not available. • Not windows friendly. • Not a financial budget monitoring and control system.

System	Main Functions	Improvements	Shortcomings
Logistical Information System (LOGIS)	• Provisioning and procurement system. • Control over consumables and moveable assets. • Provide for management information regarding stock and assets.	• Managing stock by means of minimum and maximum stock levels. • Stock is available when needed. • Overstocking is minimised and predetermined as only a determined amount of stock can be held. • Moving of assets are controlled. • Availability of audit trails on all actions. • Flexible infrastructure. • Access and profile control.	• Bar coding not available as yet. • Not a financial budget control system. • Does not interface with minor items. • Does not cater for a register on guarantees.
Management Information System (Vulindlela).	• Integrated management information. • Drill-down functionalities. • On-line, printing and downloading functionalities. • Information available on all levels. • Relevant and up to date information. • Standard reports available. • Help functions.	• Web-enabled. • In-year monitoring system.	• No budget system. • Access and profile control per institution. • No management information on ledger accounts.
Loss Control	• Registers and manages all losses.	• Inter-departmental transfer of losses was developed. • Availability of management information.	• Not integrated with other financial systems, (FMS, PERSAL, LOGIS) . • Limited consolidated data and management information is available. • Insufficient management information available to identify risk areas and items.

System	Main Functions	Improvements	Shortcomings
Source Link	• Electronic Quotation System.	• Development of monitoring reports. • Software modified to allow certain users to insert their own quotations in emergencies (extra-ordinary).	• A database of accredited suppliers not available. • Not integrated with LOGIS to form part of the procurement process.

Implementation

To ensure that implementation proceeded in a structured manner, the FMS and PERSAL Systems had been implemented at six provincial departments by 31 March 2001 and processes are currently under way to implement the systems at the remaining three provincial departments by 31 March 2002.

As no standard Management Information System for the Government as a whole existed, various software packages were utilised to provide management information, which was not only time-consuming but in general contained outdated information. In co-operation with National Treasury, a Management Information System (Vulindlela) was developed and rolled out to 106 managers at head office level within provincial departments for increased accessibility to relevant and up-to-date management information which enables more effective decision making.

Due to outdated and insufficient systems that existed for the management and control of consumables and moveable assets, the Logistical Information System (LOGIS) was rolled out to 21 self accountable stores which manage a stock value in excess of R750 million.

As no standardised system existed to register losses, the Loss Control System was developed and implemented at all head offices of provincial departments.

The traditional method of obtaining quotes for purchases required, up to certain maximum amounts, has been replaced with Source Link (an electronic quotation system) which has been installed at 70 sites with 275 registered users.

User support is provided to users of the various systems in the day-to-day management and utilisation of the systems.

Needs

A growing need exists for the interfacing and integrating of all financial systems. The following needs have to be addressed:

- Systems that cater for Generally Recognised Accounting Practice (GRAP);
- On-line systems;
- Standard chart of accounts;
- Consolidated financial statements;
- An appropriate budgeting system;
- Management information of various subject areas;
- A database of accredited suppliers;
- LOGIS to interface to minor items; and
- Access and profile control on Vulindlela.

Legislative requirements

Existing National Transversal Financial Administration Systems (FMS, PERSAL, LOGIS and Vulindlela) utilised by this Province were developed to meet the legislative requirements of the then National and Provincial Exchequer Act/Law and do not meet all the legislative requirements of the PFMA, including:

- the introduction of Generally Recognised Accounting Practice (GRAP);
- business process engineering to introduce best practice in Government and to align Government Business with the PFMA; and
- the compilation of consolidated annual financial statements.

Way forward

Ensuring that the rendering of user support to users of the various systems is further enhanced; the National Call Centre System (LOGIK) will be implemented to enable the registering of all incoming calls, the monitoring of outstanding calls and the determining of the level of service delivery.

Ensuring an uptime of at least 95% of all financial administration and management information systems.

Representation of the Province by the provincial systems controllers, situated in the Provincial Treasury, on the various national forums and user meetings.

Issue Provincial Treasury Systems Circulars/Notices regarding the effective, efficient and economical utilisation of the systems.

Financial Management System (FMS)

The daily monitoring of the system, to ensure that the available facilities – (e.g. electronic transfers, financial authorities and commitments) are utilised to their maximum. Interfaces between the various systems (LOGIS, PERSAL, TELKOM, FLEETMAN, MEDSAS and Official Banker) occur on a daily basis. Code files, access control and profiles are maintained.

Personnel and salary system (Persal)

The daily monitoring of the system to ensure that exception reports and ACB Limits are addressed. Ensuring that computer generated identification numbers are allocated only in exceptional cases and then replaced with a legal identification number, within 90 days. That access control and profiles are checked on a regular basis. Computer generated and unique reports are made available for management, budget, cash flow and monitoring purposes. Ensuring that current and updated personal information of employees is captured on the system, a project will be registered for the verification of PERSAL data in all provincial departments and repeated annually.

Logistical Information System (Logis)

The monitoring of the system to ensure that internal service delivery, cost saving and financial perspective of the 21 self accountable stores on LOGIS, comply with the national norms.

The further roll-out of LOGIS to the remaining 61 stores (mainly health institutions) over the next three years, with an estimated stock value in excess of R2,700 billion is expected.

Management Information System (Vulindlela)

The daily monitoring of the system to ensure that Vulindlela is updated with the latest data from the functional systems (FMS, PERSAL, and LOGIS).

User requests are evaluated and forwarded to National Treasury for the further development of the system and/or making available of additional information.

The further roll-out of the system to all identified users in provincial departments, by 31 March 2003.

Loss control

The daily monitoring of the system to ensure that losses are addressed timely and that data errors are corrected.

The further roll-out of the system to identified regional offices and institutions.

Source link

As from 1 April 2002 the implementation and management of the Source Link System is the responsibility of the Sub-directorate Financial Systems in the Provincial Treasury, which was previously managed by the Directorate Regulations.

The daily monitoring of the system to ensure that the software complies with the user requirements and development of a database of accredited suppliers.

In-year monitoring system

Volunteer as the pilot site for the implementation and testing of the new web-enabled, In-year Monitoring System to be developed by the National Treasury.

Enterprise application solution (EAS)

Form part of the subject area expert work groups that will oversee the development and implementation of an on-line, integrated enterprise application solution (EAS) which complies with the current legislation.

To be achieved

It is the aim to empower/assist the accounting officers in managing their revenue, expenditure, assets and liabilities within the limitations of the current systems. This will be achieved by promoting the effective utilisation of the financial, procurement and personnel systems. The ability of managers to access and interpret strategic decision making data accurately and timeously will also be promoted, thus enhancing effective decision making.

The development of a dedicated uniform integrated budgetary system that allows for budget control per expenditure item is an area of immediate concern. This must further include a holistic approach to budgeting, variable scenario analysis capacity, GFS classification mapping and an early warning system. This will be developed in co-operation with the National Treasury.

We also want to achieve improved access and profile control on Vulindlela to address current shortcomings. This will be done to the lowest user level.

Sources

- FMS, PERSAL, LOGIS AND VULINDLELA MANUALS
- Enterprise Application Solution Reference Documentation

4.3 Accounting

Historical

With the inception of the Interim Constitution in 1994, the need to re-organise and rationalise government departments was identified as a priority in order to, inter alia, improve service delivery in government departments. During this process, improving financial management in departments was also identified as a long-term goal. This, inter alia, entailed the decentralisation of the Departmental Accountant Services to provincial departments and the establishment of the Provincial Treasury to control financial management in departments. To address the limited capacity within provincial departments at the time and as a forerunner to the decentralisation of the Departmental Accountant Services, financial expertise from the Departmental Accountant was placed within the various provincial departments as Financial Management Representatives. These Representatives had extensive financial management experience and proved to be successful.

The re-adjustment of the functions of the Heads of Provincial Administrations and Provincial Departments in accordance with the Public Service Laws Amendment Act, effected in 1999, and in keeping with the spirit of the Public Finance Management Act, 1999, (PFMA) the Provincial Treasury continued the process of decentralising the Departmental Accountant Services to the respective departments. With effect from 1 April 2000 the first phase of the decentralisation process took effect with the Departments of Health and Social Services and Economic Affairs, Agriculture and Tourism and the Provincial Parliament being successfully decentralised. In the second phase, the Provincial Treasury and the Department of Planning, Local Government, and Housing were decentralised on 1 April 2001. The third phase which takes effect on 1 April 2002, will see the remaining three Departments, viz. Community Safety, Provincial Administration: Western Cape and Environmental and Cultural Affairs and Sport being finalised, hence the discontinuation of the centralised Departmental Accounting Services with effect from 1 April 2002.

The anactment of the PFMA in April 2000 also necessitated the establishment of a Provincial Accountant-General component within the Provincial Treasury. The Directorate: Accounting Control was established within the hierarchy of the Provincial Accountant-General. Its purpose is to ensure that norms and standards within the legislative framework are implemented and complied with in provincial departments. A ninety percent (90%) success rate was achieved with the first phase of the implementation of the PFMA which focussed mainly on the seven immediate priorities mentioned in the Accounting Officers Guide, viz. in-year management, monitoring and reporting; clearing up audit queries; establishing effective internal controls; improving expenditure management and transfers; establishing framework for banking arrangements; completing the financial statements on time and the delegation of responsibilities. Furthermore, financial statements in the new format (GRAP) in respect of all departments for the 2000/2001 financial year were submitted to the Auditor-General within the time-frame prescribed by the PFMA.

Internal prescripts, viz. Provincial Treasury Directives, were developed for the Province as an interim measure. These have been revisited and are in the process of being re-issued as Provincial Treasury Instructions. This will allow for the effective transition from the old to the new prescripts. Guidance was also given to departments on the issuing of departmental internal financial prescripts not inconsistent with the prescribed norms and standards.

Legislative framework

The Directorate Accounting and Regulatory Control Services operates within the legislative environment of the PFMA, 1999, and more specifically sections 18(1)(c), 18(2), 19(1),19(4) and 76(4), as well as the Treasury Regulations and the Provincial Treasury Directives. In essence the aforementioned sections of the PFMA relate to the functions and powers of the Provincial Treasury, the consolidation of financial statements and the making of regulations applicable to institutions to which the Act apply.

Accounting policy

Although the basis of accounting mentioned below is centered around cash basis accounting this will be reviewed as the Accounting Standards Board further develop GRAP standards for accrual accounting.

Basis of accounting

The financial statements are currently prepared on the historical cost basis in accordance with the following policies, which are applied consistently in all material respects.

- Underlying assumptions

The financial statements are prepared on the cash basis of accounting. Under the cash basis of accounting, transactions and other events are recognised when cash is received or paid. This basis of accounting measures financial results for a period as the difference between cash receipts and cash payments. Reliance is placed on the fact that departments are a going concern.

- Revenue

  Revenue of the Province and/or departmental receipts are paid over to the Provincial Revenue Fund. Unexpended voted funds are surrendered to the Provincial Revenue Fund.

- Expenditure

  The income statement includes both current and capital expenditure. Unauthorised expenditure is not accounted for as expenditure until such expenditure is either authorised by the Provincial Parliament, recovered from a third party, or funded from the following year's appropriation.

- Assets

  Physical assets (fixed assets, moveable assets and inventories) are written off in full when they are paid for and are accounted for as expenditure in the income statement. The balance sheet therefore excludes physical assets unless stated otherwise.

