WESTERN CAPE FISCAL POLICY

2003 – 2006

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EXECUTIVE SUMMARY

The Western Cape Fiscal Policy 2002-2006 is presented in terms of section 18(d) of the Public Finance Management Act, 1999 (Act 1 of 1999). The legislative requirement has been duly taken into account to ensure that this policy document does not materially or unreasonably prejudice national economic policy.

The provincial Treasury has a responsibility with regard to the policy-making process and making recommendations on policy issues and ultimately is the role of the Western Cape government to ultimately determine the policy direction.

The presentation of this policy document, which is supported by inputs from provincial departments and advisors, gives substance to the provincial Treasury's endeavours and objectives, to evolve provincial fiscal policy over time and to continue improving its sophistication and application.

The approach was adopted to make senior Treasury members responsible for the various chapters. The main reason for this was to build capacity in the provincial Treasury. Each author had to undertake the necessary research and analysis to come to conclusions. These members were also accorded the opportunity to interact with heads of departments (accounting officers) at a special one-day provincial top management session to debate facts, views, concerns, etc. Various advisors were also approached to make selected inputs, mainly on issues such as poverty and inequality, migration, crime, gender, household inequality and education.

The provincial Minister of Finance is due to table the Treasury's Fiscal Policy 2003 - 2006 and the associated Expenditure Review 2002 in the Western Cape Parliament on 26 November 2002. Thereafter it will be referred to an ad hoc Provincial Parliamentary Budget Committee, which will present to the Minister a report on its findings. With a view to enhancing transparency, public participation, inclusive of external expertise may be invited.

This Policy document is designed to provide certainty about the Western Cape government's fiscal direction and to create an opportunity for debate about the choices government faces to improve the lives of all communities, but particularly the poor. In broad terms the document sets out relevant financial management issues and spending proposals that will underpin Budget 2003 as well as short- and medium-term fiscal objectives.

The document explores:

- The socio-economic situation in the Province;
- Local government issues with regard to the effect the Municipal Finance Management Bill will have on provincial government departments, the shifting of functions between the local and provincial spheres of government, and integrated development planning;
- Financial management issues in relation to accountability, accounting, chief financial officers, capacity building, financial systems, cash management, contingent liabilities, departmentalisation and supply chain management;
- The fiscal envelope available for spending and reserves over the medium term.

An Expenditure Review 2002 was also undertaken, the outcome of which informs this policy document, but for practical purposes it is published separately. It gives an overview of actual spending from 1997/98 to 2001/02.

The following summary seeks to capture the main issues that are dealt with in the body of this policy document:

Socio-economic analysis (Chapter 2)

1. With regard to determining the gap between the socio-economic needs and key service delivery indicators:

   The provincial Treasury:
   - Reiterates its intention to determine and evaluate socio-economic variables and their imperatives;
   - Re-emphasises the necessity of developing of key service delivery outcome indicators for departments;
   - Is of the view that good governance through synergy – intra-provincial and with other spheres of government – has to be ensured;
   - Proposes that economic growth should be stimulated within a realistic and sustainable framework;
   - Advises that tough decisions should be taken now to create a better future.

Local government (Chapter 3)

2. With regard to the effect of the Municipal Finance Management Bill:

   The provincial Treasury:
   - Advises that the possibility of an unfunded mandate being imposed on the Province needs to be prevented;
   - Explains the preliminary division of responsibilities between the different role players.

3. With regard to function shifts between the local and provincial spheres of government: -

   The provincial Treasury:

   - Is of the view that the compilation of the position paper *Western Cape perspective on the transfer of functions and powers between the provincial and local government* and the subsequent implementation framework requires the active support of all the relevant role players.

4. With regard to integrated development planning:

   The provincial Treasury:

   - Is of the view that, although there is some participation in the formulation and implementation of integrated development plans, participation at managerial level and mechanisms to elicit greater synergy need boosting to make it a more meaningful process.

Financial management issues (Chapter 4)

5. With regard to accountability:

   The provincial Treasury:

   - Is of the view that all relevant functionaries need to meet the challenge of fully comprehending the importance of their particular role in ensuring substantive compliance with norms and standards.

6. With regard to chief financial officer (CFO) responsibilities and structures:

   The provincial Treasury:

   - Is of the view that, with the support of accounting officers, CFOs need to become the champions of higher standards of financial management;
   - Proposes that CFOs need to report directly to the accounting officer;
   - Proposes that CFO support structures should be appropriate and should be standardised as set out in the models expanded on in this policy document.

7. With regard to capacity building:

   The provincial Treasury:

   - Is of the view that, within departments, capacity building in the financial management context is a primary responsibility of an accounting officer;
   - Is of the view that a culture of life-long learning needs to be created, i.e. that the Western Cape Provincial Administration should be a learning organisation;

- Proposes that the training capacity in the provincial Treasury should be strengthened over the medium-term with a view to benefiting provincial departments.
- Proposes that a financial management training policy should be developed over the short term;
- Proposes that the provincial Treasury should register as an accredited learning and assessment centre;
- Proposes that the provincial Treasury should establish research and development capacity.

8. With regard to financial systems:

   The provincial Treasury:
   - Is of the view that the effective utilisation of the financial, supply chain management and personnel systems should be promoted;
   - Is of the view that the ability of managers to access and interpret up-to-date decision-making data should be enhanced;
   - Is of the view that it has to provide adequate support to extract full value from the various systems;
   - Is of the view that the lengthy process related to the development, testing and implementation of a new Integrated Financial Management System should be noted.

9. With regard to supply chain management:

   The provincial Treasury:
   - Proposes the introduction of the value-for-money concept;
   - Proposes the transformation of the existing rule-driven and fragmented way in which procurement and provisioning are currently dealt with;
   - Proposes the strengthening of the capacity of the provincial Treasury with regard to proper contract management, preferential procurement, black economic empowerment (BEE) initiatives and public private partnerships;
   - Is of the view that BEE vendors need to be supported to ensure that they play a meaningful role in the Province.

10. With regard to cash management:

    The provincial Treasury:
    - Proposes the promotion of money management excellence;
    - Proposes that bank accounts in the Provincial Revenue Fund configuration should remain minimally cash positive, but with no overdrawing;
    - Proposes an optimum investment policy with capitalisation of interest gains to accumulate capital reserves for infrastructure spending.

11. With regard to accounting:

The provincial Treasury:

- Reiterates its proposal that decentralisation of the shared internal audit unit should follow the decentralisation of the shared Audit Committee with regard to Education, Health, and Social Services and Poverty Alleviation;
- Proposes that internal audit units should be adequately funded.

12. With regard to contingent liabilities:

The provincial Treasury:

- Proposes reserving R100 million as a once-off provision, mainly for unforeseeable and unavoidable expenditure;
- Proposes that any unspent portion of the reserve should be rolled over into the next financial year and should be replenished to keep the real value constant.

13. With regard to debtors:

The provincial Treasury:

- Proposes the development of debt management systems;
- Advises that outstanding debtors should receive urgent attention;
- Proposes the strengthening of capacity in the provincial Treasury to assess, monitor and report on the effective functioning, efficiency and performance of debt collection systems.

14. With regard to departmentalisation:

The provincial Treasury:

- Proposes that costs should be funded from savings, efficiency gains and reprioritisation, and that the contingency reserve should be drawn down only as a last resort, after taking account of statutory obligations related to social security grants.

Fiscal envelope (Chapter 5)

15. With regard to general issues:

The provincial Treasury:

- Is of the view that professional capacity should be built and maintained to effect spending in the most efficient, economic and effective manner to achieve national and provincial policy objectives, ultimately contributing towards growth and development – *iKapa elihlumayo;*
- Is of the view that over the short-term government needs to provide targeted fiscal transfers for social security, employment creation and poverty reduction;

- Is of the view that over the medium to long term institutional infrastructure and good public services should be provided to raise the potential growth rate of the economy and incomes of the poor (to reduce the Gini-coefficient);
- Is of the view that in the long term the focus should be on -
  - Market and procurement opportunities for the historically disadvantaged;
  - Small business development;
  - Land and agricultural reform to benefit small-scale farmers;
  - Investment in quality social infrastructure (schools, hospitals etc.);
  - Deepening the skills base;
  - Investment in infrastructure to stimulate economic development and growth (roads, buildings, etc.);
  - Increasing education, focusing on mathematics and science;
  - Reducing employment poverty levels;
  - Broadening the economic base by promoting black economic empowerment;
- Advises that the provision of quality social and economic infrastructure is one of the most fundamental preconditions for economic growth, job creation and accelerated service delivery, and, ultimately, political stability and a better life for all;
- Is of the view that government needs to reduce barriers to economic growth, ensuring that regularity frameworks are conducive to investment, employment and continuous learning;
- Reiterates its stance that capacity needs to be developed in the provincial Treasury to manage a borrowing portfolio;
- Is of the view that the existing revenue base should be improved in respect of estimation and collection before venturing into complex methods of financing like borrowing;
- Is of the view that with regard to the vertical division -
  - Decision-making processes need to be reviewed so as to reflect a stronger, more articulated prior provincial presence in policy-making to counter the current *ex post facto* consultation process;
  - It must corroborate other national spending decisions that are implemented at provincial and even local government level;
  - It must shield the provincial and local spheres of government from nationally driven policy-decision shocks.
  - Imbalances in allocations between provinces need to be addressed;
  - The mode of forced reprioritisation should be countered;
  - The crowding out of other equally important services should be stopped;
  - It is not only pressure points that require adjustment;
- Is of the view that the horizontal division of revenue should fully recognise the cost drivers at provincial level;
- Is of the view that, with regard to national conditional grants:

- The many small grants need to be reduced to prevent fragmentation and administrative burdens;
- They should be incorporated into the equitable share;
- They should rather be replaced with clear, unambiguous goals incorporating the notion of integrated government, good monitoring and information sharing;

- Is of the view that, with regard to provincial own revenue:
    - Forecasting needs to be improved;
    - Administration efficiency needs to be improved;
    - Information technology systems need to be improved;
    - Interdepartmental and interprovincial tariff structure differences need to be reduced;
    - A provincial revenue-generation policy should be developed;
    - The introduction of a fuel levy should be ring-fenced for road infrastructure spending.

Expenditure Review 2002

16. With regard to general issues:

The provincial Treasury:

- Proposes that provincial Treasury capacity should be developed to equip it properly for fulfilling its role in distributing resources, on the basis of effective public programmes, to meet government's strategic objectives;
- Is of the view that current infrastructure spending is inadequate to address backlogs or preserve the capital stock;
- Advises that infrastructure spending should be based on technical, economic, socio-economic and demographic factors which are aligned with strategic planning;
- Is of the view that a closer working relationship with the local sphere of government is required to give practical effect to integrated development plans;
- Is of the view that efficiency gains should be attained through departmental interaction and promotion of the cluster concept;
- Advises that the development of proper performance indicators (financial and non-financial) is essential;
- Advises that entering into national policy agreements requires prior securing of funding arrangements.

17. With regard to Premier, Director-General and Corporate Services:

The provincial Treasury:

- Is of the view that an adequate level of funding (maturity) has been reached;
- Proposes the strengthening of resource investment in the decentralisation of Internal Audit to yield a multiplier return on efficiency gains;

- Is of the view that an appropriate mix of resources for the various programmes is required;
- Is of the view that greater efficiency gains on Information Technology services can be yielded through innovative supply chain and contract management.

18. With regard to provincial Parliament: -

    The provincial Treasury:
    - Is of the view that, with due regard to its autonomy or independence, efficiency has to be promoted;
    - Proposes adequate funding to enhance the effectiveness of legislative and oversight processes.

19. With regard to Finance (provincial Treasury):

    The provincial Treasury:
    - Is of the view that, although the funding level is nominally constant, it declines in real terms and would put pressure on fulfilling the provincial Treasury role;
    - Advises that the Municipal Finance Management Bill, once enacted, will have an effect on the resources of the provincial Treasury as well as the Department of Local Government.

20. With regard to Community Safety:

    The provincial Treasury:
    - Is of the view that a degree of consolidation and stability has been reached;
    - Is of the view that efficiency in the usage of training centres (Philippi College and Gene Louw) should be attained;
    - Advises that contingency planning related to community patrol officers should be instituted;
    - Is of the view that the evolvement of effective traffic law enforcement may translate into budget pressures, both for the Vote and on infrastructure resources;
    - Proposes that the policing efficacy of weighbridges should be strengthened to protect investment in road infrastructure;
    - Advises that the Department seriously considers a more active change agent approach.

21. With regard to Education:

The provincial Treasury:

- Finds that Education's funding level is lower in real terms in 2002/03 than what was spent in 2001/02 and drops slightly in real terms over the medium term;
- Proposes that the budget allocation should be augmented so that at least remains constant in real terms;
- Advises that the risks in personnel expenditure require careful monitoring;
- Is of the view that the "pass-through rate of pupils" and quality of education should be improved over time;
- Is of the view that benchmarks/indicators on how the quality will improve over time should be developed;
- Is of the view that greater efficiency gains in the education system should be attained.

22. With regard to Health: -

The provincial Treasury:

- Finds that negative funding growth over the MTEF period in real terms is directly attributable to reductions in national conditional grants;
- Is of the view that funds should be aligned with policy priorities;
- Is of the view that real growth in the health budget may not be adequate to deal with increased demand due to the HIV/Aids epidemic;
- Is of the view that, apart from shifting the focus from higher to lower levels of health care, the declining health budget requires reorganising, increasing efficiency and consolidation of services;
- Is of the view that stark choices need to be made, given the inflationary pressures;
- Proposes the replacement of outdated equipment to facilitate efficiency gains as a key funding consideration;
- Advises that, with regard to the national Tertiary Services Grant, the particular services to be rendered and related costs require further work to reach agreement with the national Department of Health.

23. With regard to Social Services and Poverty Alleviation: -

The provincial Treasury:

- Is of the view that the continuous growth in child support and disability grants will crowd out developmental social service delivery (jeopardising self-reliance) and other social sector services;
- Advises that only those who legitimately qualify should receive grants;

- Advises that national government policy initiatives should be fully resourced through a shift in the vertical split of revenue collected nationally;
- Is of the view that the responsible national government department should be encouraged to improve the efficiency of the SOCPEN (social security grant) system.

24. With regard to Housing:

The provincial Treasury:

- Advises that ways should be found to augment the Housing Subsidy National Conditional Grant;
- Advises that alternative programmes should be developed to respond to the housing crisis;
- Advises that housing delivery should be an integrated approach;
- Is of the view that the burden that the delivery of housing places on ownership, society and government requires further work.

25. With regard to Environmental Affairs and Development Planning:-

The provincial Treasury:

- Proposes that, as a consequence of the departmentalisation model, restructuring and consolidation is required;
- Proposes that funding of the Western Cape Nature Conservation Board should at least be kept constant in real terms;
- Advises that contingency planning related to development planning and nature conservation should be instituted;
- Is of the view that national government policy initiatives should be resourced through a shift in the vertical split of revenue collected nationally.

26. With regard to Transport and Public Works:

The provincial Treasury:

- Proposes that funding should be increased in real terms and augmented to make real inroads into infrastructure backlogs, subject to stimulation of economic activity;
- Proposes that consolidated departmental five-year accommodation plans should be compiled to determine realistic expenditure levels and attain efficiency in accommodation usage;
- Advises that funding directed towards road infrastructure should be underpinned by technical, economic and socio-economic analysis;
- Proposes that the allocation to roads should be utilised to encompass and integrate economic development and tourism to regenerate/stimulate economic growth.

27. With regard to Agriculture:

The provincial Treasury:

- Proposes that, as a consequence of the departmentalisation model, restructuring and consolidation is required;
- Finds real growth trends in funding over the medium term;
- Proposes that the pressures to fulfil commitments related to the Land Redistribution for Agriculture Programme should be a key funding consideration:
  - Small farmer settlement
  - Water engineering services
  - Technology transfer
  - Training;
- Proposes that pressures related to keeping the Western Cape agricultural sector competitive in the global environment should be a key funding consideration;
- Advises that proper output benchmarks should be developed.

28. With regard to Local Government:

The provincial Treasury:

- Proposes that, as a consequence of the departmentalisation model, restructuring and consolidation is required;
- Advises that the Municipal Finance Management Bill, once enacted, will have an effect on the resources of the Department, as also of the provincial Treasury;
- Is of the view that national government policy initiatives should be fully resourced through a shift in the vertical split of revenue collected nationally;
- Is of the view that this department has an important role to fulfil in supporting and developing municipalities.

29. With regard to Economic Development and Tourism:

The provincial Treasury:

- Proposes that, as a consequence of the departmentalisation model, restructuring and consolidation is required;
- Proposes that, apart from tourism, investment in industry development and economic development coordination should be a key funding consideration;
- Advises that apart from proper sector analysis, proper output benchmarks should be developed;
- Advises that interventions undertaken should be linked to Transport and Public Works.

30. With regard to Cultural Affairs and Sport:

The Provincial Treasury:

- Proposes that, as a consequence of the departmentalisation model, restructuring and consolidation is required;
- Reiterates its proposal that investment in sport, particularly school sport, should be a key funding consideration.

Key priority areas (Chapter 6)

31. Introduction

- The key priorities do not dilute any of the conclusions summarised previously, but attempt to concentrate on the main drivers informing the allocations for the new MTEF.

32. With regard to national policy guidelines:

- Education: Learner support materials, other non-personnel and non-capital budgets.
- Health: Medicines, drugs, equipment, medical supplies and other non-personnel and non-capital spending.
- Health: Restructuring and improving of pay packages for scarce health personnel.
- Social security grants, implementation of norms and standards, and welfare services, including the implementation of the Child Justice Bill in Social Development.
- Roads, agriculture and other economic, infrastructure and rural development programmes.
- On analysis, to achieve a balance between social and economic infrastructure spending.

33. With regard to efficiency gains – general:

- Improve efficiency overall.
- Improve efficiency, specifically in the area of non- personnel expenditure.

34. With regard to efficiency gains – supply chain management:

- Principle areas deserving attention:
  - Health:
    a. Equipment
    b. Broad range of consumables.
  - Education:
    a. Learner transport

b. Learner supply materials.
- Transport and public works:
  a. Capital projects
  b. Property management.
- Premier, Director-General and Corporate Services:
  a. Information technology.
  b. Information communication technology.
- Social Services and Poverty Alleviation:
  a. Social security.

35. With regard to efficiency gains – improvement in personnel utilisation:

- Utilise personnel to fullest potential by rearranging staffing structures and supportive retraining to best meet strategic goals of departments.
- Piggy-back on PSCBC Resolution 7 of 2002 to achieve this.

36. With regard to efficiency gains – financial management improvements:

- Strengthen provincial Parliament.
- Three new internal audit units in the Departments of Health, Education and Social Services and Poverty Alleviation.
- Once-off capital costs for Basic Accounting System implementation.

37. With regard to efficiency gains – departmentalisation:

- Full introduction of national Treasury's normative financial standards.
- Introduction of standardised chief financial officer (CFO) and human resource components.

38. With regard to own revenue improvements:

- Systematic reduction in outstanding debtors with appropriate inducements.
- Enhance baseline allocations equal to outstanding debtors as at 1 April 2002 as once-off concession, but set off long-outstanding remaining amounts (after December 2003) against future allocations.
- Maximise own revenue and adjust baselines upwards. Flip side: non-collected revenue will result in equivalent downward baseline adjustments in same financial year where linked to expenditure.
- Develop new revenue sources – envisaged fuel levy.

39. With regard to the underlying theme –iKapa elihlumayo:

- Embrace the concept of *iKapa elihlumayo*, meaning growing and developing the Cape.

- Comes at a time when provincial and local spheres of government are amenable to the idea and prepared to make trade-offs in the interest of long term benefits.
- Will coincide with NEPAD.
- Will promote black economic empowerment.
- Great deal of work lies ahead.

40. With regard to service delivery improvements:

- Social security grants to be funded out of "new money".
- Balance to maintain all other services and to provide for cost pressures; mostly improvements of conditions of service and procurement-related increases.
- After discounting for social security in a macrocontext, maintain a constant real growth overall on all other services over the MTEF.
- After discounting conditional grants with no personnel component on a vote-specific basis, apparently sufficient manoeuvring space to begin to deal with the conclusions from the Expenditure Review 2002.
- Some scope, albeit limited, to attend to the remaining national policy guidelines.
- Selective adjustments were made by the national Treasury to conditional grants to cater for non-personnel cost inflation.
- Policy boosts were given to HIV/Aids (mother-to-child prevention), Hospital Revitalisation and Integrated Nutrition Programme conditional grants.
- Measures have to be taken to ensure better disbursement of the Integrated Nutrition conditional grant.
- Own revenue shows weakening trend.
- Abolishing the provision for contingencies will assist in providing for:
    - (a) Departmentalisation costs
    - (b) Promotion of farmer settlement
    - (c) Tourism
    - (d) School sport
    - (e) Selected industry sector analysis and development - lays the basis for *iKapa elihlumayo.*

41. With regard to capital expenditure:

- Apart from conditional grants, all capital spending as originally provided for 2002-2005 MTEF, adjusted for inflation.
- Unfortunately the national conditional grant for provincial Infrastructure remains essentially the same.
- Remaining balances from capital reserves (R320 million) have been safeguarded for Transport and Public Works 2003/04 and 2004/05, together with the outstanding transfers for the Cape Town Convention Centre.
- A further dividend from money management is possible; to be allocated to:

(a) Capital formation (minimum R300 million over the MTEF) in the *iKapa elihlumayo* context.
(b) R120 million over two years towards equipment backlogs in the Department of Health subject to prior Treasury approval of their supply chain management system in liaison with the Auditor-General.
(c) Roll over the balance of the 2002/03 Contingency Reserve to 2003/04 and top up to R100 million in real terms.
(d) Subject to overall risk management, efficiency of money management operations and exogenous factors.

- Borrowing on capital markets to augment the above provisions subject to appropriate ceding of own revenue flows and a return on investment that is higher than the cost of capital.

42. Conclusion

- A tight holding budget with some flexibility over the MTEF to allow partial accommodation of spending pressures and begin laying a basis for growth.
- Proviso an unambiguous commitment to good governance and *iKapa elihlumayo.*
- National government's adjusting of the vertical share is an acknowledgement of the role that provinces need to fulfil in a balanced delivery of social and economic infrastructure.
- Provides opportunity for careful reflection on the road ahead as to how best to be an agent of change.
- Key theme has to be the substance of *iKapa elihlumayo,* a concerted drive to improve per capita levels and disparities.

CONTENTS

1

INTRODUCTION

Introduction

Fiscal policy informs the budget with the aim of achieving a predetermined set of results, taking into account external and internal variables. It therefore creates the basis for the allocation of funds to attain the desired results within the framework of finite resources.

Within the framework of the three pillars of fiscal policy, namely allocation, stabilisation and redistribution, it is designed to create certainty and confidence about the future direction that the Western Cape Government intends taking and also to form the basis for a healthy debate about the choices that are made.

This chapter sets out, as point of departure, to inform the reader of the external variables, such as the macroeconomic conditions and national policy imperatives, and the provincial strategic framework, taken up in the Western Cape Government's ten strategic goals, and the relation to policy and delivery in government.

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

In the following paragraphs we provide a glimpse of how national policy imperatives are linked to Western Cape policy imperatives and how they can be perceived as the underlying factors for compiling the WCFP for 2003 - 2006.

The State of the Nation Address by the President of South Africa on 8 February 2002 briefly emphasised the following issues:

- Eradication of poverty and underdevelopment
- Strengthening the focus on human development and deepening the skills capacity of the economy by channelling significant resources into health, education, training and skills development
- Improve capacity to combat and reduce crime
- Commitment to social transformation to improve equity
- Increased focus on issues that enhances the achievement of higher rates of economic growth and development
- Improved efficiency
- Debt redemption
- Partnerships with communities to improve access to affordable basic services.

Further policy imperatives, *inter alia* taken from the Budget Council Lekgotla decisions held in August 2002, are:

- Targeting poor households not covered by the social security net, introducing early childhood development programmes (grade R) and adult basic education, dealing with HIV/Aids, and restructuring the hospital sector.
- Alignment policy and budgets, and target spending on carefully selected components with high-impact outcomes.
- Fostering equity and redistribution by determining the optimum balance between giving direct income support in the short term, and investing in creating economic opportunities in the long-term.
- Provinces' role in improving the intergovernmental fiscal system given the need to reinforce pro-poor government programmes which constitute the core government delivery.
- Repositioning treasury as a change agent to facilitate a mindset shift required by the PFMA across government.
- Shifting the focus from inputs towards outputs and outcomes, but at the same time improving the quality of input and output information, including non-financial information.
- Assessing implications of the move towards a single civil service on an empirical basis, bearing in mind the potentially high costs of harmonising working conditions.

The Western Cape Government's strategic goals

The Western Cape Government revised and expanded its strategic framework for policy formulation to suit its current needs during December 2001. In the light of the Constitution, which enshrines the progressive realisation of socio-economic rights, this shift in priorities can be defended on equity grounds, especially in the light of the gross disparities in access to public services that existed in the past. Political ownership is critical to our fiscal arrangements, and a high level of awareness of these strategic priorities is thus important. The Western Cape Government's strategic framework is embodied in the following ten points:

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 (IDPs) 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 cooperation 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.

Budget Speech of the Provincial Minister of Finance and Economic Development on 1 March 2002

In his Budget Speech on 1 March 2002, Minister Rasool emphasised the importance of the Western Cape economy being exposed to wider participation by admitting more people to mainstream society in future. He noted that the unemployment rate was too high for the Province and that the very skewed income distribution translated into a Gini coefficient of 0,58. (According to this measure of income, inequality is excessive when values are higher than 0,50). Poverty was largely associated with many other aspects of unsatisfactory living standards. Life expectancy was thus regarded as too low and infant and child mortality rates as far too high, malnutrition and hunger was still rife amongst many and HIV/Aids was claiming many victims. In essence the Minister emphasised that the budget intent was to make the necessary resources available to the Province in a targeted fashion so as to alleviate some of the above pressures.

Linking national policy to provincial policy

[1]Mention was made in the Western Cape Fiscal Policy 2002 – 2005 that the overall aims of its policy plan were 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, and strengthen accountability and long-term growth and development. The above goals and strategies can only be achieved if they are translated into effective spending by all departments. This challenge for the Province had to be seen as a collective endeavour by all stakeholders as they were to serve and interact in order to attain improved results.

The aforementioned policy imperatives should be seen as a mission statement and the strategic direction that this Province must pursue in future. Over the medium-term these guiding principles should be landmarks for departments within the Province to ultimately enhance the quality of services to the best advantage of the Province and its people. This collective effort should not be perceived as allocating more resources to provincial departments, but rather the day-to-day concerted efforts of all the individuals within the provincial government, be it at the highest political level or the lowest level in a department. In conclusion, it is thus imperative that officials should adhere to the visions of leaders in making a difference to the province of the Western Cape.

[1] Forward to the Western Cape Fiscal Policy 2002 – 2005

The contents of the WCFP 2003 - 2006

Chapter 1: Introduction
This chapter provides a brief overview of how policy imperatives influence the WCFP 2003 – 2006 and gives a short summary of each of the chapters to follow.

Chapter 2: Economic analysis and conclusions
This chapter provides a socio-economic overview of the Province and the external environment that influences resource allocations.

Chapter 3: Local Government
The purpose of this chapter is twofold; **firstly**, to highlight the various future implications that draft legislation might have on various key role players and their readiness to deal with such implications in a coherent and constructive manner, and **secondly**, to discuss the legal and financial framework within which the transfer of functions and powers from provincial government to local government and vice versa takes place.

Chapter 4: Financial management issues
This chapter covers nine issues that are regarded as being important to fiscal policy. Although the issues appear diverse, they comprise a significant portion of the work that is delivered in four of the seven directorates of the provincial Treasury. They are accountability, accounting (debtors), Chief Financial Officer (CFO) structures and responsibilities, capacity building, financial systems and cash management, contingent liabilities, departmentalisation, financial systems and supply-chain management.

Chapter 5: Fiscal envelope
The division of nationally raised revenue between the three spheres of government is known as the vertical split of government resources, and the split between the nine provinces according to an equitable share formula as the horizontal split. This chapter provides a systematic approach to how the Western Cape province receives its total funds and concludes with a summary of its total revenue and expenditure.

Chapter 6: Conclusions and key priority areas
This chapter contains the conclusions of each section and chapter and reiterates the key priority areas. Furthermore, it summarises all the recommendations and the future work envisaged in this document. It proposes the road ahead for fiscal policy and advises the allocation process for the 2003/04 – 2005/06 MTEF period. Policy imperatives are the underlying framework of the WCFP for 2003-2006. An attempt is made to indicate how national policy links to the Western Cape fiscal policy, or alternatively, the underlying factors in how the Province, at a provincial level, provides services that ultimately benefit a geographical area of South Africa.

2

SOCIO-ECONOMIC ANALYSIS

Background

Generally, revenue and spending are driven by exogenous factors such as changes in the economic or social conditions and demographic trends within the Province. This chapter begins by describing the issues that should influence the composition of provincial expenditure. It covers issues such as key economic, poverty, social and human capital indicators and other micro-economic variables. The chapter concludes by outlining the effect of the indicators on the fiscal policy as well as providing a provisional summary of a research agenda for the next few years and an overview of the availability of data and data issues.

Central to economic analyses are: a) accurate information and information systems on which to base decisions, to evaluate the projected impact of proposed programmes on communities in the Province, the level and mix of service delivery outputs required, the financial and capacity implications of implementation; b) benchmarking, so that the Province can assess how well one is doing (both in coverage and efficiency) compared with other provinces or regions with similar incomes; and c) an awareness of some of the pitfalls.

The provincial Treasury has started a process in which economic advisors from the academic cadre are appointed, *inter alia* to identify appropriate interventions, to assess the affordability and sustainability of projects that were specifically directed to eradicating poverty, to determine backlogs on service delivery, to provide a comprehensive analysis of the actual impact of government spending on target groups, to find optimal points for intervention from limited resources, etc. This chapter is based principally on the work of the following advisors, who compiled inputs for the Western Cape Fiscal Policy 2003 – 2006. They are: Amiena Bayat, Simon Bekker, Phillip Black, Haroon Bhorat, Debbie Budlender and Servaas van der Berg. We are deeply grateful to them for the high quality of the work they did within a short time. The papers are listed in the Bibliography.

Key direction indicators

The key direction indicators are (1) economic indicators; (2) social and poverty indicators; and (3) human and intellectual capital.

A: Economic indicators

Economic Growth

Table 1: Growth of GDP and GDE, 1993 – 2001 (constant 1995 prices)

Year	1993	1994	1995	1996	1997	1998	1999	2000	2001
GDP R million	514 887	531 539	548 100	571 705	586 837	591 310	603 841	624 127	638 010
%	1,2	3,2	3,1	4,3	2,6	0,8	2,1	3,4	2,2
WC GGP R million	74 144	76 542	78 926	82 326	84 505	85 149	86 953	89 874	91 873

***Source**: Bureau for Economic Research. Trends. Second Quarter. 2002*
GDP for SA
GGP is derived from GDP figures

The determinants of growth are complex and include, *inter alia,* many aspects such as geography and natural resources; history, culture and religion; socio-political and economic effects, namely investment, savings, human capital, poverty, race and gender. It also includes government policies: legislation and regulations, outward-oriented policies, macroeconomic policies, government spending and revenues.

Leading sectors of the regional economy include manufacturing, finance and banking, tourism, commerce and agriculture. All of these have distinct growth potential. The absence of up-to-date regional output and employment figures makes it difficult to compare regional and national growth and development over a time period. The gross geographic product (GGP) for provinces was last updated in 1994. The GGP for the Western Cape was then derived at 14,4% of the gross domestic product (GDP) for SA as depicted in Table 1. Cape Metropolitan Council levy data suggests relatively high real turnover growth rates, but the figures are difficult to reconcile with GGP figures.

Inflation

Table 2: Cpi(X)

Year	1995	1996	1997	1998	1999	2000	2001
Index	68,8	73,6	80,1	86,0	92,3	100	106,9
%	7,5	7,0	8,9	7,4	7,4	8,3	6,9

***Source**: Bureau for Economic Research. Trends. Second Quarter. 2002*

Relatively high levels of inflation, as is the case in South Africa, can be regarded as a "hidden tax", with large inefficiency costs. Put differently, this inflation is a regressive, anti-poor tax that leads to currency substitution away from domestic monetary assets and reduces the return on savings. Inflation impedes capital inflows because of exchange rate variability that can reduce work effort and diminishes human capital accumulation. Inflation falls disproportionately on the financially less sophisticated households as their real incomes may shrink, while their propensity to spend their total income on satisfying basic needs is much higher than for groups who earn higher levels of income and are in a position to reduce expenditure on savings, e.g. on luxury goods.

B: Social and poverty indicators

Income inequality

Western Cape incomes may be higher than the national average, and many conditions associated with poverty less severe than elsewhere in South Africa (Table 3); however, with unemployment lower, and the labour force better educated, inequality is nevertheless high. From Table 3 it is clear that problems associated with poverty are still widely prevalent in the Province.

Table 3: Selected socio-economic indicators, Western Cape and South Africa

Demography	**Western Cape**	**South Africa**
Urbanisation level 1996	88,9%	53,7%
Mean household size	4,03	4,48
Dependency ratio (people in other age groups divided by people in economically active age group 15-64), 1996	1,20	1,90
Economic conditions and employment:		
Per capita personal income, 1996	R17 880	R11 421
Mean monthly household expenditure, 1996	R3 816	R2 769
Poverty headcount ratio, 1996 (households) (cf. Table 4)	12%	28%
Labour force participation rate, 1999: Total (age 15+)	66,4%	51,5%
Labour force participation rate, 1999: Male	74,9%	59,4%
Labour force participation rate, 1999: Female	58,3%	44,2%
Unemployment (narrow) 1999	13,7%	23,3%
Education & skills:		
Adult (20+) literacy rate 1996 (at least 4 years of schooling)	90,3%	66,9%
Mean years of schooling of 20-year olds, 1996	9,68	9,06
Not attending school, 7-15-year olds, 1996	5,5%	11,1%
Labour force without any secondary education, 1996	40,4%	48,5%
Labour force matriculated, 1996	31,6%	27,3%
Health conditions:		
Life expectancy at birth 1996: Males (years)	55,8	52,1
Life expectancy at birth 1996: Females (years)	65,7	61,6
Infant mortality rate (per 1000 infants aged under 1), 1998	8,4	45,4
Child mortality (per 1000 children aged 1-4), 1998	4,8	14,7
Children fully vaccinated, 1998 (BCG, 3 doses DPT, polio)	64,2%	63,4%
Children under 5 with diarrhoea in past two weeks, 1998	9,9%	13,2%
Total fertility rate (children born per woman given prevailing age-specific fertility), 1998	2,3	2,9
Smoking among adult males, 1998	49%	42%
Smoking among adult females, 1998	29%	11%
Social amenities:		
Households with telephone, 1996	54%	26%
Households with running water, 1996	77%	40%
Households with flush toilet, 1996	87%	45%
Position of women:		
Women abused by partner in last year, 1998	8,0%	6,3%
Women ever abused by partner, 1998	16,9%	12,5%
Adult (15-49) women ever raped, 1998	6,6%	4,0%
Teenage mothers: Women 15-19 who are mothers or have been pregnant, 1998	13,7%	13,2%

***Sources**: Data mainly taken from Statistics South Africa, October Household Survey 1999; Census 1996; and Demographic and Health Survey 1998*

Life expectancy, mortality and health

The Western Cape's life expectancy of about 61 years is the highest in South Africa and the infant mortality rate of 8,4 per 1 000 live births is the lowest in the country (Table 3). Child mortality at 4,8 per 1 000 in the age group 1 - 4 is less than one-third the national average. Higher than average vaccination levels and lower than national incidence of diarrhoea are indicative of a better (though still far from satisfactory) health status in the Western Cape. Table 3 also lists a number of important social and poverty indicators.

The Province has good medical facilities. Declines in total fertility (the number of children born to a woman in her lifetime) have proceeded further in the Western Cape to 2,3, just above replacement level, compared with South Africa's average of 2,9, but teenage pregnancies are still alarmingly high and smoking prevalence is above the national average, particularly among women.

Unemployment

The Western Cape is one of South Africa's more developed provinces with an economy that has considerably outpaced the rest of the country in recent years. However, it still faces problems of poverty and inequality fundamentally similar to the rest of the country. Employment is the single most crucial requirement for reducing poverty and inequality, and here education is central. Labour is the key provider of regular incomes. It seems necessary, therefore, as a starting point for designing poverty reduction policies through the fiscus, that the provincial Government determines precisely how the labour market has been performing over time[1].

In 1999 (Table 3) unemployment measured 13,7% for the Western Cape. It has been increasing annually, but the economy is unable to absorb new entrants to the labour market. This is regarded as an important contributing factor to crime in the Province. Key labour input costs in the public sector are largely determined by conditions of service set by the national government and by the outcomes of national wage bargaining. Significant labour shifts between the different sectors are shown in Tables 4.A and 4.B.

Table 4.A: Employment shifts by sector, 1995-1999 (OHS, 1995 and 1999)

SECTOR	% CHANGE
Agriculture	**-3.33**
Mining	**10,46**
Manufacturing	**6,65**
Utilities	**-6,61**
Construction	**31,42**
Trade	**27,81**
Transport	**15,75**
Finance	**61,35**
Commercial Services	**-6,67**

Table 4.B: Employment shifts by occupation, 1995-1999 (OHS, 1995 and 1999)

OCCUPATION	% CHANGE
Managers	**37,81**
Professors	**72,55**
Technicians	**0,28**
Clerks	**-4,49**
Sales	**16,97**
Skilled agriculture	**343,51**
Crafts	**25,15**
Operators	**1,05**
Elementary	**-33,60**

***Source**: Bhorat, H. Labour markets, poverty and inequality in the Western Cape.*

[1] A prototype of the character of such labour market analysis is provided in more detail in Bhorat (2002).

As in other provinces, women are worse affected than men by unemployment. There are further differences along racial lines. Thus, the labour force survey of September 2001 revealed that male unemployment in the Western Cape (using the official definition) stood at 21,4%, with female unemployment at 31,0%. As with other indicators, there are stark differences between the four race groups. Census 1996 used an expanded definition of unemployment, and came up with a rate of 45,1% for African women in the Western Cape, compared with 27,6% for African men. The overall unemployment rates for women and men in the Province at the time were reported to be 21,3% and 15,1% respectively.

Official unemployment statistics for the country as a whole are high. The army of unemployed is growing and the tension in this area is increasing. With concealed unemployment taken into account, this problem becomes too acute and socially dangerous. Apart from unregistered individuals with no permanent unemployment, the conceded unemployment comprises those who are formally on the staff, being in fact on unpaid leave or are only working part-time. Further lay-offs among public employees require new jobs in other sectors of the economy, as well as the establishment of a proper retraining system.

For poverty reduction, sustainable growth over a wide base and job creation continue to be the main prerequisites; the creation of a favourable environment for SMMEs will aid this. Creation of such an environment requires both changing the legal framework of entrepreneurship by making it more liberal and facilitating access to credit resources.

Many production development efforts depend on the business activities of local governments and civil society goals and on local private businesses. To support such efforts, the government must provide the basic institutional framework. Decentralisation efforts should be intensified in order to allow the development of local authority initiatives. However, financial decentralisation is needed to ensure a decisive breakthrough in this area. Financial decentralisation means that, along with responsibility for the solution of local problems, local governments have to be given access to proper funding.

Poverty and inequality

One can define poverty in terms of deprivation or in terms of lack of income. Key components of poverty and inequality are thus limited access to savings and the returns on the factors of production such as labour, land and capital. The returns of these are labour earnings or wages for each level of human capital; land rent; and the interest earned on capital, to which should be added transfer earnings such as social pensions. In the case of labour, returns are influenced not only by wages, but also by access to employment.

In terms of overall incomes, wages are dominant (69% of all household income within the Province is labour income). Thus a large part of existing inequality in the Western Cape can be ascribed to inequality in the sphere of labour: the quality of labour, access to employment, and returns on labour in the form of wages. For poverty, transfers have a major role to play and income from capital, profits and self-employment also contribute to inequality. Inequality in the Western Cape is largely driven by inequality in the access to and levels of wages. A different racial composition, lower fertility and thus a lower dependency burden, more widely available social services and amenities, available higher educational attainment, greater labour force participation, less unemployment and higher than average wage for unskilled and farm workers, all contribute to smaller overall inequality. But inequality (with a Gini coefficient of 0,602[2]) remains vast, with important racial, geographical, educational and gender dimensions: See Table 5.

Table 5: Gini coefficients for the Western Cape by race and region, 1995

Western Cape		**0,602**
By race:	Black	0,515
	Coloured	0,447
	Asian	0,339
	White	0,443
By region:	**Cape Metropolitan Area**	0,561
	Non-CMA	0,623
	- Breede River DC	0,603
	- Klein Karoo DC	0,654
	- Overberg DC	0,649
	- Central Karoo DC	0,613
	- South Cape DC	0,624
	- West Coast DC	0,568
	- Winelands DC	0,605

Source: *Oosthuizen, Morné J. and Nieuwoudt, Liezl. 2002. A Poverty Profile of the Western Cape Province of South Africa. Mimeo. Stellenbosch Department of Economics, University of Stellenbosch, Table 8, p175*

Table 5 shows Gini coefficients calculated by Oosthuizen & Nieuwoudt (2002) for the Western Cape for 1995, based on the OHS/IES95. The calculations were done using the average of per capita income and expenditure of households. These coefficients should not be taken as necessarily accurate, given problems associated with the weighting of the sample of households in this survey that gave an inordinately large population share to the non-metropolitan areas (62% versus 35% in the 1996 census), and given the relatively small sample sizes within some of the groups and regions shown. Nevertheless, it is clear that there is widespread inequality within the Province as a whole, with a Gini coefficient of 0,60 according to this estimate. Within most of the regions, excluding only the Cape Metropolitan Area and the West Coast, inequality is even worse. The Gini coefficient for blacks of 0,52 is very high and may result from major differentials in job access within this group.

[2] O'Leary, B.M.; Govind, V.; Schwabe, C.A.; & Taylor, J.M. 1998. *Service needs and provision in the Western Cape.* Pretoria: Human Sciences Research Council.: 3. The Gini coefficient, a measure of inequality, can range from 0 for complete equality, to 1 for complete inequality. Rates above 0.5 are usually internationally perceived to be excessive.

Important forces influencing patterns of the Western Cape's inequality in recent decades have been growing unemployment combined with rapidly rising wage levels at the bottom end of the wage spectrum.

Based on a similar analysis of the OHS/IES95[3] data but using poverty lines that distinguish between poverty (affecting 51% of individuals in South Africa) and ultra-poverty (affecting 19% of individuals and 12,5% of households), Oosthuizen and Nieuwoudt arrive at the data in Table 6. Again it is clear that regional differentials are considerable and that the Central Karoo, Klein Karoo and Breede River District Council areas experience most poverty, although less so than in South Africa as a whole. Ultra-poverty is particularly less common than elsewhere in South Africa. It occurs most in the Central Karoo and Breede River areas.

Table 6: Poverty rates and shares by region and area

Region	Individuals				Households	
	Poverty rate %	Poverty share %	Ultra-poverty rate %	Ultra-poverty share %	Ultra-poverty rate %	Ultra-poverty share %
Cape Metropolitan Area	**20,1**	**25,0**	**2,7**	**26,9**	**1,8**	**27,5**
Non-CMA	**35,4**	**74,0**	**4,5**	**73,1**	**2,7**	**72,5**
- Breede River	43,7	17,0	9,0	27,4	5,0	22,4
- Klein Karoo	53,0	10,0	5,2	7,9	3,3	8,1
- Overberg	29,0	7,0	0,6	1,2	0,4	1,5
- Central Karoo	56,0	8,0	9,0	9,8	6,3	11,9
- South Cape	38,0	15,0	6,5	19,6	3,9	20,0
- West Coast	21,0	8,0	1,8	5,5	1,0	5,6
- Winelands	22,0	7,0	0,7	1,7	0,8	3,0
Western Cape	**29,0**	**5,0**	**3,8**	**2,0**	**2,3**	**2,0**
- Urban	26,0	78,0	4,0	90,2	2,4	88,5
- Rural	48,0	21,0	2,9	9,8	1,9	11,5
South Africa	**50,9**	**100,0**	**18,6**	**100,0**	**12,5**	**100,0**
- Urban	29,4	29,4	7,3	20,0	4,5	19,6
- Rural	73,0	70,6	30,2	80,0	22,5	80,4

Source: *Oosthuizen, Morné J. and Nieuwoudt, Liezl. 2002. A Poverty Profile of the Western Cape Province of South Africa. Mimeo. Stellenbosch Department of Economics, University of Stellenbosch, Table 3, p.5*

As for inequalities between race groups, although coloureds make up the vast majority (69%) of the poor compared with the 28% black share, blacks account for 62% of those in extreme poverty[4]. As elsewhere, females and children bear the brunt of poverty.

Only 5,7% of Western Cape inhabitants were in **severe poverty** and 19,1% were in **poverty**.[5] Table 7 shows these poverty estimates, and those of

[3] The OHS/IES95 data may not be very accurate at the regional level, given that sampling size in each region was relatively small. Nevertheless, Figure 3 below shows that the Central Karoo, Klein Karoo and Breede River areas were the only regions that did not considerably exceed national per capita income or expenditure levels.

[4] Oosthuizen, Morné J. and Nieuwoudt, Liezl. 2002. *A Poverty Profile of the Western Cape Province of South Africa*. *Mimeo.* Stellenbosch Department of Economics, University of Stellenbosch, Table 5, p. 6-7

[5] Leibbrandt, M & Woolard, I. 1999. A comparison of poverty in South Africa's nine provinces. *Development Southern Africa*, Vol. 16(1), Table 12. **Severe poverty** is here taken to be expenditure below R2 200 per annum per adult equivalent, and **poverty** below a less restrictive R3 509.

Alderman and associates[6] that 12% of Western Cape households fell into poverty in 1996 (based on a poverty line of R800 household expenditure per month). From an inequality perspective, though, this table illustrates the extent of regional inequalities. Estimated mean monthly household expenditure of R3 816 for the Western Cape was 38% higher than for South Africa as a whole.

Table 7: Proportion of relatively poor and relatively affluent households by district council area, 1996

District Council Area	Relatively poor households (income below R12 000 p.a.) %	Relatively affluent households (income above R54 000 p.a.) %	Relatively poor households (expenditure below R800 per month) %	Mean household income per month
Breede River	37,7	14,0	21	R2 957
Klein Karoo	42,4	12,3	20	R3 132
Cape Metropolitan Area	24,3	27,1	9	R4 075
Overberg	32,7	15,4	18	R3 258
Central Karoo	49,9	10,4	21	R2 743
Southern Cape	31,6	17,3	14	R3 650
West Coast	31,6	16,6	18	R3 276
Winelands	25,8	22,6	15	R3 546
Total Western Cape	**27,3**	**23,6**	**12**	**R3 816**

Source: *Based on Census 1996, and expenditure figures on Alderman et al. 2000. Note that household size was not taken into consideration and that census income is usually not regarded as a very accurate reflection of actual income. For this last reason the last two columns, based on Alderman et al., may be more accurate.*

As Table 8 shows, in the poorest quintile (one-fifth) of the population the Western Cape's share is only 2,0%, and among the poorest quintiles (two-fifths) its share is still only 4,0%. This contrasts with its share in the total population of 9,7% and even more with its share of the rich population: 14,0% of the richest quintile of the South African population were resident in the Western Cape in 1995, and 15,1% of the richest decile (one-tenth).

Table 8: Western Cape's share in the population and in the various expenditure categories, 1995

Western Cape share in:	Percentage of SA population in category %
Total population	9,7
Poorest 20% of SA population (Quintile 1)	2,0
Poorest 40% of SA population (Quintiles 1 & 2)	6,1
Quintile 2 of SA population	4,0
Quintile 3 of SA population	11,6
Quintile 4 of SA population	14,2
Richest 20% of SA population (Quintile 5, or Deciles 9 & 10)	14,0
Richest 10% of SA population (Decile 10)	15,1

Source: *Based on data from the OHS/IES95*

[6] Alderman, Harold; Babita, Miriam; Lanjouw, Peter; Makhatha, Nthabiseng; Mohamed, Amina; Özler, Berg & Gaba, Olivia. 2000. Combining census and survey data to construct a poverty map of South Africa. Ch. 2 in Statistics South Africa. *Measuring poverty in South Africa*. Pretoria: Statistics South Africa: 5-52

Poverty is a multidimensional phenomenon. According to Table 9 almost 5,7% of Capetonians were living in poverty in 1995, if the minimum living level is taken as a yardstick.

Table 9: Poverty by province, 1995 and 1996

Province	Severe poverty ratios (% of individuals), 1995	Poverty ratios (% of individuals), 1995	Poverty ratios (% of households), 1996
	Poverty line = R2 200 per adult equivalent per year	Poverty line = R3 509 per adult equivalent per year	Poverty line = R800 per household per month
Western Cape	5,7%	19,1%	12%
Gauteng	4,9%	12,7%	12%
Kwazulu-Natal	22,1%	42,4%	26%
Northern Cape	26,1%	46,0%	35%
Mpumalanga	28,0%	49,2%	25%
Limpopo	31,7%	50,8%	38%
North-West	34,0%	54,3%	37%
Free State	38,0%	57,5%	48%
Eastern Cape	42,2%	64,1%	48%
South Africa	**24,7%**	**42,3%**	**28%**

Source: *Woolard and Leibbrandt 1999: 21, Table 12; Alderman et al. 2000.*

Table 9 shows further that the Western Cape and Gauteng have much less poverty than other provinces, irrespective of which poverty measure is used, but that poverty still is substantial.

Poverty is not a static condition among individuals, households or communities: while some are permanently poor, others move into and out of poverty due to life-cycle and other changes. It is therefore important to apply the concept of vulnerability to poverty to understand the processes of change. Vulnerability to poverty is countered by accumulating assets and managing them in such a way that sustainable livelihoods can be generated. Therefore, poverty is characterised not only by a lack of assets and inability to accumulate them, but also by an inability to devise an appropriate coping or management strategy in the face of shocks or crises.

- At the heart of a fiscal policy that assists in reducing poverty must be an integrated set of programmes designed to effectively strengthen the income base of the poor, and reduce the geographic dislocation between livelihoods, assets and infrastructure.
- A set of better targeting of social assistance needs to be put in place. Social assistance will develop by becoming better targeted. It is the disabled and poor who should be eligible for such assistance.
- Through education, human capital embodied in labour can be augmented.
- For those who can work, jobs need to be located. It is very important to find new solutions to this problem, including self-employment, export of labour and developing local initiatives to address social issues. That is why decentralisation and the transfer of additional authority to local governments will be playing a special role in solving social problems.

- Effective public expenditure planning and management has a central role in the realisation of national poverty reduction strategies.
- We should also change the structure of category and adjustment, and the distribution of grants and continue to provide critical transfers while broadening the tax base of local budgets.

The Province may also consider monitoring "poverty" and "targeting" more closely, bearing in mind that government revenues are not the only, nor the most important, instruments for poverty reduction. It is the combination of revenues and the use of those resources, channelled through spending programmes, which proves effective in reducing poverty.

Poverty and gender issues

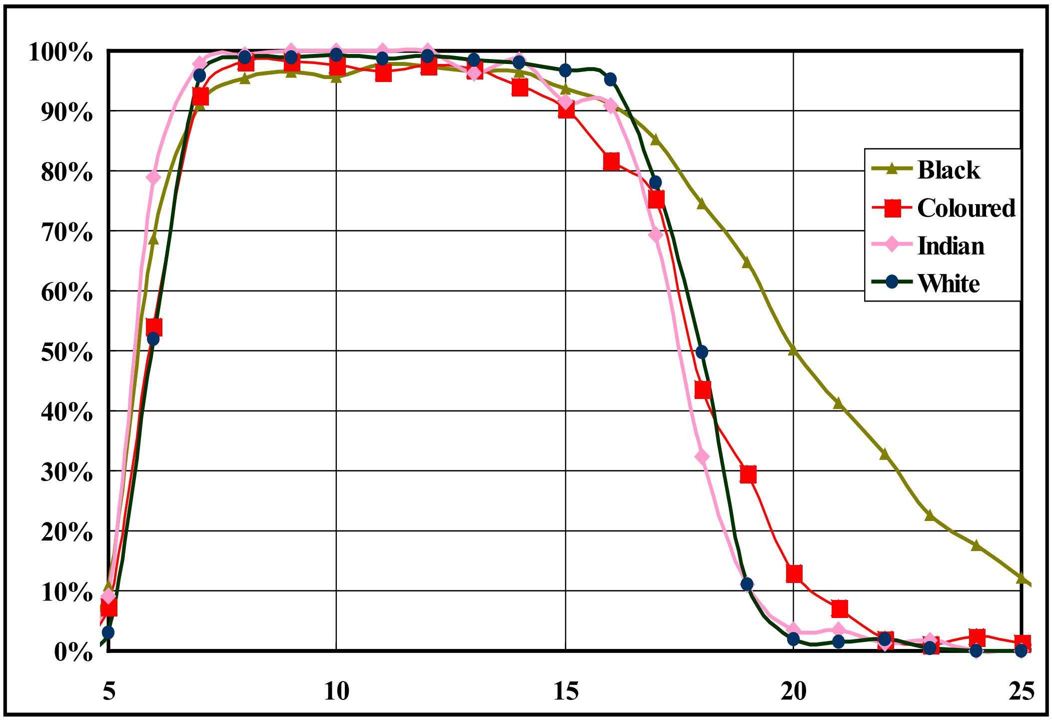
Overall, households headed by women tend to be poorer than those headed by men. For example, the income and expenditure survey of 1995 revealed that for the country as a whole, 37% of rural households headed by women were among the poorest fifth of households, compared with 23% of rural households headed by men, 15% of urban households headed by women, and 5% of urban households headed by men (Budlender, 1998: 5). Female-headed households were not much worse off in terms of service provision (water, electricity, sanitation and even telephones) than other households, in stark contrast; there were hardly any discernible differences in educational levels of adult males and females. Although large gender differences exist in the labour market (male unemployment at 12,7% was well below the 14,9% of women), this differential was much smaller than for the country as a whole. There is also greater labour force participation among women in the Province. There would, no doubt, be further differences between urban formal and urban informal settlements. The reasons for the tendency for women-headed households to be poorer include lower average earnings of women, lower rates of paid employment, and the fact that many of the woman-headed households are headed by pensioners. For example, in 1996, 75% of male household heads in the Western Cape were employed, compared with only 49% of female heads in the Province. Conversely, 13% of male household heads were retired or pensioners, compared with 23% of female heads. Among African households, the picture is different. While there is still a big difference in the percentage of male and female heads who are employed (71% and 55% respectively), the percentage of older heads is relatively similar for male and female heads (6% and 10%).

Earnings for women are lower than for men, and lower for rural than urban within both male and female groupings. Census '96 revealed that 8,8% of Western Cape urban men had monthly incomes of R500 or less per month, compared with 17,9% of urban women, 40,4% of rural men, and a massive 71,4% of rural women. Among rural African women, the percentage was even higher, at 74,4% (Statistics South Africa, 1999). Some of these patterns can be explained by the fact that women are more likely than men to be employed in domestic work and other parts of the informal sector. Domestic and agricultural workers are among the lowest paid employees in the economy. Government has recently introduced a minimum wage for domestic workers. Census '96 found that, overall, 28% of the Western Cape households were headed by women.

Education: An international perspective

At one level, school enrolment, South African education is performing quite satisfactorily. Net enrolment (percentage of relevant age group actually at school) has grown to close on 100% of the age group up to 15 (Figure 1); thereafter there is a considerable drop-out, but enrolment rates are fairly good for a developing country and access to education at primary and secondary level is no longer a problem even among the poor. According to World Bank figures[7], South African net enrolment in the primary school ages rose from 68% in 1980 to 100% in 1997, and at secondary school age from 62% to 95% in the same period. However, at tertiary level enrolment rates are still low even for a developing country, and strongly differentiated by socio-economic status, geography and race.

Figure 1: Net school enrolment (proportion at school) by age and race, South Africa 1995



***Source**: October Household Survey 1995*

Increased enrolment has ensured satisfactory growth in educational attainment over time. Figure 2 shows that South African educational attainment levels (years of education completed) have grown quite well for the black population, even during the days of apartheid, and the attainment

[7] World Bank. 2001. *World Development Report 2000/1*. World Bank: Washington, D.C.: 285, Table 6

gap between the race groups has narrowed. In a comparative investigation into educational progress and income distribution by race groups, Lam[8] contrasts the South African performance with the situation in Brazil, where there has not been similar progress in the educational attainment of the black population. But this ignores the quality issue. In the South African case differential school quality leads to vastly different pass rates at the matriculation level; pass rates of black and white pupils who reach matric have been estimated at 42% and 98% respectively[9] – a similar differential as before the political transition.

Table 10: International data on educational attainment

		Local		OECD																										Developing countries							
	Country	RSA	Western Cape	Australia	Austria	Belgium	Canada	Czech	Denmark	Finland	France	Germany	Greece	Iceland	Ireland	Italy	Japan	Luxembourg	Korea	Netherlands	New Zealand	Norway	Portugal	Spain	Sweden	Switzerland	Turkey	U.K.	United States	Argentina	Brazil	India	Indonesia	Malaysia	Paraquay	Thailand	Uruguay
Barro-Lee	No schooling	9.4	3.7	2	1	5	2	1	0	0	1	4	6	2	3	14	0	0	9	3	0	1	14	4	2	5	31	3	1	6	22	52	44	17	10	20	3
	Primary	3.3	4.4	25	32	49	20	35	34	31	48	28	52	48	35	43	31	0	18	32	34	12	61	56	18	26	47	41	8	53	59	28	33	34	64	62	54
	Secondary incomplete	13.4	19	28	25	20	16	33	8	14	15	31	7	21	26	21	30	0	16	32	18	22	8	16	15	24	9	27	20	15	7	10	9	19	9	5	23
	Secondary complete	5.9	7.9	21	31	10	13	22	39	35	22	23	24	16	20	12	17	0	36	14	9	44	6	13	44	31	7	13	24	10	5	6	10	24	10	4	9
	Tertiary	2.8	5.5	24	12	16	49	9	19	19	15	15	11	13	16	12	22	0	21	19	39	21	10	12	21	15	7	16	47	16	8	5	4	7	8	9	10
	Average years			10	8.4	8.6	11	9.3	9.9	9.8	7.9	9.6	8.1	8.4	8.8	6.6	9.4	0	10	9	11	12	4.5	6.6	11	10	4.6	9	12	8.1	4.3	4.2	7.7	5.7	5.7	5.7	6.9
OECD	Below upper secondary			47	31	47	25	17	38	35	32	16	57	0	53	65	0	71	40	39	41	19	80	72	25	18	77	24	14	73	75	92	81	67	67	5.7	73
	Upper secondary			29	62	29	28	73	42	45	50	61	25	0	27	27	0	18	42	39	34	53	9	12	46	61	15	54	53	18	16	3	15	26	19	87	12
	Tertiary			24	8	25	47	11	20	21	19	23	17	0	20	8	0	11	18	22	25	29	11	16	28	21	8	21	33	9	9	6	4	7	14	3	14

Source: *This table was taken directly from Barro-Lee International Data on Educational Attainment: Updates and Implications and adjusted with data taken from Statistics South Africa. Census 96.*

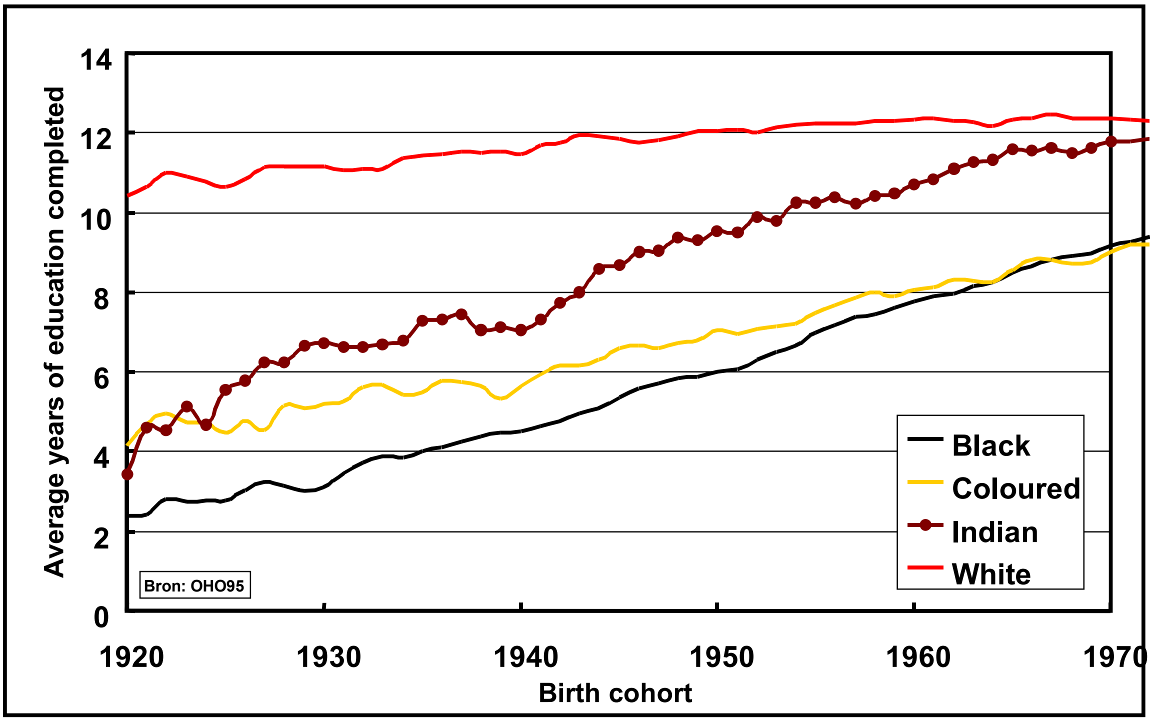
Reference: International Data on Educational Attainment: Updates and Implications. Barro J and Wha Lee J. 2000.

Table 10 shows the percentage levels of schooling of the populations in different countries, including South Africa and the Western Cape province. The data is based on populations of countries aged 25 and older (based on Barro-Lee data) and 25 – 64 years for the Organisation for Economic Cooperation and Development (OECD) countries. The data coming from two sources, namely Barro-Lee International Data and OECD data, has to be interpreted with caution and was adjusted according to 1996 census figures for South Africa and the Western Cape. However, it serves as a useful tool to compare data between OECD and developing countries and compare the two sets of data.

8 Lam, David. 1999. *Generating Extreme Inequality: Schooling, Earnings, and Intergenerational Transmission of Human Capital in South Africa and Brazil*, Research Report 99-439, Ann Arbor: Population Studies Center, University of Michigan.

9 Van der Berg, Servaas. 2002. *Education, poverty and inequality in South Africa*. Paper to the Conference of the Centre for the Study of African Economies. Oxford. March**;** Van der Berg, Servaas & Burger, Ronelle. 2002. *Education and socio-economic differentials: A study of school performance in the Western Cape.* Mimeo. University of Stellenbosch: Stellenbosch.

Figure 2: Years of education completed by birth cohort and race, South Africa



***Source**: October Household Survey 1995*

International comparisons, though scarce, support the conclusion that the vast majority of South African pupils fare far worse than their counterparts in most middle-income or even low-income countries for which such data is available. One source of international comparison is the Mathematics Literacy Attainment (MLA) data, which relates to Grade 4 achievement in literacy and numeracy in a number of African countries, with South Africa performing worst of the 12 African countries in numeracy and coming third to last of these countries in literacy.

Another source of data for international comparison relates to the data: Third International Mathematics and Science Study (TIMSS). South Africa participated in some of the 1995 and 1999 modules of this study, with extremely disturbing results:

- In 1995, for the final year of secondary school, South Africa was placed 21st and last in Mathematics Literacy and Science Literacy, scoring on average 352 compared with the average of 500 in the two disciplines. The second to last country on the list, Cyprus, had a score of 447. Most countries participating, though, were developed countries or middle-income countries from the former Soviet Bloc.

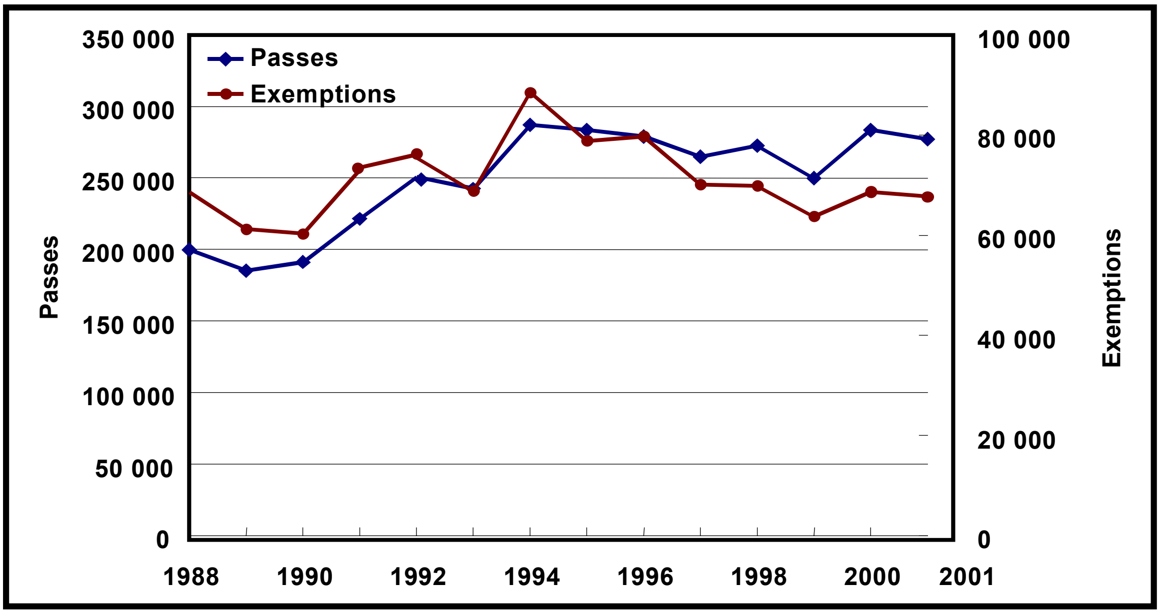
- Also in 1995, for Grades 7 and 8, South African scores were again lowest in both grades and for both disciplines (Mathematics and Science), but this time there were around 40 participating countries (41 in Grade 8, 39 in Grade 7), including a few more developing countries. Again the South African Mathematics score (around 350) as well as the Science Score (around 320) were far below the international average of 500.
- In 1999, similar studies were conducted for Grade 8 in 38 countries, including many middle-income developing countries (e.g. Morocco, Philippines, Chile, Tunisia, Turkey, Indonesia, Iran, Thailand and Malaysia). Again South Africa had the lowest scores in both Mathematics and Science, viz. 275 and 243 compared with the 500 for all participants. The second lowest Mathematics score was 60 points above South Africa's, and in Science 80 points more.

These figures show that South Africa has a considerable backlog to catch up to attain levels of educational quality which would allow the country to perform well in international economic competitiveness. This relates especially to the two areas for which international comparative data is available, viz. Mathematics and Science, both important for the labour market. Improvement in the school system is essential for improving the quality and productivity of the labour force, and the prospects for economic growth, which are crucially influenced by technological competitiveness.

Education: A national perspective

Education in South Africa already takes a large share of national resources, placing the country near the top of the international league as to proportion of national resources (GDP) devoted to education spending. Yet, because of a very poor conversion of inputs into outputs in the education system – in numeric terms educational outputs are only weakly related to educational resources – educational output remains poor. Since the transition to democracy, resources for school education have increased considerably and large fiscal shifts have taken place to poorer schools, yet numbers of successful matriculants or of those matriculating with university exemption are stagnating or declining (Figure 3).

Figure 3: Matriculation passes and exemptions, South Africa 1988-2001

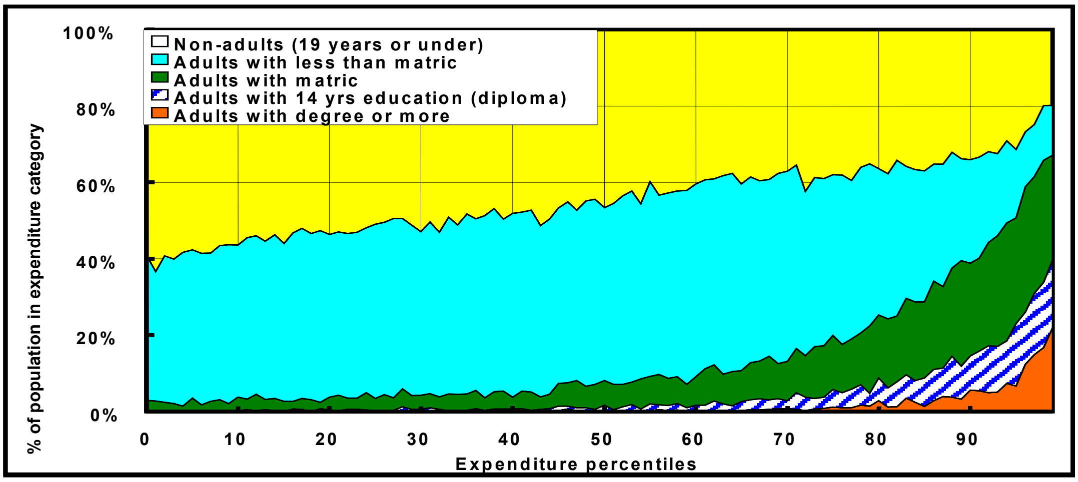


Source*: Servaas van der Berg: Education in the Western Cape, September 2002*

There are also serious quality problems with educational output. This is apparent from high matriculation failure rates (indicating lenient promotion policies at lower educational levels may be a problem), from poor performance in international tests, and from a small minority of matriculants electing to do subjects such as Science and Mathematics that are crucial to further technical education required by the labour market.