- Receivables and payables

  Receivables and payables are not normally recognised under the cash basis of accounting. However, receivables and payables included in the balance sheet arise from cash payments which are recoverable and cash receipts which are due to either the Provincial Revenue Fund or another party.

General concerns with accounts in the Province

- Establishing the net effect of assets and liabilities in the Province

  There is a genuine concern for establishing the net effect of assets and liabilities in the Province, in order to be in a position to commit unattached reserves. In the light of possible hidden liabilities in the books of accounts emanating from the rationalisation process of the tricameral system and the former Cape Provincial Administration, this aspect was taken up under Statement of Contingent Liabilities in Chapter 5 of this document.

- Qualified Auditor-General reports

  The trend regarding the qualification of Audit reports for the 1998/1999 and 1999/2000 financial years reflected a decrease from 47 % to 28 %. However, qualification of the audit reports for the 2000/2001 financial year reflected a marginal increase to 30 %. The qualification of audit reports in general is largely due to the lack of capacity in departments, which was further aggravated with the implementation of the PFMA on 1 April 2000. The key area of audit qualification is poor internal checking and control, and particularly non compliance with financial prescripts. This will be addressed through complying with section 18 of the PFMA by the Provincial Treasury, the increasing of resources allocated to the Internal Audit Component and the development of capacity in departments.

- Limited interpretative skills, coupled with nominal compliance with the PFMA, by departments and the Provincial Treasury

  Departments have shown limited knowledge with regard to analysing accounting reports, financial statements, etc. in order to take timeous corrective actions to remedy identified shortcomings. This could lead to poor financial management, including an unhealthy state of the books of account or unauthorised expenditure, which in turn could result in poor financial statements and qualified audit reports. In addition, departments have shown a tendency of nominal compliance with certain requirements of the PFMA and not with its true intent.

The following are concerns where departments have nominally complied with the PFMA, but without adding value to the standard of service delivery, performance and effective financial management:

- Macro risk assessments were carried out in departments instead of detailed risk analysis;
- Resultant strategies, viz. fraud prevention plans, are largely ineffective to manage risks due to macro assessment; and
- Poor analysis of audit reports in order to prevent repetition of shortcomings.

In general the focus by departments needs to shift from nominal compliance to value adding and substantive compliance with the PFMA. The Provincial Treasury needs to prioritise and champion the implementation of the PFMA and ensure that the implementation is in line with the objectives and spirit of the PFMA. This is receiving the on-going attention of the Provincial Treasury, for example, controlling the implementation of the PFMA in provincial departments and provincial public entities.

Way forward

The successful implementation of the first phase of the PFMA in public entities and the second phase in provincial departments, shifting the focus from nominal compliance to value adding and substantive compliance with the PFMA. The key focus would be to analyse progress reports of public entities and departments on the implementation of the PFMA together with their Audit Reports to identify shortcomings and where necessary issue best practices on transversal concerns. This will in effect also reduce the number of qualified reports by the Auditor-General. However, this process will evolve over time as capacity and expertise are developed.

To comply with the GRAP standards set by the Accounting Standards Board for the compilation of financial statements. This will entail interacting with departments on the formats of annual financial statements and training departments in the compilation of financial statements. More important is to monitor the quality of accounts in departments in order to produce quality financial statements. This will be enhanced by the development of appropriate interpretative and analytical accounting skills in departments, public entities and the Provincial Treasury as we progress towards accrual based accounting. The current transversal accounting systems are however inadequate to fully meet the requirements of GRAP as well as accrual accounting. The training and system deficiencies are addressed under the heading Systems (Financial).

Sources

- Guidelines for Accounting Officers: National Treasury
- Baseline Implementation Guide: Department of Public Service and Administration

4.4 Capacity building

Historical background

The past six years have been characterised by a reconstruction and development process resulting in a loss of skilled and competent personnel through the introduction of voluntary severance packages. Furthermore, stipulations in the Public Finance Management Act placed accountability with the heads of departments, resulting in the decentralisation of certain core responsibilities to departmental level.

The Western Cape Government realised that in order to be successful in improving service delivery, it has to adapt to the changing work environment and made a commitment to human resource development. A formal financial training component, broadly operating under the auspices of the Western Cape Administration Academy, was established in the Provincial Treasury during 1995 with a vision to supply functional financial training in a professional manner to ensure excellence in financial-, personnel- and provisioning administration. Since 1995, a total of 11 400 officials were nominated to attend 24 courses, 9 practical seminars and information sessions.

Training needs growth

In the document "Training Framework for Government Finance Staff: IPFA 2001" the conclusion was drawn that there are significant gaps in competence levels of middle and senior management as they relate to the current and future requirements of legislated transformation.

With the departure of huge numbers of skilled and experienced financial functionaries taking the voluntary severance package a skills gap in the operation and maintenance of financial systems (FMS PERSAL and LOGIS) led to a decline in the quantity and quality of services that the Provincial Treasury was in a position to render. To remedy this situation a strategy of delivering functional training on the various systems was embarked upon.

The aggressive marketing, regular updating of training material with the latest Acts, prescripts and best practices, the development of new courses to satisfy user demands and the professional ethos of the training component resulted in the explosion in the demand for training.

The pace of legislated transformation has had the effect that the output of suitably qualified individuals is not sufficient to provide for medium and long term needs of both private and public sector organisations and the dynamic demands being placed on them.

Under these conditions the creation of a learning organisation and a culture of learning as well as the adoption of a life-long learning philosophy becomes imperatives.

The establishment of a world-class learning centre at the Western Cape Administration Academy at Kromme Rhee that engenders local and international respect is envisaged.

Current resources

The approved personnel strength of the current training component has expanded to twelve trainers and two administrative personnel under the supervision of a deputy director, currently presenting a range of 24 formal courses and nine practical seminars.

New training facilities were put into service, consisting of three computer rooms accommodating 10 students each and one standard training room accommodating 20 students situated at 4 Dorp Street, Cape Town. In addition to the above facilities a computer room accommodating 10 students is also available at Kromme Rhee. The facilities in the training component were also upgraded with the latest technology in the form of laptop computers, electronic video projectors, colour printers, a scanner and a laminator.

Legal framework for training

Human resource development is impacted on by the following legislation and other relevant policy directives:

- The Constitution, 1999
- Public Finance Management Act, 1999
- Public Service Act, 1994
- Labour Relations Act, 1995
- Employment Equity Act, 1998
- Basic Conditions of Employment Act, 1998
- Skills Development Act, 1998
- South African Qualifications Authority Act, 1995
- White Paper on Transformation in the Public Service
- White Paper on Affirmative Action in the Public Service
- White Paper on Service Delivery in the Public Sector (Batho Pele)
- White Paper on Education and Training
- White Paper on Human Resource Development

Requirements vs current position

A key area to the provision of an effective and efficient professional Human Resource Development service is the availability of suitably qualified and trained personnel. With the present skills levels of the training facilitators the component is in a position to accommodate current training requirements. However, the vision of the future will require more highly skilled personnel with a different set of competencies. This would enable the component to register as an accredited learning centre and an accredited assessment centre.

The current course material is being re-organised into modules for accreditation with the South African Qualification Authority and the National Qualification Framework via the Financial Sector Education and Training. At this stage upgrading of course material for LOGIS and PERSAL training is already in progress. This matter is being driven by the National Treasury. The FMS course material is being re-organised into modular courses for which the accreditation process is currently in progress.

Further to this the component's priorities regarding training can be divided into the following categories:

- Functional training, which will concentrate on systems training;
- Vocational development, which will be focused on accredited work place skills development as in the Competency Based Education and Training model promoted by the Institute for Public Finance and Auditing;
- Fiscal strategic management training, which will be focused on finance and economic management skills development; and
- Qualification training, focused on the administration of bursaries to promote a higher level of professional qualifications in the Provincial Treasury.

The component is being geared towards presenting the foundation and intermediate phases of the Competency Based Education and Training programme in-house and to this end analysis, investigation and research is being carried out to develop the required course material.

In order to provide for future requirements the ideal is to increase the level of funding to 4 % of the personnel budget. This is considered a standard for effective human resource development at a macro level.

The first step would be the re-organisation of the component at directorate level with the necessary infrastructure to drive this process successfully. The re-organisation of the component would include a dedicated research and development component as well as a vocational development component.

As already mentioned above, the component is currently utilising four training rooms. The new vision requires the establishment of a dedicated campus or learning centre. This would entail more classrooms and other facilities with a view to expanding the facilities as and when the vision is realised. These facilities would include computers and related equipment as well as other support facilities.

The way forward

The processes have the following long term, medium term and short term requirements:

Long term

The creation of a culture of life-long learning through:

- The implementation of a workplace skills plan
- Recognition of prior learning
- Implementation of qualifications education and learnership programmes
- Implementation of a quality assurance system (accreditation, assessment, moderation and certification)

The Provincial Treasury is to become a true learning organisation by recognising that learning should take place at all levels for all employees and is to include this goal in its strategy, structure and culture.

It is envisaged that in consultation with the Director-General, the Branch Corporate Services and with the support of the Board of the Western Cape Administrative Academy, at Kromme Rhee, and the Provincial Cabinet a School for Public Accounting and Economic Studies be established at the Academy that provides for short courses in finance, economics, analytical, interpretation, functional and Competency Based Education and Training programmes that all will lead to an internationally recognised tertiary qualification.

The development and implementation of a promotions policy that is directly linked to development in which the progress of individuals is linked to the successful completion of various competence modules and learnership programmes without which upward mobility would be impaired.

Medium-term

Establish an effective human resource system that addresses performance management, attracts and retrains highly skilled personnel, and implement learning and career paths for all personnel.

Strengthening the management capacity of training and development within the Provincial Treasury.

Design, finance and develop a learning centre.

Implement development strategy through the expansion of course programmes based on the needs of the target market.

Short term

Develop a training policy.

Identify the target market and set training priorities at all levels.

Register as an accredited learning and assessment centre.

Provide functional financial training through the presentation of accredited short courses structured in a modular outcomes-based format and presented by accredited training officials.

Create a component responsible for vocational development through the implementation of a workplace skills plan based on the minimum competency levels linked to each post.

Restructure the component to provide for research and development.

Research, develop and implement a computer-based training system.

Requirements

In terms of what is required to achieve these objectives the need for the required funding, personnel and leadership stands out. Management decisions relating to the expansion of the component, the envisaged course programmes and the establishment of a human resource development philosophy become indispensable. This is also based on the Provincial Treasury's ability to develop and accept an inclusive value-driven approach to human resource development.

Resources and how to achieve them

The development of facilities at an institution such as the Academy at Kromme Rhee, the ideal budget at 4 % of provincial treasury personnel expenditure and the fiscal policy that makes it possible, need to be put in place. Management throughout the Provincial Government needs to buy into this vision and the processes which drive it.

Training providers

In order to deliver effectively on the ground, the recruitment of suitably qualified human resource development practitioners and a working relationship with all providers of training, including the five tertiary institutions in the Western Cape, become necessities. Amongst these the Departmental Training Committees, Cape Administrative Academy, the National Treasury, the South African Management

Development Institute (SAMDI), the Provincial Training Bodies, the external training providers, the tertiary education institutions, IPFA and other professional councils and bodies in training and education, relevant civil society stakeholders and business organisations, financial and procurement personnel and the Senior Management Service of provincial departments are the important role players.

REFERENCES

Legislation and other relevant policy directives mentioned on page 71.

Institute for Public Finance and Auditing, 2001. The development of a framework for future training in government financial management.

Department of Public Service and Administration, 2000. Baseline Information on Public Service Training and Education.

4.5 Procurement

Historical Review

The Western Cape Tender Board Law (Law 8 of 1994) was passed by the Western Cape Parliament in 1994 in terms of section 187 of the Interim Constitution of the RSA (Act 200 of 1993). The Tender Board Law provided for the cessation of the regional tender board established for the Western Cape in terms of the State Tender Board Act (Act 86 of 1986), and the establishment of a provincial tender board for the Western Cape with the powers and functions as stipulated in the Tender Board Law. The Western Cape Provincial Tender Board ("-the Board") was accordingly established on 9 April 1996 with its objectives, powers and functions as set out in the Law.

Policy debates during the development of the Constitution in the early stages of 1990 placed particular emphasis on procurement as a policy measure to achieve reconstruction and development objectives in the South African economy. The importance thereof has been emphasised in a number of government white papers developed and adopted during this period, after the adoption of the Constitution (e.g. Small Business White Paper).

In 1995, under the initiative of the then national Minister of Finance, steps were taken to reform government procurement. The Green Paper on Public Sector Procurement Reform in South Africa (published 1997) is notably one of the more important documents and spells out the role of procurement in achieving reform objectives. It recognises that good governance is essential whilst reiterating the importance of using procurement as a tool to achieve economic ideals. This view forms the foundation of the procurement reform process and the development of policies and procedures. At the same time, the Green Paper recognises that an effective and efficient procurement system will permit organs of state to deliver the quality and quantity of services demanded by its new constituency in accordance with its policies, which are articulated in the Reconstruction and Development Program and the Growth, Employment and Redistribution Strategy.

The Board, in line with the objectives outlined in the Green Paper and the 10 point plan strategy designed by the National Cabinet in consultation with the Provincial Cabinet, introduced a preference point system on 1 November 1998 to enhance the participation of historically disadvantaged persons in provincial procurement. This system was introduced in selective industries where participation of historically disadvantaged persons (HDP's) was either non-existent or limited. This policy had the desired effect and contracts awarded to HDP's have grown as follows:

1998/99	± R 90 million
99/2000	± R 138 million
2000/2001	± R 207 million

To enable departments to enhance service delivery it was recognised that alternative procurement systems needed to be put in place. Similarly it was important to demystify the procurement process and make it accessible to as many suppliers as possible. As a result, an Electronic Purchasing System was introduced during 1998 to simplify the way the Western Cape Government procures goods and services up to the value of R20 000. It further centralised the procurement requirements to make purchasing opportunities accessible to businesses without their incurring additional expenses in visiting all departmental purchasing points. Currently 65 departmental purchasing sites (450 buyers) and 1600 suppliers are connected to the system.

The introduction of the Electronic Purchasing System was a first for any national or provincial government department and generated widespread interest that culminated in visits from the Office of the State Tender Board and other Provincial Tender Board Offices to the Western Cape. This also sparked the notion of E-procurement with the National Treasury.

On 3 February 2000, National Treasury promulgated the Preferential Procurement Policy Framework Act (Act 5 of 2000) (PPPFA) with the intention to legislate the introduction of preferential procurement to target historically disadvantaged persons (HDP's) and promote the objectives of the RDP. This was followed by the Procurement Regulations promulgated on 10 August 2001. The PPPFA requires that all organs of State determine their preferential procurement policy and implement it in terms thereof. Prior to this the Board appointed a consultancy to assist with the compilation of such policy. After much deliberation by various stakeholders (including departments and business associations), the policy was eventually accepted by the Board on 6 November 2001 with the recommendation that it be submitted to the Provincial Cabinet for approval. It is envisaged that this policy will be implemented as rapidly as possible within all provincial departments.

As part of its procurement reform initiative the National Treasury presented a Report on Opportunities for Reform of Government Procurement in South Africa during October 2000. The following is a summary of the envisaged direction of the National Treasury as outlined in the aforementioned Report.

That -

- National Treasury in conjunction with departments establish methodologies for measuring government's objectives under the Preferential Procurement Policy Framework Act, 2000;
- National Treasury be responsible for broad policies and good practices;
- Provincial tender board acts be repealed and Tender Boards abolished;
- Procurement be fostered with accounting officers;
- "Accredited Procurement Units" be established in each department, which will be responsible to the "Head of Procurement" of that department; and
- A supply chain management approach be followed by establishing a "Common Service Provider" responsible for procurement, stock control, quality management etc., which will render a service to departments on a cost recovery basis.

In its response to the above mentioned Report the Provincial Treasury pledged its support to the spirit thereof, but explicitly indicated that the Provincial environment differs from that of the National, and that the Provincial Tender Board is still regarded as an important body in the provincial procurement system. It further indicated that the Provincial Treasury itself would in future play a much larger role as far as provincial procurement is concerned.

In terms of the Western Cape Provincial Tender Board Law, officials within the Provincial Treasury shall perform all administrative work on behalf of the Board, including performing the functions and exercising the delegated powers of the Board. An office of the Western Cape Provincial Tender Board was initially established within the Provincial Treasury to perform the aforementioned functions. This component has been upgraded and expanded to more effectively serve the Board, particularly in the area of formulation, monitoring, analysing and advising on procurement systems and processes and enforcing adherence thereto. Other than those already mentioned, achievements to date include:

- compilation and issuing of regulations with regard to general conditions applicable to tenders, contracts and orders (KST36);

- development of procurement policy for the security industry;
- development of standard specifications and contracts in the transport industry;
- enhancement of decision-making by the Board as a result of the manner and the format in which tender submissions and resolutions are presented to the Board; and
- the creation of a web-site where relevant procurement documentation and prescripts can be viewed.

Legislative framework

In performing its functions the Tender Board and the Provincial Government are governed by the following legislation:

- Section 217 of the Constitution of the RSA, 1996 (Act 108 of 1996)
- Section 62 of the Constitution of the Western Cape,1997 (Act 1 of 1997)
- Western Cape Provincial Tender Board Law, 1994 (Law 8 of 1994)
- Preferential Procurement Policy Framework Act, 2000 (Act 5 of 2000) and its regulations
- Public Finance Management Act, 1999 (Act 1 of 1999)

In addition to the above, procurement activities in the Province are also carried out in accordance with the KST 36 Regulations (Conditions and Procedures) and KST 37 (User Manual). Further, the Green Paper on Public Sector Procurement Reform in South Africa is used as a guideline by the Tender Board and the Provincial Treasury in achieving procurement reform objectives.

Issues of concern

Current and future initiatives for procurement reform require fundamental institutional reform and development of effective procurement systems and practices which will enable government to deliver the required quantity and quality of service. The aforementioned also provides for a dynamic shift in the way procurement should be dealt with. This shift requires a skills level which does not currently exist in departments and to a lesser extent, in the Provincial Treasury. Of concern is also the lack of understanding of the basics of procurement and its possible impact on the financial position of the Province. Further, it is important that departments are equipped to take full responsibility for certain aspects of procurement as required in terms of the Public Financial Management Act, 1999 (PFMA). The challenge therefore will be to ensure that skilled personnel are recruited and/or current procurement personnel are properly trained to enhance their skills level.

Until recently, procurement has always been seen as a subsection of financial management, with the result that no provision has been made for more advanced training on procurement. Furthermore, training is not provided on a continuous basis as a result of a lack of skilled training personnel who are able to provide the necessary training on procurement.

Procurement is also part of the Supply Chain Management System and should be integrated with other facets of provisioning administration. However, this integration however seems distant but is important to ensure cost effective procurement of goods and services and proper asset management.

The current procurement system is inflexible to specialised departmental needs, which results in the fact that procurement is not done in the most cost- effective manner. This entails that the necessary research should be undertaken to assist departments to procure in an economical, effective and efficient manner.

Way forward

In terms of the PFMA, accounting officers must ensure that their departments have and maintain appropriate procurement and provisioning systems which are fair, equitable, transparent, competitive and cost effective. To give effect to the aforementioned, the role of the Board, Provincial Treasury and that of accounting officers needs to be clearly defined in order to foster accountability regarding procurement.

Firstly, it is necessary to shift the focus of the Board to concentrate on the establishment of procurement practices to address specific departmental needs. This will necessitate the amendment of the Tender Board Law and the creation of an adequate legislative environment within which the Board should function. The Board and/or the Provincial Treasury, as applicable, will further be responsible for designing and overseeing the successful implementation of bespoke and efficient procurement systems within the Provincial Government, providing advice to departments and ensuring that the necessary capacity to deal with procurement has been introduced in departments.

Secondly, the power to adjudicate contracts will increasingly devolve to accounting officers in the departments. However, these powers will only be granted once the proper infrastructure to effectively deal with procurement, is instituted on departmental level. This implies that the extent of the powers granted to accounting officers will be in direct proportion to their competency in dealing with procurement matters.

More emphasis will be placed on improving the current manner in which contract administration and contract management are dealt with, with the aim of ensuring that the Province gets value for its money.

Procurement Administration and Provisioning Administration will be integrated to ensure that the direct link between the process of the identification of needs, the appointment of a service provider, timely delivery of the required quality, timely payment and inventory control are maintained.

The current Electronic Purchasing System applicable to contracts to the value of R20 000 will be further developed with the intention of catering for all levels of procurement (E-procurement) and expanded where possible to serve rural areas to promote local economic development.

The Preferential Procurement Policy will be introduced by way of a structural implementation plan within all departments and the necessary reporting mechanisms will be put in place to ensure that the Board and the Western Cape Parliament are continuously informed of its impact, from both a financial and socio-economic perspective.

REFERENCES

Green Paper on Public Sector Procurement Reform, an initiative of the Ministry of Finance and Ministry of Public Works, Government Printer Government Gazette 17928 dated 14 April 1997.

5

CONTINGENT LIABILITIES AND DEBTORS

5.1 Contingent liabilities

Introduction

Apart from legislative compliance, as set out under the sub heading Legal Framework below, the Western Cape Government (hereafter referred to as WC Government), cannot afford to overlook obligations taken outside its budgetary system. If the Government is to avoid sudden fiscal instability and to realise long term policy objectives, all sources of fiscal risk needs to be addressed.

This Chapter, for all intents and purposes, should be seen as a second attempt to provide information on the WC Government's contingent liabilities. The first attempt was captured in Chapter 14 of the Western Cape Fiscal Policy 2001 – 2004 that was generally adopted by the WC Government during August 2000.

Apart from the R101 million (1998/99) and R139 million (1999/2000) respectively allocated by the National Government for debt redemption, the WC Government also managed to set aside R157 million (1999/2000), R46 million (2000/01) and R8 million (2001/02) for the same purpose. These funds are mainly used to redeem the cash short falls resulting from overspending on the budget in the past.

Prior to the implementation of the PFMA, which provides for a similar intervention, the WC Government took the policy decision[1] that budget over-expenditures and amounts under-collected on the revenue side, will be recovered from departmental budgets in the subsequent year or years.