Education has a crucial role in reducing socio-economic inequalities, but many poor pupils attend schools which underperform as measured by matriculation results, particularly in subjects most sought in the labour market. Figure 4 below shows that the small number of relatively well-educated adults, e.g. those with a degree, are concentrated in the upper part of the income distribution. Their numbers are not being augmented rapidly, however, mainly because few pupils leave the school system adequately prepared for university studies.

Figure 4: Distribution of total population by education over national expenditure percentiles, 1995



Source*: Calculated from OHS/IES95*

Another way of considering this data is presented in Table 11, which shows that adults with degrees constitute only 1,6 % of the total South African population, yet they constitute 10,0 % of the population in the top decile of the expenditure distribution.

Table 11: Share of non-adults and adults in various educational categories in the population and in the various expenditure categories, 1995

Share of educational group in:	Non-adults %	Adults with less than matric %	Adults with matric %	Adults with diploma (14 yrs) %	Adults with degree or more %	Total popu-lation %
Total population	44,0	40,8	10,0	3,2	1,6	100,0
Poorest 20% (Quintile 1)	56,3	40,4	2,6	0,2	0,0	100,0
Poorest 40% (Quintiles 1 & 2)	53,4	42,5	3,2	0,3	0,0	100,0
Quintile 2	50,5	44,6	3,8	0,4	0,1	100,0
Quintile 3 of SA population	45,1	47,3	5,9	0,9	0,2	100,0
Quintile 4 of SA population	38,3	46,5	11,1	2,9	0,6	100,0
Richest 20% (Quintile 5, Deciles 9 & 10)	31,6	26,2	24,8	10,5	6,4	100,0
Richest 10% (Decile 10)	28,2	19,2	28,5	13,5	10,0	100,0

Note: Non-adults are here defined as people below 20 years of age
Source: *Based on data from OHS/IES95*

The South African educational system appears to face serious problems in motivating many teachers and pupils. For this reason the national Department of Education has introduced a programme to improve the culture of learning and teaching in schools – an acknowledgement of serious incentive problems in schools.

Education: A Western Cape perspective

This is fully covered in the Expenditure Review 2002. Suffice it to say that, given the importance of education for both poverty reduction and economic development, and in the face of the public resource constraints in the Western Cape, the sector reform strategy should focus on:

- Increasing efficiency in the use of resources, improving the quality of education services and reducing the identified inequities in access, particularly in basic education.
- Improving the quality of education through introduction of a new system of student assessment and monitoring (shifting focus from input to output/outcomes).
- Improving budgeting and transparency in the resource allocation process on the basis of number of students rather than the conventional notion of physical norms.
- A system of accountability to the population of the Western Cape.

Converting provincial income into longevity, literacy and education for the mass of the population can be conceived as good poverty reduction performance.

HIV/Aids

Aids is a disease that takes people in the prime working years of life, rather than in their old age, negatively affecting households through the loss of the main income earners. Aids has a direct cost in the form of health care benefits and related expenditure of afflicted individuals and households, and secondly, an indirect cost through employee absenteeism, lower productivity and lost skills, reduced markets for goods and services and increased production costs. There is a direct impact on the health system and an indirect impact on the macroeconomy and economic growth and the labour market. Aids in the long-term will undermine social and economic development because it undermines the determinants of development, which include social and human capital and savings. The socio-economic impact of HIV/Aids also combines to create a vicious cycle of poverty in which affected households are caught up.

HIV/Aids has a gender bias. Women are more vulnerable than men to infection, both because of their biology, and because of social relations which place them at a disadvantage in relationships and thus less able, for example, to insist on the use of a condom. Women also tend to become infected at an earlier age than men. Women bear the main responsibility for caring for children. For example, the October household survey of 1995 revealed that about two-fifths of children under seven years of age were living with both parents, whereas 42% were living only with their mother, compared with 1% living only with their father[10]. The gendered impact of HIV/Aids goes further than this, in that women usually hold primary responsibility for caring for those who are ill in their own homes and the community, more broadly. HIV/Aids will add to the unpaid work burden already borne by women in bearing, caring and rearing family and community members. This added burden will in many cases make it difficult for women to earn income, and thus add to their relative poverty burden.

The Western Cape is fortunate in having the lowest level of HIV prevalence of all the provinces in the country. Nevertheless, the model of the Actuarial Society of South Africa (ASSA) puts the number of HIV infected people in the Province at over 200 000 in mid-2002. The ASSA model estimates the number of children orphaned by HIV/Aids in the Western Cape at over 10 000 in 2002. The number will increase, as the total number of Aids orphans in the country is predicted to peak only at around 2015 unless there are serious interventions.

[10] (Budlender, 1998: 7 in Budlender)

Housing

The resources available to the provincial government are insufficient to address the current housing backlog and as a result only a few households will benefit from public housing provision, leaving many poor households unserved. Despite the shortage of financial resources, low-cost housing provision can still be enhanced by the effective management of the housing market. There are a host of demand, supply and institutional interventions that could lead to positive housing outcomes. The key is to choose appropriate interventions that enable the public and private sector to address the needs of the poor. The aim of housing sector interventions should be to enhance the performance of the housing sector as a whole and to leverage the limited resources for housing to the greatest extent possible.

On the demand side, government can intervene by providing secure tenure. A lack of secure tenure leads to under-investment in housing and reduces housing quality. Conversely, secure tenure is associated with high levels of investment in construction and housing. Insecure tenure results in poor environmental health and thus increased vulnerability for the poor, as households are less likely to invest in improving the quality of their local environments.

Another key factor that impacts on housing provision is households' access to private sector funding. Access to funding increases the ability of households to accelerate their purchase or construction of housing. The provincial government can explore ways of improving access to market-related housing finance and encourage the private sector to assist with the provision of low-cost housing finance.

On the supply side, housing outcomes can further be improved by influencing the housing regulatory framework, which deals with building codes, infrastructure standards and land use. Cumbersome regulation impacts negatively on housing investment. The responsiveness of supply to shifts in the demand for housing impacts on housing outcomes. If regulation is simple and bureaucracy is reduced, then supply can adjust quickly to changes in housing demand. A key supply-side constraint has been the slow release of spatially appropriate land for low-cost housing developments.

Under-investment in infrastructure such as roads, water, sanitation and drainage also impacts on housing provision. Inadequate infrastructure planning and investment lead to spatial distortions and poor environmental health with an increase in waterborne and waterwashed diseases. Housing outcomes can be improved by providing and upgrading basic infrastructure in slum and other informal settlements and by opening up urban land for residential development. Existing communities should be encouraged to participate in the planning and building of infrastructure projects.

From an institutional perspective there is a need for an integrated approach to housing delivery. Too often there has been a mismatch between the providers of bulk and connector infrastructure (the municipalities) and those primarily responsible for housing development. One way of improving the co-ordination between municipalities and housing authorities is to allow those municipalites which are capable of providing housing to act as housing providers for their areas. This would improve service delivery.

Examination of data from Census ’96 reveals that 62% of both black male- and female-headed households lived in informal dwellings, compared with 7% or fewer of households in each of the other race groups. In terms of housing, the race of the household head is an important factor. As the number of male-headed households is far greater than the number that is female-headed, there are more poor women living in male- than female-headed households. Within these male-headed households, women may be in a less strong position than women in similar households headed by women because of differences in relative power of women and men. The category of women-headed households includes both single-person households consisting of one aged woman, a larger household consisting of a single mother and her children, as well as a range of other configurations. Each of these households might have needs which government must address, but the needs are not the same.

Examination of data from Census ’96 reveals that women were the largest income recipients in over one-fifth of Western Cape households. Some of these women are social grant recipients, and the welfare of the household then depends on the efficiency with which the Social Development and Poverty Alleviation department does their job. Many other women earn their income by working. Both their own welfare and that of their households then depends on these women being able to earn as much as possible under favourable conditions.

Major inequalities characterise the housing sector: for white the average floor area per person is about 33 m^2, whereas for blacks it is 9 m^2 in formal housing and a meagre 4 - 5 m^2 in informal housing.[11] Overall it is clear that the current housing situation does not offer the poor an asset that can reduce their vulnerability and promote their socio-economic development.

From an international perspective Africa is regarded as the continent with the highest rate of urbanisation. The latest trends at international level is to move away from only providing housing with an integrated developmental approach that includes human settlement development and the eradication of poverty. In this regard, South Africa’s role as leader on the African continent has therefore become more important, with greater expectations for the international arena.

[11] Inequality in South Africa – Summary Report (part 2)

Crime

South Africa has experienced an increase in its overall crime rate of 1,83% between 2000 and 2001, as shown in Table 12:

Table 12: Percentage change in total crime per province 2000 – 2001

PROVINCE	TOTAL		
	2000	**2001**	**% CHANGE**
1 WESTERN CAPE	310 640	321 966	3.51
2 GAUTENG	519 977	527 188	1.3
3 EASTERN CAPE	209 546	207 548	-0.96
4 KWAZULU-NATAL	302 364	307 079	1.53
5 NORTH WEST	120 316	122 749	1.98
6 FREE STATE	114 376	117 178	2.39
7 MPUMALANGA	110 703	112 633	1.71
8 NORTHERN PROVINCE	99 224	104 760	5.28
9 NORTHERN CAPE	50 830	51 318	0.95
TOTAL RSA	**1 837 976**	**1 872 419**	**1.83**

In the Western Cape, however, the crime rate has increased by 3,5% during the same period, which is the second highest recorded percentage increase among all the provinces in South Africa. Apart from the Northern Province's 5,3%, the remaining provinces have experienced an average increase in crime of close to 1,7%.

Table 13 shows the figures for 21 categories of crime in South Africa compared with the Western Cape for the period 1994 – 2001:

Table 13: Crime per police area: January to September 1994-2001

Crime per police area : January to September 1994-2001										
Crime category	Republic of South Africa					Western Cape province				
	1994	1997	2000	2001	% CHANGE 2000-2001	1994	1997	2000	2001	% CHANGE 2000-2001
Violent Crimes					**6,86**					**7,77**
Murder	19 672	17 709	15 457	15 054	-2,68	1 869	2 269	2 380	2 385	0,21
Attempted murder	20 100	20 516	20 134	21 207	5,06	1 837	2 681	2 956	2 819	-4,86
Robbery with aggravated circumstances	62 877	50 406	79 561	87 610	9,19	4 957	3 865	7 572	9 743	22,28
Other robbery	23 380	37 841	61 468	65 766	6,54	4 149	5 342	9 449	10 919	13,46
Public violence	**987**	**831**	**822**	**607**	**-35,42**	**226**	**114**	**168**	**158**	**-6,33**
Illegal strikes	**230**	**40**	**24**	**28**	**14,29**	**7**	**5**	**1**	**0**	**100,00**
Sexual Offences					**0,37**					**5,75**
Rape and attempted rape	29 399	37 905	37 556	37 711	0,41	3 750	4 862	4 752	4 626	-2,72
Intercourse with a girl under the prescribed age and/or female imbecile	571	412	384	371	-3,50	137	125	74	97	23,71
Indecent assault	2 798	3 715	4 718	5 060	6,76	805	1 156	1 559	1 575	1,02

Crime per police area : January to September 1994-2001										
Crime category	Republic of South Africa					Western Cape province				
	1994	1997	2000	2001	% CHANGE 2000-2001	1994	1997	2000	2001	% CHANGE 2000-2001
Cruelty towards and ill-treatment of children (excluding sexual offences, assault and murder)	1 893	1 742	1 814	1 813	-0.06	534	358	490	495	1.01
Kidnapping	2 830	3 007	3 670	3 521	-4.23	261	291	367	399	8.02
Abduction	2 039	1 874	2 558	2 225	-14.97	175	230	433	397	-9.07
Assault					-0.74					-4.55
Assault with the intent to inflict grievous bodily harm	147 551	166 775	192 750	188 961	-2.01	23,602	23,175	26,530	25,858	-2.60
Common assault	137 303	146 174	181 056	182 110	0.58	24,514	27,397	36,240	34,028	-6.50
Burglary					0.31					3.27
Burglary and attempted burglary : business premises	67 098	65 515	68 103	67 279	-1.22	11,034	11,625	12,638	12,689	0.40
Burglary and attempted burglary : residential premises	167 983	183 239	221 326	223 045	0.77	25,568	29,045	38,639	41,163	6.13
Stock-theft	32 507	32 022	30 763	30 668	-0.31	1,504	1,406	1,598	1,451	-10.13
Shoplifting	50 158	47 717	50 455	49 661	-1.60	8,123	7,483	8,336	8,300	-0.43
Theft					3.90					7.18
Theft of motor vehicles and motorcycles	77 429	74 476	74 657	74 281	-0.51	6,985	6,872	8,632	9,335	7.53
Theft out of or from motor vehicles	136 056	130 199	147 286	151 277	2.64	24,783	28,161	35,797	38,819	7.78
Theft not mentioned elsewhere	283 815	285 907	404 256	426 065	5.12	43,481	45,741	68,942	73,507	6.21
Arson	8 616	7 353	6 523	6 657	2.01	647	655	718	648	-10.80
Malicious damage to property	89 314	93 088	100 681	103 495	2.72	14,218	16,011	19,212	20,124	4.53
All fraud, forgeries, malappropriations, embezzlements, etc	47 308	48 402	51 828	46 600	-11.22	6,688	7,762	6,611	6,743	1.96
Drug-related crime	36 211	32 926	35 171	36 756	4.31	9,204	8,113	10,930	9,758	-12.01
Driving under the influence of alcohol or drugs	19 581	17 926	18 422	18 774	1.87	3,289	3,274	3,353	3,541	5.31
Illegal possession of firearms and ammunition	8 071	9 389	11 159	11 264	0.93	615	1,180	1,634	1,651	1.03
Explosives Act	404	101	68	88	22.73	25	15	5	3	-66.67
Hijacking					-5.60					9.62
Carjacking (accounted for under robbery with aggravating circumstances)	-	9 869	11 191	11 186	-0.04	-	236	430	547	21.39
Hijacking of trucks (accounted for under robbery with aggravating circumstances)	-	3 138	3 624	2 843	-27.47	-	32	143	140	-2.14
Robbery of cash in transit (accounted for under robbery with aggravating circumstances)	-	181	179	111	-61.26	-	15	16	9	-77.78
Bank robbery (accounted for under robbery with aggravating circumstances)	-	353	312	325	4.00	-	25	35	39	10.26
TOTAL			1 837 976	1 872 419	1.83			310,640	321,966	3.51

The following observations can be made from Table 13:

- Of the identified categories, 11 have shown an increase over the period. The highest increases are those pertaining to bank robberies (10,3% per annum), violent crimes (7,7%), hijacking (9,6%), kidnapping (8%), theft (7,2%), sexual offences (5,6%) and driving under the influence of alcohol (5,3%). Other categories, such as burglary, malicious damage to property, fraud and illegal possession of firearms, have seen increases of less than 5%.
- Ten of the identified crime categories have shown decreases. The incidence of illegal strikes, robbery of cash-in-transit and explosive acts have declined considerably since 1994, i.e. by 100%, 77,8% and 66,7%,

respectively. Other crimes have experienced smaller decreases, including public violence (6,3%), abduction (9,1%), assault (4,6%), stock-theft (10,1%), shoplifting (0,4%), arson (10,8%) and drug-related crime (12%).

When the crime situation in the Western Cape is compared with that for the country as a whole, some salient facts emerge. The increase in the number of violent crimes in the Western Cape was 7,8% between 2000 and 2001, compared with 6,9% for the country as a whole, indicating a higher incidence of crimes such as murder, attempted murder, robbery with aggravating circumstances, and other robberies in the Western Cape. Kidnapping in the Western Cape increased by 8%, compared with 4,2% for SA, with the number of hijackings also increasing more rapidly than in the rest of the country. Surprisingly, drug-related crimes in the Western Cape have decreased between 2000 and 2001, whereas at national level they increased by 4,3%. Overall, the Western Cape has experienced higher increases in critical categories of crime than the rest of South Africa, indicating a need for appropriate interventions aimed at turning around the trends shown above.

Poverty and crime

Poverty – in its absolute and relative forms – lies at the root of the crime in the Western Cape. Several recent studies have confirmed the high levels of poverty in the Province, coupled with an unacceptably high degree of inequality between the different population groups and local municipalities.

Poverty exists when individuals and households have no or limited access to the labour market or to any other income-earning opportunities. The decision to do crime is often a rational one on the part of the individual in question. Such an individual would compare the net present value of the expected stream of income for committing a crime, with that of starting a new business, borrowing money or begging. The crime option does of course carry a high risk, depending partly on the probability of being arrested, prosecuted and punished, which in turn depends on the extent and efficacy of the judicial system and police services in particular. But the alternative options – borrowing, begging and starting an own business – also carry high risks: borrowing from informal money-lenders is both costly and hazardous; starting own businesses tends to have high failure rates and begging has become more competitive and thus less remunerative.

Although the long-term solution clearly lies in the eradication of poverty, there are important short-term steps that need to be taken – two of which suggest themselves from the foregoing discussion. Policies need to be put in place to strengthen access to finance and facilitate small business development among poor communities in the Western Cape.

On the macroeconomic effects of crime

High levels of crime may deprive a region of the critical resources it needs to achieve such as sustainable GGP growth – skills, investment and tourism. When escalating crime scares off tourists and investors and drives away skills GGP for the province will be effected negatively, and the number of job opportunities fewer, than in the absence of crime. High crime levels also place extra strain on the public sector generally, and on those politicians and departments responsible for public safety, health care and social work in particular.

Microeconomic effects

Crime ultimately impacts on all individuals living in or visiting the country or Province. It does so both directly and indirectly. Its direct effects are felt, first and foremost, by victimised households and by the families of criminals. Individuals who experience the direct brunt of crime incur various direct and indirect costs, including additional medical, psychiatric and reparations expenses. Such expenses often have to be defrayed from an already limited household budget, thus further impoverishing victimised households.

Likewise, criminal activity by a member of a family may temporarily enrich that family, but when that member is injured, arrested or prosecuted, such activity will impoverish the family, especially if the criminal was the sole breadwinner, putting extra strain on other members, often forcing them to do crime as well, and splitting up the family. Many younger members of such families end up being 'street children', having to beg or do crime themselves in order to survive. Crime therefore impacts negatively on the social existence of such individuals.

But the impact of crime goes well beyond victimised and criminalised households. With escalating crime rates and high risks of becoming a victim, most households spend large amounts of their income on private protection to ensure the safety and security of their loved ones. Further pressure is put on individuals' economic situation when they seek to secure their own and their families' lives, health and physical possessions through the purchase of insurance. This gives the individual a sense of comfort when confronted by the inevitable hand of crime.

Crime ultimately affects the social fabric of the community. If drug trafficking can be linked to "organised" or "syndicated" criminal activities, for example, then it follows that crime also lies at the root of the many social problems associated with increased levels of drug abuse in the broader community.

Migration

The main engines driving migration are:

- A search for income and jobs. This is the primary engine of migration, pushing people out of poorer regions and pulling them toward better-off regions. This engine driving people from one place to another operates on the basis of a migrant's experience in the sending area and the migrant's knowledge of the receiving area. In other words good knowledge about possible receiving areas is crucial, but migrants may be able to obtain only incomplete information.
- A search for superior infrastructure, land and improved housing, water and sanitation, electricity, and better transport (known as economic infrastructure); as well as better school and health facilities (known as social infrastructure);
- Political factors;
- Anxieties about a secure living environment;
- Deteriorating state services;
- Differing perceptions.

There are two issues about the second engine worth mentioning. The **first** is that the first engine never shuts down completely. Thus, if a poor household migrates to a town and settles in a new state-subsidised housing scheme, this household may well leave this town and the new house if household members remain unemployed and hear about job opportunities elsewhere. The **second** issue is that, for poor households driven by this second engine, the positioning of state-subsidised housing schemes and their associated infrastructure will influence the direction of migration flows, for this infrastructure often acts as an attractor for households forced to leave impoverished regions.

The Western Cape is currently a net receiving province - estimated on balance at 48 000 people per annum. This represents an increase due to in-migration of more than one per cent of the total population. The main reasons are the perceived better job opportunities, more accessible and effective infrastructure, and superior quality of life available In the Western Cape. These differences are particularly striking with regard to the two neighbouring provinces of the Eastern and Northern Cape, where much of the migration originates. Economies are stagnant and infrastructure inferior in these regions, leading to continuing in-migration streams of poor individuals and families, which are shallow from the underpopulated Northern Cape and powerful and fast from the heavily populated Eastern Cape. This second stream may well represent the largest and most rapid demographic flow in South Africa at the moment. Simultaneously, the Western Cape continues to offer work, infrastructure and a quality of life perceived to be good enough to attract better-off individuals and families arriving from a much larger national and international region. There is no good reason to believe that these trends will change in the near future.

For historical reasons, the present migration patterns of the three main ethnic populations of the Province are reasonably coherent although differing sharply from one another. The long-established coloured population is deeply rooted in both Cape Town and its hinterland districts. However, in metropolitan and non-metropolitan areas a growing divide seems to be developing between these two sub-populations, with diminishing exchange and a consequent loss of family ties. An increase in provincial in-migration from neighbouring provinces is currently underway towards non-metro districts, whereas, largely from Cape Town, substantial out-migration to the north of the country of skilled workers and labour migrants appears to be taking place. The white population also has an important deeply-rooted sub-population, with many being migrants from far afield. Many whites accordingly appear to have no roots any longer, migrating both into, and between, metro and non-metro areas within the Western Cape. Net white flows are clearly into the Province. A large majority of adults in the African population are recent Western Cape residents with roots in the Eastern Cape, in the former Transkei in particular. Simultaneously, it appears that a new non-metropolitan sub-population is establishing itself in the east of the Province. In so far as this is continuing, the common perception of gradual gravity-flow migration from the Eastern Cape down the South Coast and on to Cape Town is being replaced by one of two split flows, one towards Cape Town and the other to selected districts. Overall, net African flows, which are high are into the Province.

Poor households will continue to migrate in search of better opportunities within the Cape System (between and within the three provinces of Eastern, Northern and Western Cape). Not only job opportunities but state-provided infrastructure will act as important magnets in this System. Accordingly, state spatial planning needs to be regional in scope, synthesising demographic and socio-economic data from the various urban and rural areas within the Cape System. Such spatial planning implies systematic exchange of information and ongoing cooperation between district councils at sub-provincial level, and between the three provinces. Without such exchanges and cooperation, the influence of state-led infrastructural provision is bound to have at least some negative consequences for the sustainability of the multiple livelihood strategies of many migrating households.

In the light of the large annual net in-migration flow into the Western Cape, it is apparent that the provision of housing and its associated infrastructure as well as of town and regional planning will need to extend beyond existing backlogs. Such provision may be quantified in terms of estimates given above. Steps also need to be taken to launch a state planning process aimed at establishing a major urban area in the Southern Cape.

Within the Province, substantial population exchanges continue between Cape Town and provincial districts. These are significantly higher for the african and white populations than for the coloured population. Simultaneously, most districts have recently been suffering from economic recession in the agricultural sector and, in the case of the West Coast, in manufacturing and commerce. This has led to substantial population instability in non-metropolitan areas, driving coloured farm workers toward provincial towns and African and white non-metropolitan residents toward the metropole.

The impact of Fiscal Policy

The impact of fiscal policy in the Province can be broken down into three main areas:

1. Higher levels of expenditure stimulate changes in the levels of economic activity.
2. Social equity, or the extent to which there is a redistribution of income, or a reduction in levels of inequality.
3. Spatial or interregional inequality, or the extent to which there is a redistribution of resources or growth between deprived and economically wealthier areas of the Province.

Measuring whether the actions of our provincial government have had an effect on any or all of these areas are fraught with enormous difficulties. Some of the reasons include, *inter alia*, insufficient data, incomparability of data collected and the lack of indirect measures.

<u>Spatial equity</u>

With the exception of the black population, there is not that much income inequality *within race groups* in the Province. Inequalities *in regions*, however, are considerable, as Table 5 (on page 10) shows. But differential per capita incomes and distribution patterns in different regions lead to different poverty experiences in the various regions. Table 6 (page 11) shows that poverty is most endemic in the Central and Klein Karoo, with affluence being concentrated in the CMA and the Winelands. Regional inequalities are considerable, particularly with regard to **severe or ultra-poverty**. Despite lower poverty rates, the more populous Winelands, Southern Cape and Cape Metropolitan Area house most of the poor.[12]

Because of a progressively competitive and fluid environment and diminishing resources, the provincial government, in the past year, has had to reconsider the way in which services are to be rendered. These new demands have compelled the Province to pay more attention to growth and poverty reduction strategies and good governance issues.

The policy options that the Western Cape government may wish to follow are as follows:

[12] Using an alternative estimate, household poverty levels fluctuate between 21% in the Central Karoo and Breede River District council areas and 20% in the Klein Karoo District Council Area, to only 9% in the Cape Metropolitan Area. (Alderman, Harold; Babita, Miriam; Lanjouw, Peter; Makhatha, Nthabiseng; Mohamed, Amina; Özler, Berg & Gaba, Olivia. Combining census and survey data to construct a poverty map of South Africa. Ch. 2 <u>in</u> Statistics South Africa. *Measuring poverty in South Africa*. Pretoria: Statistics South Africa: 5-52)

- Sustainable growth; and
- Pro-poor policies that are biased to benefit the poor, even if they do not have a well-defined effect on economic growth.

There is a strong association between growth and poverty. Causality can be bi-directional (growth translates into lower poverty indicators, but significantly high poverty rates can impede growth, owing to insufficient savings, to waste of human potential, and to social unrest and political instability).

Economic growth in the Province

Fiscal policy may influence economic growth by:

- Efficiently providing basic public services, physical capital and human capital; and
- Financing its own activities in a manner that:
  - Minimises the negative effects on the efficiency with which private physical and human assets are combined in production;
  - Minimises distortions of private accumulation and labour incentive, and of economic activity more generally (technical advance).

An example of government expenditure that influences economic growth is expenditure on public works programmes that are discussed in the following paragraph.

Infrastructure

There are both direct and indirect benefits of ***infrastructure*** investment for poverty alleviation in the Western Cape relating to *rehabilitation, upgrading, reconstruction and construction*. In particular the Community Access Road Programme is specifically directed at combining infrastructure investment, poverty alleviation, increasing employment in rural areas and enhancing access. This has a beneficial effect on producer prices, employment and market opportunities, all of which have a real effect on the income of the poor and on growth. Although empirical research does not exist in the Province, economic development could have the following benefits; urban revenues increase, access to and from areas is improved, small-scale industry that creates employment is stimulated and higher levels of income for the poor are generated.

A pro-growth strategy requires a policy climate, which stimulates the acceleration of job creation; increases income-generating opportunities and creates a favourable climate for stimulating investment and productivity. This strategy also underscores the need to integrate a comprehensive provincial education and training system and the current industrial policy direction.

Good governance

Policy-making should be marked by not only good substantive outcomes (such as rising living standards) but also "good" process (accountability, transparency). Rajkumar and Swaroop in their article: "Public Spending and Outcomes: Does Governance Matter?", find that public health spending lowers child and infant mortality rates in countries with good governance. The results also indicate that, as countries improve their governance, public spending on primary education becomes effective in increasing primary education attainment. These findings have important implications for enhancing the development effectiveness of provincial public spending and should address:

- A broader approach to accountability, which focuses on improved accounting, reporting, and information systems, clearly defined financial and fiscal rules, setting fiscal and financial rules and targets, and defining a clearer role for government and, more specifically, the provincial Treasury.
- Micro-level accountability programmes that entail transparency-enhancing and monitoring measures. Transparency strengthens the incentives and pressures for public sector performance while lowering the scope for corruption, reducing transaction costs, and improving the efficiency of resource allocation.

The search for maximum cost-effectiveness on the planning and expenditure side, effecting policy priorities, and achieving efficient delivery of public services, requires a broad review by the provincial government of its governance issues. This not only concerns expenditure control, but also the quality of expenditure decision-making and budgetary systems, and government systems of accounting and financial reporting. Building capacity and establishing a database to make assumptions more plausible and improve public service delivery, both in terms of technical efficiency (producing more while employing the same amount of resources) and allocative efficiency (in terms of generating the right mix of outputs to achieve national and provincial objectives) thus become a necessity.

In summary, economic growth, good governance and poverty reduction largely go together. Measures to tackle one objective in isolation will not suffice. What is therefore needed is synergy and an interactive approach so that the poor can benefit by good governance and economic growth for the Province. Interplay between fiscal policy and institutional arrangements is increasingly important. In particular, incentives embedded in the institutional arrangements for fiscal management need to be strengthened so that policies, resources and outcomes can be better aligned, and fiscal adjustments are consistent with qualitative considerations.

From a macroperspective the challenge facing the provincial government is not so much a question of redistributing resources to the poor to promote equity. This option will only be feasible if substantial increases in real expenditure growth occurs. However, this is not viable in the current economic climate of rising inflation and reduced economic growth in South Africa and severe expenditure demand pressures experienced at all levels of government.

The emphasis for the future is, **firstly**, to ensure that synergy within all provincial departments is improved and that the same goals are attained by all the departments. **Secondly**, the strengthening of good governance between all spheres of government is needed to ensure that provinces and local authorities abide by and support the sound and prudent fiscal policy that is set at national level. What is important in this regard is not only to play an interactive role but to support government at national level and all other provinces and other spheres of government. **Thirdly** it must be accepted that the Western Cape, as also South Africa as a whole, is part of a global village and cannot succeed in implementing changes if externalities are not taken into account and managed in advance. This again calls for the support of a wide spectrum of role players, be they in government or the private sector. This ultimately leads to the **fourth** challenge, i.e. to increase the skills base of the population of the Province so as to become more competitive for the future and strengthen human capital resources in the short term, thereby reaping the benefits for the Province and the country over the medium to longer term.

Without improving the investment climate, the Province will be unable to achieve economic growth. Provincial Treasuries, unlike the national Treasury, currently do not have the tools of taxation or borrowing to increase expenditure levels. Expenditure levels are thus usually increased in specific sectors by means of reprioritisation, with concomitant reductions in other sectors or the same sector. Private investment chances to raise expenditure levels are remote.

Conclusion

The external environment in which the Province operates is very complex and its challenges are immense. Changes in fiscal policy are also very difficult to implement because of the limited resources and fiscal tools that are at the Province's disposal.

The following recommendations are made for the medium-term, or next four to five years:

Firstly, the four strategic objectives, as contained in the provincial Treasury's Strategic Plan for 2002/03 – 2004/05, should be driven forward with the assistance of outside expertise. They include:

- Determine and evaluate the socio-economic needs that exist in the Province.

* Develop key service delivery outcome indicators for the provincial departments.
* Determine the gap between the socio-economic needs and the key service delivery indicators.
* Determine spending priorities for the provincial government.

Secondly, synergy with all role players within the Province and other spheres of government must be enhanced to ensure good governance.

Thirdly, it must be accepted that the available database to analyse, and make meaningful recommendations on, the socio-economic and macroeconomic variables has to be improved as a matter of urgency. This will place the provincial government in a more informed position to make better decisions and ensure better allocative efficiency. Again the assistance of outside expertise must be emphasised.

Fourthly, it must be accepted that the provincial government has limited capacity to bring about change. The challenge to stimulate economic growth and reduce poverty and inequalities in the medium to longer term is no easy task. This can only be achieved within a realistic framework that is affordable and attainable over time.

Fifthly, it must also be accepted at political level and by the bureaucrats that, in order to achieve success, tough decisions are to be taken at present if a better future for the Province is to be envisaged in the longer term.

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3

LOCAL GOVERNMENT

Abbreviations:

LGTA	:	Local Government Transition Act, 1993 (Act 209 of 1993)
MFMB	:	Local Government: Municipal Finance Management Bill (as introduced in the National Assembly as a section 75 Bill: explanatory summary of Bill published in Government Gazette No. 22641 of 31 August 2001)
Structures Act	:	Local Government: Municipal Structures Act, 1998 (Act 117 of 1998)
Systems Act	:	Local Government: Municipal Systems Act, 2000 (Act 32 of 2000)
DPLG	:	Department of Provincial and Local Government
Constitution	:	The Constitution of the Republic of South Africa, 1996 (Act 108 of 1996)
PFMA	:	Public Finance Management Act, 1999 (Act 1 of 1999, as amended by Act 29 of 1999)
SALGA	:	South African Local Government Association
IMFO	:	Institute of Municipal Finance Officers
DORA	:	Division of Revenue Act, 2002 (Act 5 of 2002)
TCF	:	Technical Committee on Finance
DFA	:	Development Facilitation Act, 1995 (Act 67 of 1995).

Introduction

This chapter on local government does not contain a trend analysis or projections of municipal budgets, revenue and expenditure, nor does it express an opinion on the financial sustainability of municipalities in the Western Cape province. The approach is premised on the notion that provincial treasuries have, in terms of the LGTA, no legislated mandate to monitor or oversee municipal financial matters. In the Western Cape, this legislated mandate currently resides with the provincial Department of Local Government.

From the abovementioned perspective the purpose of this chapter is twofold. **Firstly**, to highlight the possible implications of legislation in the making which will affect local government budgeting and financial management, namely the effect the MFMB might have on various key role players and their readiness to deal with the possible implications in a coherent and constructive manner. **Secondly**, to discuss the legal and financial framework for the transfer of functions and powers (and the possible implications) from provincial government to local government and vice versa.

The methodology followed was to synthesise important elements of legislation without going into a great deal of detail, while other legislation that has a more peripheral impact on local government financial management has not been analysed. The analysis highlights the implications of the new legislative framework for local government budgeting and financial management. It further identifies crucial legislated provisions enacted which regulate the transfer of functions and powers between spheres of government and signify the complexities thereof.

The legislation affecting local government management requires exploration. Managers operating within the three spheres of government need to familiarise themselves with the new context of local government financial management, especially bearing in mind the new competencies required of them. This chapter is a modest attempt to stimulate the thought processes on the complexities and implications of the financial and fiscal landscape within which local government will have to operate.

Local Government in transformation

Since 1994, local governments have gone through three stages of transformation, starting with the pre-interim phase in 1994 and 1995, the transitional phase from the November 1995 elections to December 2000, and now the final phase of newly demarcated municipalities following the December 2000 elections. This transformation aimed to make municipalities more accountable, financially sustainable and able to deliver critical services to all residents. This is in line with the constitutional vision of the role of local government and the policies outlined in the 1998 White Paper on Local Government. The purpose of the White Paper on Local Government was to democratise local government, bolster service delivery capacity, enhance integrated development planning and management, direct organisational transformation towards these ends, and develop legislation for a fiscally sustainable approach. Subsequent legislation like the Structures Act and the Systems Act took these policies further. The MFMB and related budget reforms, driven by the national Treasury and by DPLG's Property Rates Bill, are intended to add impetus to this process.