To improve sophistication in dealing with contingent liabilities, and weighing up the options with regard to resource allocation, the WC Government made the policy choice [2] to set aside R50 million over each of the medium term expenditure frameworks, commencing in 2001/02, as a contingency reserve. This contingency reserve is mainly used to provide for variables such as internal and external shocks that emanate from economic and other factors, in particular unforeseeable and unavoidable expenditure. Such expenditure in term of the Treasury Regulations, 2001 does not include:

[1] Western Cape Cabinet Minute 515/1996 of 12 November 1996
[2] Western Cape Fiscal Policy 2001 - 2004

- expenditure that, although known when finalising the estimates of expenditure, could not be accommodated within allocations;
- tariff adjustments and price increases; and
- extensions of existing services and the creation of new services that are not unforeseeable and unavoidable.

The down side of the practice of creating a contingency reserve to reduce the pressure on the budget when contingencies fall due is that fewer funds are available for other spending. Over the medium term, 2001 to 2004, it represents on average 0,4 % of voted/baseline funds.

Purpose

The purpose of this section of Chapter 5 is to:

- Inform decision-makers of the legal requirements placed upon the Western Cape Treasury and Accounting Officers to manage contingent liabilities;

- Comply with legal requirements, in letter and spirit, through a process of identifying, recording, understanding, assessing and updating the information on contingent liabilities and enhancing the quality of such information;

- Provide better information on contingent liabilities and by so doing further promote accountability and transparency;

- Determine the magnitude of the fiscal impact that the contingent liabilities could have on financing resources;

- Acknowledge the importance of managing contingent liabilities; and

- Describe the lessons learnt from the past and the challenges facing the future management of contingent liabilities.

Legal framework

An appropriate departure point for this Chapter, from a public finance management perspective, would be to take cognisance of the stipulations of the PFMA, which took effect on 1 April 2000, as well as the Treasury Regulations, 2001, subsequently issued in terms of the latter legislation.

The PFMA, section 18(c), places a clear responsibility on the Provincial Treasury by including in its functions and powers the imperative to promote and enforce transparency and effective management in respect of liabilities of provincial departments and provincial public entities.

Accounting officers of provincial departments and trading entities do not escape this imperative. In their general responsibilities as contained in the PFMA, it is explicitly required from them, in terms of sections 38(1)(a)(i) and 38(1)(d), respectively, to ensure that they have and maintain effective, efficient and transparent systems of risk management, and to responsibly manage any liabilities.

Section 38(2) prohibits the accounting officer from entering into any commitment for a liability for which money has not been appropriated.

In terms of section 66(2) of the PFMA and Treasury Regulation 13.1.1, the WC Government may only through the Provincial Minister, responsible for financial matters, borrow money, or issue a guarantee, indemnity or security, or enter into any other transaction that binds or may bind the Provincial Revenue Fund to any future financial commitment.

In terms of section 67 of the PFMA, the Government may not borrow money, or issue a guarantee, indemnity or security or enter into any other transaction that binds it to any future financial commitment, denominated in foreign currency or concluded on a foreign financial market.

Treasury Regulation, 2001 13.1.4 requires accounting officers to report on all contingent liabilities, such as with regard to borrowing, guarantees, securities or indemnities of their department in its annual report.

Definitions

A range of factors may influence the actual budget (revenue and expenditure) outcome in future years. However, sound fiscal policy should require these to be disclosed in each budget process. Occurrences, apart from changes in economic and other parameters, that could affect fiscal outcomes are matters that have not been included in the budget estimates because of uncertainty about their timing, magnitude, or eventuality. In some cases, the events will simply raise the possibility of some fiscal impact. In other cases, some fiscal impact will be reasonably certain. These fiscal risks may affect both revenue and expenditure.

Contingent liabilities are broadly defined as costs a government will have to face if a particular event occurs. However, for purposes of this section of Chapter 5 contingent liabilities have been categorised as **liabilities, commitments, contingencies** and **provisions.** They have the following meanings:

- A **liability** is a present contractual or legal obligation of the department arising from a past event, the settlement of which is expected to result in an outflow of economic benefits from the department's resources, typically a payment of cash or the transfer of another asset. Three essential characteristics of a liability are –
  - the existence of a present obligation (i.e. the department must have a duty or responsibility to a third party which has not yet been satisfied) to act or perform in a certain way;
  - it must involve a cost to the department, in that the department is obliged to incur, substitute or replace liabilities, or dispose of cash or other assets to one or more institutions (sacrifice service potential or future economic benefits); and
  - the transaction or event (e.g. the receipt of goods or services or other benefit) which gives rise to the obligation to sacrifice service potential or future economic benefit (e.g. the making of a payment) must have occurred.
- A **commitment** is an obligation or undertaking to make a payment, typically in return for goods, services or other assets, on or after acceptance of the goods, services or other assets concerned (any remaining obligation or undertaking outstanding after acceptance becomes a liability). In the case of governments, commitments also may entail the making of transfer payments, such as grants, without any reciprocal exchange of value. A commitment normally involves an irrevocable agreement to honour an obligation and the institution has little, if any, discretion to avoid the payment or other outflow of resources to another party once the other party has fulfilled its obligation, if any, under the agreement.
- **Contingencies** are conditions or circumstances arising from past events that -
  - exist at the balance sheet date;
  - give rise to uncertainty as to the possibility of gain (asset) or loss (liability) to the institution; and
  - will be confirmed only on the occurrence or non-occurrence of one or more uncertain future events that are outside the control of the department.

Contingencies therefore refer to conditions, situations or circumstances that exist but which involves uncertainty, the outcome of which will be resolved in the future. Examples of contingent losses or liabilities include loan guarantees (where a liability only arises if the party in respect of which the guarantee was given, defaults on a loan repayment) and indemnities.

- A **provision** is a liability in respect of which the amount or timing of the expenditure that will be undertaken is uncertain (e.g. a provision for doubtful debts). Provisions are a sub-class of liabilities, not a separate element of the balance sheet, and can be distinguished from other liabilities such as trade creditors and other accrued amounts payable. The distinguishing feature of a provision is uncertainty over either the timing or amount of the expected cost or loss of benefit.

In terms of the National Treasury's Guide for the Preparation of 2001 Annual Financial Statements of Departments and Constitutional Institutions issued by the Office of the Accountant-General - 5 August 2001 version – "Contingent liabilities" are defined as:

"Present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential. (IPSAS 2)

- Current: A liability should be classified as a current liability when it
  - Is expected to be settled in the normal course of the entity's operating cycle; or
  - Is due to be settled within 12 months of the reporting date.(Source IPSAS 1)

- Non-current: All liabilities that are not current liabilities should be classified as non-current liabilities. (Source IPSAS) "

Managing contingent liabilities

The intention of the following is not to go into a full discussion on the issues but merely, in a concise manner, to convey a sense of importance of why a government should be aware of the extent of its exposure to contingent liabilities:

- To prevent the central government from having to intervene when provincial governments find themselves unable to meet unexpected obligations;
- To prevent a provincial government of having to intervene when departments, provincial public entities or trading entities find themselves unable to meet their unexpected obligations;
- Credit rating agencies are paying more attention to contingent liabilities when assessing government's creditworthiness;
- Government's ability to identify, measure and evaluate contingent liabilities will result in a significant move towards controlling their expansion and reducing overall risk. Techniques thus also need to be constantly developed and applied to manage risk;
- Predictability is of great value for a government. With respect to future public financing requirements, government could be in a position, for example, to make

choices between providing direct budgetary support and keeping reserves for uncertain events or off-budget liabilities;

- To attain fiscal stability, government needs to be in a position to identify, classify and understand the consequences of the full range of contingent liabilities. A large number of contingent liabilities could threaten future budget stability;
- Costs of liabilities met from a contingency reserve would not directly affect the budget. However, there are opportunity costs as the reserving of funds in a Provincial Revenue Fund reduces the amount available for other programmes, projects and services. On the other hand, a government should be allowed the choice to create adequate reserve funds to reduce the above effects on budgeted spending plans when contingent liabilities fall due;
- Hidden costs, for example, contractual defaults, can result in growing claims on the budget and thus needs to be determined as accurately as possible;
- Government should subject contingent liabilities to the same level of scrutiny as its direct spending programmes;
- Concerns for the implementation of contingent liabilities in an ad hoc manner need to be addressed;
- Weaknesses in the financial management, regulatory and supervisory systems, and disclosure practices that would result in larger and growing contingent liabilities, need to be prevented.
- A balanced budget does not in itself prove that a government has been fiscally prudent, nor does it assure future fiscal stability; and.
- Matters not currently under active consideration by a government, or pressures from interests outside the government for changes in spending levels should not be treated as fiscal risks.

Statement of contingent liabilities

The Provincial Treasury has for some time now assimilated and assessed data in an endeavour to adequately capture the net liabilities of the Province. This has been difficult in the light of possible hidden liabilities in the books of accounts of particularly the centralised Departmental Accountant Services which originated during the rationalisation process of the tricameral system with the former Cape Provincial Administration during the 1994/1995 and subsequent financial years. It is imperative that these amounts be identified as they may influence contingent liabilities. The decision to decentralise the Departmental Accountant Services resulted in separate Financial Management Systems (FMS) being implemented for each department and the intended closing down of the centralised Departmental Accountant Services with effect from 1 April 2002. The final net assets or liabilities of the centralised Departmental Accountant Services will have to be determined once all suspense accounts have been cleared, by either pairing off entries or transferring entries to the newly established Financial Management System. The balances of the three remaining Provincial Departments which operated on the centralised basis can only be transferred after closing off the 2001/2002 financial year (after April 2002). To check whether all contingent liabilities have been identified, departments were also requested to carry out a similar exercise, in particular the Department of Education, who inherited balances from the previous Administration: House of Representatives. Since the books of the former Cape Provincial Administration and the centralised Departmental Accountant Services are dormant, or will soon be, with no financial and human resource allocation , a project team funded out of a special allocation will be appointed by the Provincial Treasury to determine the contingent liabilities.

To date the following summarised Statement of Contingent Liabilities as from 1 April 1995 can be tabled. The numbers given are preliminary and subject to further research and verification.

Liabilities

The cumulative liabilities of the Province, inclusive of the definitive carry-through effects and other contractual liabilities as at 31 October 2001, are captured in table 1 below.

Table 1

Liability	R'000 2002/03	R'000 2003/04	R'000 2004/05
Cumulative unauthorised expenditure: 1994/95 to 2000/01	328,594	-	-
Ex Cape Provincial Administration suspense accounts	53,293	-	-
Ex Cape Provincial Administration surplus to be refunded to the National Treasury	41,483	-	-
Vote 7: Social Services - In validation of Regulation 11 (out of court settlement)	135,439	-	-
Sub total	558,809		

Commitments

Commitments to various contracting parties are reflected in table 2.

Table 2

Commitment	R'000 2002/03	R'000 2003/04	R'000 2004/05
Vote 1: Premier, Director-General and Corporate Services - Exchange rate depreciation for the Health Information System (HIS)	8,031	8,031	8,031
Vote 1: Premier, Director-General and Corporate Services - Once-off payment to Northern Cape Provincial Government: Provincialisation of Lanok (Pty) Ltd and related audit fee	1,841	-	-
Vote 6: Health - Transfer of laboratories to National Health Laboratory Services	41,247	-	-
Vote 10: Economic Affairs, Agriculture and Tourism - Roads construction partnership	45,000	45,000	45,000
- Construction of International Conference Centre, Cape Town	85,000	-	-
Sub Total	181,119	53,031	53,031

Contingencies

Departments have identified a number of this category of contingent liability shown in table 3 below.