Changes included rationalising 843 municipalities to 284, enacting new legislation on operational and financial management, and reassigning powers and functions in respect of municipalities outside the metropolitan areas.

The different categories of municipalities that were established in terms of the Constitution and the Structures Act are as follows:

Category A : A metropolitan municipality that has exclusive executive and legislative authority in its area.

Category B : A local municipality that shares municipal executive and legislative authority in its area with a district municipality within whose area it falls.

Category C : A district municipality that has municipal executive and legislative authority in an area that includes more than one municipality.

Presently there are:

6 Category A – Metropolitan Municipalities;
231 Category B – Local Municipalities;
47 Category C – District Municipalities.

Government policy on the division of powers and functions between district and local municipalities is set out in the Municipal Structures Act, as amended by the Municipal Structures Amendment Act. Chapter 5 of the Act deals with the functions and powers of municipalities, the division of those powers and functions between district and local municipalities, and any adjustments to this division.

Section 83 of the Act clearly provides that all municipalities have the functions and powers assigned to them in terms of sections 156 and 229 of the Constitution. Section 84 of the Act (as amended) effectively divides these powers and functions between district and local municipalities, in that section 84(1) lists the powers and functions allocated to district municipalities, while 84(2) allocates all the remaining powers and functions to local municipalities.

Section 84(3)(a) (as amended) empowers the Minister, after consulting with the relevant Cabinet Minister and MEC for local government, to authorise a local municipality to exercise powers and perform functions relating to the matters mentioned in the following section:

84(1)(b) Potable water supply systems;

84(1)(c) Bulk supply of electricity, which, for the purposes of such supply, includes the transmission, distribution and, where applicable, the generation of electricity;

84(1)(d) Domestic waste-water and sewage disposal systems, and

84(1)(i) Municipal health services.

In the run-up to the 2000 municipal elections it was decided to maintain the *status quo* in respect of the four national functions so as to ensure that service provision was not disrupted and that the transfer of staff was restricted to a minimum. In eight of the nine Provinces, the MECs have maintained the *status quo* in respect of all the other section 84(1) functions and section 84(2) functions.

The authorisations were gazetted in November 2000 and provided for the newly established local municipalities to "*perform the functions and exercise the powers mentioned in section 84(1)(b), (c), (d) and (i) of the Structures Act, or any aspect thereof, to the extent that they were performed by the transitional local councils or transitional rural councils mentioned in the definition of 'disestablished municipality' in the section 12 notice*" (Government Gazette No. 21807, 28 November 2000).

In the Western Cape Province the MEC has allocated all section 84(1) functions except for firefighting, which will in all probability be allocated at the end of November 2002, for implementation 1 July 2003. With regard to section 84(2) functions all have been allocated. The Provincial Gazettes No. 5639 dated 4 December 2000 and No. 5703 dated 26 April 2001, refer.

As a result of these *status quo* authorisations, newly established local municipalities continue to perform the functions that disestablished local municipalities performed within their areas. In almost all cases this has resulted in multiple municipalities being responsible for the same power and function within a single municipal area.

The Ministry of Provincial and Local Government commissioned a national review of the powers and functions as well as a fresh study of key criteria for allocations. It is expected that the Minister of Provincial and Local Government will soon report on the outcome of this review and communicate his final decision on the division between powers and functions.

The outcome of the local government process should be well-managed municipalities, representative of their residents, developmental in their approach, and financially sustainable in extending service delivery. To achieve this, municipalities and other spheres of government must base their efforts on the principles of cooperative governance and intergovernmental relations as contained in Chapter 3 of the Constitution. Section 154(1) of the Constitution requires local government and provincial governments, by legislative and other measures, to support, and strengthen the capacity of, municipalities to manage their own affairs, to exercise their powers and to perform their functions. In addition, they need to be alert to the financial pressures of transformation and the fragile trade-offs and choices these pressures require. The challenge is to effectively manage the cost of transformation.

The Municipal Finance Management Bill

Objectives

The management of local government financial matters is currently contained in section 10G of the LGTA. This section, which was intended to regulate municipal finances during the transitional phase, will soon be repealed by the enactment of the MFMB. As such, the MFMB is a critical element in the final transformation phase of local government currently underway within the policy framework established by the White Paper on Local Government and the various pieces of legislation that emanated from it.

The purpose of the MFMB is to:

- Regulate municipal financial management;
- Set requirements for the efficient and effective management of the revenue, expenditure, assets and liabilities of municipalities and municipal entities;
- Define responsibilities with regard to municipal financial management;
- Determine a financial management governance framework for municipal entities;
- Put in place a municipal borrowing framework;
- Provide for a framework for financial emergencies.

The MFMB is intended to enforce new financial management procedures and accountability processes uniformly in respect of all municipalities, from the big metropolitan councils to the smallest, fiscally weak rural municipalities. It is aimed mainly at modernising municipal budgeting and financial management and introducing a governance framework for municipal entities. In addition, it aims to restore municipal access to capital markets by clarifying the legislative framework and the rights of borrowers and lenders. It further extends the philosophy of financial accountability to municipalities and also strengthens their borrowing powers. It facilitates the restructuring of municipalities through the formation of corporate entities, although it prohibits the creation of entities for investment and speculation or to avoid regulations.

The MFMB sets requirements for the efficient and effective management of the revenue, expenditure, assets and liabilities of municipalities and municipal entities and also defines responsibilities concerning municipal financial management. It covers a wide range of issues, including national and provincial supervision, municipal revenue and budgets, municipal debt, budget and treasury processes, council responsibilities, and financial misconduct.

Like the PFMA, the basic philosophy is to improve financial management and to foster greater transparency. The MFMB seeks to bring local government in line with the financial management objectives of the PFMA. The PFMA, which came into effect in April 2000, sought to modernise financial management of government departments and entities, and make public sector managers more accountable. The MFMB defines the relationships between the different spheres of government in terms of local government financial management. Section 216 of the Constitution envisages uniform treasury norms and standards for all spheres of government. Norms and standards for financial management in the national and provincial spheres of government were provided by way of the PFMA. The MFMB will provide uniform treasury norms and standards for the local sphere of government.

Legislative progress

The MFMB, which transforms the financial management of municipalities and extends accountability to all spheres of government, was tabled in Parliament on Monday, 4 February 2002. Soon thereafter it was referred to the Portfolio Committee on Finance, which since then held public hearings and had various deliberations. Among those who presented their comments at the public hearings were the Office of the Auditor-General, SALGA and IMFO.

The enactment of the MFMB is subject to the approval of a constitutional amendment. The thrust of the constitutional amendment is to regulate provincial supervision of and intervention in local government and, where this fails, national intervention. The Constitution of the Republic of South Africa Third Amendment Bill is currently under deliberation by the Justice and Constitutional Development Portfolio Committee. It is not certain when the constitutional amendment will be promulgated.

After various comments and views had been taken into account, many chapters of the MFMB were amended, rewritten and reworked by the Portfolio Committee on Finance, while work on other chapters is still in progress. It is envisaged that the MFMB will be enacted during the 2002/03 financial year, with phased implementation starting in the 2003/04 financial year.

Unfunded mandate

In terms of section 35 of the PFMA, draft national legislation that assigns an additional function or power to, or imposes any other obligation on, a provincial government must, in a memorandum to be introduced in Parliament with that legislation, give a projection of the financial implications of that function, power or obligation to the province. It requires that national legislation which has financial implications be costed. Notwithstanding this legislative requirement, there is no empirical evidence that national legislation in the form of the MFMB has been costed. If complied with, it would substantially reduce the risk of unfunded mandates being imposed on provincial governments.

Comprehensive costs based on new draft national legislation that confers new obligations, functions and powers on provinces are invariably significant, and provinces face the challenge to manage these costs so as to contain them generally. The provincial Treasury's view is that the national Treasury must as a matter of urgency cost the MFMB in order to determine its financial implications with a view to increasing the provinces' share of revenue collected nationally to cover the related cost of the MFMB. Failure to increase the provincial share will result in an unfunded mandate and create moral hazard. This is of particular concern in the case of the Western Cape province, as an environment of declining intergovernmental transfers (phasing in the equitable share) from national government prevails.

Provinces' revenue-raising powers compared with those of the national and local spheres of government are limited and rely heavily on the provincial share of revenue collected nationally. Failure to adjust the provincial share upwards will jeopardise the implementation of the MFMB.

Implications for the provincial Treasury

As alluded to earlier, the provincial Treasury has no powers in terms of section 10G of the LGTA regarding municipal financial matters. In the absence of such a legislated mandate, the provincial Treasury is hindered from constructively involving itself in the broad financial and economic matters of municipalities.

The MFMB is set to change the mandates of the respective key role players. The national view is that provincial treasuries are best placed to exercise financial oversight over local governments for the following reasons:

- Provincial treasuries have a fiscal perspective, as opposed to a strictly functional perspective, and are expected to be involved in this function in a like manner as with all other functions within provinces.
- Weaknesses in financial management are not just a capacity issue but structural and require a fiscal perspective. This will only be attained through the effective involvement of provincial treasuries.
- Provincial treasuries have experience in implementing budget and financial management reforms and are therefore perhaps better placed to play a supporting and nurturing role in this respect as far as local government is concerned. Further, the monitoring framework and information flows require treasuries to replicate the monitoring role played by national treasury *vis-à-vis* provincial finances in terms of monitoring and understanding local government budgets.
- Greater involvement with local government budgets will enable provincial treasuries to play a guiding and coordinating role in respect of infrastructure. Unless local and provincial (and national) infrastructure planning is better co-ordinated, the current dysfunctional approach will continue to undermine government's capacity to deliver.
- To the extent that a province transfers funds to municipalities, provincial treasuries are best placed to publish such information per provincial department (as they are required to do in terms of the DORA).

The experiences of provincial treasuries in budget and financial management reform over the past five years stand them in good stead in helping to build a viable local sphere that is responsive, fiscally stable and sustainable. Because of their specific financial experience in implementing reforms, provincial treasuries can support local government budget and financial transformation. Provincial treasuries need to play a guiding and supporting role in monitoring municipal budgets for the credibility and soundness of their finances, in the early diagnosis of problems, and in rendering timely support together with provincial departments of local government. Provincial treasuries should therefore work closely with their departments of local government to enhance financial management in the sphere of local government. Indeed, as the system develops and capacity is created in provincial departments, both local government departments and treasuries should be encouraged to visit municipalities together to ensure that both are able to understand the real pressures facing the municipalities.

The role of provincial treasuries is therefore rooted in their fiscal perspective, their own experiences in fiscal management, and their direct interest in the economy of their province. It is along these lines that the following functions normally fall within the terrain of treasuries:

- assess the budget adopted and implemented by a municipality is a balanced budget;
- help municipalities introduce three-year budgets;
- modernise the municipal budgeting process and system;
- monitor finances at a departmental and municipal level;
- improve the fiscal framework by mitigating province-wide economic, fiscal and financial risks;
- co-fund selected services;
- assess the income projections and assumptions made by municipalities in their budgets;
- assess the sustainability of capital investment in infrastructure and services, including provision made for repairs and maintenance;
- ensure coordination of infrastructure investments;
- ensure that adequate provision is made in expenditure estimates to allow for the cash collection of service charges and rates due;
- help contain personnel costs;
- guide municipalities – alongside other stakeholders – in attracting investments to grow the economy;
- facilitate the coordination of infrastructure so that local decisions are aligned with provincial ones, and vice versa;
- play a supportive role in capacity-building initiatives targeted at municipal finance management, accounting, budgeting and reporting;
- assist in monitoring and consolidating grants made to municipalities by provincial line departments.

Until such time that the MFMB has been promulgated it would be premature to express an exact and accurate opinion on the division of functions between treasuries and the Provincial Local Government departments. Provincial treasuries, together with the local government departments, should identify the real budgetary pressures facing municipalities. They need to ensure that municipalities which have difficulty collecting their revenues are supported appropriately to do so and are not, for example, rewarded with more funds. Better coordination between the two will also ensure that the Budget Forum is more effective in articulating the needs of the local sphere.

In anticipation of the enactment of the MFMB and the powers it indirectly grants provincial treasuries with regard to municipal financial matters, the Western Cape provincial Treasury has established a local government component within its organisational structure. Currently the approved staff establishment consists of 1 post of Deputy Director and 2 posts of Senior Financial Administration Officers, of which the latter two are still vacant. Apart from the powers possibly derived from the MFMB, the national Minister of Finance, in executing his legislated mandate, may delegate assigned national Treasury powers to provincial treasuries. It is envisaged that the Minister of Finance will follow the route of delegating most of these national treasury powers or duties to provincial treasuries. This will test the human resource capacity of provincial treasuries, with accompanying financial implications.

Initiatives by the Technical Committee of Finance (TCF) are underway for the appropriate restructuring of provincial treasuries, among others to establish organisational synergy between national and provincial Treasuries. The TCF has produced a working document, adopted by the Budget Council, which expresses their views on how synergy could best be established.

The Western Cape provincial Treasury has taken advantage of the benefits of Collective Agreement 7 of 2002 (Public Service Coordinating Bargaining Council), which serves as a framework within which national and provincial departments may restructure with the intention of becoming more efficient and effective. In particular, it should make departments more responsive to the needs of the communities, especially communities that are short of resources. Hence, the provincial Treasury has engaged in a twofold process, which should bolster knowledge, skills and the human resource capacity. Against this background it is believed that from a human resource perspective the local government component will benefit to tackle the uncharted territory of the local government financial and fiscal landscape head-on.

In terms of the LGTA the national Minister of Finance could have delegated national treasury powers and duties to provincial treasuries, but chose not to do so. On account of uncertainties surrounding the exercise of treasury powers by provincial treasuries, the response of the latter in respect of the development of skills and competencies to assess and monitor local government budgets has been delayed. Mindful of this, it is critical that provincial treasury staff should be trained by national Treasury on their existing budget database. This training can be supplemented by appropriate service providers.

Financial implications/resources

As alluded to previously, there is no empirical evidence that the implementation of the MFMB has been costed. The Western Cape Treasury holds strong views that only empirical information will reveal the comprehensive cost. As the information is not available, it prevents all three spheres of government from developing a proper understanding of the financial implications of, and fiscal adjustments involved in, the MFMB.

These circumstances present a strong case for national Treasury to provide funding, increasing the equitable share to provinces equivalent to the cost of the MFMB. Failure to do so can cause the implementation of the MFMB to be applied inconsistently across provinces.

In this regard the principle applies that funds must be made available to give effect to new national policy on regulatory or legislative changes. Provinces must thus be wary that the advent of the MFMB does not constitute another unfunded mandate, putting unnecessary pressure on provincial financial resources.

Implications for the provincial Department of Local Government

Currently municipal finances are monitored by the provincial Department of Local Government on a broad-based level and only a few financial indicators are monitored on a quarterly basis. The legislative mandate to request these indicators is contained in Regulation R.1536, issued in terms of section 10G of the LGTA. The only other financial monitoring by the Department of Local Government is to ensure compliance by municipalities with current financial legislation and prescripts.

The MFMB proposes that the responsibility for the monitoring of municipal finances as well as assistance with municipal capacity building in respect of municipal finances rests primarily with the national Treasury. However, it makes provision for the delegation of national Treasury powers, among others to the head of a provincial department. It remains to be seen to what extent these powers will be delegated to the provincial department responsible for local government.

The various monitoring functions, as described in the MFMB, are new functions and not functions currently performed by the provincial Department of Local Government.

A limited number of functions with regard to municipal finances are assigned directly in the MFMB to a MEC for local government.

The role and responsibility of the provincial Department of Local Government in respect of the financial management of municipalities are not limited to the functions assigned to it in the MFMB as it has a much broader monitoring and support mandate which might not be affected by the MFMB.

From a fiscal adjustment perspective, the current resources available to the provincial Department of Local Government and equally so to the Provincial Treasury, i.e. personnel, infrastructure and financial resources, need to be taken into account when the MFMB is implemented.

Implications for the municipalities

The following important issues should be taken into account when evaluating the impact of the MFMB on municipalities:

- Role: The effect that the Bill will have in terms of the manner in which municipal personnel execute their functions and account for their responsibilities.
- Resources: The effect that the Bill will have on human resource capacity, financial resources and infrastructure.

Only a detailed exposition of resources at the disposal of local government and how these resources will be affected by the implementation of the MFMB will indicate the level of readiness of local government to implement the MFMB. It would therefore be premature to express a view on the readiness of local government until such an analysis is undertaken.

Conclusion: Municipal Finance Management Bill

The ambitious competencies that the envisaged Municipal Finance Management Act intends granting provincial governments will strain the resources of provincial governments. In practice, the level of readiness of provincial governments to deal with these in a constructive and coherent manner is an area requiring a considerable amount of additional work. Although the provincial Treasury, after restructuring, should be robust enough to shoulder its share of the burden, successful delivery would be jeopardised without the assistance of national Treasury and the provincial Department of Local Government. Assistance will have to come in the form of financial resources, human resources, guidance, training and infrastructure. In this regard the way forward is proposed as follows:

(a) Steps should be taken to ensure that the MFMB is properly costed.

(b) The imposing of a possible unfunded mandate by the national government on the provincial government needs to be resisted.

(c) In the case of function shifts due to the delegation of assigned functions, the funds – follow – function – principle needs to apply.

(d) There needs to be a clear shift in the vertical division of funds between the three spheres of government in favour of the provincial government.

(e) Conditional grants should not be considered as an option as this restricts flexibility in resource allocation and the discretion of the provincial government to allocate funds where most needed.

(f) Affected provincial departments need to incorporate the implementation of the envisaged Municipal Finance Management Act into their strategic planning to position themselves for implementation of the legislation in question. Likewise municipalities, as the main "beneficiaries" of the MFMB, should prepare themselves for the implementation of this legislation.

(g) The national Treasury and DPLG must be persuaded to develop implementation plans in concert with provincial treasuries and local government departments.

The transfer of functions and powers from the provincial sphere of government to the local sphere of government

The transfer of functions and powers in perspective

The final phase of local government restructuring is characterised by:
- The interim remaining in force of section 10G of the LGTA;
- The implementation of the Structures Act and the Municipal Systems Act;
- The establishment of a new local government dispensation as provided for by the Constitution.

The full implementation of Chapter 7 of the Constitution towards the establishment of the new local government dispensation in December 2000, fundamentally affects the provincial government's relationship with the local sphere of government regarding powers and functions.

Schedule 4 of the Constitution lists the functional areas of concurrent national and provincial legislative competence, while Schedule 5 lists the functional areas of exclusive provincial legislative competence. Both Schedules 4 and 5 are divided into two Parts, A and B, of which Parts B relate to local government executive matters. However, certain functions listed in Parts A of Schedules 4 and 5, which are concurrent and exclusive functional areas of provincial legislative competence, have historically been performed and are currently still being performed by municipalities. These functions include, among others:
- Maintenance and upkeep of provincial roads
- Administration and management of libraries

- Administration and management of museums
- Rendering of primary health care services
- Nature conservation
- Pollution control
- Disaster management
- Housing.

Generic difficulties experienced with current agency services or other service-level agreements that departments have entered into with municipalities, either formally or informally, are often problematic, *inter alia*, for the following reasons:
- The definition of services to be rendered is messy.
- The setting of service standards and accountability measures is vague or completely lacking, resulting in a gap between delivery expectations and actual services rendered.
- The financial obligations and responsibilities of the principal and agent are undefined, resulting in conflicting financial claims. The services actually delivered and the actual cost to municipalities are often unrelated to the services outlined in the agreement or the resources transferred, resulting in conflicting interpretations and escalating deficit claims.
- Agreements are mostly not in line with new legislative requirements regarding financial accountability and obligations of principals.
- Agreements do not reflect the new post-election municipal institutional structures or functional division.

Taking the aforementioned into account, the provincial government is currently not geared to adequately comply with its financial accountability responsibilities. Municipalities, likewise, given the new local government dispensation, seem to deliver services and incur expenditure on provincial functions without proper authorisation, risking the integrity of municipal budgets and exposing themselves to possible unauthorised expenditure.

Given the level of capacity and the current limited resource envelope (financial, human and capital) at provincial level, makes it extremely difficult and practically impossible for the provincial government to fulfil its constitutionally mandated functions. Therefore, prudent consideration should be given to this situation, which should be regulated by means of formal transfers of the affected functions to local government utilising the various mechanisms provided for in the Constitution and supporting legislation.

The Minister of Finance and Economic Development, during the delivery of his Budget Speech 2002, requested that any initiatives contemplated to transfer functions and powers should be placed on hold to allow for people assessment and research into the available options. In pursuance of this statement the provincial Treasury on 30 April 2002 requested departments to put on hold all initiatives to transfer functional areas of exclusive provincial legislative competence to local government.

Notwithstanding this request, some departments expressed the need to press ahead with negotiations with municipalities about agreements to transfer functions and powers or to order existing service arrangements or relationships.

Against this background a *practical and sustainable framework* within which the transfer of functions and powers between provincial and local spheres of government should be managed needs to be developed with urgency.

The legislative framework

The distribution of powers and functions between the national, provincial and local spheres of government is set out and entrenched in the Constitution.[1]

Chapter 3 of the Constitution, entitled "Co-operative Government", establishes the framework for the cooperative relationship between the three spheres of government, and it is worth noting that the overriding principle is that of *independence* of each of the three spheres. The powers and functions accorded to municipalities in terms of the Constitution are re-iterated in section 83 of the Structures Act.

The Structures Act further provides for a division of powers and functions between district and local municipalities.[2] Historically, municipalities have performed a number of functions that in terms of the Constitution, are now seen to be allocated to provincial governments or the national government (e.g. the maintenance and upkeep of provincial roads, the administration and management of libraries and museums and the management of primary health care facilities). Since the enactment of the triad of legislation governing local government[3], local authorities believe that they have not been constitutionally mandated to continue performing functions on behalf of provincial government.

However, the Constitution and the complementary local government legislation (especially the Structures and Systems Acts) provide for a number of mechanisms to regulate the transfer of functions from the provincial sphere to the local sphere of government and vice versa. These mechanisms can therefore regulate existing intergovernmental relationships and agreements concerning service delivery and ensure uninterrupted and sustainable service delivery. They include *assignment, delegation, and transfer by way of an agency agreement*.[4]

The mechanism concerned will govern the process, as each has a legally prescribed process with distinct consequences. The appropriate mechanism in

1 Sections 44,85,104, 125 and 156
2 Section 84 of the Structures Act
3 The Structures Act, the Local Government: Municipal Systems Act, Act 32 of 2000, and the Local Government: Municipal Demarcation Act, Act 27 of 1998.
4 There has been debate on the relevance of section 197 of the Labour Relations Act, Act 66 of 1995, as an option. This provision provides for the transfer of a contract of employment from one employer ("the old employer") to another ("the new employer"). Section 197 has nothing to do with the transfer of the function. It concerns the staff (employment issues) when a business or undertaking is sold or transferred as a going concern.

any given case will depend largely on the facts of each scenario, including the nature of the function or power to be assigned, the capacity and willingness of the municipality to perform it, and the willingness of each sphere to honour the spirit and principle of cooperative government.

Delegation

The principle of delegation of powers and functions from one sphere of government to another is contained in section 238 (a) and (b) of the Constitution. The power to delegate does not automatically exist. It must be either provided for expressly in legislation, or implied. When powers are transferred by delegation, "the authority and duty to exercise them, *and* the responsibility for their exercise are transferred in full."[5]

Delegation in the context of section 238 (a) involves the transfer by an "*executive organ of state"* of any power or function that is to be exercised or performed in terms of legislation, to another "*executive organ of state"*, *provided* the delegation is consistent with the legislation concerned.

The Constitution does not define the term "executive organ of state", but section 125 read with section 239 (b) permits the interpretation that a Member of the Executive Council (a provincial Minister) is an executive organ of state. Section 238 (a) therefore allows the delegation by a provincial minister to a local government counterpart, or vice versa, of any power or function to be exercised or performed in terms of legislation, as long as the delegation is consistent with the legislation concerned.

The procedure to be followed will invariably be prescribed by the legislation concerned. The party that has the discretion to delegate brings about the delegation by notice in writing. It can be revoked at any time, unless otherwise provided for.

Agency

Agency in the context of section 238 (b) involves the exercise of any power or the performance of any function by one executive organ of state for another. This will effectively allow a provincial minister to contract a local government counterpart to perform any function or exercise any power on his or her behalf.

Delegation and agency are perfectly distinguishable. Delegation, on the one hand, is limited by the legislation that provides for it, whereas agency is not. A provincial minister, for example, may not delegate a power if the legislation governing the exercise of that power does not provide for it to be delegated. A

[5] Baxter "Administrative Law", page 432

further distinguishing factor can be found in the procedure and consequences of each mechanism.

The transfer of the exercise of a power or the performance of a function on an agency basis is ordinarily effected by way of a written agency agreement (a contract) between the parties. Delegation, on the other hand, is effected by the delegating authority compiling and signing a written notice to this effect.

In an agency agreement, the initiating authority remains the principal, and as such retains the authority and the responsibility for the exercise of the power. The agent assumes the duty to perform, subject only to the terms of the agency agreement and the ability of the initiating authority to ensure compliance. A major problem with agency agreements is the obvious dilution of accountability and the concomitant probable loss of efficiency.

Assignment

The Constitution refers to "assignment" in a number of different contexts, for example, the assignment of "the administration of a matter,"[6] the assignment of "legislative authority"[7], the assignment of "any power or function exercised or performed in terms of an Act."[8] It is not always easy to distinguish the practical differences between them. This is further complicated by an inconsistency in the language used in both the Constitution and the complementary legislation. The terms "assignment" and "delegation" appear to be flexibly used as a concept covering the notion of transferred authority or function.

Assignment in the normal course has a permanent scope in that the risk is transferred permanently, and the assigning authority divests itself of all responsibility for and authority over the matter concerned.

Assignment of legislative authority

Section 104(1)(c) of the Constitution confers on a provincial legislature the power to assign any of its legislative powers to a municipal council in the province. This can be done by way of proclamation by the premier, or by legislation. If the assignment of a legislative power to municipalities generally takes place by way of provincial legislation, then a process of consultation with the provincial ministers about finances and with local government, as well as publication of the draft legislation, is mandated by section 9 of the Systems Act.

The Systems Act further compels the provincial minister initiating the legislation to take appropriate steps to ensure funding and capacity-building initiatives if:

[6] Section 156(4)
[7] Section 104(2)
[8] Section 126

- the assignment imposes a duty on the municipality concerned;
- the duty is not listed as a local government matter in part B of Schedules 4 and 5 of the Constitution;
- the performance of the duty has financial implications for the municipality concerned.

In addition, the provincial minister must request the Financial and Fiscal Commission ("FFC") to make an assessment of the financial implications of the legislation.

If the assignment of legislative authority by way of provincial legislation is to a specific municipality (as opposed to municipalities generally), then a similar process is prescribed by section 10 of the Systems Act.

The effect of such a legislative assignment is permanent. There is no provision for a conditional assignment of legislative powers, or one that allows the provincial parliament to recall or revoke the assignment. The provincial parliament divests itself totally of that authority. The risk is transferred together with full authority and responsibility. This accords with the ordinary interpretation of "assignment" within a legal context.

Assignment of any power or function in terms of legislation

Section 126 of the Constitution authorises a member of a provincial cabinet to assign any power or function that is to be exercised or performed in terms of an Act of Parliament or a provincial law to a municipal council.

This in effect allows for the assignment of any power or function authorised in a piece of legislation. The provision stipulates that it must be in terms of an agreement, and must be consistent with the Act that authorises the exercise or performance of the power or function concerned. It takes effect upon proclamation by the premier.

There is uncertainty around the issue of the permanency of this kind of assignment, as the scope (at least conceptually) allows for a combination of legislative and executive powers to be assigned, provided they are authorised by legislation. The assignment of legislative powers is permanent.

Section 126 of the Constitution must be read in conjunction with section 10 of the Systems Act. Section 10 governs assignments to specific municipalities by way of provincial legislation or an agreement in terms of section 126 of the Constitution.

If the assignment in terms of section 126 imposes a duty on the municipality, then the provincial minister initiating the assignment is obliged to consult the national minister responsible for local government before an agreement is concluded.

If, in addition, the assignment places a duty on the municipality that falls outside the local government matters listed in part B of Schedules 4 and 5 to the Constitution and the performance of that duty has financial implications for the municipality concerned, the provincial minister must take appropriate steps to ensure sufficient funding, and capacity-building initiatives.

Assignment of the administration of a matter

In addition to the assignments referred to above, section 156(4) of the Constitution **mandates** the national government and provincial governments to assign to a municipality the administration of a matter listed in Part A of Schedules 4 or 5 if:

- the matter would be administered most effectively locally, and
- the municipality has the capacity to administer it.

This kind of assignment must take place by agreement. The administration of such matters cannot therefore, be forced on unwilling municipalities, or on those willing but without the capacity/infrastructure/expertise to fulfil the function.

This provision does not intend an interpretation of assignment in the normal course. The authority to legislate on such matters will remain with the national and provincial governments. The administration of the matter is what will be assigned. To attach an interpretation consistent with "assign" in the normal course would lead to an absurd result. **Firstly**, the effect would be a permanent divestment of the provincial or national government's authority over the Part A matters, which would effectively constitute an amendment of the Constitution, and the Constitution cannot be amended by way of interpretation. **Secondly**, section 156 (4) permits the assignment to be "subject to any conditions". Assignment in the ordinary course is not conditional. It is permanent.

With an assignment in terms of section 156 (4), the extent of the risk and responsibilities transferred versus the risk retained will depend largely on the particular circumstances of each situation, and should be spelt out in the agreement that gives effect to the assignment.

Unlike an assignment in terms of section 126 of the Constitution or a delegation in terms of section 238 of the Constitution, the agreement provided for in terms of this provision does not necessarily have to be concluded by an executing authority. The agreement will be between the provincial government of the Western Cape and a particular municipality. Any official authorised to represent the provincial government will therefore be entitled to conclude the agreement with the municipality concerned.

Contextual comments

What is abundantly clear from the legislation is that the Constitution, read with the complementary local government legislation, intends the expansion and development of local government powers, but in cooperation with, and with the support of, provincial and national governments.

The objectives of local government are to provide democratic and accountable government for local communities, ensure the sustained provision of services, promote social and economic development and a safe and healthy environment, and encourage community participation in local government.[9] Municipalities have the legislative and executive authority conferred on them in terms of Chapter 7 of the Constitution.

The powers of municipalities may be extended by way of the delegation or assignment of powers and functions by the national and provincial governments.

Section 154 (1) of the Constitution mandates provincial governments and the national government, by legislative and other means, to support and strengthen the capacity of municipalities to manage their own affairs, exercise their powers and perform their functions. All of this is a prominent feature of the principle of cooperative government, which obliges the various spheres of government to work closely together.

Assignment and delegation, with the exception of an assignment of legislative authority, will invariably involve coresponsibility for sustainable service delivery and finance, at least for the short to medium-term. The mechanism for transferring the power or function will depend on the nature of the function or power concerned and the status of existing assignments, delegations and agency agreements between provincial departments and local authorities.

Fiscal and financial implications

Although the primary and peripheral legislation governing the various mechanisms by which functions and powers can be transferred between different spheres of government are distinct, explicit and conspicuous in nature, the same cannot be said of the accompanying financial arrangements and fiscal adjustments. The inhibiting factor in transferring functions and powers is not the legislation but the financial arrangements and fiscal adjustments. It is therefore critical to develop an appropriate fiscal and financial framework to ensure not only fiscal stability but also continued service delivery to inhabitants of urban and rural towns.

[9] See section 152 of the Constitution, and section 4 of the Systems Act

In view of the underlying factors it is at this stage very difficult to express an opinion on the composition and content of a sustainable fiscal and financial framework. This will require additional work, research and investigation and, given the passage of time, needs to be undertaken urgently.

The human resources, infrastructure, assets and liabilities relating to the transfer of a function or power are equally problematic. These issues require vigorous investigating as well as consultation and negotiation with affected parties and key role players.

Conclusion: Transfer of functions and powers

Disciplined effect should be given to the various requirements of the Constitution and related legislation, so as to properly formalise the Province's relationship with municipalities and determine municipalities' role in delivering functions of concurrent and exclusive provincial competence. To this end:

(a) A position paper is currently being compiled titled "*The Western Cape perspective on the transfer of functions and powers between the provincial and local spheres of governments*" which will inform the framework. The position paper will deal with and include, among others:

  i. The identification, and compilation of an inventory, of relevant legislation governing the **mechanisms available** for the transfer of powers and functions and the assessment thereof.

  ii. The identification, and compilation of an inventory, of applicable legislative provisions governing the **performance of the functions/delivery of the services** concerned and the assessment thereof.

  iii. The identification, and compilation of on inventory, of applicable legislative provisions governing the **funding arrangements** for the transfer of powers and functions and the assessment thereof.

  iv. The range, and an inventory, of affected functions and services at provincial government level and an assessment thereof.

  v. The range, and an inventory, of affected functions and services at local government level and an assessment thereof.

  vi. Intergovernmental financial and fiscal arrangements and an assessment thereof.

  vii. Strategic considerations.

  viii. Economic considerations.

ix. Institutional arrangements.

x. The current status and assessment of service relationships (agreements) between the provincial government/provincial departments and individual municipalities.

(b) A practical and sustainable framework to govern the transfer of functions and powers needs to be compiled. The framework will articulate provincial interests, prescribe mechanisms for efficient and effective service delivery and promote democratic accountability. It will deal with and include, among others:

i. Legal guidelines and implementation processes.

ii. Financial and fiscal guidelines.

iii. Assessment criteria for provincial departments to transfer functions and powers.

iv. Process guidelines for the approval of transfers.

v. Assessment criteria in respect of municipalities receiving functions and powers from provincial departments.

vi. Assessment criteria in respect of institutional capacity.

vii. Pro forma agreements as contemplated in relevant legislation.

(c) The position paper and framework need to be discussed with the affected departments and organised local government during the compilation and editing phases and eventually submitted to the Cabinet for endorsement.

(d) A Memorandum of Understanding, which will serve as an interim intergovernmental instrument, needs to be entered into between the relevant parties, to ensure continued service delivery by municipalities within the Western Cape province, to strengthen a relationship of cooperative governance, and to ensure fiscal stability.

(e) In view of the nature and transfer of the particular service, further work and research needs to be done to determine appropriate funding mechanisms such as:

i. Shifts in the vertical division of revenue collected nationally.

ii. Grant funding (conditional).

iii. Co-funding.

iv. Matching grants (50:50).

(f) In order to establish a practical and sustainable framework, provincial departments should compile a detailed report on the affected functions and powers, which should contain the following, among others:

i. Composition of affected functions.

ii. Historical overview.

iii. Applicable national and provincial legislation (legislative framework).

iv. Current financial arrangements.

v. Proposed future financial arrangements.