Table 3

Contingencies	R'000 2002/03	R'000 2003/04	R'000 2004/05
Vote 1: Premier, Director-General and Corporate Services - Increase in SITA expenses due to increase of user base	2,000	4,000	6,000
Vote 1: Premier, Director-General and Corporate Services - Unforeseeable litigation, particularly of a constitutional nature	500	500	500
Vote 3: Finance - Possible litigation claims	21,660	-	-

Contingencies	R'000 2002/03	R'000 2003/04	R'000 2004/05
Vote 5: Education - Possible litigation claims	210,000	-	-
Vote 5: Education Transactions which may result in debits against voted funds:		-	-
- Over expenditure of the Western Cape Education Department and previous departments	72,000	-	-
- Owed by other provinces and other departments	115,000	-	-
- Owed by individuals and other departments	16,000	-	-
Vote 9: Environmental and Cultural Affairs and Sport Western Cape Nature Conservation Board:		-	-
- Claims for fire damage	8,871	-	-
- Damages due to loss of income	53	-	-
Vote 9: Environmental and Cultural Affairs and Sport - Legal, mediation and court costs arising from compensation claims or court actions with regard to environmental management:	15,000	15,000	15,000
- Financing fully all public library services in the Western Cape Province	205,044	247,217	264,522
Vote 10: Economic Affairs, Agriculture and Tourism - Flood/drought relief to farmers in affected areas	3,000	3,000	3,000
- Outbreak of a Controlled Animal Disease: African Horse Sickness and Foot and Mouth Disease – Purchase of vaccine and equipment and increased laboratory tests	2,000	2,200	-
- Public private partnership contribution	35,000	-	-
- Flood damage: road construction	28,000	28,000	28,000
Sub total	734,128	299,917	317,022

Provision

Departments recorded provisions shown in table 4 below.

Table 4

Provision	R'000 2002/03	R'000 2003/04	R'000 2004/05
Vote 1: Premier, Director General and Corporate Services - Infrastructure price increases due to new technology developments and exchange rate fluctuations	6,000	8,000	10,000
- Utilisation of Information Technology in Education Delivery	5,000	6,000	7,000
Vote 8: Planning Local Government and Housing - Financial assistance to local authorities for provision of rudimentary services to alleviate hazardous conditions in areas and instances where the unlawful occupation of Western Cape Housing Development Board properties occurs	2,000	2,000	2,000
Sub total	13,000	16,000	19,000

Financial impact over the medium-term

To cater for the sum total of contingent liabilities a minimum amount will have to be set aside as first claim against any surplus revenue/financing capability to meet such liabilities. The worst case scenario is set out in table 5.

Table 5

Summary	R'000 2002/03	R'000 2003/04	R'000 2004/05
Liabilities	558,809	-	-
Commitment	181,119	53,031	53,031
Contingencies	734,128	299,917	317,022
Provisions	13,000	16,000	19,000
Total	1,487,056	368,948	389,053

Lessons learnt/challenges

Given known or expected fiscal risks, including major natural disasters and major unforeseen and unavoidable events, an amount has to be set aside for such eventualities to be used only where current budgets, even with reprioritisation, cannot absorb the impact without undesirable lasting damaging effects on essential services. It is proposed that R100 million be set aside as provision for contingent liabilities, as follows:

- R50 million in real terms over the MTEF period for unforeseeable and unavoidable expenditure; and
- R50 million in real terms over the MTEF period for the contingencies as shown in this Chapter.

This is done with the understanding that the risk is spread between the Provincial Treasury, to the above limit, and the provincial departments concerned and that the latter will need to take primary responsibility for the difference, except when the magnitude of such risk(s) impacts unreasonably on the functioning of the said department, beyond which other departments will collectively be required to provide financial support in liaison with the Provincial Top Management and the Cabinet.

If the reserve is not used it will be rolled over into the next financial year. If drawn down, any remaining balance will have to be augmented in future financial years to bring it back up to minimum level. In essence this becomes a shock absorber for external shocks to the budget.

From the legal framework referred to above it can be deduced that the legislature and regulator is sending a clear signal to the WC Government, *inter alia*, to identify and record contingent liabilities, disclose pertinent information about its exposure to risks pertaining to the contingent liabilities, give at least as much attention to contingent liabilities as to spending programs and reform its analytical, policy and institutional public finance frameworks to address all major fiscal risks.

It is clear from the above definitions that there is some difference in the approach from an accounting to that of a fiscal adjustment/budgeting perspective. These apparent inconsistencies require further engagement through debate and interrogation to be able to give clear guidelines on definitions to managers.

As indicated earlier it is required that some information with regard to contingent liabilities be captured in the annual reports of provincial departments. An assessment of the 2000/01 Annual reports that includes the financial statements, revealed that on aggregate the following items were presented:

Housing guarantees	R	56 172,560
Guarantees issued for building of schools	R	1,885
Capital commitment in respect of Health Information System project	R	97,865

Based on the magnitude and scope of operations of the WC Government and all its complexities in comparison with the listed contingent liabilities, it is questionable whether the recorded information is a fair representation of the WC Government's contingent liabilities. Further investigation, functional and effective systems and institutional arrangements are necessary to identify, record, classify, measure, evaluate, report, assess and interpret the fiscal impact of liabilities and the extent of disclosure. Provincial departments and the WC Treasury need to engage to establish institutional capacity to achieve these objectives.

Although legal requirements need to be complied with, care needs to be taken not to just comply with the letter of the law. What is often neglected or misread is the intention or spirit of the requirements and that these need to be explored and used as tools in the management of contingent liabilities.

It is fact that a weakening exchange rate of a country increases prices of imported goods. Examples of such goods that have a direct bearing on government service delivery are medical equipment, pharmaceuticals, library books, information technology, etc.

A combination of a decreased value in the Rand and the nature, volume and timing of goods purchased from foreign countries may threaten budget stability.

The following serves as an illustration:

For 2001/02 the provincial library services received R18,5 million for the purchase of library material. Available information indicates that approximately 60 % of the materials are purchased from foreign countries and in most cases at the rand/pound exchange rate.

It should be noted that the exchange rate in November 2000 against the pound was ± R11 and has weakened to R13,68 (or 24,45 %) against the pound in November 2001. In effect this decrease implies R2,75 million (60 % of R18,5 million) less library materials bought.

Facing this dilemma departments need to introduce measures to monitor the exchange rate and in relation to its budgets understand the consequences and management thereof.

Intergovernmental function shifts may also threaten future budget stability. The general trend is that transfer functions evolve from national to provincial to local government or from provincial government to local. However, with regard to library services a new phenomenon has surfaced. In this regard the Constitution of South Africa 1996 (Act no 108 of 1996), per Schedule 5A, identifies libraries (excluding national libraries) as a function area of exclusive provincial legislative competency. The implication therefore is that the Western Cape Government should take full responsibility for public library services – this includes the full financing of local public services that are currently being co-funded by the local sphere of government.

The withdrawal of the local sphere of government from the co-funding arrangement could result in additional expenditure shown in table 3 above over the MTEF period.

Clearly this would seriously threaten the stability of the budget. The challenge is to approach the situation with caution from amongst others a management, legal, political and financial perspective. With regard to the financing perspective the principle of funds follow function should apply. This will entail for example an inter-governmental agreement on an adequate and appropriate shift in resources from the local to the equitable share through the vertical split mechanism, or by some other acceptable means. The drafting of a legal opinion on the position of the Western Cape Government is in progress.

A further challenge is to subject contingent liabilities to the same level of scrutiny as direct spending programmes. This will require measures to be instituted to prevent growing under-recorded claims on the budget, expansion of contingent liabilities and the undermining of budget stability and integrity, as well as to prevent government from not meeting its obligations.

5.2 Debtors

Introduction

The recovery of outstanding debts in the Western Cape Government has deteriorated to such an extent that it has become a reason for serious concern. The statistics of outstanding debt as at 30 September 2001 in provincial departments stands at over R0,5 billion.

The financial systems currently employed by the Western Cape Government to administer debts are the Financial Management System (FMS), the Cape Hospital System (CHS) and the National Traffic Information System (NATIS). The limited capacity in the Province coupled with the inadequacies of the aforementioned systems to effectively administer debts have contributed to the current financial state of affairs. Some of the shortcomings/limitations identified are:

- Not user friendly;
- Cannot effect interest adjustments;
- No provision for age analyses of accounts;
- Follow-up processes and procedures unnecessarily long;
- No diary function for follow-up purposes; and
- No electronic filing system

Purpose

The purpose of this sub section of Chapter 5 is to:

- Inform decision-makers of the legal requirements placed upon the Provincial Treasury and accounting officers to manage debtors;
- Comply with legal requirements in letter and spirit through a process of identifying, recording, understanding, and assessing and updating the quality of information on debtors;
- Provide better information on debtors pertaining to the WC Government and by so doing further promote transparency;
- Determine the magnitude of the fiscal impact that the debtors could have on financing resources; and
- Describe previous lessons learnt and the challenges for the future management of debtors.

Legal framework

An appropriate departure point to address this section would, from a public finance management perspective, be to take cognisance of the stipulations of the PFMA, which came into effect on 1 April 2000, as well as the subsequently issued Treasury Regulations.

Section 18(1)(c) of the PFMA, places a clear responsibility on the Provincial Treasury by including in its functions and powers the imperative to promote and enforce transparency and effective management in respect of assets of provincial departments and provincial public entities.

Accounting Officers of provincial departments and trading entities do not escape this imperative. In their general responsibilities as contained in the PFMA, it is explicitly required of them, in terms of section 38(1)(c)(i) and 38(1)(d), respectively, to ensure that they have and maintain effective, efficient and transparent systems of risk management and to manage debts responsibly.

Definitions

Debtors are a part of assets, and as such are resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.

Managing debtors

In order to take the process for the effective management of provincial debtors forward, it is imperative that all types of debt within the Province be identified and addressed. An organisational development investigation was requested to determine the most viable option for the control of debtors, i.e. either a central debt bureau or a debt management system within departments. The objective is to provide departments with an option to follow up debts, especially problem cases, effectively and efficiently. The Directorate Organisational Development of the Province recommended that an appropriate debt management system be acquired for the Province through the tender process. It also recommended that a matrix model be followed, i.e. each department will be fully responsible for its debt management and the Provincial Treasury will be responsible for providing policy and guidelines on debt management to all departments.

In order to assist in addressing the debtors situation of the Province, the Provincial Treasury issued a best practice document to departments. The purpose of the document is to provide a framework of control measures to departments, for implementing an effective, efficient, transparent and consistent mechanism for the recovery and management of debtors in terms of section 38(1)(c)(i) and (d) of the PFMA. Departments further need to ensure that they have a debt policy in place while the best practice will serve as a guide to develop such a departmental debt policy. Due to the emphasis of effective and efficient debt collection referred to in the PFMA, departments were advised to ensure that the necessary control measures are put in place to comply with the PFMA.

The Provincial Treasury will in future monitor the progress made by departments with regard to reducing the outstanding debtors and report quarterly to the Provincial Treasury Committee on the progress made.