Integrated development plans (IDPs)

Legislation for the development of integrated development plans was first initiated in the Development Facilitation Act, 1995 (DFA) and the LGTA. The White Paper on Local Government emphasises the developmental role that municipalities should fulfil and prescribes the use of integrated development plans as the process through which a municipality should establish a development plan for the short, medium and long-term. The Systems Act currently legislates IDPs and the IDP process. Section 23(1) of the Systems Act prescribes that a municipality must undertake development-oriented planning so as to ensure:

- that it strives to achieve the objectives of local government as set out in section 152 of the Constitution;
- that it gives effect to its developmental duties as required by section 153 of the Constitution, and
- that, together with other organs of state, it contributes to the progressive realisation of fundamental rights contained in sections 24, 25, 26, 27 and 29 of the Constitution.

Consequently, all municipalities must compile and adopt an integrated development plan for a five-year period. This plan is to be reviewed annually and, if necessary, amended.

The process to be followed by a municipality in drafting its integrated development plan, including its consideration and adoption of the draft plan, must be in accordance with a predetermined programme. It requires municipalities to adopt a process set out in writing. The written document is referred to as a process plan and must include a programme with timeframes for the different planning phases.

The various chronological planning phases in the IDP process can be described as follows:

(1) Analysis - the local issues, problems, potentials and priorities need to be determined during this phase.

(2) Strategies - the local vision and a set of objectives should be defined; and

- local strategies per priority issue on the basis of the district level analysis must be formulated.

(3) Projects - local council projects per strategy need to be designed and identified projects must be financially viable.

(4) Integration - a set of local integrated programmes for managing implementation needs to be compiled; and

- a financial plan, spatial development framework and disaster management plan, for example, form part of the IDP document.

(5) Adoption - each municipal council must adopt the IDP within a prescribed period.

An IDP has many benefits for a municipality and its community. It is:

- a device to improve the quality of people's lives through the formulation of integrated and sustainable projects and programmes;
- a conduit for attracting investment;
- an instrument for ensuring more effective and efficient resource allocations and utilisation;
- a mechanism for the alignment and coordination of spheres of government;
- an instrument for guiding and informing all planning, budgeting, management and decision-making processes in a municipality;
- a mechanism for managing the affairs of a municipality and its municipal area and hence is accorded a very high status within a municipality;
- a barometer for political accountability, and
- a yardstick for municipal performance.

In the Western Cape, the provincial Cabinet, to illustrate their level of commitment to governing the Province, adopted 10 strategic objectives on 5 December 2001. One of the 10 strategic objectives is "To develop the capacity of local government to ensure rapid and comprehensive implementation of **Integrated Development Programmes (IDP)** and free basic services."

Notwithstanding this Cabinet objective, the current legislative framework makes it practically impossible to match the strategic, financial and budgetary planning processes of the national and provincial government with those of local government. This is largely due to the fact that the planning processes of the respective spheres of government have different timeframes. In this regard, the gaps in the different planning processes need to be identified and addressed. Major changes are not suggested; instead specific amendments to synchronise planning processes are needed. The various planning phases of the three spheres of government need to be reviewed and streamlined to ensure greater synergy and integration of development planning. In the absence of such a strategy, integrated development planning will lack sufficient coordination, be inherently fragmented and take place in isolation.

In line with the visionary approach to IDPs, all provincial departments must identify sustainable development projects for execution at local government level. These projects, which must be included in the annual strategic plans of individual provincial departments, need to be evaluated, agreed upon and distilled into a consolidated document.

The IDP should guide the provincial and national sector departments when allocating resources to local government. Municipalities, again, should consider the sector departments' policies and programmes when developing their own policies and strategies. It is in the interest of sector departments to participate in the IDP process so as to ensure that their programmes and those of municipalities are aligned. Although the Department of Local Government has done extensive work to foster alignment by means of the IDP Assessment Committee, senior management involvement is required.

As for the local sphere of government, the provincial sphere of government must prevent the IDP from becoming an instrument of charity for the indigent and those with few resources in the Province. Instead, the execution of identified projects must be turned into service delivery. This must become standard practice for the operations of both local and provincial government. Similarly, municipal and provincial budgets need to be driven by their respective IDPs; hence these should become the centre of all activities. The budget is an essential part of the IDP as it lays down the financial parameters for planning and development. Therefore, to fabricate a budget and a capital programme at the end of the IDP process is a futile exercise if the planning was not done in terms of sustainable financial parameters.

The natural flow should be a collective decision based on the context of a consolidated document by the provincial Treasury and the Department of Local Government on the priority issues for fiscal policy. From this perspective, it is critical to give prudent consideration on a sub-regional level, among others to socio-economic priorities, infrastructure, health and culture. The result must be fiscal allocations and budgets that reflect the priority development priorities.

To establish greater synergy with regard to integrated development planning between the provincial and local spheres of government requires greater co-ordination and cooperation, with a leading role being played by the Department of Local Government – this could prove to be decisive. Provincial departments must collectively give effect to the Cabinet objective regarding integrated development planning and heed the call to turn sustainable projects into service delivery.

Conclusion: Integrated development plans

In view of the above, the following is suggested:

(a) Current intergovernmental coordination, which includes planning processes and fiscal allocations, should be reviewed.
(b) Mechanisms for effecting greater synergy between planning processes undertaken by the different spheres of government should be established.
(c) Maximum senior management support and involvement should be encouraged.
(d) Provincial departments should participate meaningfully in the formulation and implementation of IDPs.
(e) A particular facet to be taken forward is the necessity to improve the working relationship and cohesion between provincial and local government. Apart from the issues referred to earlier (organisation of services, funding arrangements, legal framework, IDPs, etc.), such an endeavour will also have to deal with skills, perception and information gaps wherever they occur.

4

FINANCIAL MANAGEMENT ISSUES

Introduction

Sound financial management is the effective allocation of resources and their efficient and economic utilisation to the optimal advantage of the community. This chapter focuses on ways of, enhancing the efficient utilisation of resources.

This is brought about by the following:

- Accountability and Chief Financial Officers: Identifying accountability, standards of performance with adequate structures to achieve this, evaluating performance (e.g. audit reports) and instituting corrective measures by the various oversight bodies.
- Capacity building: Identifying and addressing current and future training requirements, determining minimum competency levels and establishing of a School of Public Accounting and Economic Studies.
- Financial systems: The implementation and management of transversal financial administration systems to assist accounting officers in the execution of their responsibilities.
- Supply chain management: The introduction of supply chain management to bridge the gap between traditional methods of procuring goods, services and property, stock control and obsolescence planning whilst at the same time addressing the issue of economic empowerment.
- Cash management: Controlling the Provincial Revenue Fund and ensuring that there are at all times sufficient funds to meet expected expenditure.
- Accounting: Providing information on accounting policies and the challenges facing the implementation thereof.
- Contingent liabilities, including debtors: Providing information on the contingent liabilities and debtors of the Province and the challenges facing the future management thereof.
- Departmentalisation: Introducing the new departmentalisation model and assessing the financial implications and benefits relating thereto.

Each of the above is addressed more extensively below.

4.1 Accountability

Overview

Community expectations about public sector performance and conduct are, quite correctly, very high. In many ways, more stringent standards are applied to the public sector than elsewhere in society. Those working within the public sector therefore need to be mindful at all times of the trust put in them by the public they serve.

Unlike the private sector whose aim is to maximise profits, the public sector focuses on maximising service delivery to the community. The key to maximising service delivery is sound financial management. The aim of financial management in the public sector is the effective and efficient achievement of desired outcomes with limited financial resources. This is brought about by effective accountability.

This section aims primarily at increasing awareness of **accountability**, which affects everyone working in the Western Cape public sector. It highlights the responsibilities of individuals and the role they play in fulfilling community expectations of accountable government.

While it brings together a number of accountability obligations which exist in the public sector, this section may also serve:

- to assure the community that the public sector has comprehensive processes in place to maintain a high level of accountability.
- as a useful reference whenever accountability processes are reviewed or new ones proposed.

It is also important to note that the existence of effective accountability mechanisms is fundamental to good corporate governance in the public sector. This section therefore contributes to corporate governance and relevant management processes by highlighting accountability as a critical issue to all involved in public sector administration and the delivery of services.

Accountability is a relationship based on the obligation to demonstrate and take responsibility for performance in the light of agreed expectations. Definitions of the concept of accountability include the following:

> “By accountability is meant the imperative to make public officials answerable for their behaviour and responsible to the entity from which they derive their authority. Accountability also means establishing criteria to measure the performance of public officials as well as oversight mechanisms to ensure that standards are met” (ACAG, 2000).

All office holders have a *responsibility* that is defined by their authority. First and foremost, they are responsible the proper carrying out of their authority for the purposes for which it was given, getting the job done within the law and with respect for ethical values. And, should problems arise, they are responsible for correcting them and doing whatever is reasonable to ensure that they do not recur. The main focus is on performance and on continuous improvement, but the notion of accountability is very much part of responsibility. Accountability can be thought of as enforcing or explaining responsibility. Accountability involves giving an account to somebody who has authority over one, such as Parliament or a superior, of how or how well one's responsibilities are being met (including the actions of subordinates), on actions taken to correct problems and to ensure that they do not recur. It also involves accepting personal consequences for problems that could have been avoided had one acted appropriately.

The concept of accountability thus broadly encompasses who is accountable, to whom, for what, and how accountability is enforced.

Categories of accountability

Political accountability is defined as accountability to the institutions that provide the political legitimacy of the organisation, for example the chain of accountability that links a minister or MEC to Cabinet or the provincial executive council, to Parliament or the provincial legislatures and, ultimately, to the electorate. Managerial accountability refers to the chain of accountability that links individual public servants with the head of department, and the head of department to the Minister or MEC. Public accountability is accountability to citizens outside the public sector organisation and is a combination of ultimate political accountability and client accountability, since citizens are normally the intended recipients of public goods and services. Other accountabilities may include the professional accountability of staff to their professional peer group.

One of the major themes of public sector reforms is "letting managers manage", i.e. devolution of authority to managers coupled with increased accountability. A critical tenet of the managerial models of accountability underpinning recent international reform initiatives is that those with the delegated authority are answerable for producing outputs or the use of resources to achieve certain ends. This is promoted through the specification of outcomes, outputs and performance targets, accompanied by formalised controls over inputs and processes. The focus tends to be on programme accountability (whether the desired results have been achieved) and fiscal accountability (whether funds are spent as appropriated), rather than on procedural accountability (whether certain processes have been complied with) (Vitanen, T 1997). The Public Finance Management Act, Act 1 of 1999, reflects this philosophy.

Legislative framework

In terms of the Constitution of the Republic of South Africa, Act 108 of 1996, (*"the Constitution"*) the three spheres of government are made the stewards of public resources in the public interest rather than in the interests of individuals and interest groups. This fiscal accountability refers not only to avoiding financial irregularities such as fraud and corruption by exercising financial controls, but also to achieving value for money (the effective, efficient and economical use of financial resources).

The Constitution also envisages the separation of the powers of the legislative, executive and judicial branches of government as a system of checks and balances. It assigns separate responsibilities and accountability to each of them.

Prior to the commencement of the Public Finance Management Act, 1999, on 1 April 2000, the accounting officer for the Provincial Administration Western Cape was the Director-General. This was determined in terms of the Western Cape Exchequer Law, 1994. The Public Finance Management Act ("the Act") was promulgated pursuant to section 216 of the Constitution, in terms of which national legislation had to be passed for purposes of establishing a national treasury and prescribing measures to ensure transparency and expenditure control in each sphere of government by introducing (a) generally recognised accounting practices, (b) uniform expenditure classifications and (c) uniform treasury norms and standards.

In terms of section 36, read with section 49, of the Act, every department and every constitutional institution must have an accounting officer who is the head of the department or the chief executive officer of the constitutional institution. Every public entity must have an accounting authority in the form of the board, controlling body, chief executive officer or other person in charge of the public entity, as the case may be.

Section 38 sets out the general responsibilities of accounting officers, and their responsibilities relating to budgetary control and reporting are set out in sections 39 and 40 respectively. The statutory obligation of accounting officers to submit all relevant information to the Treasury or the Auditor-General, as prescribed or required, is enshrined in section 41. Whenever assets and liabilities are transferred to another department or an institution, the two accounting officers concerned must comply with the provisions of section 42.

While provincial MECs are responsible for policy matters and outcomes, including the approval and adoption of the relevant department's budget vote, accounting officers are responsible for outputs and budget implementation to ensure the desired outcomes. As such, accounting officers are accountable to provincial legislatures for the management of the implementation of their departments' budgets.

Accounting officers may face disciplinary sanctions, including dismissal, if they fail to comply with their responsibilities.

Section 44(1) empowers accounting officers to delegate in writing any of the powers entrusted or delegated to them in terms of the Act, to an official in that department or constitutional institution or to instruct any official in that department or constitutional institution to perform any of the duties assigned to the accounting officer in terms of the Act.

Although section 44(2) provides that an accounting officer is not divested of the responsibility concerning the exercise of the delegated power or the performance of the assigned duty, officials acting under a delegation or assignment of power in accordance with section 44(1) must also comply with the provisions of the Act to the extent applicable to that official (section 45(d)).

Similar provisions applicable to accounting authorities are detailed in sections 49 to 57 of the Act.

It follows that both the accounting officer/authority and the official performing a delegated or assigned power or duty are coresponsible and accountable for exercising or performing that power or duty in accordance with the provisions of the Act. The official is primarily accountable to his or her accounting officer/authority, while the accounting officer/authority remains accountable to his or her provincial minister and, ultimately, the provincial legislature.

In fact, no official whose area of responsibility includes compliance with any of the provisions of the Act, whether or not it entails acting under a delegated or assigned power, can escape the chain of accountability and the consequences of failure to act in accordance with the provisions of the Act and the Regulations issued in terms thereof. As in the case of accounting officers/authorities, such failure may give rise to disciplinary action against the official. Depending on the circumstances, the official's conduct may likewise result in dismissal.

In this regard it is important to bear in mind that the Disciplinary Code must be consulted in the event of disciplinary action against officials based on a contravention of the provisions of the Act. Insofar as non-compliance with the Act may also constitute a transgression as contemplated by the Disciplinary Code, accounting officers and officials may have to answer to a variety of charges based on a single transgression.

Chapter 10 of the Act deals with the circumstances in which the conduct of accounting officers/authorities and other officials would constitute financial misconduct. An official, however, can only be held to have committed financial misconduct if he or she wilfully or negligently fails to exercise a power or perform a duty assigned to him or her by the accounting officer in terms of section 44(1) or by the accounting authority in terms of section 56(1).

The national legislative framework is completed by the National Treasury Regulations and supplemented by the provincial Treasury Instructions, circulars and other policy documentation issued by the national and provincial Treasuries and aimed at improving and enhancing compliance with the nationally determined norms and standards.

Mechanisms of Accountability

Mechanisms of accountability can either be internal or external to the public sector organisation. They can also be formal or informal. Internal accountability refers to accountability to principals within the boundaries of the public organisation, e.g. to immediate superiors, top management and fellow workers. External accountability refers to principals within the organisational operating environment, e.g. clients, the Auditor-General, the colleagues of one's profession, a MEC and the legislature.

Formal accountability mechanisms include financial and performance management systems, the publication of annual reports and audited financial statements, performance reviews, protocols for promotion, disciplinary proceedings or other measures which create incentives or sanctions. Informal accountability mechanisms would include peer pressure, organisational culture and reputation. Adequate formal systems of financial and performance management are necessary to achieve a culture of accountable governance, but they are not sufficient. The values and ethics of individuals are also crucial in ensuring accountability and integrity in the public sector.

International best practice suggests that it is important for the top management of public sector organisations to take the lead in promoting accountability through personal responsibility and demonstrating by example. It is equally important that each civil servant behaves accountably within his or her area of authority. This thinking is reflected in section 45 of the Act, in terms of which each official is accountable for the effective and efficient use of public resources within his or her area of responsibility.

Principles of effective accountability include:

- Clear definition of roles and responsibilities;
- Clarity of performance expectations;
- Balance of expectations and capacity [(i.e. performance expectations must be clearly linked to and be commensurate with capacity (authority, skills and resources) of either party to deliver)];
- Credibility and transparency of reporting on performance achieved;
- Reasonableness of review and feedback, where achievements and difficulties are recognised and corrections made (OACG, 1998).

The principles of effective accountability demonstrate that, in order to ensure accountability for the use of government resources, formal budgeting, financial and performance management systems and human resource management will be required, as well as changes to the culture of public sector organisations and the individuals who comprise them.

This therefore requires not only compliance with the requirements of the Act, but also a genuine desire among all officials, at all levels, to comply with the spirit of the Act, namely to utilise provincial resources effectively and efficiently on an individual basis. This may take time, but it is most certainly a challenge that must be overcome.

In the short term, some measure of the success of the above ideal will be the frequency of reported cases of unauthorised, irregular, fruitless and wasteful expenditure through shortcomings identified and reported on by the Auditor-General, the Audit Committee, the accounting officers/accounting authorities and other officials in the organisation.

Oversight functionaries

The effectiveness of oversight functionaries (listed below) also largely determines the level of efficiency and effectiveness in the utilisation of resources, and therefore the value of the oversight functionaries cannot be overemphasized. It is imperative that each oversight functionary notes this and takes decisive steps to be effective in their respective roles. However, they should as far as possible also assist accounting officers/accounting authorities in achieving their objectives so that they do not only focus on punitive measures.

While each oversight functionary has a unique role to play, the following functionaries together have the role of ensuring effective accountability, effective evaluation of performance and effective consequences (corrective action), which are essential ingredients for good financial management. This, together with the duties performed by accounting officers/authorities (i.e. compliance with the spirit of the Act), will achieve the ideal referred to above. The oversight functionaries are:

- The Standing Committee on Public Accounts

  This committee interrogates and investigates, and subsequently passes resolutions on, matters reported on by the Auditor-General and by other functionaries. The committee is the last link in the accountability chain and should focus on matters that previous links in the chain have failed to resolve.

  Performance results as against predetermined objectives must be included in departments' annual reports to be submitted to the committee, who would then be able to evaluate departmental performance in achieving planned outputs, and hence progression towards desired outcomes. This measure satisfies the constitutional requirement of accountability and transparency.

  The committee, in terms of section 25 of the Constitution of the Western Cape, 1997, may, *inter alia* summon any person to appear before it to give evidence or to produce documents, and may require any natural or juristic person or provincial organ of state to report to it. The committee may recommend sanctions against accounting officers/authorities ranging from salary deductions or demotion to dismissal. It is, however, up to the Executive Authority to act on these recommendations after following due process.

- The Auditor-General

  The Auditor-General uses the norms and standards derived from the Public Finance Management Act and other financial legislation to audit compliance by accounting officers/authorities. Audits are conducted in accordance with the Statements of South African Auditing Standards, which require the Auditor-General to plan and perform audits to obtain reasonable assurance that departments' financial statements are free of any material misstatement.

  An audit includes (a) an examination, on a test basis, of the evidence supporting the amounts and disclosures in the financial statements, (b) an assessment of the accounting principles used and significant estimates made by management, and (c) an evaluation of the overall financial statement presentation. An audit also includes an examination, on a test basis, of the evidence supporting compliance in all material respects with the relevant laws and regulations applicable to financial matters.

  During the last three years the percentage of qualified Auditor-General's reports has dropped from 47% in previous years to 30% in the 2001/02 financial year. All departments must strive to achieve unqualified Auditor-General's reports. It is also the responsibility of accounting officers/accounting authorities to take appropriate steps to ensure that qualifications contained in the reports or concerns or queries raised by the reports do not resurface in subsequent reports.

- Audit Committees

  The Western Cape Provincial Cabinet approved on 14 August 2002[1] that three different Audit Committees should be established in the Western Cape Provincial Administration, one for each of the Departments of Education and Health[1] and one for the other departments. It also resolved that the establishment of an Audit Committee for the Department of Social Services and Poverty Alleviation should be investigated.

  The Audit Committees report to the respective accounting officers, who are then required to take corrective action. Each committee is responsible for evaluating whether Internal Audit performs satisfactorily by ensuring that:
  - Internal Audit achieves their performance goals;
  - risks are identified;
  - specific issues requiring attention are highlighted;
  - the cost of auditing is minimised;
  - the services of the auditing function are optimised.

  Each committee must ensure that systems of accounting and financial control are established and maintained to manage financial risk and that effective internal monitoring systems are in place so that the objectives of the organisation are achieved without unacceptable risk. The committees must

[1] Provincial Cabinet Resolution 274/2002

also ensure that laws, regulations, treasury instructions and policy statements are complied with and that appropriate procedures are in place to address any fraudulent or corrupt activities affecting the organisation.

The committees investigate any matters referred to it by the provincial Cabinet. In doing so, the committees must maintain free and open means of communication between the Auditor-General, Internal Audit and provincial management.

Further reference is made to Audit Committees and Internal Audit in section 5.7 of this chapter.

- The provincial Treasury

  The provincial Treasury promotes sound financial management by enhancing the national norms and standards (which are encompassed by the Public Finance Management Act and the National Treasury Regulations) by issuing provincial Treasury Instructions, as well as financial best practices via the use of circulars and policy documents.

  As an oversight functionary the provincial Treasury further promotes sound financial management by ensuring compliance with those norms and standards and the proper implementation thereof in departments/public entities by accounting officers/authorities. It is important for the provincial Treasury to obtain essential information and to interpret the information properly for purposes of fulfilling its oversight role.

  The provincial Treasury also recognises the need for it to act as a change agent (catalyst) to ensure that various role players interact effectively within the scope of their responsibility, which in turn is bound to result in the effective and efficient management of revenue, expenditure, assets and liabilities (*"REAL"*) within departments and public entities.

Way forward

Compliance with the national and provincial norms and standards will result in sound financial management through the effective and efficient utilisation of resources of provincial departments and provincial public entities. This will also result in:

- unqualified consolidated financial statements for the provincial government (accrual basis);
- unqualified financial statements for provincial departments (accrual basis);
- provincial public entities being regulated;
- sound financial management systems and processes;
- timely provision of quality management information.

Ultimately, the benefits offered by the Public Finance Management Act, 1999, are dependent on the will and ability of accounting officers/authorities to comply properly (substantive compliance) with its requirements. The combined successes of the various oversight bodies in ensuring that accounting officers bring this about are equally important. The challenge thus is for each relevant functionary (whether an accounting officer, an official utilising the resources of a department/public entity or an oversight body performing its relevant functions) to fully comprehend the importance of their particular role in ensuring substantive compliance with the norms and standards. For example, oversight bodies should reflect on whether they are making a real and noticeable difference in improving service delivery and ensuring the more efficient utilisation of limited resources. Where this is found lacking, it should be addressed urgently. Dedicated focus by all relevant role players is required over the next few years for a marked improvement.

4.2 Chief Financial Officer (CFO) responsibilities and structures

Overview

The first and foremost area that needs immediate attention in addressing the standards of financial management in the public sector is improving the effectiveness of CFOs and their support structures. It is recognised that the quality of financial management in public sector organisations is directly related to the ability of Accounting Officers to recruit and retain competent chief financial officers, finance support staff and programme managers. The approach of management for results, with its associated flexibility in the use of resources but greater emphasis on accountability, will enable accounting officers together with their CFOs to achieve the agreed outputs of each department with an appropriate standard of financial management.

The role and responsibilities of the CFO

There is clearly a need to revisit the role of the CFO in departments. CFO appointees should be high-calibre individuals with:

- Credibility with senior managers in the department
- Relevant experience at a senior management level
- Demonstrated capacity to interpret, analyse and present complex information
- Capacity to bring independent and impartial advice into departmental decision-making
- Direct access to the accounting officer.

The CFO must combine timely, materially accurate, relevant, complete and suitably presented financial results and trends with interpretative professional advice. In addition, he or she must play a major role in preparing strategic plans and ensuring that best practice is followed. The CFO must have the appropriate infrastructure and staff to allow sufficient opportunity to provide analysis, interpretations and appraisals that will assist and improve decision-making in the department.

Within a department, the role of the CFO is:

- To respond to changing needs for financial information and advice
- To undertake product and service costing tasks
- To meet reporting requirements (for example, monthly reports and annual financial statements)
- To assist with the formulation of medium-term objectives, policies and strategies in support of the strategic and operational plans of the institution
- To consider the financial impact of departmental outputs aimed at providing economical, efficient, effective and appropriate services
- To ensure proper planning for the acquisition of assets, including the need to consider alternative strategies to achieve objectives
- To implement and maintain an effective and efficient system of risk management and of sound internal controls.

- To oversee all financial management activities of the institution, including managing accounting and finance staff

In pursuance of the above, the following is recognised as critical areas of CFO performance:

Capacity building

Planning and budget management:
- Budgeting
- Expenditure
- Revenue

Asset management:
- Planning
- Procurement
- Provisioning
- Property and inventory management

Supply chain management

- Financial assets

Liability management:
- Debtors
- Creditors
- Risk management
- Internal control
- Internal audit

Accounting and accountability:
- Delegations and instructions
- Accounting
- Reporting
- Disciplinary actions
- Integrity of financial information and systems

The above are critical areas, but mere mechanical execution of the responsibilities is not enough. For each of the above, the CFO needs to interpret the inherent dynamics, e.g. instead of doing a mere budget coordination exercise, they need to challenge the objectives set, i.e. will they achieve the desired outcomes, and will service delivery be truly enhanced by augmenting the budget through innovative revenue initiatives and management, including sound debtor administration. In addition to this, performance of the concept of cost centres should be enhanced and benchmarked. CFOs also need to look at maximising delegated powers at the right levels to enhance effectiveness, while at the same time having good control and reporting mechanisms for effective accountability. To achieve this, CFOs must not only think innovatively and with greater vision but start encouraging and developing this in their support staff. The CFO is a manager with specific responsibility to the finance component, but like any other manager he or she may not abrogate line function manager responsibilities. All finance staff would work towards the CFO, whose independence would be the same as that of any other manager. It is fundamental that accounting officers support their CFOs and enhance their profile in the department to allow the CFO to become the champion of higher standards of financial management. Accounting officers and CFOs should form a partnership in promoting the benefits of the PFMA.

Clients of Chief Financial Officer

The Chief Financial Officer does not operate on his or her own nor unattached to management. Successful financial management is the result of a collective conscious effort from everybody in the organisation, as guided by a technically trained and proficient Chief Financial Officer who is objective and performs his or her duties with due professional care. In this regard the Chief Financial Officer, through effective service delivery, must establish relationships with clients on a basis of integrity, reliability, objectivity and usefulness. These core values must be evident in the relationship with the following clients:

- Accounting Officer
- Programme Managers
- Internal audit and the Audit Committee
- External Audit
- Budget Committee/Top Management
- Premier's Office, relevant MEC and Cabinet
- Portfolio Committee
- Joint Standing Committee on Public Accounts
- Treasury
- Public Entities.

Achieving these core values requires adequate education and training and maintaining the highest possible degree of professionalism in the delivery of financial services.

Qualifications, core competencies and skills required for CFOs

A bachelor's degree in finance, accounting and economics should be the minimum academic qualification for CFOs. However, employers increasingly seek qualified chartered accountants or graduates with a masters degree, preferably in economics or accounting. These academic programmes develop analytical skills and provide knowledge of the latest financial analysis methods and technology. In addition, CFO's should also have at least five years management experience in finance.

Against the background of the role and responsibilities of CFOs, it is recognised that they should preferably be technically trained and proficient in at least the following subject areas:

- Strategic management
- Business planning and design
- Performance measurement
- Financial accounting

- Management accounting
- Internal control
- Internal and external audit
- Information systems
- Economy
- Negotiation skills
- Communication skills
- Analytical skills.

Criteria for establishing posts of CFO

The following should be borne in mind when establishing posts of CFO:

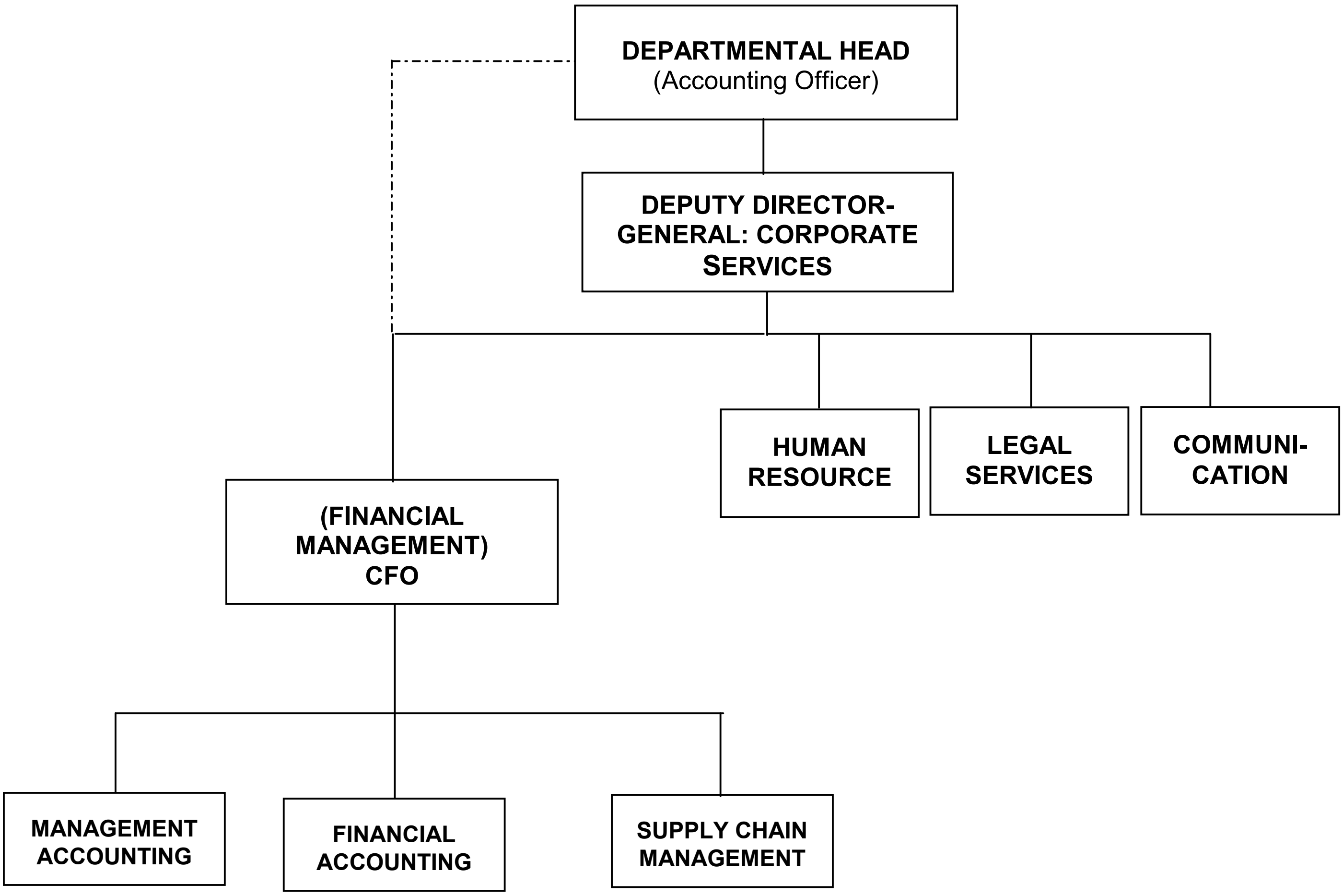
- Must be appropriately placed in the hierachy of the organisation to allow for direct accountability to the accounting officer.
- Must be established at a level which will allow authority over financial affairs.
- Position should not be linked to the size of the budget.
- Must have responsibility for establishing measures for proper financial management and authority to implement them.
- Must be included in the top management of the institution.

The CFO must have an appropriate support structure and competent staff to allow him or her sufficient opportunity to provide analyses, interpretations and appraisals that will assist and improve decision-making in the institution.

The following are examples of organograms reflecting the ideal placement of CFOs together with their support structure. Experience has shown that CFOs are more effective when reporting directly to the accounting officer. The standardisation of the CFO support structures should be centred around these models.

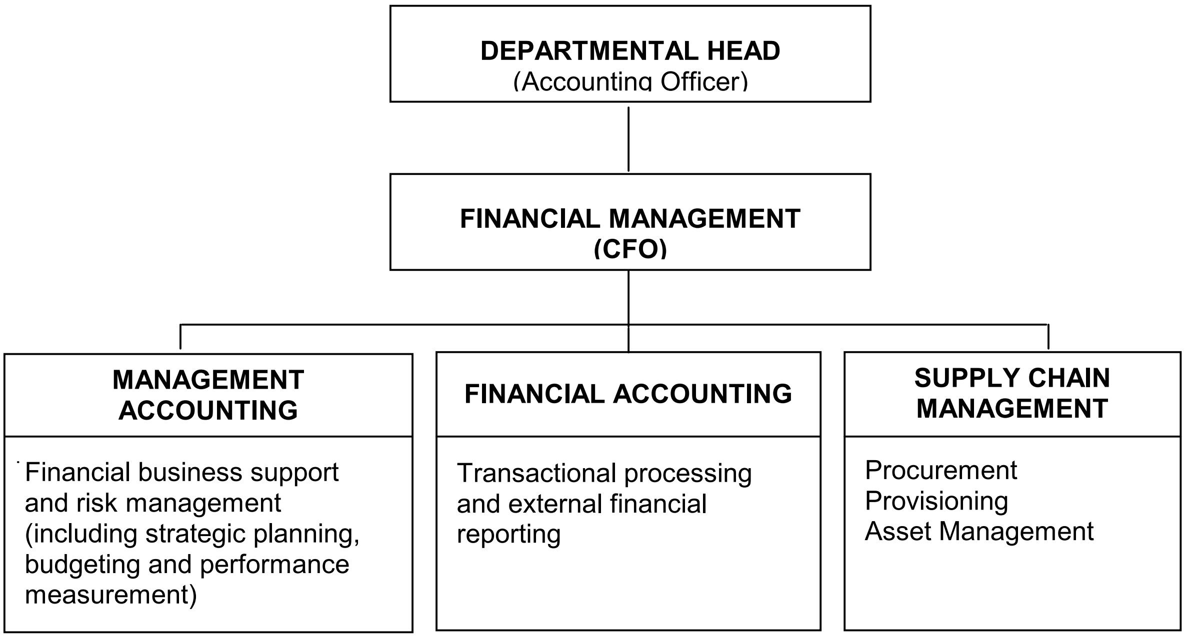
Example 1

CORPORATE AFFAIRS



Example 2

FINANCIAL MANAGEMENT



4.3 Capacity Building

Overview

The past seven years have been characterised by a number of restructuring processes. This resulted in the loss of skilled and competent personnel through the introduction of voluntary severance packages. Furthermore, stipulations in the Public Finance Management Act, 1999, place 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 had to adapt to the changing work environment. It therefore 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. Its vision was to supply functional financial training in a professional manner to ensure excellence in financial, personnel and provisioning administration. Since 1995, a total of 12 700 officials have been 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 with regard to current and future requirements of legislated transformation.

In order to stay abreast of the demands made by the 21st century on managers in general, chief financial officers and treasury officials, a training programme should be developed to enhance their skills and competencies in analytical abilities, problem solving, performance management, etc.

Furthermore, the Public Finance Management Act, 1999 (Act 1 of 1999), places responsibilities on officials which have a direct impact on the management principles they are required to comply with.