Statement of debtors

Table 6 below reflects the outstanding debtors per department as at 30 September 2001.

Table 6

Department	1 March 2001	September 2001	Variance %
Community Safety	36,672	30,219	-17,60
Education	49,244,346	47,376,283	-3,79
Health	112,925,998	90,920,687	-19,49
Social Services	*13,573,056*	10,846,396	*-20.09*
Finance	1,721,147	1,426,686	-17,11
PAWC	52,746	34,956	-33,73
Environment and Culture	82,478	53,244	-35,44
Economic, Agriculture and Tourism	330,556,315	341,156,176	+3,21
Planning and Housing	22,800,998	# 22,800,998	#
Total	**530,993,756**	**514,645,645**	**-3,08**

Updated figures not available

Challenges

The challenge lies in developing systems and processes that meet the objective of effective and efficient management of debtors. Cognisance is taken of the National Treasury's initiative to develop a debt sub-system on the Financial Management System which is user friendly, able to effect interest adjustments and provide age analysis. To this end, representations will be made to National Treasury to enhance the system further to include debt follow-up procedures, viz. generate letters of demand, diary functions and electronic filing systems.

6

POLICY IMPERATIVES

National imperatives that play a role in the fiscal policy of the Western Cape

The President's opening address to Parliament on 9 February 2001

In his opening address to the Parliament on 9 February 2001[1], the President *inter alia* referred to four main issues that the people of South Africa as a Country need to address for the immediate future. These issues can be summarised as follows:

- The low economic growth rates and aggregate savings that are still too low. To summarise, the levels of poverty, unemployment and under-development in some parts of the Country are still too high;
- The necessity to move the economy to a higher rate of growth, increasing competitiveness and efficiency, which in turn could raise the level of employment and reduce poverty and persistent inequalities. However, to improve competitiveness, input costs should be lowered throughout the economy;
- Government as a whole, in all its spheres, together with the entire public sector, must make decisive and integrated contributions towards meeting the economic challenges the country faces; and
- The central aim of the country is to conduct a sustained campaign against rural and urban poverty and under-development, bringing in the resources of all three spheres of government in a co–ordinated manner.

The broad strategic issues are critical factors that should receive attention in the short to medium term if improvement is intended for the longer term. An extract of the Budget Council Lekgotla decisions for 2001 in the next paragraph reflect a further attempt by the Minister of Finance and his Provincial counterparts to set benchmarks against which the government should improve in future.

Public Finance Community decisions

The Budget Council Lekgotla can rightfully be seen as the starting point of each future budget cycle whereby the Pubic Finance Community sets the pace, not only for provincial treasuries, but also for their provincial governments over the medium term to improve on fiscal policy. For the purposes of this document an extract of the decisions are listed below.

The challenges facing the National and provincial treasuries in the Country are enormous, and if the challenges can be met, it should ensure fiscal austerity that will ultimately benefit the people of South Africa:

- The need to deepen budget reforms and strengthen links between policy and budgets requires development of non-financial and service delivery indicators and activity-based costing;
- It can be accepted that social services delivery had improved, but that the quality and effectiveness of services remain a priority. Against this background, the Budget Council agreed that the focus on improving delivery of social services should continue to feature prominently on the budget agenda;
- The complexities of and need for a framework to guide the decentralisation of health services to local government is important;
- Cognisance was taken of ongoing pressure for real growth in welfare budgets because of the phasing in of the child support grant, the growth in the number of other grants and the need to maintain the real value of grants;
- It was agreed that there is a need for a retrenchment tool for personnel, which will enable reduction of excess staff and attainment of an appropriate skills mix;
- It was agreed that mechanisms and incentives to attract and retain management and professional skills should be explored to speed up and improve service delivery quality;
- The critical shortage of housing, especially in rural areas, and the weak involvement of the private sector in the provision of housing in general was noted;
- It was noted that fiscal consolidation since 1996 made a more expansionary budget possible over the next three years, but prudent financial and fiscal management remain key to sustainable macroeconomic management in the long term;
- It was agreed that poverty-related programmes should be reinforced in the fiscal policy:
  - Recognising that social grant programmes should effectively reach the poor;
  - Re-assess specific poverty-alleviation projects which are not sustainable; and
  - Low wage employment has the potential of raising the income for the poor while contributing to self-esteem.
- It was noted that alternative fiscal scenarios are not likely to produce the results desired by Government because of capacity constraints and poor quality of spending that hamper Government from achieving its objectives (such as infrastructure allocations and the capacity to spend the funds);
- It was agreed that a lack of capacity in government is a serious concern that must be addressed in the fiscal policy. The challenge is how government improves both the capacity to spend and the quality of spending;
- The changed budget process environment under which treasuries operate were noted, given the success of stabilised budgets. The politics of relative abundance present

treasuries with a different set of challenges, and will require that they earn the right to leadership over budget and spending decisions;

- The following aspect in the budget process were identified as key steps to be taken in the short- to medium-term:
  - Deepening of co-ordination between policy and budgeting, and improving relationships with line-function departments;
  - Effective communication of the important role played by joint MINMECs in facilitating better alignment between policy and budgets; and
  - Provincial visits by the national Minister and Deputy Minister of Finance with a view to sharing ideas with executive members in provinces on progress with implementation of current reforms and championing implementation of new reforms.
- It was agreed that there was a need to build the capacity of all treasuries, including the employment of more skilled staff;
- It was agreed that there might be a need to develop a set of benchmarks to be used in assessing the performance of provincial treasuries in its capacity;
- It was agreed that National Treasury will prepare a position paper, to be submitted to the Budget Council, which identifies what the key systems requirements are and to prepare proposals for a way forward;
- It was agreed that given the need for integrity of the budget process, MECs of Finance must have oversight over all revenue-raising activities in the province, in line with the approach of the Constitution with regard to money bills; and
- The nurturing role of provincial treasuries in implementing budget and financial management reforms at local government level was noted.

Challenges facing provincial treasuries

The public finance community generally accepts that provincial treasuries lack the capacity to attract qualified financial personnel[2]. Provincial treasuries often also do not have sufficient capacity to assess the non-financial information in budgets and budget-related documents. The conclusion can be made that by losing key personnel in provincial treasuries a dangerous vacuum could be created. It is also accepted that the implicit assumption that all treasuries are at the same level of capacity either fails to deal with their lack of capacity or punishes those that perform well, and it was also accepted that this approach had to be reviewed.

The list of decisions in the previous paragraph provides a clear picture of the challenges facing the Western Cape Treasury. With regard to human resource development, the relevant section in Chapter 4 spells out the strategy the Provincial Treasury envisages in the medium-term. Another serious consideration the National Treasury could take note of, is that skills in South Africa is not generally on a par with the level of skills in developed countries.

The following example may illustrate the point raised in the previous paragraph. Huge efforts have been made and are currently being investigated to implement new computerised systems for the government as a whole, but many departments and provinces are not yet capable of capturing basic information on their existing systems. This often leads to a situation that the brunt of the blame is placed on the current systems and not on the lack of skills, of the officials working with the systems. It would appear that the National Treasury has overlooked the issue of investigating how the implementation of new systems will solve the problem of having incomplete or poor data.

Budget Forum Intergovernmental Fiscal Principles

During the Budget Forum of 21 September 2001 it was also agreed that seven high-level principles were introduced to protect the coherence of the intergovernmental system and that policy, practice and legislation remain consistent with these principles. It was accepted that all three spheres of governments have to take full responsibility for their actions, or the omission lack thereof. Although by and large autonomous, the three spheres are nevertheless interdependent and should have the necessary mutual respect for each other, both in theory and in practice.

Briefly the seven principles to be adhered to between the three spheres of government[3] are:
- Autonomy and accountability;
- Good governance;
- Redistribution and fiscal equalisation;
- Increased access to services;
- Revenue sharing and fiscal capacity;
- Vertical Division; and
- Fiscal efficiency.

The Western Cape Treasury and its role in relation to National Treasury

The Western Cape Government since 1998 has made some advances with the compilation of fiscal policy and setting of strategic goals for the Province to which budgeting could be aligned. These policy initiatives were always formulated to be in congruence with the National Treasury's fiscal policy.

The four years prior to 1998 were just as important, as it laid the foundations on which the Province built its fiscal policy progress. During this earlier period expenditure within departments was brought under control and fiscal propriety was vested within the Province, while massive restructuring took place in an effort through which approximately 20 000 officials were voluntarily retrenched. This in itself created capacity gaps that have placed a burden on service delivery which will take time to recover from.

Although the process that evolved is to be perceived as positive, many challenges still lie ahead. One of the greatest is to attain workable, comparable and measurable objectives for departmental strategic plans with adequate feedback to be given in the annual departmental reports tabled after the closing of a financial year.
In the second section of this Chapter the views of the Provincial Parliament, the Public, outside institutions and the National Treasury will be reflected to provide some ideas on how fiscal policy and planning can be improved on in future.

Achievements of fiscal policy to date and the way forward

Western Cape Government Strategic Objectives (WCGSO's)

The Provincial Cabinet compiled ten strategic objectives (WCGSO's), listed below, and departments endeavoured to align their own departmental measurable objectives to attain these ultimate goals or outcomes. A great deal of effort went into the compilation of the ten chapters of the WCFP 2001 – 2004 to demonstrate these endeavours:

- Contribute to the creation of a safer environment for our people;
- Create an enabling environment for economic growth;
- Prepare the people of the Western Cape for the knowledge economy of the 21st century;
- Contain the spread of HIV/AIDS and tuberculosis;
- Empower the poor people of our Province through the provision of basic services;
- Improve the quality and accessibility of services provided by the Provincial Government;
- Protect, enhance and promote the total environment for the optimal development of our people;
- Maintain and improve the physical infrastructure required for the development of this Province;
- Bind the Province, as the Gateway to Africa, ever stronger to the country and the continent; and
- Promote rural development.

The five priorities of the Premier's Speech

In his opening address to the Provincial Parliament on 6 February 2001 the Premier identified five priorities that are imperative to the Western Cape:

- Improving the security situation in the Province;

- Promote economic growth;
- Fight HIV/AIDS;
- Rural development; and
- Drive a clean-up campaign in the Province.

Priorities two to four are directly in line with national fiscal policy and were already alluded to in the President's address and the subsequent Lekgotla decisions, while the reduction of crime is a priority issue that counteracts vulnerability which is correlated to poverty. It must be noted that special allocations have been made to promote the clean-up campaign.

Some critique

The main theme of provincial spending is that additional allocations within provincial governments for the coming MTEF period should be directed towards the acceleration of service delivery and improving the quality of public services in line with the overall government priorities of reducing poverty, inequality and vulnerability. The question then arises whether Provincial department's planning intentions have as yet been fully aligned with the more detailed strategic objectives of the Provincial Cabinet.

The comments received from Idasa[4] on the WCFP 2001 – 2004 is an important point of departure that should be taken into account when attempting to answer some of the issues. In summary, Idasa's critique was:

- Budgetary issues received more attention than managerial reform issues;
- In South Africa, in general, it can be accepted that policy does not drive resource allocations, mainly because proper policy on how to achieve priority objectives are not available and objectives are not prioritised;
- Both at the National and the Western Cape Provincial level of Government no linkages exist between economic growth and the reduction of poverty; and
- It would appear that high level objectives or outcomes are formulated without determining the steps or planning properly how the higher level priorities/objectives or outcomes should be reached.