With the departure of large 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 on 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 an explosion in the demand for training.

New training material was designed in an outcome-based, modular format and includes the latest policies and procedures.

The range of courses was expanded, with the focus on functional training in the work environment.

The value of the new range and format of courses was very evident from the greater response to the need analysis that was done to determine the demand for training by departments.

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

Under these circumstances the creation of a learning-orientated organisation and a culture of learning and the adoption of a philosophy of life-long learning become imperatives.

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

Current resources

The approved personnel of the current training component within the provincial Treasury has expanded to twelve trainers and two administrative personnel under the supervision of a deputy director. It is 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, a computer room accommodating 10 students is 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 highlighted in 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 in 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. The training facilitators were accredited by various role players to present selected courses on their behalf. All the training facilitators were accredited by financial sector education and training (FASSET) as registered assessors, which enables them to drive the assessment process individually. However, the future vision 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.

All course material was reorganised into an outcome-based format to comply with accreditation requirements of the South African Qualification Authority and the National Qualification Framework via the Financial Sector Education and Training.

The training manuals were designed to be user-friendly, include various practical exercises and workbooks, and can be used in the work environment as a work procedure guide and reference book. The modules were further designed to provide “just in time” training to students in a simulated work environment. Computer courses simulate live systems and an actual work environment and training databases provide the opportunity to work on a simulated live system.

The course material allows for various forms of assessment to ensure that the training provided is of a high standard and that the transfer of skills and competencies has in fact taken place. The first phase of an evaluation and follow-up framework has been implemented whereby managers will be informed about student satisfaction with the course and whether they have mastered the course content.

The second phase will provide information on the application of skills and competencies acquired and the impact on the performance of the student back in the workplace.

The Institute for Public Finance and Auditing (IPFA), funded by FASSET, introduced two learnerships to uplift accounting skills in the public sector. These learnerships will be piloted in the Department of Finance, whereafter it will be rolled out to the other departments.

The successful completion of these learnerships will lead to a Certificate in Public Sector Accounting (NQF level 5) or a Diploma in Public Sector Accounting (NQF level 6).

The component's training priorities can be divided into the following categories:

- Functional training concentrating on systems training
- Fiscal strategic management training focusing on finance and economic management skills development
- Qualification training focusing on the administration of bursaries to promote a higher level of professional qualifications in the provincial Treasury.

The first step would be the reorganisation 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 and a vocational development component.

The training component empowers the Western Cape province to act as change agent that can enhance the skills and competencies of other provinces, in particular the Eastern Cape and the Northern Cape.

As already mentioned, the component is currently utilising five 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.

Way forward

The following long-, medium- and short-term requirements will mark the capacity building restructuring processes. It should, however, be noted that the responsibility for ensuring that adequate capacity building takes place in departments is primarily that of accounting officers. Competency profiles being developed by departments will go a long way in assuring this.

- **Long-term**

  - The creation of a culture of life-long learning through:
    - 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 to become a true learning-orientated 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.

- The envisaged establishment at the Academy, in consultation with the key role players and with the support of the Board of the Western Cape Administrative Academy at Kromme Rhee and the provincial Cabinet, of a School for Public Accounting and Economic Studies. The school should provide for short courses in finance, economics, analytical, interpretative, functional and competency-based education and training programmes that will all lead to a nationally recognised tertiary qualification registered at NQF level 7.

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

- **Medium-term**

  - Establishment of an effective human resource system that addresses performance management, attracts and retrains highly skilled personnel, and implements learning and career paths for all personnel.

  - Strengthening the management capacity of training and development within the provincial Treasury.

  - Designing, financing and developing a learning centre.

  - Implementing a development strategy through the expansion of course programmes based on the needs of the target market.

- **Short term**

  - Developing a training policy.

  - Identifying the target market and setting training priorities at all levels.

  - Registering as an accredited learning and assessment centre.

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

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

  - Restructuring the component to provide for research and development.

- Implementing 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

What needs to be put in place is the development of facilities at an institution such as the Academy at Kromme Rhee, the ideal budget that would provide for an appropriate percentage of the provincial Treasury personnel expenditure, and the fiscal policy that would make this possible. 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. Among 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 training and education councils and bodies, relevant civil society stakeholders and business organisations, financial and procurement personnel and the Senior Management Service of provincial departments are the important role players.

4.4 Financial Systems

Overview

Currently there are four major systems, the Personal and Salary Administration System (PERSAL), Basic Accounting System (BAS), Financial Management System (FMS) and Logistical Information System (LOGIS) that are maintained by the National Treasury for national and provincial departments. The various systems are managed as separate stand-alone "silos" and not as a single integrated systems unit. In addition, the national Treasury also maintains a Management Information System (Vulindlela).

Apart from these legacy systems, certain national and provincial departments have acquired a number of software solutions that are operated and maintained as separate "sub-systems". Over time, a great number of interfaces have been developed between the legacy systems and the "sub-systems" in a mostly uncoordinated fashion, following a process of "least resistance". (Currently, for example, there are more than 100 interfaces with BAS alone.)

The legacy systems within the national Treasury were developed as in-house proprietary solutions over a period of many years and in almost an evolutionary fashion.

The Financial Management System (FMS) is a cash-based accounting and batching system that was developed way back in 1973 and is now outdated. After a processing run, the expenditure data in FMS1 is carried over to FMS2, where the information is available on an on-line basis. It is, however, still functional in the Western Cape, Free State and KwaZulu-Natal provinces and at a few national departments. Currently, no enhancements are made to FMS and support is only focused on maintaining the system.

The Personal and Salary System (PERSAL) is the central system used for the administration of the public service payroll. PERSAL is very stable from a payroll perspective.

Over the years, PERSAL has expanded by increasing the spectrum of data fields to hold part of the information prescribed by national reporting requirements. In this respect, PERSAL offers personnel administration, holds information in a database of approximately 1,1 million employees, and offers standard and ad hoc reporting.

PERSAL was developed in an ad hoc fashion, with developments being mainly driven by legislative requirements rather than a Human Resource Strategy. New developments were therefore not informed by a systems life-cycle approach.

Salary payment and HR requirements are integrated into one system and therefore the database cannot be separated. The user focus is more on the salary function than on the HR function. The result is that HR data on PERSAL is neglected and often incomplete and inaccurate.

PERSAL interfaces manually with other systems (both internally and externally) through Magnetic Tape. An on-line interface with Vulindlela and other external systems is also in place.

The Basic Accounting System (BAS) is a basic accounting system (also cash based) that was developed in 1992 to cater for government's basic accounting needs. The architecture is more modern than that of the other systems and is assessed as being roughly in the middle of its normal systems life-cycle. The system is not a full-fledged accrual accounting system. It is only when the Accounting Standards Board makes the criteria known in respect of GRAP that one will be able to gauge whether BAS meets the specified requirements.

Some enhancements have been made to the system to accommodate the PFMA requirements. These enhancements mostly address "Commitments" and "Liabilities". The further advantages of BAS are a budget-blocking functionality that will make a significant contribution to limiting possible overspending, a cheque-release functionality that will assist in preventing cheque fraud, and a standard chart of accounts that will standardise and enhance reporting at all levels within government.

The Logistical Information System (LOGIS) in its current format was developed in 1998. LOGIS was developed in an evolutionary way to cater for government's provisioning and administration requirements in respect of the control of movable assets and stock.

The advantages of LOGIS include:

- Management of stock and stock levels (maximum and minimum levels).
- On average, a reduction of previous stock levels by a third (↓).
- Automatic reordering according to maximum/minimum stock levels.
- Automated inventories (movable assets).
- Commitment of all orders placed.
- Automated chief users.
- Automation of the provisioning environment.
- Availability of audit trails on all actions executed.
- Access and profile control.
- Availability of various detail and management reports, including the status of orders, goods received, inventories, store statistics, approved shortages, etc.
- Availability of a balanced scorecard which provides management with an internal service delivery, cost saving, improvement and financial perspective.

Even though LOGIS is not an asset management system, it complies with the provisioning administration processes and procedures and is an integral part of supply chain management.

The Management Information System (VULINDLELA) is a data warehouse that provides HR, finance and logistics reports. It relies on the PERSAL database and enhances access to reports, which offers high-level trends for management information.

On 1 April 1992 the Financial Management System (FMS) and Personnel and Salary Administrative 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 to improve the quality of financial management and building capacity in provincial departments was identified as a priority by the Provincial Treasury.

However, it was not before the Public Service Act, 1994 (PSA) and the Public Service Regulations issued on 1 July 1999, whereby a provincial department was established as an autonomous entity, that the necessary impetus was provided to proceed with the devolution of financial functions. A further factor necessitating the devolution of financial functions to the departments was that the provincial Treasury could no longer 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 (dichotomy).

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 the FMS and PERSAL Systems commenced during the 1999/2000 financial year and was completed on 1 April 2002 in respect of the then ten provincial departments. The departmentalisation model, which was approved in June 2002, necessitated the further decentralisation of PERSAL and FMS to a further three provincial departments with effect from 1 August 2002. For further details of departmentalisation, see section 4.9.

In the latter part of the 2002/03 financial year, the Department of Finance and the provincial Parliament that have the necessary infrastructure and capacity potential will migrate from FMS to BAS.

Owing to outdated and insufficient systems that existed for the management and control of consumables and movable assets, the Logistical Information System (LOGIS) was piloted by the national Treasury and the provincial Treasury during 1999 at the Department of Agriculture. During the period 1 April 2000 to 31 October 2002, LOGIS was rolled out to a further 28 sites in the Province, with a further six sites to be implemented by 31 March 2003. By then it will manage a total stock value in excess of R1,2 billion.

As no standard Management Information System for the government as a whole existed, various software packages were utilised to provide management information. This was not only time-consuming but also provided outdated information in general. In cooperation with National Treasury, a Management Information System (Vulindlela) was developed and rolled out to 157 managers at head office level within provincial departments for increased access to relevant and up-to-date management information, enabling more effective decision-making.

As no standardised system existed to register losses, the Loss Control System was developed by the Department of Finance and implemented at all head offices of provincial departments. On 1 April 2000 the function was transferred to the provincial Treasury. As the system was developed for a centralised environment, the devolution of financial functions necessitated the redevelopment of the system to cater for the various component structures and delegations of provincial departments. Further development included availability of management information, improved response time and interdepartmental transfers of losses.

Current financial administration and management information systems

The following table illustrates the current systems in operation, the main functions of the individual systems, the main 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 • Month close info available in electronic format • Enhanced debtors sub-system (includes age analysis) • Fleetman interface • Electronic downloading of reports • Debtor system further enhanced • User manuals available on national Treasury WEBSITE	• Not an on-line system • Allows for overspending on budget • Does not cater for General Recognised Accounting Practice (GRAP) • No standard chart of accounts
FMS 2	• Maintenance of code files • Budget capturing tool • Various management reports available (monthly and to date)	• User code/password revoke function • Operating system upgraded to link 17 • Identification of conditional grant objectives • Improved response time • Batch/payment enquiries • Cheque release functionality • Virement function available	• No on-line data-capturing facility • Not a budget system • No consolidated financial statements functionality available

SYSTEM	MAIN FUNCTIONS	IMPROVEMENTS	SHORTCOMINGS
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, i.e. salaries and state contributions of medical and housing allowances • Management Information: Various reports are available	• Caters for: • CORE • Magnetic tape interface for insurance companies • New resolution 7 leave dispensation • SMS packages • S&T claims to comply with SARS requirements • Access and profile enhanced • Enhancement • Interface with Government Employee Pension Fund • Introduction of "Entire" facility allows for transfer of data between Bureaus • Persal notices and manuals available in Intranet • Provides for reprint of IRP5 certificates and local printing • Skill development enhancements • The operating system upgraded to optimise performance (Sysphex) • Various reports available in electronic format • Verification of data with Home Affairs	• Does not cater for total personnel administration of educators • Does not optimally cater for certain control measures • Scanning facilities not available • Not Windows-friendly
Basic Accounting System (BAS)[2]	• Cash-based online system • Accounting Transactions • Payments • Debtors • Bank reconciliation • Detailed reports • Online enquiry • Maintenance of code files • Various management reports available • Budget-capturing tool available • Various levels of authorisation of payments	• Budget blocking • Commitments & liabilities • GG transport interface • Debit order interface • Budget Interface • Procurement/LOGIS interface • Standard chart of accounts	• Does not cater for Generally Recognised Accounting Practice (GRAP) • Not a full-fledged accrual accounting system • Scanning facility not available

2 The implementation of the Basic Accounting System (BAS) is scheduled for the latter part of 2002/03

SYSTEM	MAIN FUNCTIONS	IMPROVEMENTS	SHORTCOMINGS
Logistical Information System (LOGIS)	• Provisioning and procurement system • Control over consumables and movable assets • Provides for management information regarding stock and assets	• Managing stock by means of minimum and maximum stock levels • Over-stocking is minimised and predetermined as only a determined amount of stock can be held • Moving of assets is controlled • Availability of audit trails on all actions • Flexible infrastructure • Access and profile control The following functionalities are available: • Online printing • Guarantee register • Petty cash • FMS interface report • A4 order forms	• Not a financial budget control system • Does not interface up to minor item level • Not an asset management system • No BAR coding functioning • No BAS interface
Management Information System (Vulindlela).	• Integrated management information • Drill down functionalities • On-line, printing and downloading functionalities • Information available at all levels • Relevant and up-to-date information • Standard reports available • Help function	• Web-enabled • In-year monitoring system • Monthly employment equity stats available on national WEB • Availability of PERSAL, LOGIS Information	• No access and profile control per institution • No management information on ledger accounts • Slow response time
Loss Control	Registration and management of all losses	• Interdepartmental transfer of losses • Availability of management information • Restructuring of application to enhance functionality and response time • Improved usage of component structures and delegations	• Limited consolidated data and management information available • Scanning facility not available

System Implementation

The Basic Accounting System replacing FMS will be rolled out to the remaining 12 provincial departments in a phased approach during 2003/04.

The Logistical Information System (LOGIS) will be rolled out to a further 20 self-accountable stores (health institutions) during 2003/04 and the remaining 15 self-accountable stores during 2004/05. This would increase the estimated stock value managed to more than R2,7 billion.

Vulindlela will be further rolled out to regional offices and institutions, subject to the necessary information technology infrastructure being in place and adequate to cater for the additional volume of transactions.

The Loss Control system will be rolled out to regional offices and institutions subject to the information technology infrastructure being in place and adequate.

Needs

A growing need exists for the interfacing and integrating of all financial systems. The following needs have been identified:

- A functionality that fully accommodates personnel administration of educators
- Optimal control measures in PERSAL
- Systems that cater for General Recognised Accounting Practices (GRAP)
- Budget control on LOGIS and PERSAL Systems
- Consolidated financial statements
- An appropriate budgeting system
- Management information on ledger accounts
- LOGIS to interface to minor item level
- An asset management system
- Barcoding
- Access and profile control on Vulindlela per institution
- Consolidated data and management information in Loss Control
- Scanning facilities in all systems
- BAS interface.

Way forward

Transversal issues

To further enhance the rendering of user support to users of the various systems, the National Call Centre System (LOGIK) will be implemented to enable the registering of all incoming calls, monitoring of outstanding calls and determining the service delivery level. Further, to ensure an uptime of at least 95% of all financial administration and management information systems.

The provincial system controllers (FMS, BAS, PERSAL, LOGIS and Vulindlela) in the provincial Treasury will represent this Province at the various National Forums, user meetings and workshops.

The provincial Treasury will, as assessed, issue the necessary Treasury Circulars, System Circulars/Notices regarding the effective, efficient and economical utilisation of the systems in all provincial departments.

Financial Management System (FMS)

On account of the high cost of maintaining two financial systems and the non-compliance of FMS with current requirements, the national Treasury has taken a policy decision to migrate all FMS departments/provinces to BAS in a phased approach by no later than 1 April 2004; to continue, for the interim, with the daily monitoring of the system so as to ensure that the available facilities (e.g. electronic transfers, financial authorities and commitments) are utilised to their maximum; that interfacing between the various systems (LOGIS, PERSAL, TELKOM, FLEETMAN, MEDSAS and official banker) occurs on a daily basis; that code files, access control and profiles are maintained.

These systems will be fully replaced by the Basic Accounting System (BAS) by 1 April 2004 (target date).

Personnel and Salary System (PERSAL)

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

Basic Accounting System (BAS)

As its implementation is phased in, migrating from FMS, the daily monitoring to ensure that the available facilities (e.g. electronic transfers, online enquiry and debtors) are utilised to their maximum potential; to monitor and ensure that interfacing between the various systems (LOGIS, PERSAL, TELKOM, FLEETMAN, MEDSAS and official banker) occurs properly five days a week; that code files, access control and profiles are maintained. BAS is to be fully implemented in all departments by 1 April 2004.

Logistical Information System (LOGIS)

The monitoring of the system to ensure that internal service delivery, cost saving and financial perspective of the 34 self-accountable stores on LOGIS comply with the national norms; that current and updated logistical information of movable assets and consumables is captured on the system; daily, that the available facilities (Balanced Score Card and reports) are utilised and followed up on a regular basis.

Developing and maintaining a digital catalogue (including photos), item description and item identification number of movable assets and consumables to enhance the procurement and provisioning process.

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, BAS, PERSAL, and LOGIS).

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

Loss Control

The daily monitoring and maintenance of the system to ensure that the facilities to register losses are utilised effectively. The further development of the system to provide for consolidated data and management information.

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.

Further to this aim it is important to ensure that the decision-making data is up-to-date and that all available reports that reflect the data are utilised effectively. This data will be analysed to identify areas of risk and concern. These areas will be vigorously pursued with departments and corrective action will be enforced. If systems are utilised optimally, the Accounting Officer and Chief Financial Officer will be in a good position to prevent overspending.

The provincial Treasury forms part of the Technical Committee on Finance (TCF) work group, a sub-committee of the Budget Council, which will actively participate in finalising the TCF position paper on a management strategy in respect of an integrated financial management solution. It hopes to play a significant role in the planning, development, testing and implementation phases of the project. However, all stakeholders agree that the development, testing and implementation of a new Integrated Financial Management System will be a lengthy one, and there is a need to maintain and improve the current systems in the interim.

4.5 Supply chain management (Procurement and Asset Management)

Overview

The current systems of Procurement and Provisioning are fragmented owing to the fact that Tender Boards are at present responsible for procurement and provisioning, which is largely driven by norms and standards set by the national Treasury and partly executed within the framework of the Logis system. The division causes the current systems to be inefficient as far as the method of procurement, contract management, stock control and obsolescence planning are concerned.

Since the advent of the PFMA it has become increasingly important to reassess the functions of Tender Boards and their contribution to effective and efficient financial management within the provincial government. The value of the Western Cape Provincial Tender Board with regard to the processes of fairness, equitability, objectivity and impartiality is indisputable. However, as a result of the cumbersome procurement process and intricate chain of authority, unused funds at the end of financial years have forced departments to use these funds to acquire goods and services without taking into account the principles of effective buying, resulting in poor decision-making. Similarly, provisioning that is mainly driven by the Logis system is time-consuming and does not make provision for immovable property. The management of provincial immovable property, on the other hand, is governed by the Western Cape Land Administration Act, 1998, and is mainly the responsibility of the Department of Transport and Public Works.

It is imperative that a system be developed to eliminate fragmentation and integrate the manner in which procurement and provisioning is being dealt with. Therefore, firstly the Western Cape Provincial Tender Board is being restructured and it is envisaged that it will be replaced by a supply chain management Advisory Council that will, among others, have the following functions:

- promotion of fair, equitable, transparent, competitive and cost-effective supply chain management;
- monitoring and reporting on the fairness, equitability, transparency, competitiveness and cost-effectiveness of supply chain management;
- advising the Minister of Finance on the fairness, equitability, transparency, competitiveness and cost-effectiveness of supply chain management;
- acting as a body of appeal.

Secondly, the responsibility and accountability for procurement and provisioning will be gradually devolved to accounting officers. Thirdly, the provincial Treasury will effectively perform the functions concerned as set out in section 18(c) of the PFMA.

It is recognised that the abovementioned “procurement model” will best serve the interest of the provincial government. Procurement is a powerful tool in the hands of government, and if used more strategically and effectively, a greater number of socio-economic goals, as identified in the RDP, can be achieved. Thus, by developing best practices and procuring in a better, smarter, faster and more cost-effective way, procurement can be used to directly target SMMEs and, among others, enhance the participation of historically disadvantaged individuals (HDIs) in provincial procurement.

In order to achieve this and thereby establish a sensible way forward, a common thread must be sought between procurement and provisioning. This is done by moving towards the process of supply chain management. Supply chain management forms an integral part of Financial Management and introduces international commercial best practices. It seeks to bridge the gap between traditional methods of procuring goods, services and property, stock control and obsolescence planning whilst at the same time addressing procurement-related matters that are of strategic importance.

Supply chain management starts of with the process of demand management and acquisition management that in effect constitutes the procurement process and then moves into the next phase, which is logistics management (in effect provisioning). It finally concludes with the process of disposal management that constitutes the disposal at the end of the useful economic life span of an item and ends the cycle with a performance or **value for money** assessment phase. In practise these phases run concurrently as different items have vastly different useful economic life spans.

The fact that there is no integrated process or strategy with regard to the acquisition, control and disposal of provincial goods, services and property poses the question whether the provincial government is utilising the resources at its disposal to its maximum benefit. The introduction of Public Private Partnerships will be an important tool to improve infrastructure and service delivery efficiency and will bring about a new approach in the optimal utilisation of state resources.

In addition, government's priority is to meet the socio-economic needs of all South Africans and in particular to alleviate poverty. The challenge will therefore be to use procurement as a tool for economic development. The introduction of the concept of black economic empowerment within the supply chain management process is essential for providing more economic opportunities to those historically disadvantaged and therefore seriously facilitates meaningful and sustainable empowerment.

Central to the aforementioned is the budgetary capacity of the provincial government, which will always be a factor that needs to be taken into account. A balance must therefore be struck between affordability and the pursuit of socio-economic objectives. It is important that the provincial government tap the wealth of innovative and specialist skills that is available in the private sector to complement their budgetary capacity to meet the challenge of effective and efficient procurement of goods, services and property whilst ensuring that this process also addresses socio-economic issues.

Procurement

The current system of procurement is rule-driven and it is debatable whether or not it constitutes value for money. It also limits procurement personnel in coming up with innovative procurement practices. The rule-driven approach stems from the fear of unfair practices and the introduction of punitive measures where such rules have been broken. As such it has created a procurement environment in which emphasis is placed on the adherence to rules and minimising possible irregularities instead of encouraging smarter and better procuring and having a more entrepreneurial approach to buying. Procurement personnel in the government are performing procurement administrative functions rather than buying functions. The current system of procurement also has the following inherent risks:

- The different markets and their specific requirements are not fully understood.
- Needs/Requirements of departments are not properly addressed and therefore not clearly defined and specified.
- Bid/tender documents are not prepared effectively.
- Proper cost and benefit analyses are not being done.

The knowledge of procurement personnel is mainly confined to legislation issued by the Western Cape Provincial Tender Board. Limited contract management skills exist, creating unnecessary budgetary pressures due to the inability to deal adequately with contract price adjustments and rates of exchange claims. Limited knowledge of the legality of contracts also extensively increases the Province's risk of possible litigations arising from the conclusion of contracts.

These factors are of concern if it is taken into account that procurement expenditure forms a substantial part of the provincial budget. It is also one of the few areas of considerable discretion whether to spend and on what. As such it should be a high-focus area to ensure that departments stay within their budgets.

The amount spent by the Western Cape government in the 2001/02 financial year through the procurement process is depicted below:

Department	Amount R'000
Premier, Director-General and Corporate Services (PAWC)	180 756
Finance	10 519
Community Safety	20 668
Education	271 397
Health	861 483
Social Services	87 023
Planning, Local Government and Housing	13 814
Environmental Affairs and Cultural Affairs and Sport	39 573
Economic Affairs, Agriculture and Tourism	862 444
Grand Total	**R2 347 677**

These amounts were mainly spent on the following:

Industry/Sector	Amount R,000
Agriculture, Hunting, Forestry and Fishing	81
Mining and Quarrying	2 035
Manufacturing	522 846
Electricity, gas and water supply	77 185
Construction	239 154
Wholesale and retail	417 589
Transport, storage and communication	518 875
Financial and Business Services	386456
Community, social and personal services	181 375
Private house and other activities	2 081
Total	**R2 347 677**

Efficient, effective and economical procurement of goods and services becomes more important if it is taken into account that it is the intention of the provincial government to use it as a tool for economic development, with specific emphasis on the development of small, medium and micro enterprises and increasing the participation of historically disadvantaged individuals in provincial contracts. With regard to the latter, various initiatives were spearheaded over the last couple of years, with the 10 Point Plan Strategy, the Green Paper on Public Sector Procurement Reform, 1997, the Preferential Procurement Policy Framework Act, (2000) and its Regulations (2001) being the most important. These documents established the concept of Preferential Procurement in government service. Although preferential procurement was, to a limited extent, introduced in 1998 in the provincial government, it only took shape with the introduction of the Western Cape Preferential Procurement Policy on 1 January 2002 and the institution of Departmental Plans for Preferential Procurement.

As a result of the introduction of preferential procurement, historically disadvantaged individuals are slowly starting to play a meaningful role in the Western Cape government's procurement environment. Contracts to the value of R207 million and R238 million in the 2000/01 and 2001/02 financial years respectively were awarded to historically disadvantaged individuals. These, however, are not sufficient to facilitate meaningful participation and broaden the economic base. The Minister of Finance and Economic Development therefore directed that at least 40% of the value of provincial contracts awarded needs to flow to historically disadvantaged individuals. As such, departments were requested to reflect their "procurement budget" and the amount earmarked for preferential procurement for the 2002/03 financial year. Preliminary indications are that contracts awarded to historically disadvantaged companies for 2002/2003 will be ± R350 million, which is a substantial increase compared with the previous years.

However, cognisance should be taken of what has been experienced since the full introduction of preferential procurement on 1 January 2002. The concept of preferential procurement has not been fully embraced as the opinion was held that, **firstly**, it would create a burden on the budget, **secondly**, that it would bring complexity to the procurement process, and **thirdly**, that the skills needed to build it into bid/tender documents were inadequate. Further to that, there was a lack of clear strategy at national and provincial levels on how to deal with and effectively implement this concept.

Nevertheless, there is a clear indication of the possible impact of preferential procurement in the provincial procurement environment. Apart from the health and roads construction industries, the province can make a substantial impact on companies owned by HDIs. Within the health industry it was found that HDI companies range from few to non-existent. This is mainly because of the structure of the health industry and the various laws in place governing health products and services. Most of the health products/services are imported and supplied by multinational companies and entry to this market requires a fair amount of capital.

Simultaneously, entry to the roads industry is not easy owing to its complexity and technical nature. In both the aforementioned industries, and others to a lesser extent, it is quite clear that preferential procurement based solely on equity of companies will not bring about the necessary change to facilitate meaningful participation by HDIs, and that other initiatives will have to be pursued. These initiatives would include the promotion of joint ventures between the more established companies, on the one hand, and HDIs and small and emerging companies on the other. A component of such joint ventures will need to be an adequate skills transfer, be it management or technical.

Although the initial aim of preferential procurement is to broaden the economic base and to empower those disadvantaged, there are certain allegations and evidence of possible abuse by established businesses that change their shareholding but not the management structure of their companies so as to take advantage of the system. Likewise, there are allegations that “black” companies obtaining contracts “sell” these to the more established companies. The aforementioned practices are certainly not in the spirit of the Preferential Procurement Policy Framework Act, and if found to be true, strong punitive action should be instituted against offenders.

Public Private Partnerships

Public Private Partnerships (PPPs) are an integral component of the state’s overall strategy for the provision of public services and public infrastructure across all sectors. This does not imply that PPPs are the preferred option for improving the efficiency of service delivery, but rather that they enjoy equal status among a range of possible service delivery options available to departments in all spheres of government.

Infrastructure development through the procurement process, especially through a public private partnership initiative has long-term contractual commitments in mind. However, it must be affordable, provide good value for money and transfer appropriate technical, operational and financial risk to the private sector party. Limited experience with regard to PPP initiatives, specifically those entailing private finance, has produced mixed results. However, if correctly structured, PPPs are a useful service delivery option from both an operational and a strategic perspective.

Existing procurement legislation and regulations are, however, geared to conventional procurement activities, as for civil works construction and the purchase of equipment and services. Existing procedures are neither designed to address the complexities of PPPs nor do they provide a basis for ensuring that the key dimensions (e.g. affordability, value for money and efficient risk allocation) are appropriately evaluated.

Ensuring effective service delivery through PPP arrangements typically requires additional functional capacity in financial, technical and managerial areas that is not normally associated with the operation of a government department. Moreover, while it could be argued that government officials have developed skills as contract managers for simpler forms of PPP arrangements, such as service and basic management contracts, this is not true for more complex PPP contracts. The requisite skills for long-duration contracts that entail significant risks are still in relatively short supply in the public sector and will have to be developed over time. A balanced approach is therefore required, both to build the required capacity and to reduce the demand on capacity, for example, by adopting measures that reduce the complexity of PPP arrangements.

Opportunities for potential PPPs within the Western Cape government and the need to build capacity must still be explored. The Province has identified projects for the nature reserves in the Western Cape, hospitals and clinics, and toll roads, of which the Chapman's Peak Drive is the most advanced PPP thus far. However, the constraints that the provincial government faces are no different from the constraints identified in the national Treasury's Strategic Framework.

Apart from the latter, however, the provinces have inherent constraints that only they themselves can remove, eliminate or find solutions for. Some of the constraints include, among others, the following:

- The PPP unit of the national Treasury and the provincial treasuries needs to build the necessary capacity for the identification and managing of PPPs.
- Treasury Regulations vest all the powers for the approval of PPPs with the national Treasury. Provincial treasuries' role at this stage is undefined and the rules are written in such a way that provincial treasuries can easily be bypassed with the conclusion of a PPP agreement. This can result in unmandated guarantees being imposed on provincial treasuries.
- Provincial treasuries cannot conclude or give authority for the conclusion of a PPP transaction until such time as the national Treasury has given accreditation to a province to do so.

Another potential constraint is that provincial treasuries do not have a dedicated unit to identify and pursue potential PPPs. Should such a unit be established, it would require access to departments to identify potential projects. Apart from that, it would also require greater coherence and cooperation within the provincial Treasury to clear contentious aspects such as the directing of revenue generated by the PPP project and confirmation that provision has been made for related expenditure during the MTEF period. Furthermore, since PPPs normally stretch over longer periods than the MTEF period, suitable budget provisions need to be developed to incorporate expenditure related to PPP agreements.

The level at which PPPs are being pitched are high and indeed rightfully so when looking at the amount of skill that is required to conclude long-term agreements that must stand the test of time in a dynamic legislative and economically sensitive environment. Provincial treasuries must give attention to this aspect and need to develop mechanisms to guide departments. Notwithstanding this, departments must continue to identify possible areas which can be best served via the PPP process.

Asset management

Under the PFMA, accounting officers will be required to compile a balance sheet. Part of that balance sheet will be departmental assets, the management of which is currently covered by Treasury Instructions that are highly prescriptive in terms of both record keeping and procedure.

The current system of procuring goods for departmental use, storing it, accounting for it, and providing it to end users, can best be described as cumbersome. It is probably also very expensive but there are no readily available figures to determine the costs of storage space or the costs of staff and equipment that operate a store. The staffing components in a typical store comprise of: accounting (the paperwork); warehouse (physical storage, issue and receipt notes); transit (checking for quality and quantity); and a limited amount of distribution (delivery to end users).

The summarised process is:

(a) an end user places a request on the store for an item;
(b) the store draws it from stock or, if not held in stock, places an order under a period contract, or seeks quotes, or goes out on tender depending on the money value of the order;
(c) the item, if placed on order, is received into store;
(d) the end user collects the item or it is delivered.

A computerised mainframe-based logistical system (LOGIS) has been developed by the national Treasury over the last decade to try to provide a form of store administration, to monitor stock levels and generate procurement needs, and to provide asset management that is compliant with current Treasury Instructions. LOGIS is not seen to be user friendly, is difficult to comprehend and to operate, and so far has only been installed in limited sites. Many departments are still operating on manual systems, which are very labour intensive. The national Treasury is therefore seriously considering stopping any further enhancements and further roll out of the Logis system.

The databases and the asset and inventory control functions on Logis have some value and should be maintained. Until such time as finality is reached on the life of Logis, the implementation of Logis within institutions in the Western Cape will proceed as planned.

Acquisition and disposal of immovable property

The acquisition and disposal of provincial immovable property also needs to be done with the utmost care and in a transparent manner. From a financial perspective, property represents capital expenditure and wise and careful consideration of such expenditure is required. Property is considered an asset which, in future, may provide a major part of provincial accreditation for accessing loans. Property may also be a productive asset in that it generates additional revenue for the Provincial Revenue Fund.

The usage of provincial properties (land and buildings) needs reviewing in order to ascertain whether or not the properties are in fact being utilised to their optimum. Property is also used in support of socio-economic development. Providing suitable accommodation to client departments dealing with socio-economic matters could contribute towards this. This is done by allocating to the needy and previously disadvantaged individuals and groups suitable premises in order for them to undertake business initiatives. Once again, a demand-driven approach is followed whereby needs are identified and then related to individual properties. The provincial government has already approved a Green Paper for the Management of Provincial Properties in the Western Cape. One of the major recommendations in the Green Paper is the establishment of a Provincial Strategic Accommodation and Infrastructure Plan for the Province. This plan will address the accommodation needs of the Province and redundant properties, and properties that are not needed for the short-term will be identified and can be used for other than provincial users. The eventual White Paper will also address the best use of properties to ensure that they can be utilised for redressing the past as well as making money for the Province to utilise for the maintenance, upgrading or acquisition of properties for the Provincial Property Portfolio.

This White Paper is now in its final stage.

Socio-economic development may also be obtained through utilising individual properties for land restitution purposes. This is not a provincial demand-driven function, but individual provincial properties may become involved. In this instance, therefore, an individual property-driven approach is followed whereby the property determines the action.

In addition, property has the potential to generate income for the Province and its people. Properties with possibilities for business promotion and the generation of revenue for the Province will support economic development and socio-economic development through job creation. Small, medium and micro enterprises (SMMEs) as well as historically disadvantaged individuals and groups will be supported when competing for the utilisation of such properties. Obviously, the additional revenue generated can be redirected into socio-economic development by providing more accommodation to be utilised for that purpose.

As with the procurement of goods, services and property, the disposal of any asset of the Province needs to run through the whole supply chain management process.

Black economic empowerment

Over the past number of years, government has initiated a number of strategies over a broad front to bring about structural change in the economy. In all government programmes, the extent to which black people benefit is a fundamental criterion of operation and success. This has consequently resulted in actions and policies that will have the effect of bringing about black economic empowerment in many spheres of society and the economy.

Government, by introducing the then 10 Point Plan Strategy on Procurement and the Preferential Procurement Policy Framework Act, 2000 and its Regulations, 2001, has endeavoured to promote black economic empowerment (BEE).