Process how comments were invited on fiscal policy

With the compilation of the Western Cape Revenue and Expenditure Policy Framework 2000/01 – 2002/03 (first attempt) and the WCFP 2001 – 2004 (second attempt), provincial departments were provided the opportunity to participate in establishing this document. Invitations were sent by the Provincial Minister of Finance to the private sector, organised labour and metropolitan local government requesting their response. In addition advertisements were placed in the major local newspaper calling for public participation.

In preparation for the compilation of the WCFP 2002 – 2005 a similar process had been followed. During the last week of September 2001 advertisements were placed in local newspapers and during the first week of October 2001 comments were invited per letter from the Speaker of the Western Cape Provincial Parliament, selected role-players in the business sector, organised labour and metropolitan and local government. In addition specific information and inputs were requested from departments, which were further followed up by critical sessions with them in order to obtain a comprehensive picture of individual and aggregated departmental direction special needs and contingent liabilities. All inputs and comments received were assessed and the key issues considered for inclusion in this document. It should, however, be noted that the latest round of inputs was requested on the WCFP 2001 – 2004, which was published during 2000 and which now forms the basis for the WCFP 2002 – 2005. The latter was compiled during the first three weeks of November 2001.

The reduction of poverty, vulnerability and inequality

Origins of poverty in South Africa

Research in South Africa has shown that access to employment is the single most crucial requirement for reducing poverty and inequality. Despite the continued existence of low wage rates in certain sectors of the national economy, low wages are today less pervasive and contribute far less to poverty than in the past. Access to employment and the earnings of the employed are usually linked to education. For this reason, the distribution of education, and its quality, are crucial in determining who has access to well-remunerated jobs. In those districts and amongst those groups with the greatest educational backlogs, poverty is most prevalent.

Thus the crucial factor in improving poverty and inequality lies in accelerated job creation. These conclusions probably apply equally to the Western Cape (although no separate research has yet been done to show this at the provincial level), with the further complicating factor that if jobs were to be created in the Western Cape but not in the rest of South Africa, the positive effect on Western Cape poverty and distribution would probably be undone by migration of unemployed people from other Provinces. National growth therefore remains imperative.

Poverty and vulnerability

According to Woolard and Leibrandt[5] poverty and vulnerability are not synonymous but the two concepts are related. Some groups of people may be at risk of becoming poor (inherent vulnerability) because of class discrimination ethnicity or gender. Although some combinations of vulnerability will strongly correlate with poverty, such as households living without parents, or families living in deep rural areas it can still not be deduced that all the members of a vulnerable group of people will necessarily be poor. The important distinction to be made between the two concepts is that poverty is related to deprivation, while vulnerability should be seen as a function of external risks, shocks and stresses. Key results published by (Bhorat et al, 2001) indicates that farm workers and domestic workers are the two most vulnerable groups in the labour market. The predominance of Coloured and African race groups and of women among the most vulnerable is still very prominent.

A distinction should also be made between long- and short-term poverty. While the former could be ascribed to intergenerational and long-term persistent poverty, the latter could be the result of the loss of a job or financial misfortune in a family. It should be noted that poverty surveys generally do not differentiate between the two. The lack or better utilisation of data to investigate poverty and vulnerability in future should be a higher priority that the Western Cape Government cannot ignore.

Causal factors for income disparity in the Western Cape

Although the Western Cape's per capita income is substantially higher than the national average, the Gini coefficient of income inequality of 0,58 is slightly lower than the national average of 0,65, but nevertheless very high and indicative of great income inequality within the province. (The Gini coefficient, a measure of inequality, ranges from 0 for complete equality, to 1 for complete inequality. Rates above 0,5 are usually internationally perceived to be excessive.)

Despite continued inequalities and pervasive poverty, strong community networks and a broad base of smaller entrepreneurs have enabled the province to spread the benefits of economic development more widely than most other provinces.

Policy imperatives that determine poverty in the Western Cape

Health conditions

Life expectancy is a measure both indicative of access to health services and sensitive to nutritional status, violence in society, personal income, education, services such as sanitation, housing conditions and the environment. It thus provides a fuller measure of economic and social well-being than income poverty measures. The infant mortality rate also reflects poor living conditions, because it partly depends on the adequacy of prenatal and neonatal care and the ability of health staff to attend births.

AIDS is estimated to have had a lesser impact in the Western Cape than in most other provinces, partly due to its geographic position further from South Africa's northern neighbours, and perhaps also because higher education levels amongst the province's population have assisted AIDS education.

Education

According to the 1996 census, almost 96 % of children aged 6 - 15 were enrolled in education. The adult literacy rate of 90 % in 1996 (those 20 years or older who had completed four years education) was well above the national average of 67 %. The 1999 matriculation pass rate of 79 % was 30 percentage points above the national average, and the 24.4 % of matriculants who obtained university exemptions was double the national rate. Not surprisingly, then, an above average proportion of the Western Cape labour force is matriculated, but there is still far too large a part of the labour force with very low educational levels in 1996 more than 40 % had no secondary education (compared to almost 49 % nationally). However, if the Western Cape's literacy levels are compared to seventeen countries in Africa where comparable statistics are available, eleven countries' literacy levels exceeds that of the Province.

Urbanisation and Migration

The Western Cape has a very high degree of functional urbanisation (89 % as opposed to the national average of 54 %, according to the census), yet agriculture continues to play an important role in the provincial economy. Agriculture is also an important source of employment in the rural areas, one of the reasons for the relatively low rate of rural unemployment. Influx of migrants from other provinces that augmented much lower natural population growth, especially to the Cape Metropolitan Area where the bulk of the provincial labour force is located, has stimulated rapid expansion of the labour force of an estimated growth rate of 3,8 % per annum during 1980-95.

Regional Inequalities

Regional inequalities in the Western Cape are considerable, with 12,1 % of individuals in the Karoo experiencing ultra poverty compared to the provincial average of 4,4 %, based on 1995 data. The other easternmost region, the Southern Cape, has a lower relative poverty rate among individuals (30 %); these figures are nevertheless considerably higher than the national average of 18,7 % and the Cape Metropolitan Area rate of 8 %. However, despite lower poverty rates, the more populous Winelands, Southern Cape and CMA regions have a higher proportion of the province's poor individuals than the sparsely populated Karoo and Overberg regions.

With regard to magisterial districts in the Province, poverty is largely concentrated in the rural districts in the eastern and north-western peripheral areas such as the cluster consisting of Calitzdorp, Ladismith, Laingsburg, Uniondale, Prince Albert and Beaufort West.

Using the alternative estimate of poverty of Alderman et al., household poverty levels fluctuate between 21 % in both the Central Karoo and Breede River District councils and 20 % in the Klein Karoo District Council Area, to only 9 % in the Cape Metropolitan Area, where most of the population is concentrated. In terms of magisterial districts, poverty rates of above one-quarter of households are recorded for Murraysburg (32 %), Uniondale (31%, Prince Albert (28 %), Calitzdorp (28 %), Laingsburg (26 %) and Ladismith (26 %), whilst Bellville (4 %), Cape (4 %), Wynberg (5 %), Simon's Town (6 %) and Somerset West (7 %) fare the best.

Racial and Intra-Regional Inequalities

Partly due to their large share of the provincial population, coloureds make up the vast majority (71 %) of the poor compared with the 28 % share of blacks and negligible shares of Whites and Indians. However, blacks account for almost half of those in extreme (ultra-)

poverty in the Province. Thus, although coloureds form the majority of the Western Cape's poor, blacks are even poorer. As elsewhere in South Africa, females and children bear the brunt of poverty in the Western Cape.

Gender Inequalities

Women, like children and old people, are vulnerable to poverty and social inequalities. Although gender inequalities are less in the Western Cape than elsewhere in South Africa, they are still large in some respects. The proportion of individuals in female-headed households, at 26 % in 1996, was less than in any other provinces and far lower than the national average of 39 %. Also, female-headed households, who are usually disproportionately poor, were in the Western Cape not much worse off in terms of service provision (water, electricity, sanitation and, to a lesser extent, telephones) than other households, in stark contrast to the national situation.

Lack of Demographic data for the Province

Economic and demographic data in South Africa are in many cases not available at a regional or provincial level. Unlike national accounts data, which appear quarterly, alternative data sources that allow for provincial level analysis only become available as part of bigger surveys that appear less regularly. For example, the combined October Household Surveys/Income and Expenditure Survey of 1995 is the latest available source of data on income distribution across and within provinces. (October Household Surveys were also done for all years since, with the 1998 one the latest released thus far, but these surveys do not contain income and expenditure data and are therefore of limited value for analysis of income distribution.)

Concluding remarks *

According to Van den Berg[5] substantial shifts in government policies towards poverty alleviation have been made over the past years which leave the scope for a further outlay of resources very limited. However, three areas for increased government attention to reduce poverty over the medium to long term are suggested:

- Improving the quality of education, through better information systems and improvement of the cognitive levels of education;
- Expanding public works programmes to cater for low-wage projects to alleviate unemployment; and
- Government intervention to ensure enhanced access to capital by the poor, by means of entrepreneurial efforts that educate this portion of the population.

The three above policy areas will not attain the achieved results in isolation, but should be part of sustained economic growth and the GEAR strategy that could ameliorate the poverty policies.

*** FOOTNOTE**

As a last comment, although the policy imperatives discussed in this chapter are the result of extensive inter-governmental processes, it might be that a new Executive for the Province would wish the policy framework to be revisited: See Addendum.

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[1] State of the Nation Address of the President of SA, Thabo Mbeki, At the National assembly Chamber, Cape Town, 9 February 2001.

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[3] Budget Forum Memorandum: Intergovernmental Fiscal Principles, 21 September 2001.

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NEW STRATEGIC FRAMEWORK FOR POLICY FORMULATION BY THE WESTERN CAPE GOVERNMENT AS FROM 5 DECEMBER 2001

1. To establish the Western Cape Government as caring and representative, providing quality, equitable and accessible services to all its people.

2. To orientate Government towards the poor by ensuring basic services, an indigent policy, a safety net and a caring budget.

3. To fight HIV/AIDS and other diseases in a co-ordinated and comprehensive manner which includes the provision of anti-retroviral drugs, lifestyle intervention and sustained action against poverty.

4. To deracialise and integrate all state financed institutions in a responsible manner to maintain stability and good order.

5. To develop the capacity of local government to ensure the rapid and comprehensive implementation of Integrated Development Programmes (IDP) and free basic services.

6. To stimulate economic growth – both in the traditional and emerging sectors – with appropriate infrastructural development, and to the benefit of all through, amongst others, procurement reform.

7. To focus on agriculture and tourism towards rural development so that all inhabitants can live harmoniously and in safety.

8. To promote policies which will maintain a healthy balance between protecting the environment and developing the economy.

9. To contain and eradicate crime through good intergovernmental co-operation so that the Western Cape can be a safe and secure home, especially for its women and children.

10. To nurture our diversity and promote our various cultures, religions and languages to become the source of our unity and strength.