Notwithstanding the above, economic power is mostly still in the hands of the few and economic performance overall is still disappointing. The anticipated transfer of ownership to the black majority has not materialised, trapping most in a vicious cycle of extreme poverty, unemployment and underdevelopment. The perception persists that racial inequality remains fundamentally ingrained across all sectors of the business community. This is a structural impediment that continues to distort the efficient functioning of markets in South Africa and reinforce marginalisation, rather than promoting viable and sustained economic participation.

It would appear that the manifestation of low levels of economic participation, especially among young and female South Africans, is due in part to the combined effects of institutional barriers, uncompetitive markets, and inadequate information about job opportunities.

The challenge facing South Africa dictates a fundamental change in approach in all sectors of society, particularly in established business. There should be a sustained effort to mobilise all South Africans to arrive at national consensus on the priorities of economic transformation and the roles and obligations of all stakeholders in helping achieve these objectives. This, by definition, has to be a State-driven programme. Markets tend to reinforce an existing distribution of incomes and assets. This is unacceptable in a country such as South Africa, where the market mechanism was deliberately distorted to allocate incomes and assets on non-price criteria such as race. The private sector needs to recognise its collective responsibility to invest in the country and assist government in achieving development goals. The private sector should be encouraged to take into account private and social returns and factor longer-term and strategic considerations into investment decisions. This is an inclusive process and its outcomes are for the benefit of the whole nation and future generations.

Needless to say, the immigration from the existing to the ideal situation will require national and associated provincial strategies which will probably take about 10 years to come to fruition. However, one should not lose sight of immediate interventions that should be put in place to strengthen such a national strategy.

Government procurement has long been identified as a strategic tool to ensure that certain socio-economic goals are attained. The estimated R60 billion spent by the local, provincial and national spheres of government has therefore over the last couple of years been targeted to a large extent to increase the participation of black businesses in government contracts. Unfortunately no meaningful data exists to establish the contribution of these spheres of government.

The Western Cape government's overall expenditure on procurement is R2,3 billion, and although it is relatively small in the national context, one should not underestimate the value that it can add to black economic empowerment. However, it is imperative that one should have a deeper understanding of the Western Cape economy to identify its dynamics, backward and forward linkages, constraints, enabling factors and skill requirements to promote black economic empowerment.

Way forward

The aforementioned paragraphs illustrate the fragmented approach within which government resources are being utilised. As mentioned earlier, a common thread must be introduced to integrate these processes so as to form one process referred to as supply chain management, which will seek to bridge the gap between traditional methods of procuring goods, services and property, stock control and obsolescence planning, whilst at the same time addressing procurement-related matters that are of strategic importance.

The key to supply chain management is the introduction of the value-for-money concept, of which the following requirements are an integral part:

A total needs assessment dealing with -
- an understanding of future needs and making provision for it in the MTEF;
- the identification of critical delivery dates and the frequency of needs;
- the determination of proper bid specifications addressing the relevant needs and not a specific product or service in the market.

The development of proper documents fully addressing:
- preferential procurement requirements;
- the strategy on how to approach the market;

- the concept of total cost of ownership, including life cycle and inventory carrying cost;
- bid evaluation in criteria, how bids will be evaluated and how contracts will be administered and managed.

Proper logistical management, including -
- the coding of items and setting of inventory levels;
- placing, receiving, expecting and distributing national warehouse management orders;
- transport management and supplier performance.

Obsolescence planning to achieve the best returns for the Province by -
- maintaining a database of materials and redundant stock;
- determining the economic life of an item;
- determining the best possible disposal strategy.

Each phase of this concept, as depicted above, requires its own set of standards, some regulated by the national Treasury, the rest in a cascading manner by provincial treasuries, accounting officers and accounting authorities, as provided for by the PFMA and other supporting legislation respectively. Apart from acquiring the systems, building the capacity in departments, schools and public entities, making sure at least of nominal compliance with any prescribed standards (regulations) and developing the substantive standards (benchmarking, including practice notes) to effectively roll out this new concept of achieving value for money throughout the supply chain management cycle, implies a whole set of new challenges for provincial treasuries.

The challenge within the provincial government will be to transform the existing rule-driven and fragmented way in which procurement and provisioning (assets) are currently being dealt with. Systems need to be put in place that can generate the management information needed for sound financial and economic decision-making. Current personnel need to be re-skilled and/or adequately skilled personnel should be recruited to drive supply chain management within the provincial government. The provincial Treasury needs to increase its capacity with regard to proper contract management, black economic empowerment initiatives and public private partnerships. In addition, they need to put the necessary policy and monitoring mechanisms in place to assist departments to achieve the provincial Government's goals with regard to black economic empowerment.

The ability of the historically disadvantaged to take advantage of the economic opportunities presented by an expanding economy must be increased. The contribution of R2.3 billion (provincial procurement) is relatively small compared with the Western Cape's GGP, and although it is not significant enough to change the structure of the provincial economy, it will create opportunities for BEE companies to get a foothold in the economy and to benefit from the multiplier effect. The reallocation of expenditure to BEE companies will have a significant impact on stimulating growth and job creation. It is, however, important that further research should be undertaken to identify the inhibitive and promotive factors for BEE in order to establish successful models which could be emulated by the private sector.

Creating opportunities for BEE companies will, however, not be enough. The provincial government will need to decide to what extent it will provide additional support, which will include hand-holding and access to finance, to BEE companies to ensure that they play a meaningful role in the Western Cape economy.

4.6 Cash management

Overview

After this country's first democratic elections in 1994, the new provincial dispensation was constituted. Similarly, the functions pertaining to the high-priority task of cash management were devolved to the provincial treasuries. This meant that the provinces would be solely accountable for their financial position, thus ensuring that the unique needs of each province could be served. Accordingly, the Western Cape Exchequer Law, (Law 4 of 1994), stipulated, inter alia, that a prescribed banking account configuration should be held at a commercial bank.

On 1 April 1995, a Provincial Exchequer Account and two Paymaster General accounts were opened, viz. the Department of Education and a single account "Other Departments" to service the needs of the remainder of the departments within the provincial government.

On 1 July 1999, amendments to the Public Service Act, 1994 (PSA) and the Public Service Regulations, 1999, were effected, which devolved considerable powers to executing authorities (national and provincial), and established provincial departments as autonomous entities, which provided for the further devolution of financial functions to the departments. The Public Finance Management Act, 1999, (Act 1 of 1999), as amended, applicable with effect from 1 April 2000, which has as its main objective to secure accountability and sound management of the revenue, expenditure, assets and liabilities within government spheres as a whole, was instrumental in permitting the decentralisation of cash flow management to the various provincial departments.

In terms of this policy of decentralisation, a Paymaster General Account has been opened for each of the thirteen provincial departments. This has contributed largely to effective cash flow management in the provincial government.

Legal Framework

- The Constitution, 1996
- The Public Finance Management Act, 1999 (Act 1 of 1999)
- National Treasury Regulations
- Provincial Treasury Instructions
- Western Cape Exchequer Law, 1994 (Law 4 of 1994)
- Direct Charges Act, 2000 (Act 6 of 2000)
- Division of Revenue Act, 2002 (Act 5 of 2002).

Mechanisms

The source of this Province's funding originates mainly (94%) in the national Treasury by way of the payment of an equitable share and conditional grants, whilst the remainder is sourced from provincial own revenue such as motor licence fees, hospital patient fees and gambling taxes. The national share is transferred to the Province on a weekly basis by means of an electronic funds transfer into the Provincial Exchequer Account, which is the accredited account of the Province into which all revenue flows. These transfers are credited in terms of a payment schedule, which is made available by the national Treasury prior to the commencement of the financial year and reflects the total allocation originating in the national Treasury. A unique bookkeeping system, which does not form part of the transversal financial systems used by government, is maintained which records all income and expenditure pertaining to the Provincial Revenue Fund, to ensure accountability and an accurate audit trail. Each provincial department within the provincial government provides the provincial Treasury, prior to the commencement of the financial year, with estimates of revenue and expenditure for the following financial year, which facilitates the cash management process. Each departmental Paymaster General Account is funded on a daily basis from the Provincial Exchequer Account in terms of daily cash flow inputs from the various departments. The cash management system of the provincial banker, to which the province has a direct link, is utilised to perform such electronic transfers. Once the daily cash flow has been finalised, any moneys which are not immediately required to defray expenditure are invested at financial institutions, in terms of an internal investment policy. At any given time, the Provincial Revenue Fund experiences a temporary accumulation of funds as a result of "delayed payments", i.e. orders that have been placed, but in respect of which, owing to delivery periods, the necessary invoices have not yet been received and payment therefore has not been made.

Challenges

The ever present challenge with regard to cash flow management is the continued striving for improvement and refinement of the various planning and work procedures, utilised to perform the tasks related to this function, which will culminate in the enhancement of effective cash flow management in the Province.

The training of the relevant officials within the provincial departments in so that they can provide the provincial Treasury with accurate cash flow information on a daily basis is a further challenge. This will greatly improve cash flow management.

The envisaged cash flow model, which the national Treasury is considering implementing within provincial governments, will result in a new working environment, thereby presenting fresh challenges with regard to cash flow management.

In order to increase provincial revenue by means of interest on investments, optimum interest rates must be obtained from financial institutions, taking into account the maximum exposure to these institutions, associated risks and investment periods.

The ultimate challenge, however, is to ensure that, on the one hand, the accounts within the provincial government remain minimally cash positive on a daily basis and, on the other, that no overdrawn situation occurs at any time.

Fiscal adjustments (Risk management)

The national Treasury may amend the monthly percentage attached to the payment of the equitable shares of the provinces. This could result in a decreased amount being transferred to the Provincial Exchequer Account.

Provincial departments own revenue may not reach the budgeted amount, or may experience dips in anticipated revenue flows, which will reduce the flow of income to the Provincial Revenue Fund. If a provincial department does not realise its budgeted revenue for a specific financial year, the expenditure levels must be reduced accordingly.

The financial institution with which investments are placed may for many reasons not be in a position to repay the capital and interest upon maturity.

The national Treasury has recently proposed that the equitable share and conditional grants earmarked for this Province should, be credited directly to an account held at the Corporation for Public Deposits. This mechanism has, however, not been finalised but if implemented, there is a real risk that the interest earnings will be substantially less than is currently generated and that the interest projections in terms of the Medium-Term Expenditure Framework will not be realised.

An initiative launched by the national Treasury that questions large provincial bank and cash balances has recently been presented to provinces for discussion. Apart from running counter to the principles underpinning financial asset management, assessing accumulated capital cannot be done on a simplistic cash basis, but requires taking aboard accumulated liabilities or commitments, inclusive of specific economic infrastructure investment initiatives. Therefore balances at face value cannot be regarded as an unfettered cash reserve. In any case, if balances were to be artificially reduced, the risk of an overdraft situation is a real possibility.

Liabilities versus cash

Cash reserve

The increasing demands being made on the Social Services budget in the Province will most likely result in overspending by this department for the current and ensuing financial years. Further pressures are building up at Education and Health, requiring rather innovative steps apart from adjustment, particularly for Social Security, of the vertical share distribution of nationally received revenues between the three spheres of government. If additional resources cannot be found and directed to these sectors, the continued provision of services of an acceptable standard might be jeopardised. If such moneys do not materialise, funding will have to be obtained by restructuring the Province's own resources to finance any shortfalls.

Currently, the Provincial Revenue Fund has a net uncommitted cash reserve of about R33 million, which represents the beginning of the second cash transfer to the Department of Transport and Public Works for agreed to infrastructure investment in synergy with other economic development initiatives currently under consideration.

Smoothing

To compensate for the variability in internal revenue flows, it was necessary to smooth the Province's current and capital outlays with total revenue received over the 2002/03 – 2004/05 MTEF period to ensure that expenditure is kept relatively constant in real terms for all departments. The current smoothing was financed from anticipated revenue receipts over the full MTEF term, but work is underway to find a more efficient method. One possibility is to put the outstanding cheque list to better use. Smoothing in this manner should not have a negative impact on cash flow as the outstanding cheque list, amounting on average to R30 million after allowing for electronic funds transfers (EFT's), should allow the availability of funds on a rolling basis. The gap between orders placed and payment on delivery allows a further cushion.

Conclusion

The main intention is to ensure that cash flow management in the Province is maintained at its current high levels of efficiency and to keep on striving for improvement in all the spheres related thereto. The positive spin-off of these practices will be to place investments at various financial institutions according to an approved investment policy, which will result in the receipt of optimum interest gains. This in effect will mean that interest will be constantly capitalised, resulting in the accumulation of capital, which will in turn be utilised to finance major infrastructure projects. In maintaining minimal cash and bank balances, the risk of an overdrawn position is ever present and will require innovative steps to remain cash positive.

4.7 Accounting

Overview

With the inception of the Interim Constitution in 1994, the need to reorganise and rationalise government departments was identified as a priority, *inter alia* to improve service delivery in government departments, which functioned in terms of the old Exchequer Act (Act 66 of 1975) and Treasury Instructions. 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 readjustment 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, which operated on the centralised Financial Management System (Department 70), to the respective departments. This was a phased approach, with the first phase taking place during the 1999/2000 financial year, the second phase during the 2000/2001 financial year and the third and final phase during the 2001/2002 financial year. Hence, the discontinuation of the centralised Departmental Accounting Services with effect from 1 April 2002. Each department now operates as a separate department on the Financial Management System and can be held accountable for its actions.

The enactment of the PFMA in April 2000 also necessitated the establishment of a provincial Accountant-General component within the provincial Treasury, whose main purpose is to ensure that norms and standards within the legislative framework are implemented and complied with in provincial departments. An evaluation by the Norms and Standards component in the provincial Treasury on the implementation of the PFMA for the period post-2000 revealed a 90% success rate in provincial departments. It should, however, be noted that the evaluation was based on nominal compliance with the PFMA and focused 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 a framework for banking arrangements; completing the financial statements on time, and the delegation of responsibilities. It is pleasing to note that the financial statements in the new format (GRAP) were submitted to the Auditor-General within the prescribed timeframes by all departments for the two years running.

Internal prescripts, viz. Provincial Treasury Directives, were developed for the Province as an interim measure. These have been revisited and were reissued with effect from 1 December 2001 as Provincial Treasury Instructions. This allowed 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. The provincial Treasury is in the process of revising the existing Provincial Treasury Instructions, which will be in line with the new Treasury Regulations issued on 27 May 2002.

Accounting policies and related matters

The financial statements are prepared in accordance with the following policies, which are applied consistently in all material respects. However, where appropriate and meaningful, additional information is disclosed to enhance the usefulness of the financial statements and to comply with the statutory requirements of the Public Finance Management Act, Act 1 of 1999 (as amended by Act 29 of 1999), the Treasury Regulations for Departments and Constitutional Institutions issued in terms of the Act, and the Division of Revenue Act, Act 1 of 2001.

- Basis of preparation

  The financial statements are currently prepared on the cash basis of accounting except where stated otherwise. 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. The basis of preparation will, however, evolve as we progress towards accrual based accounting.

- Revenue

  Voted funds are the amounts appropriated to a department in accordance with the final budget (original plus the adjustment estimate). Interest received is recognised upon receipt of the funds, and no accrual is made for interest receivable from the last receipt date to the end of the reporting period. Unexpended voted funds are surrendered to the Provincial Revenue Fund.

  Dividends received are recognised as revenue in the financial statements of the department, however, it is also recognised as an expense in the same year, as the dividends are paid over to the Provincial Revenue Fund.

- Expenditure

  Capital and current expenditure is recognised in the income statement when the payment is made. Interest paid is also recognised when paid and no accrual for interest is made between the payment date and the reporting date.

- Unauthorised, irregular, and fruitless and wasteful expenditure

  Unauthorised expenditure means the overspending of a vote or a main division within a vote, or expenditure that was not made in accordance with the purpose of a vote or, in the case of a main division, not in accordance with the purpose of the main division. Unauthorised expenditure is treated as a current asset in the balance sheet until such expenditure is recovered from a third party, authorised by the provincial Parliament, or funded from future voted funds.

  Irregular expenditure means expenditure, other than unauthorised expenditure, incurred in contravention of or not in accordance with a requirement of any applicable legislation, including the Public Finance Management Act, the State Tender Board Act, or any regulations in terms of this Act, or any provincial legislation providing for procurement procedures in that provincial government . Irregular expenditure is treated as expenditure in the income statement until such expenditure is either not condoned by provincial Treasury or the Western Cape Provincial Tender Board, at which point it is treated as a current asset until it is recovered from a third party.

  Fruitless and wasteful expenditure means expenditure that was made in vain and would have been avoided had reasonable care been exercised. Fruitless and wasteful expenditure is treated as a current asset in the balance sheet until such expenditure is recovered from a third party.

- Debts written off

  Debts are written off when identified as irrecoverable. No provision is made for irrecoverable amounts.

- Assets

  Physical assets (fixed assets, movable assets and inventories) below R5 000 are written off in full when they are paid for and are accounted for as expenditure in the income statement. Physical assets above R5 000 are capitalised and are accounted for in the balance sheet. Depreciation on capitalised assets is accounted for in the income statement.

  Receivables

  Receivables are not normally recognised under the cash basis of accounting. However, receivables included in the balance sheet arise from cash payments that are recoverable from another party.

- Payables

  Payables are not normally recognised under the cash basis of accounting. However, payables included in the balance sheet arise from cash receipts that are due to either the Provincial Revenue Fund or another party.

- Provisions

  Provisions are not normally recognised under the cash basis of accounting.

- Lease commitments

  Lease commitments for the period remaining from the accounting date until the end of the lease contract are disclosed as a note to the financial statements. These commitments are not recognised in the balance sheet as a liability or as expenditure in the income statement as the financial statements are prepared on the cash basis of accounting.

- Subsequent payments

  Payments made after the accounting date that relates to goods and services received before or on the accounting date are disclosed as a note to the financial statements. These payments are not recognised in balance sheet as a liability or as expenditure in the income statement as the financial statements are prepared on the cash basis of accounting.

- Employee benefits

  Short-term employee benefits

  The cost of short-term employee benefits is expensed in the income statement in the reporting period that the payment is made. Short-term employee benefits that give rise to a present legal or constructive obligation are deferred until they can be reliably measured and then expensed. Details of these benefits and the potential liabilities are disclosed as a note to the financial statements and are not recognised in the income statement.

  Termination benefits

  Termination benefits are recognised and expensed only when payment is made.

Retirement benefits

The department provides retirement benefits for its employees through a defined benefit plan for government employees. These benefits are funded by both employer and employee contributions. Employer contributions to the fund are expensed when money is paid to the fund. No provision is made for retirement benefits in the financial statements of the department. Any potential liabilities are disclosed in the financial statements of the Provincial Revenue Fund and not in the financial statements of the employer department.

Medical benefits

The department provides medical benefits for (certain/all) its employees through defined benefit plans. These benefits are funded by employer and/or employee contributions. Employer contributions to the fund are expensed when money is paid to the fund. No provision is made for medical benefits in the financial statements of the department.

Retirement medical benefits for retired members are expensed when the payment is made to the fund.

- Capitalisation reserve

  The capitalisation reserve represents an amount equal to the value of the investments and/or loans capitalised, or deposits paid on behalf of employees of a foreign mission, for the first time in the previous financial year. On disposal, repayment or recovery, such amounts are transferable to the Provincial Revenue Fund.

- Recoverable revenue

  Recoverable revenue represents payments made and recognised in the income statement as an expense in previous years, which have now become recoverable from a debtor due to non-performance in accordance with an agreement. Repayments are transferred to the Provincial Revenue Fund as and when the repayment is received.

- Comparative figures

  Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year. The comparative figures shown in these financial statements are limited to the figures shown in the previous year's audited financial statements and such other comparative figures as the department may reasonably have available for reporting.

General concerns with accounts in the Province

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

  There is genuine concern to establish 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 in respect of the tricameral system and the former Cape Provincial Administration, this aspect was taken up under Statement of Contingent Liabilities in section 4.8.1.

- 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 and 2001/2002 financial years reflected a marginal increase to 30%. The qualification of audit reports in general is largely due to the lack of capacity in departments. The key areas of audit qualification are poor internal checking and control, and asset management.

- Internal audit/Audit Committee

  Notwithstanding this Province having a shared Audit Committee and a centralised Internal Audit unit, the reliability of these units, which is an important tool for proper fiscal discipline, appears to be of concern. The Auditor-General, in his audit report for the 2000/01 financial year, could rely on the work of the Internal Audit unit only to a limited extent. Capacity constraints were cited as the primary factor that hampered the work of Internal Audit. Although the Auditor-General's opinion for the 2001/02 financial year progressed to moderate reliance on the work of the Internal Audit unit, full reliance should be the ultimate goal pursued by the Internal Audit unit.

  Some of the benefits of internal audits are:

  - ♦ Internal Audit reviews operations and programmes to evaluate whether (a) goals and objectives which are consistent with those of the organisation have been established, (b) adequate performance criteria have been established to measure accomplishment, (c) goals and objectives are being met, (d) the manner in which goals and objectives are met is consistent with organisational values, and (e) accountability has been established.

  - ♦ It also carries out risk assessment pertaining to the information systems environment, the reliability and integrity of financial and operational information, the effectiveness and efficiency of operations, the safeguarding of assets and compliance with laws, regulations and contracts and must be conducted at least annually. Based on the results of the risk assessment, internal audit should evaluate the organisation's controls to determine their effectiveness and efficiency and make recommendations aimed at improving them.

- Limited interpretative skills, coupled with the lack of understanding of the financial reforms required of the PFMA.

  Departments have shown limited knowledge with regard to analysing accounting reports, financial statements, etc. with a view to taking timeous corrective actions to remedy identified shortcomings. This could lead to poor financial management, including an unhealthy state of the books of account, which, in turn, could result in poor financial statements and qualified audit reports. In addition, departments have shown a tendency to comply only nominally with the requirements of the PFMA instead of invoking the financial reforms intended by the PFMA. The following are areas of concern where departments have complied only nominally with the PFMA without adding value to the standard of service delivery, performance and effective financial management:

  - Macro risk assessments have been carried out in departments instead of detailed risk analyses;
  - Resultant strategies, viz. fraud prevention plans, are largely ineffective to manage risks due to macro assessment;
  - Analysis of audit reports has been poor, if done properly, such analysis would prevent repetition of shortcomings.

- Replacement or upgrading of financial systems

  Having highlighted the above concerns, it is also important to highlight the inadequacies of the financial administration systems as a concern. The existing financial administration systems need to be upgraded if departments, including the provincial Treasury, are to reap the full benefits intended by the PFMA and to enable accounting officers to discharge their financial management obligations properly, as required by the PFMA. Slow progress in this regard hampers the full implementation of GRAP, especially with the intended shift from a cash to accrual basis of accounting, and the facilitation of proper performance management by accounting officers. Progress in this regard is therefore also of paramount importance. The national Treasury has identified the Integrated Finance Management Solution as the system to resolve these shortcomings. For more details, see section 4.4.

  Way forward

- 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 the spirit of the PFMA. In order to improve fiscal discipline in the Province, it is essential that the provincial Treasury should enforce the national and provincial norms and standards in provincial departments and ensure the proper functioning of intergovernmental systems, internal controls, risk management processes and the accountability chain.

- Mooting the idea of a separate Audit Committee and Internal Audit units by the provincial Treasury can be seen as the first steps towards improving the effectiveness and reliability of these units by the Auditor-General. The first phase involves the decentralisation of the shared Audit Committee during the 2002/03 financial year, followed by the decentralisation of the centralised Internal Audit unit during the 2003/04 financial year as the second phase. The Western Cape Cabinet approved on 14 August 2002 that three different Audit Committees be established in the Western Cape Provincial Administration. The decentralisation was based on the 80/20 principle, which in effect will mean that the bigger departments, viz. Education and Health and possibly Social Services and Poverty Alleviation will have their own Audit Committee and Internal Audit units. The remaining departments will have a shared Audit Committee and a centralised Internal Audit unit. If necessary, the future position of the shared Audit Committee and centralised Internal Audit units for the remaining departments will be reviewed for the purpose of maintaining their effectiveness.

  There is considerable value in investing in Internal Audit. Thus it is essential that accounting officers should allocate adequate funds to ensure effective Internal Audit units.

- Although it is essential that departments should comply at least nominally with the relevant prescripts (regulatory framework, reporting requirements and timelines) it is also important that the financial practitioners should start grappling with substantive implementation of the PFMA, which will entail the ability to set benchmarks (quality) for financial management and financial functionaries (CFO structure) standards. Central to the success of this is capacity building.

- The process of setting standards of generally recognised accounting practice and of publishing directives and guidelines concerning the standards should be prioritised and expedited by the Accounting Standards Board. Although we are aware that the Accounting Standards Board is in its early stages of operation, the following are priority areas that the Board needs to focus on:

  - The Chart of Accounts that will ensure transparency in government accounting,
  - GRAP standards for financial statements;
  - Standards for asset management, in particular asset valuation and depreciation.

  This will enhance accountability by producing quality financial statements coupled with appropriate interpretative and analytical accounting skills in departments, public entities and treasuries as accrual-based accounting evolves.

- In terms of sections 6(2)(c) and 18(2)(d) of the PFMA, the relevant Treasury is required to monitor and assess the implementation of national and provincial norms and standards in public entities. In order to assist the designated department in playing an effective oversight role in respect of public entities, a "PFMA checklist for public entities" was developed and implemented. This should be seen as the first step towards promoting public entity compliance with the basic requirements of the PFMA, in other words, nominal compliance. Based on the progress reports received for the first quarter of 2002, the following key focus areas have been complied with by public entities:
  - Processes have been established to oversee public entities (section 63(2) of the PFMA);
  - Public entities have submitted quarterly reports to executive authorities (TR 26.1.1);
  - All public entities have submitted their strategic plans for the 2002/03 financial year to the relevant executive authority for approval;
  - Written assurances in terms of section 38(1)(j) have been obtained;
  - All public entities have submitted their financial statements for the 2001/02 financial year to the Auditors and the provincial Treasury in terms of section 55(1)(c).

- As we progress towards accrual-based accounting, recording and reporting of assets in the books of account is increasingly becoming a priority. In order to facilitate the process, national Treasury has suggested the following:

  Assets acquired from 1 April 2002 should be capitalised and reflected on the financial statements for 2002/03. The recording of existing assets by all the departments should be completed by:

    - December 2002 for assets bought in 2001/2002
    - March 2003 for assets bought in 2000/2001
    - September 2003 for assets bought in 1999/2000
    - March 2004 for assets bought prior to 1999/2000

Assets valued at R5 000 and above are to be capitalised and depreciated over its useful life (major asset), and assets valued below R5 000, expensed and classified on the assets register as controlled assets (minor asset). The classification of asset categories (for disclosure in financial statements and recording in fixed asset register) is adopted from the various accounting standards, International Federation for Accountants (IFAC), Accounting Standards Board (ASB) and Government Financial Statistics (GFS). A straight-line depreciation method is used for all asset categories in the departments. Depreciation is an instrument used to recognise the cost of consuming the service potential of an asset over time and provides a means of accounting for the cost of an asset over its useful life.

4.8 Contingent liabilities and Debtors

4.8.1 Contingent liabilities

Overview

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

This section should be seen as a further attempt to provide information on the WC government's contingent liabilities and intends to:

- Inform decision-makers of the legal requirements prescribed for the provincial Treasury and for accounting officers for managing 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;
- Describe the lessons learnt from the past and the challenges facing the future management of contingent liabilities.

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.

Prior to the implementation of the PFMA, which provides for a similar intervention, the WC government took the policy decision[3] that budget overexpenditures and amounts undercollected 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[4] to set aside R50 million over each of the medium-term expenditure frameworks, commencing in 2001/02, as a contingency reserve. In the 2002 Budget this provision was increased to R102,850 million (R52,750 million for contingent liabilities and R50,000 million for unforeseen and unavoidable contingencies). This contingency reserve is used mainly to provide for variables such as internal and external shocks that emanate from economic and other

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

factors, in particular unforeseeable and unavoidable expenditure. Such expenditure in term of the Treasury Regulations, 2002 does not include:

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

The downside 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, 2002 to 2005, it represents on average 0,74 % of voted/baseline funds.

Legal framework

An appropriate departure point for this section, 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, 2002, subsequently issued in terms of this 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 of them, in terms of section 38(1)(a)(i) and (d), respectively, to ensure that they have and maintain effective, efficient and transparent systems of risk management, and to manage any liabilities responsibly.

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 WC 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, 2002 13.1.4 requires accounting officers to report on all contingent liabilities, e.g. 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 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 may also 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 which exist but involve 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 as to 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 from 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, for example, be in a position 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 need 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;
- 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 in respect of the tricameral system with the former Cape Provincial Administration during the 1994/1995 and subsequent financial years. It is imperative that these amounts should be identified as they may influence contingent liabilities. The decision to decentralise the Departmental Accountant Services resulted in a separate Financial Management System (FMS) being implemented for each department and the closing down of the centralised Departmental Accountant Services, i.e. after 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 last three provincial departments which operated on the centralised basis could only be transferred after the closing of the 2001/02 financial year (after April 2002). To check whether all contingent liabilities have been identified, departments were requested to carry out a similar exercise, in particular the Department of Education, which 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, with no financial and human resource allocation, the provincial Treasury appointed a project team funded out of a special allocation to determine the contingent liabilities. The final report of the project team will be received by the end of the 2002/03 financial year.

Some departments misused the opportunity of “Contingent Liability” to list some other spending pressures which they could not accommodate within their normal budget allocations. It also appears that departments experience interpretation problems with the definitions. Further work is thus required to refine the definitions.

Although “Contingent Liabilities” is not captured and reflected here, departmental budgets are under tremendous pressure due to, among others, high inflation, court cases (claims and legal cost) and the weakening exchange rate.

Conclusions

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 programme, and reform its analytical, policy and institutional public finance frameworks to address all major fiscal risks.

It is clear from the definitions furnished earlier that there is some difference in approach from an accounting and 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 a requirement that some information with regard to contingent liabilities should be captured in the annual reports of provincial departments. An assessment of the 2001/02 annual reports that include the financial statements revealed that on aggregate the following items were presented:

	R’Million
Housing guarantees	189,489
Guarantees motor vehicle	0,280
Capital commitment in respect of Health Information System project	63,239
Legal claims	45,374
Other	0,535
Total	**298,917**

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 provincial Treasury need to engage in order to establish institutional capacity to achieve these objectives.

Although legal requirements need to be complied with, care needs to be taken not merely to 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 a fact that the 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. It is therefore possible that a combination of the decreased value of the rand and the nature, volume and timing of goods purchased from foreign countries may threaten budget stability.

Intergovernmental function shifts may also threaten future budget stability. The general trend is that functions are transferred from national to provincial to local government spheres or from provincial to local government. However, in the case of library services a new phenomenon has surfaced. In this regard, the Constitution of the Republic of South Africa, 1996 (Act 108 of 1996), in Schedule 5A, ostensibly identifies libraries (excluding national libraries) as a functional area of exclusive **provincial legislative competency**. The usual implication is that the WC 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 or, alternatively, complete cessation of these services.

Clearly this would seriously threaten fiscal and service stability. The challenge is to approach the situation with caution, among others from a management, legal, political and financial perspective. With regard to the financing perspective, the principle of funds-follow-function should apply. This will, for example, entail an intergovernmental agreement on an adequate and appropriate shift in resources from the local to the provincial equitable share through the vertical share mechanism, or by some other acceptable and sustainable means. The drafting of a position paper on how to deal with the vexing challenges is in progress. (See Chapter 4: Local Government for further details.)

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 so as to prevent growing underrecorded claims on the budget or expansion of contingent liabilities and the undermining of budget stability and integrity, as well as to prevent government from not meeting its obligations.

Recommendations

Given current challenges to the budget, expenditure to date, enormous needs and requirements, 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 an once off provision mainly for unforeseeable and unavoidable expenditure.

This is done on the understanding that the risk is spread between the provincial Treasury, to the above limit, and the provincial department 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 that department, beyond which other departments will collectively be required to provide financial support in liaison with the Provincial Top Management and the Cabinet. Decisions on the utilisation of the R100 million, set aside for unforeseeable and unavoidable expenditure to assist provincial departments, cannot be taken bilaterally, but only after wider consultation.

If the reserve is not used, it will be rolled over into the next financial year but topped up to keep the real value constant. If drawn down, any remaining balance will similarly have to be augmented in future financial years to bring it back to the minimum real level of R100 million in 2002 rand value. In essence this becomes a shock absorber for external shocks to the budget.

Further work will have to be undertaken to refine the definitions in this section and their interpretation.

4.8.2 Debtors

Overview

The recovery of outstanding debts in the WC government has deteriorated to such an extent that it has become a matter of serious concern. The nominal outstanding debt in provincial departments since March 2001 stands at about R0.5 billion.

The financial systems currently employed by the WC 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 some of these systems to administer debts effectively 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
- No electronic filing system.

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 service potential or benefits are expected to flow to the entity.

A debtor is a person who owes an account receivable. This includes claims, damages, fees, fines, forfeitures, loans, overpayments, tuition, penalties, interest and other costs authorised by law.

Managing debtors

The Province is faced with increasing demands for funds to provide for education, health care, law enforcement and other programmes, but it must also contend with limited resources and strong opposition to higher user fees or taxes. It is therefore important that all money owed to the Province should be collected effectively and efficiently.

There may be social or economic reasons that outweigh the need for vigorous collection of some provincial debts — for example, debts owed by extremely poor persons. Conversely, overdue debts must be vigorously pursued in order to encourage future voluntary payment of accounts receivable. Also, the Province is expected to collect its accounts receivable in a manner that is fair and equitable (consistently treating taxpayers and other debtors in similar circumstances in the same manner). This limits the extent to which the Province is willing to negotiate compromise arrangements whereby a debtor pays only a portion of the amount owed.

The provincial Treasury recognises the above, but is also convinced that, as a general rule, overdue accounts are more likely to be collected if efforts to collect are made soon after the debt becomes due and if the debtor believes that the creditor will be persistent in its efforts to collect. It therefore requires departments to take prompt and vigorous action to collect outstanding accounts receivable.

Overall, debt collection processes are fragmented and inconsistent and some are poorly resourced. Some departments have only recently become involved in collection and they lack the expertise and resources to do the job properly. Many of the debts owed to the Province are difficult to collect, but we believe the results could be improved by setting a clear direction for collection, looking for opportunities to improve effectiveness of collection, introducing resources to collect debts, and making judicious use of private sector collection agencies. Management processes for debt collection activities need to be improved. Performance measurement is minimal and good data is scarce. Finally, we find that departments produce little or no information about the collection of overdue accounts receivable.

The Province's efforts to recover overdue accounts have been hampered by inadequate computer systems, poor support structures, and insufficient knowledgeable staff. However, the Province's performance may improve as a result of the Public Finance Management Act (PFMA), which makes accounting officers accountable for the financial performance of their departments and the extra efforts as a result thereof. We acknowledge the difficulties facing the departments; however, we believe that performance by them can and should be improved, even if this implies that departments have to make use of manual follow-up procedures and systems. This is a further illustration of poor capacity, system problems, and the inability of CFOs to carry out their responsibilities properly because of system deficiencies. Each of these facets is dealt with separately in this policy; however, the problems encountered should be seen holistically if we are to bring about effective debt management.