7

PROPOSALS ON THE FUTURE BUDGET ALLOCATIONS OVER THE MTEF PERIOD 2002 – 2005

Fiscal Framework

As alluded to in earlier chapters, the overall available fiscal envelope is dependent on a large number of factors, mostly beyond the control of provincial governments. The overall amount that general government has at its disposal for expenditure depends, firstly, on the country's economic performance in a world environment that has become increasingly competitive, not only in the usual first/third-world dichotomy, but also between developing countries. In the latter category there are those which have distinguished themselves as resilient, fast-growing and adaptable economies and those who have been less successful. South Africa probably finds itself somewhere between these two poles and needs to answer the question of why it cannot do better and what it has to do not only to raise itself from a middle-income country category[1] towards higher per capita levels, but also to a substantially less inequitable society.

Seen from a national perspective, most of these vexing issues have been rightly picked up in the National Treasury's Medium Term Budget Policy Statement as recently tabled in Parliament by the National Minister of Finance. However, from a provincial perspective there remains much to do, not only in formulating appropriate policies and strategies, but also in understanding the problem and ensuring that policies and strategies are translated into effective spending by departments. In addition, it should be realised that no single sphere of government can hope to effect remedial steps on its own, but has to do so in close co-operation with its partners in the other two spheres. Given the limitations on resources such an approach is not only advisable, but also essential if the current persistent levels of relative and absolute levels of poverty are going to be reduced.

As argued previously, key to any long-term solution, both for economic growth and for any significant improvement in equity (via improved access to the labour market and greater economic opportunities) to be realised, is greater efficiency of the education system. What has to be achieved is well-known to the education authorities, so these aspects will not be expanded on in this chapter. However, from a fiscal perspective, the degree of drop-outs from especially the secondary school system, translates into holding the allocation to education basically constant in real terms at least over this medium term framework, after controlling for virements and other dynamics. Beyond this period, a combination of assessing efficacy of spending and demographics should determine future spending levels.

Allied to equity considerations in a regional government context is access to proper health care. For reasons of national equity in tertiary health care, although the assumptions underlying this rationale could be questioned, national government has decided that the teaching hospital grants[2] to Gauteng and Western Cape be decreased and the resultant balances shifted to other Provinces, who on the information provided, were funding tertiary services from their equitable shares, a patently inequitable situation. Unfortunately, shifting funds does not necessarily equate to a shifting of health services to similar degree, which in itself could lead to a drop in country-wide tertiary services. However, time and strenuous efforts by the recipient provinces will tell to what extent an improvement in tertiary services were indeed realised.

A further factor is that the greater majority of poor people living in the Cape Metropolitan region are very much dependent on the services of the three teaching hospitals. Another is the not so easily replaceable accumulated human capital in these facilities, something that South Africa can ill afford to do without, apart from its impact on sustainable economic growth. Given these arguments, brief as they are, it also follows that over the next medium term framework, the reductions in the conditional grants have to be covered from the equitable share.

In a more general sense, seen against a rather less than encouraging health environment, together with the former argument, it strongly suggests that health services should be kept constant in real terms. However, judging from audit reports over the last few years, it would appear that further strengthening of financial management and administration would be necessary to improve better utilisation of resources and support of direct health functionaries. This would add extra impetus to the national initiative to improve hospital management, particularly of the larger institutions. Doing so does not detract from the necessity for further restructuring to improve the overall functioning of the health system over the long term but also to timeously and judiciously position the health system for further shifts in health (tertiary) funding away from this Province. Associated with health spending are preventative and curative measures required to curtail the spread of HIV/AIDS, to be funded not only from the national conditional grant, but also from a contribution of the provincial equitable share. As it is not only Health, although it might be the principal agent, that is responsible for HIV/AIDS preventative actions, but also Education and Social Services as the two other main agents, such facts need to be suitably apportioned between these three.

Although spending on physical infrastructure (roads and buildings) in the Western Cape, in South African terms, have not been bad, in absolute terms the story is somewhat different. The necessity and economic arguments need not be regurgitated, although better priority determination might be required to take into account more than purely technical arguments, so as to give effect to spending on those portions of the road network or provincial buildings which will yield the greatest returns. With the adoption of a less conservative or precautionary stance by the Provincial Treasury, made possible through better and steadily improving fiscal management by all departments, a lower level of fiscal liquidity should possibly suffice for the foreseeable future. That would make it possible to inject an initial lump sum of funds into physical infrastructure, spread over the next three years and should ameliorate the current backlogs to a significant extent. This is to be augmented by national conditional grants (Provincial Infrastructure and Hospital Rehabilitation).

However, this would probably not be sufficient to make a real dent in physical infrastructure spending requirements over the long term. At minimum, current spending would have been kept constant in real terms so as not to exacerbate the situation. Optimally, spending on physical infrastructure should be sustainably increased in real terms over the long term. That, in turn, would depend on the Provincial Government's revenue flows, and as the amounts that are required are substantive, they are not going to be obtained from reprioritisation from current allocations to other functions. Accordingly, it is proposed that a significant proportion of new revenue flows mainly from the Provincial Infrastructure Grant be additionally apportioned for this purpose, to stretch available rands further and to also shift some responsibility to user departments', needs to make provision for day-to-day maintenance on the budgets of those with substantive regional and field service facilities. This approach has led to significant benefits in the health arena, and latterly also in Education, preventing an unnecessary deterioration of buildings and so achieving better preservation of the building capital stock and relative savings on major maintenance interventions.

From a welfare perspective, changes in the social security grant system with the phasing out of the child maintenance system, in spite of its perverse incentives and country-wide unaffordability, have led to a significant fall in the income levels of poor households, perhaps as much as 20%. The subsequent child support grant will partially compensate for this, depending on its take-up and spread. As reported earlier, the Province has seen a very rapid take-up over the last year, easily surpassing previous estimated targets with a new upper limit estimated at roundabout twice that of the previous limit. That in itself, apart from the laudable aim to relieve poverty, will make substantial claims on the Provincial Exchequer and thus on the equitable share.

Additionally, initiatives are underway to raise the current upper age barrier for child support grant eligibility and on the more extreme side of the welfare scale, to examine seriously the introduction of a basic income grant.

Also adding to the improvement of living conditions and general well-being of lower income people, is the necessity to provide housing of an acceptable standard. Even though the national conditional grant for housing has been increased, limited augmentation of the latter might still be required from the provincial equitable share to eliminate increasing backlogs and to steadily reduce current arrears over a period of 15 years, especially in the metropolitan area.

To increase South Africa's position in the primary product and semi-processed goods market, and additionally in attempting to improve employment and poverty in the more rural areas, real increases to agriculture might prove beneficial through fostering of greater research into appropriate cultivars, quality and disease-free certification and small farmer settlement, amongst other possibilities.

Although Safety and Security remain one of the high priorities of the Provincial and National Governments, a period of consolidation of one year might be required, given large percentage increase awarded to this nascent function over the last two financial years, but aiming for further increases from the 2003/2004 financial year onwards to further strengthen road traffic law enforcement capabilities, to cite one target area.

In the interests of good governance and to enhance the integrity of fiscal performance, provision will continue to be made to ensure that creditors in arrears be paid within a acceptable repayment framework that treats all participants equally and fairly. The Provincial Treasury will make the necessary provision for this eventuality, which should reach conclusion in the 2002/2003 financial year, with the finalisation of the 15/50/70 book clearing project to be conducted under its auspices.

Beyond this, an analysis of all other contingent liabilities indicates that risks in meeting these should be shared between the Treasury and the departments concerned. To achieve this, the Provincial Treasury will only meet unforeseen and unavoidable expenditure up to the same current limit, escalated over the medium term to remain constant in real terms. Secondly, for all other risks, if they indeed materialise, the Treasury will only accept liability up to the maximum of the amount set aside for this purpose or can be made available from such an amount, given other considerations, with the relevant department making up the balance of the shortfall in liaison with the Treasury.

For the remaining departments, apart from those already increasing in real terms due to earlier prioritisation provisions and possible amounts to also improve financial management and capacity building/training, it is proposed that they also be held constant in real spending terms, after controlling for virements, shifts, one-off expenditures and incorporating the latest amendments in improvement of service conditions. The latter will also apply to the other departments/functions already discussed. The rationale behind this, as was also argued in last year's fiscal policy framework, that departments by and large have gone through a transformation process that does not require their entertaining of any real reductions. As was also emphasised last year, the focus needs to fall on service delivery and consolidating previous initiatives. These will only be attainable if proper strategic planning under conditions of relative fiscal stability pertain.

Furthermore, it is recognised that there is room for improvement in future for accounting officers, assisted by their chief financial officers, to be more participative in the fiscal policy formulation process.

It is recognised that due to various internal and external factors and practicalities members of the provincial top management are not always individually involved in all the discussions in the various forums which have an influence on fiscal adjustment.

Sequential Priority Framework in summary

- Keep departments basically constant in real spending terms, after adjusting for inflation, virements, function shifts, once-off expenditures, earlier prioritisation decisions and the latest improvement of conditions of service agreement, and accommodating the fall in the National Tertiary Services and Professional Training and Development grants.
- Provide for the increased beneficiaries of the Child Support grant, its raised limits, as well as those of other social security grants.
- A limited provision under the auspices of the Provincial Treasury for contingent liabilities:
  - R50 million in real terms over the MTEF for unforeseeable and unavoidable circumstances; and

- To a maximum of R50 million in real terms for all other contingencies as referred to in Chapter 5, bringing the gross provision to just under 1% of the gross budget, similar to that of the National Treasury in the first year of the MTEF, spreading such risks between Treasury and the Department concerned.

- Provide for actual creditors in arrears, mainly focussed on intergovernmental claims as part of the 15/50/70 project.
- Extending the provision for ring-fenced financial management improvement (quality of spending) at departments where it is already in force and augmenting the current provision at Health.
- Provide for the following national conditional grants not already included in the constant real growth baseline amounts:
  - Provincial Infrastructure grant;
  - Hospital Rehabilitation grant;
  - HIV/AIDS grants for Health, Education and Social Services;
  - Poverty and Infrastructure Development;
  - SA Housing Fund; and
  - Human settlement.
- From cash financing and a concomitant reduction in cash liquidity provide lump-sum financing, spread over three years, for physical infrastructure (buildings and roads, including Convenco) on the assumption that the accounting officer of Vote 10 will do his own internal prioritisation between these two functions and in collaboration with all client departments within the overall framework as agreed to with other departments, the Director-General and Provincial Top Management.
- From the 2001/2002 reserves, smooth/cushion the effect of the rapidly escalating effect of the child support grant over the MTEF period.
- From the net amounts available for distribution for **recurrent** expenditure, provide for:
  - Day-to-day maintenance at selected departments with district and field offices/ facilities within a framework as determined by the Works Branch;
  - Incremental additions to agriculture for the reasons as described previously;
  - HIV/AIDS, in addition to the conditional grant amounts;
  - Community Safety, but only from the 2003/04 financial year; and
  - IT, primarily to take account of the HIS system suitably attenuated to take account of Health's real needs and fiscal prudence.

- Other specific special needs on the margin as determined by the Provincial Top Management, using the following suggested criteria:
  - Economic growth contribution/poverty reduction;
  - Rural development;
  - Safety and security;
  - Promotion of better management information;
  - Promotion of investment; and
  - Promotion of school sport.

Note:
The promotion of Tourism and Agriculture in the Province, as major creators of employment in the Province. Expenditure on infrastructure (Convenco) and agriculture reflects this priority.

REFERENCES

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