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 should be identified and addressed. In order to assist in addressing the debtors situation of the Province, the provincial Treasury has issued best practice documents to departments. The purpose of the documents 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 and a debt write-off policy in place, and the best practices serve as a guide to develop such departmental debt policies. Owing to the emphasis of effective and efficient debt collection referred to in the PFMA, departments have been advised to ensure that the necessary control measures are put in place to comply with the PFMA.

Finally, we are concerned at the lack of meaningful information reaching the provincial Parliament regarding overdue debts. The amounts are large and, in this era of scarce resources, this can only have a negative impact on provincial service delivery. We believe the provincial parliament should receive all relevant information regarding departments' goals with respect to the collection of debts, and obtain assurance that these goals are being pursued and reached.

Statement of debtors

Table 6 below reflects the outstanding debts per department as at 31 March 2002.

DEPARTMENT	31 March 2001 R' 000	31 March 2002 R' 000	INCREASE/ DECREASE R'000	Variance %
Education	73 675	71 200	(2,475)	-3.36
Health	112 926	112 844	(82)	-0.07
Social Services	13 573	18 288	4,715	+34.74
Parliament	97	69	(28)	-28.87
Finance	16	9	(7)	-43.75
PAWC Dept. 70*	2 440	3 151	711	+29.14
Planning, Local Government & Housing	238	233	(5)	-2.10
Economic Affairs, Agriculture & Tourism	268 758	303 498	34 740	+12.93
TOTAL	**471 723**	**509 292**	**37 569**	**+7.96**

* Consolidated debts in respect of departments falling within the centralised Departmental Accountant Services (FMS Dept 70), viz. Community Safety, Provincial Administration: Western Cape and Environmental and Cultural Affairs and Sport.

Note: Due to the split of the Department of Health and Social Services during the 2000/01 financial year the amount of R13,573 million reflected against the Department of Social Services as at 31 March 2001 was only in respect of social pensions and grants and did not include any other types of debts which at that stage were included in the amount of R112,926 million reflected against the Department of Health. This has been reclassified in the figures for March 2002.

Way forward

The challenge lies in developing systems and processes that meet the objective of effective and efficient management of debtors. To this end, representations will be made to the principals of the various systems to enhance the system further.

Departments should provide sufficient information to the provincial parliament to enable the members to assess the effectiveness and efficiency of its debt collection, including the extent to which their objectives have been achieved and the cost of doing so. A system of monitoring and benchmarking performance should also help improve performance and cash flow to the Province. The primary sources of accountability information are the annual reports of the various departments, since all departments should include certain basic collection management performance information in their annual reports. The provincial Treasury will in future monitor the progress made by departments in reducing the outstanding debtors and report quarterly to the provincial parliament on the progress made.

We believe that departments should take the following steps:

- **Clearly define its objectives for the collection of overdue accounts.** In doing so, we can also evaluate the impact of the collection of overdue accounts. This may mean pursuing marginally economic (or even uneconomic) collection activities for the sake of establishing and maintaining an enforcement presence.
- **Determine who will be responsible and accountable for the collection of overdue accounts.** We believe, given the uneven results we observed, that departments should assess the benefits of its collection activities.
- **Identify appropriate performance measures and establish data-gathering processes required to monitor performance.** Establish benchmarks describing performance expectations and goals. Define internal and external reporting requirements.
- **Determine and allocate the resources required to do a proper job.** Decisions should be based on comprehensive cost-benefit analyses, including consideration of non-financial objectives.
- **Monitor actual performance, compare this with benchmarks, and evaluate variances.** Review objectives, goals, performance measures, data-gathering processes and resources.
- **Provide timely information to SCOPA on performance goals and actual results, including appropriate contextual information.**

The role of the provincial Treasury will be to perform its regulatory functions in terms of the PFMA, relative to the management of debtors. It will also set policy for, direct, and oversee the general internal processes of, departments regarding debt management. The aim is to provide departments technical support in developing departmental policy that will encourage performance-based management rather than traditional control procedures. As far as the preparation of performance information that is provided to the provincial parliament is concerned, it will provide leadership to departments in an endeavor to ensure prompt and accurate reporting. During the above process transversal system deficiencies and needs will be identified and reported on, in order to ensure that the matter is appropriately addressed. The provincial Treasury will also set specific annual performance goals and measures in order to report success in the management of debtors.

4.9 Departmentalisation

Overview

The purpose of this section is to provide an overview of the departmentalisation model approved by the Western Cape government and implemented with effect from 1 August 2002, and to propose a framework within which financial resource allocation for this purpose needs to be considered for the Medium-Term Expenditure Framework period commencing 1 April 2003.

The concept of departmentalisation is not new to the Western Cape government, and various initiatives in this regard to a greater or lesser extent and for different reasons were seen over the past eight years.

The new democracy that took effect in April 1994 caused the transition of the then four (4) departments to about ten (10). These increased to thirteen (13) in 1997 and thereafter dropped to eight (8) in 1999.

Subsequently, the Western Cape government approved an organisational structure which became effective from 1 August 2002. This initiative brought an end to the situation where ten (10) provincial departments were serving twelve (12) members of the provincial Cabinet in the Western Cape.

The new structure allows for thirteen (13) provincial departments. Each Member of the Provincial Cabinet takes responsibility for a single[5] department.

Furthermore, each provincial department is linked to a specific Vote[6], whereas in the past to a limited extent, there has always been a disjuncture between the vote and departmental structure.

The new government of the Western Cape – formed by the African National Congress and the New National Party - was sworn in during December 2001. Following this, the new government announced its Strategic Framework for Policy Formulation, which took effect on 5 December 2001. This Framework set out the parameters for policy within which each provincial department would operate. A further challenge with which the new government was confronted was the further appropriate transformation of the instruments of the State in the Western Cape province. One of the initiatives included the rethinking of the then departmentalisation model, which was seen to be based on central command and control and diffused accountability.

A further initiative was to re-establish political leadership in the Province through a clear understanding of the relative roles of provincial ministers and accounting

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5 An exception is the Department of Economic Development and Tourism, which cannot easily be separated due to its integrated nature.

6 According to the Public Finance Management Act, 1999 (Act 1 of 1999) it means one of the main segments into which an Appropriation Act is divided and which specifies the total amount usually appropriated per department in an Appropriation Act and separately approved by the provincial parliament before it approves the relevant Draft Appropriation Act as such.

officers, a review of delegated authority between the aforementioned and closer attention to the signing of performance agreements with heads of departments.

The original Department of Economic Affairs, Agriculture and Tourism was split into two from 1 April 2002, i.e. the Department of Transport and Public Works, and Economic Affairs, Agriculture and Tourism.

Discussion

Departmentalisation in its broad sense refers to the logical grouping of government functions into organisational components (or departments) in a manner that will ensure effective and efficient service delivery. In the case of a province, the following are some of the key factors that will influence departmentalisation in an interrelated manner:

- Functions entrusted to provincial governments in terms of the Constitution of the Republic of South Africa, 1996 (provincial legislative competencies are broadly set out in Schedules 4 and 5 to the Constitution).

- Political executive arrangements, referring to the composition, and allocation of portfolios to members, of the provincial Cabinet, where the ideal is to create single lines of responsibility between provincial ministers and departments, i.e. one provincial minister responsible for one department.

- Political strategic goals as reflected in, among others, the allocation of resources to the various provincial functions in order of priority.

- Relative magnitude of the various provincial functions in terms of the allocated financial and human resources, as well as the complexity of service delivery in terms of centralised or decentralised structures – large, decentralised functions such as health and education will require single organisational arrangements.

- Relationship between and compatibility of provincial functions, where the norm will be to group related and compatible provincial functions together to form a synergistic, manageable whole.

In terms of current statutory provisions, provincial departments are formally established in terms of the Public Service Act, 1994 (as amended) (section 7(2) and (5)(a)(ii) read with Schedule 2).

The result of the 1 August 2002 departmentalisation model, is summarised below, which recommends that seven of the existing ten provincial departments should remain unaffected.

The three (3) departments: Economic Development, Tourism and Agriculture, Environmental and Cultural Affairs and Sport and Planning, Local Government and Housing, considered to be insufficiently focused or too diverse, were split into six:

- Agriculture
- Cultural Affairs and Sport
- Economic Development and Tourism
- Environmental Affairs and Development Planning
- Housing
- Local Government

The new departmentalisation model creates a decentralised structure in which each provincial minister takes responsibility for a single department[4], each head of department is the accounting officer for that department, and each department represents a vote in the annual provincial budget and in the relevant Appropriation Act.

The most significant improvement is the fact that each provincial minister takes responsibility for a single[3] department and that all the key components are aligned to ensure effective accountability and enhanced maximisation of efficiency, creativity, direct accountability and rapid service delivery.

Arrangements were made to enable comprehensive personnel, finance and other staff functions to be rendered on an interim agency basis by the so-called parent departments to the new departments. The following departments will be responsible for the rendering of agency services to the departments as indicated:

- *New Department of Environmental Affairs and Development Plannin*g: To the Department of Cultural Affairs and Sport (also responsible for the phasing out of the Department of Environmental Affairs and Cultural Affairs and Sport, which is to be abolished).

- *New Department of Housing*: To the Department of Local Government (also responsible for the phasing out of the Department of Planning, Local Government and Housing, which is to be abolished).

- *Department of Transport and Public Works*: To the Department of Agriculture and the Department of Economic Development and Tourism (also responsible for the phasing out of the Department of Economic Development, Tourism and Agriculture, which is to be abolished).

From a financial management perspective there are a host of issues that need to be addressed in 2002/03, with carry-through effects into 2003/04 and beyond, to create a relatively stable environment that would promote continuous sound financial management, service delivery, and accountability. Of these the following key issues are singled out:

- The creation of new structures on the Financial Managements System (FMS) to adequately accommodate budgets, and receipts expenditure, assets and liabilities (REAL).

4 An exception is the Department of Economic Development and Tourism, which cannot easily be separated due to its integrated nature

- The coupling of the new structure codes to the personnel and salary system (PERSAL), to ensure the correctness of pay points, salary payments and deductions.

- Organising budget issues to facilitate the determination of programme structures, agreement between accounting officers on the split in the budget allocations, the shifting of funds, and the appointment of programme managers and accounting officers for the new votes.

- The arrangement of the ledger accounts through the transfer of balances between the relevant departments and reaching agreement on actual transactions between accounting officers.

- The transfer of assets between the affected departments.

- Planning with regard to reporting to the relevant authorities.

- Compiling financial statements (memoranda accounts) in respect of the abolished departments, the auditing thereof, and the inclusion in the annual reports of the new principal departments in terms of the normal prescripts.

From the aforementioned it is clear that a number of issues need to be coordinated and monitored to ensure smooth transition. For this purpose a Task Group: Departmentalisation was established under the leadership of the Provincial Accountant General.

Clearly the implementation of the new departmentalisation model has financial implications for provincial departments. A rough initial cost estimate for a 12-month period using 2002/03 could amount to the following:

Expenditure	Recurrent R'000	Non-recurrent R'000
Personnel: Senior Management Service	3,823	
Personnel: Other	17,203	
Non-personnel	4,200	
Accommodation, etc.		5,300
Subtotal	25,226	5,300
Total	30,526	

However, Organisational Development reports on the restructuring of the affected departments are in progress and the outcome of these will give a deeper understanding of the actual financial impact, inclusive of trade-offs, to be entertained.

Way forward

In conclusion, and taking account of accounting officers' concerns with regard to the uncertainties surrounding the funding arrangements, it is proposed that owing to financial constraints, resources for the implementation of the departmentalisation model should be allocated within the following framework:

- Affected departments need to manage the financial implications closely.[7]

- Financial implications are subject to final assessment through the application of due prudence subsequent to more detailed investigations.[5]

- Transfer of funds between the baseline allocations of affected departments in relation to own revenue estimates and expenditure budgets needs to be signed off by the receiving and transferring accounting officers.

- Such transfer of funds must take account of the:

  - Legislative provisions in the Public Finance Management Act, 1999.

  - Carry-through costs in respect of the improvement of conditions of service related to 2002/03.

  - Provisions for public works in favour of the affected departments under the Vote of the Department of Transport and Public Works.

- Interdepartmental financial arrangements for agency services continuing beyond 2002/03 must be captured in service level agreements between accounting officers.

- Funded from savings, efficiency gains, reprioritisation and, as a last resort, by drawing down the Contingency Reserve.[5]

- Distinguish between recurrent and non-recurrent expenditure.[5]

- Before any draw-downs of the Contingency Reserve, the budgetary pressures related to social security grants, as a statutory obligation, should be taken into account.

[7] Cabinet Minute No 242 dated 3 July 2002
[5] Cabinet Minute No 242 dated 3 July 2002

Conclusion

The key elements of the chapter can be summarised as follows:

Compliance with the national and provincial norms and standards will result in sound financial management through the effective and efficient utilisation of resources. These benefits, however, are dependent on the will and ability of accounting officers/authorities to comply properly with the norms and standards referred to above, together with the combined successes of the various oversight bodies. Internal reflection by the various oversight bodies on their actual successes to date in improving service delivery and efficiencies is necessary.

An essential requisite for accounting officers/authorities to comply with the norms and standards referred to above is a competent Chief Financial Officer (CFO) with an adequate CFO support structure. The CFO support structure must also be provided with competent staff. Departments therefore need to take full advantage of the provincial Treasury's capacity building initiatives referred to in this chapter.

The developments regarding transversal financial systems are to be noted. Also to be noted is that, notwithstanding the shortcomings of the current financial administration systems in complying fully with Generally Recognised Accounting Practice (GRAP), asset management, etc., which are being addressed, *inter alia*, by the Technical Committee on Finance (TCF) workgroup, the optimal utilisation of the current systems can go a long way in assisting accounting officers to execute their responsibilities more effectively. Accounting officers should take more advantage of this.

The introduction of supply chain management (SCM) will transform the existing rule-driven and fragmented way in which provisioning and procurement are currently dealt with. Supply chain management will primarily focus on the concept of value for money and the effective and efficient use of available resources, as well as assisting with sound financial and economic decision-making. Instrumental to SCM will be the meaningful and sustainable empowerment of those historically disadvantaged.

The provincial Treasury and accounting officer need to prioritise and champion the implementation of the PFMA. In addition to the matters referred to above, special focus should also be given to:

- Adequately funded Internal Audit units;
- Departments always remaining cash positive;
- The process for the setting of standards of GRAP by the Accounting Standard Board (ASB) being expedited.

Given the known or expected fiscal risks, including major natural disasters and major unforeseen and unavoidable events, an once-only amount of R100 million (topped up as necessary in outer years to keep the amount constant in real terms) should be set aside as provision for contingent liabilities as follows:

- R50 million for unforeseeable and unavoidable expenditure
- R50 million for the contingencies as shown in this chapter.

The recovery of outstanding debts should receive urgent attention by accounting officers. The provincial Treasury and SCOPA should closely monitor progress on the recovery of debts.

The departmentalisation model implemented on 1 August 2002 as well as its underlying principles should be noted. Also to be noted is the framework for financing it.

The financial management issues discussed in this chapter pertain only to provincial departments and provincial public entities, and there is no reference to Local Government, other than under section 4.6, supply chain management.

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5

FISCAL ENVELOPE

5.1 Introduction

The Constitution, 1996[1], establishes national, provincial and local government as autonomous spheres that are “distinctive, interdependent and interrelated”. South Africa’s fiscal system, which is formalised by the Intergovernmental Fiscal Relations Act, 1997[2] (“IGFRA”), is based on a revenue-sharing model or intergovernmental fiscal transfers to address, among others, the “vertical imbalances” across the different spheres of government. The Constitution requires that all revenue raised nationally should be divided equitably between the three spheres of government.

The equitable division of revenue aims to provide each sphere of government with the necessary funds to provide the services and perform the functions assigned to it under the Constitution. This division is done after taking into consideration each sphere’s ability to raise its own revenue, the expenditure limits set by the government to meet its stated macro-economic objectives and a careful weighting of the functions of the different spheres of government, which are then matched by the affordability constraints set by the size and growth of the South African economy.

Transfers from the national budget to provinces, which dominate provincial budgets, take two forms – the provincial equitable share (without any conditions), which is a direct charge against the National Revenue Fund, and conditional grants (a supplement) which are used to ensure that national priorities are adequately provided for in provincial budgets, to support compliance with national norms and standards, and to compensate provinces for providing services that may extend beyond provincial boundaries.

The Constitution, 1996 requires the annual enactment of the Division of Revenue Act (“DORA”) at the time of the national budget, and the Intergovernmental Fiscal Relations Act, 1997, prescribes the process of consultation that must take place before the annual DORA is introduced. The DORA enhances transparency in the allocation of the national resources by setting out the equitable share for each sphere[3] (“vertical division”) and the division between the nine provinces (“horizontal division”), including a detailed schedule of all other allocations from the budgets of national departments to provinces and local governments.

[1] The Constitution of the Republic of South Africa, 1996 (Act 108 of 1996)
[2] The Intergovernmental Fiscal Relations Act, 1997 (Act 97 of 1997)
[3] National, Provincial and Local Government

Despite provinces' significant expenditure responsibilities set out in Schedules 4 and 5 of the Constitution, which are primarily funded from the national fiscus, provinces have limited sources of own revenue to augment the funding of services. In this Province, in respect of the 2002/03[4] financial year, the total revenue envelope constitutes the equitable share of 80%, conditional grants of 14,3% and own revenue of 5,7%. From the above, it is evident that the equitable share allocation is used to fund the bulk of public services rendered in this Province.

This chapter focuses on the Province's total revenue envelope, which includes the equitable share, conditional grants and own revenue. It will provide a review of the components within the revenue envelope, an analysis of national revenue transfers over the rolling MTEF[5], application of such revenue received within the Province, own revenue information, borrowing powers and other financing arrangements.

5.2 Division of revenue

5.2.1 The division of revenue raised nationally is regarded as one of the most important decisions made in the budget process. In practice, the annual Division of Revenue proposals are formulated by the national Treasury and submitted to Cabinet and thereafter, to the National Assembly (Parliament), but only after an extensive consultation process at various intergovernmental forums, including the annual Division of Revenue workshop[6], the Budget Council[7] and the Budget Forum[8] incorporating organised local government, the Ministers' Committee on the Budget and the constitutionally independent Financial and Fiscal Commission ("FFC"). national Treasury, the Cabinet and Parliament are also required to take into account any recommendations from the FFC. Finally, provincial premiers are invited to an extended Cabinet meeting where the final division of revenue proposals is decided before submission to Parliament[9].

5.2.2 Legal framework

Section 214 of the Constitution requires that there must be an Act of Parliament (referred to as the DORA) to provide for the vertical division of revenue (i.e. between the three spheres of government) and horizontal division (i.e. across the components making up the various spheres of government (provincial and local government). The

4 Includes adjustments from the 2002/03 adjustment estimates.
5 Medium term expenditure framework covering 3 financial years.
6 Division of Revenue Workshop is made up of senior representatives from national and provincial treasuries and national departments.
7 The Budget Council consists of the National Minister of Finance, Members of the Executive Councils responsible for financial matters in the various provinces and the FFC. It is a body in terms of the IGFRA that consult on any fiscal, budgetary or financial matter, proposed legislation or policy with financial implications or any matter concerning financial management which affect provinces.
8 Budget Forum, another consultative body set up by the IGFRA, consisting of the same representatives as the Budget Council plus representatives from South African Local Government Association and Department of Local Government.
9 Fiscal Decentralisation in South Africa – Paper by I Momoniat.

DORA may only be enacted after account has been taken of the ten factors set out in section 214(2)(a)-(j), which are as follows:

- the national interest
- any provision that must be made in respect of national debt and other national obligations
- the needs and interests of the national government determined by objective criteria
- the need to ensure that provinces and municipalities are able to provide basic services and perform the functions allocated to them
- the fiscal capacity and efficiency of the provinces and municipalities
- developmental and other needs of provinces, local governments and municipalities
- economic disparities within and among provinces
- obligations of the provinces and municipalities in terms of national legislation
- the desirability of stable and predictable allocations of revenue shares
- the need for flexibility in responding to emergencies or other temporary needs, and other factors based on similar objective criteria.

The DORA aims to:

- provide for the equitable division of revenue raised nationally among the three spheres of government;
- promote cooperative governance in the budget allocation and transfer process;
- promote better coordination between policy, planning, budget preparation and execution processes;
- promote predictability and certainty in respect of all allocations to provincial and local government to enable such governments to plan their budgets over a multi-year period;
- promote transparency and equity in all allocations, including the criteria for their division;
- promote accountability for the use of public resources by ensuring that all transfers are reflected on the budget of benefiting provincial and local governments, and are subject to an audit;
- ensure that proper financial management is applied;
- ensure that legal proceedings between organs of state of the three spheres of government are avoided.

5.2.3 Vertical division

The Constitution does not provide guidance as to exactly how decisions on the vertical division should be made, or even who or which body or bodies should be responsible for making this decision. What is important to note is that the decision on the final annual division of revenue proposals is essentially a **political decision**, taken as part and parcel of the extensive consultation process described in paragraph 5. It is political judgement reflecting priorities determined ultimately by the national Cabinet. Momoniat referred to this in his paper, “thus if school education is identified as a new or higher priority, the provincial share increases over the baseline allocation from the current three year allocation; if policing is a priority, the national government share is increased"[10]. Unfortunately, in real life most policy-making decisions do not make any clear distinction between trade-offs or the cost implications of new initiatives.

Nevertheless, one can boldly say that too little attention has been paid in recent years to the vertical division of revenue process. The Budget Council and its technical committees have expended a great deal of time and effort on analysing and debating the horizontal division of revenue and its associated equitable share formula. On the face of it one can argue that the current process used to decide the vertical division of revenue is inevitably biased in favour of national government priorities. This is to say that in any given situation where the competing budgetary demands and the priorities of the national, provincial and local governments are weighed up against each other before deciding the vertical division, the national viewpoint will inevitably prevail despite the extensive "consultation" process required in terms of the Constitution.

Provinces are allocated the responsibility for providing the vast majority of the basic social services[11] and rights entrenched and prioritised in the Constitutions' Bill of Rights, without efficient concomitant revenue assignment, and despite the "elasticities" in expenditure involved in providing these basic social services, over which provinces have little or no control, it may still happen that national priorities are accorded a "more equal" status than provincial priorities, even in circumstances where an objective assessment of the situation might not justify this[12]. As provinces, from a reduction in social inequality perspective, are mostly responsible for both in-kind and cash transfers, this creates a dilemma.

There are many factors that have an impact on the amount earmarked to be allocated to the three spheres of government, which *inter alia* include changes in economic growth, inflation rates, interest rates and exchange rates. These influence total national revenue and debt servicing cost, to name only two. National government could also decide to make certain explicit policy decisions, which could lead to trade-offs between whether government expenditure as a percentage of GDP should change and what the socio-economic consequences for the country could be. Prior to the actual division of the revenue raised nationally, the cost of servicing debt as well as the provision for a contingency reserve are first met. The reasoning behind this is that all spheres of government benefit from the aforesaid.

An analysis of the 2002/03 financial year shows that provincial governments' portions of the total revenue source nationally constitutes in the region of 56,0%, and that of national and local government shares 40,4% and 3,6% respectively, whereas debt

[10] Fiscal decentralisation in South Africa – paper by I Momoniat
[11] Constitutionally mandated basic services as per Schedule 4 and 5 of the Constitution of South Africa, 1996.
[12] Key Features of South Africa's intergovernmental system; The intergovernmental fiscal arrangements: A KwaZulu-Natal perspective (specifically the KwaZulu-Natal Provincial Treasury) – Budget Council Legotla 21-24 August 2002.

servicing cost and the contingency reserve are excluded from the allocations to the three spheres of government. It is projected that the provinces' share will increase slightly to 56,2% in 2003/04, while local governments' portion will increase to 4,3%. The projections for 2004/05 will see provinces' share increase to represent 56,4% of the total allocation, with local governments' portion remaining constant at 4,3%. Over the period 1998/99 to 2005/06, provincial governments' share of the total national revenue available for division decreased by 4,1 percentage points, whereas national and local governments' portions increased by 0,9 and 3,2 percentage points respectively. The aforesaid is clearly in line with national government's intention to strengthen the local sphere of government somewhat at the expense of provincial governments and, marginally, national government. It is contended that provincial governments should at least be adequately funded to perform its constitutionally mandated basic services[13].

Table 5.1 gives an indication of the vertical division[14] of actual and estimated nationally raised revenue among the three spheres of government from 1998/99 to 2005/06:

Table 5.1(a)

EQUITABLE DIVISION OF REVENUE RAISED NATIONALLY									
		Actual			Estimated Actual	Budget	MTEF		
R'000		1998/1999	1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
Total nationally raised revenue		202 574 000	214 751 000	233 943 000	262 674 000	**291 753 000**	329 418 000	358 424 000	388 100 000
Less:	State debt cost	42 669 000	44 290 000	46 321 000	47 571 000	**47 236 000**	51 463 000	54 599 000	57 853 000
	Contingency reserve	0	0	0	0	**0**	2 000 000	4 000 000	8 000 000
Total nationally raised revenue available for allocation		159 905 000	170 461 000	187 622 000	215 103 000	**244 517 000**	275 955 000	299 825 000	322 247 000
Less: Allocation to three government spheres									
National allocation (revised)		**60 877 000**	**64 523 000**	**73 142 000**	**87 317 000**	**98 778 000**	**108 977 000**	**117 700 000**	**125 813 000**
Equitable share (initial)		60 877 000	64 523 000	73 142 000	87 317 000	**95 406 267**	101 807 000	107 911 000	114 109 000
Inflation adjustments (NT, 16/10/2002)						**1 114 733**	2 265 000	2 841 000	3 082 000
Policy adjustments "New Money" (NT, 16/10/2002)						**2 257 000**	4 905 000	6 948 000	8 622 000

13 This view is in line with a note of the Budget Council Lekgotla, 2002
14 Includes proposed adjustments (inflation, social welfare and ICS) and a "new money" allocation as per Technical Committee of Finance (TCF) meeting of 19 September 2002.

Table 5.1(b)

EQUITABLE DIVISION OF REVENUE RAISED NATIONALLY								
	Actual			Estimated Actual	Budget	MTEF		
R'000	1998/1999	1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
Provincial allocation (revised)	**97 065 000**	**101 532 000**	**108 904 000**	**121 205 000**	**136 922 000**	**155 127 187**	**169 089 880**	**182 325 015**
Equitable share	84 342 000	89 095 000	98 398 000	107 460 000	**119 452 000**	127 728 031	136 002 096	144 032 442
Conditional grant	12 723 000	12 437 000	10 506 000	13 745 000	**12 968 000**	15 121 156	16 366 784	17 478 573
Inflation adjustments (NT, 16/10/2002)					**2 185 000**	5 534 000	6 512 000	7 010 000
Policy adjustments "New Money" (TCF, 19/9/2002)*					**2 317 000**	6 744 000	10 209 000	13 804 000
Local government allocation (revised)	**1 963 000**	**4 406 000**	**5 576 000**	**6 552 000**	8 817 747	**11 856 000**	**13 041 000**	**14 115 000**
Equitable share	1 963 000	2 163 000	2 315 000	2 618 000	**3 852 478**	5 022 000	5 461 000	6 112 000
Conditional grant	0	2 243 000	3 261 000	3 934 000	**4 728 000**	5 213 000	5 393 000	5 393 000
Inflation adjustments (NT, 16/10/2002)					**100 269**	171 000	187 000	198 000
Policy adjustments "New Money" (NT, 16/10/2002)					**137 000**	1 450 000	2 000 000	2 412 000

** New money for provinces includes inflation adjustments to conditional grants*

The following table represents a total view of the nominal and real growth in each sphere's allocation and each sphere's share of the total national revenue using the Gross Domestic Product inflator[15]:

Table 5.2: Growth in budget allocations

Nominal year-on-year growth per sphere allocation		1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
National		6,0%	13,4%	19,4%	**13,1%**	10,3%	8,0%	6,9%
Provincial		4,6%	7,3%	11,3%	**13,0%**	13,3%	9,0%	7,8%
Local		124,5%	26,6%	17,5%	**34,6%**	34,5%	10,0%	8,2%
Total revenue (amount available for allocation)		6,6%	10,1%	14,6%	**13,7%**	12,9%	8,6%	7,5%
GDP inflation	**7,0%**	**6,3%**	**7,0%**	**7,6%**	**9,3%**	**6,6%**	**5,1%**	**4,4%**

15 Source: National Treasury: Medium Term Budget Policy Statement 2002, p.26

Table 5.2 *(Continued)*

Real year-on-year growth per sphere allocation	1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
National	-0,3%	6,4%	11,8%	**3,8%**	3,7%	2,9%	2,5%
Provincial	-1,7%	0,3%	3,7%	**3,7%**	6,7%	3,9%	3,4%
Local	118,2%	19,6%	9,9%	**25,3%**	27,9%	4,9%	3,8%
Total revenue (amount available for allocation)	0,3%	3,1%	7,0%	4,4%	6,3%	3,5%	3,1%

Percentage of shared total	1998/1999	1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
National	38,1%	37,9%	39,0%	40,6%	**40,4%**	39,5%	39,3%	39,0%
Provincial	60,7%	59,6%	58,0%	56,3%	**56,0%**	56,2%	56,4%	56,6%
Local	1,2%	2,6%	3,0%	3,0%	**3,6%**	4,3%	4,3%	4,4%
Total	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**

It is certainly a view from the provinces' perspective that could be perceived as being positive, given the real growth[16] percentages in its total national allocation of 3,7% for 2002/03, 6,7% for 2003/04, 3,9% for 2004/05 and 3,4% for 2005/06. This represents a cumulative real increase of 17,7 percentage points, compared with National's portion that will experience a cumulative real increase of 12,9 percentage points over the same period. Furthermore, if the total nominal growth in the different allocations to the three spheres of government for the period 1998/99 to 2001/02 is compared with the base year, being 1998/99, one would find that provincial governments are worst off with a total nominal increase of 24,9% compared with the nominal increase of 43,4% and 233,8% for the national and local governments respectively. However, if a similar comparison is made, but this time over the period 2001/02 to 2005/06 with 2001/02 as the base year, then one would find that the nominal increase in provincial governments' share is marginally higher at 50,4% compared with that of the national government's 43,9%, and local government is substantially better off with a nominal increase of 115,4%.

Notwithstanding the above, it is maybe time for some serious introspection and objective analysis of the manner in which the vertical division of revenue is done and, more importantly, the longer-term implications it might have. The whole vertical decision-making process needs to be reviewed so as to reflect greater, more forceful and better articulated prior provincial presence in policy-making at the national level. This, in turn, arises from the unique nature of the constitutional assignment of concurrent responsibilities referred to earlier, and the latent tension and contradiction which the system can give rise to if the supporting decision-making processes and policies are not correctly drafted and structured.

It does not make sense, for example, for sectoral policy decisions to be made at national level, with major cost implications for the implementing agencies (e.g. provincial governments), if the division of revenue decision-making process itself is not nimble or flexible enough to link the additional costs by the provinces with the

[16] Need to say what deflator rate/inflation rate has been used to calculate real change per year

same timeframe in which the expenditure is incurred. An example is the disproportionately high expenditure which of necessity has been incurred by provinces in the last three years in respect of the social welfare sector arising out of policy decisions and tariff levels determined at national level. With some caveats[17], provinces have no control over the number of qualifying applicants for social security grants (constitutional prerogative of qualifying applicants), the rate at which these applications have to be considered and ultimately processed (payment has to be made from date of application) or the monetary amounts of the various grants (these are set and adjusted by national government). Funding shortfalls, on the other hand, due to meeting these social security grant obligations are due to factors totally beyond their control such as the regulatory governing social grants changes implemented by the national government. It also has to be mentioned that, out of the total amount of new money meant for provinces in 2003/04, only R6,744 billion countrywide has been provided by the national Treasury for mainly social grant cost increases, although the estimated cost increase for the provinces alone is way beyond that amount and rising significantly in the outer years of the new MTEF. To put it mildly, it is deemed unfair to expect provincial governments to fund these shortfalls from their own budget, thereby not only distorting the entire provincial budget process, but also the ideals of achieving social equity because of the very high perverse social costs being imposed on society.

One could strongly argue that such issues have to be accommodated in the vertical division of revenue and not the horizontal, as is currently the notion. With increasing budget pressures from social security payments and health budgets, one could deduce that the time had come to review the vertical division process in its entirety, as the equitable share formula is not designed to cater for these types of cost pressures or national policy/legislative changes.

5.2.4 Horizontal division

The equitable share

The equitable share is allocated "horizontally" among the nine provinces according to the equitable share formula. Based on the 1996 recommendations of the Financial and Fiscal Commission (FFC) and modified by the national Treasury, it recognises that provinces have markedly different economic development profiles, demographic variations and significant variations in socio-economic circumstances. The equitable share formula, which is highly distributive (allocating more funds per capita to the poorer rural provinces) was first introduced for the 1998/1999 budget, and is designed to assist the provinces in providing the basic services for which they are constitutionally responsible.

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[17] Provinces indeed are responsible for efficient and diligent administration of social assistance applications, and although subject to much criticism elsewhere, this Province has seen tremendous improvements in processing efficiently, perhaps ultimately to its detriment.

The formula is made up of seven components, which are illustrated in Table 5.3 below:

Table 5.3: Components of equitable share formula

Equitable share component	Weights	Data used	Source
Education	41%	Total enrolment numbers	National Department of Education: Enrolment figures
		Average of school-age population (6-17) years	Stats SA: Census
Health	19%	Population with and without medical aid support	Stats SA: October household Stats SA: Census
Welfare	18%	Target population of each grant type	Stats SA: Census
		Weighted with poverty index	Stats SA: 1995 Income and Expenditure Survey
Economic activity	7%	Remuneration data	Stats SA: Remuneration data
Backlog	3%	Schools Survey of Needs 1998	National Department of Education: Enrolment figures
		Audit of hospital facilities; and Share of rural population	National Treasury: Coordination of sectoral reports
Basic	7%	Each provinces' share of population	Stats SA: Census
Institutional	5%	Cost of running a provincial government equally divided	Independent data

The weights assigned to the individual social services components (education, health and social development) are based on historical expenditure trends, with elements within each component being based on policy considerations relating to the social services sectors. Together, the three social services components accounted for 78% of the equitable share allocation in the 2002/03 MTEF for these functions (including building and IT provision). The basic component is based on the proportion of population residing in a specific province and acknowledgement that there is a close correlation between demand for public services and population irrespective of the demographic composition thereof. The institutional component provides for provinces to create and maintain administrations and institutions of governance and is allocated to provinces on an equal proportion basis. The economic activity component recognises the correlation between the demand for public services and the level of economic activity and acts as an incentive to sustain and expand economic activity. The backlog component acknowledges that some provinces have disproportionately large backlogs in infrastructure in mainly health and education and in rural areas generally.

The equitable share formula was designed to be phased in over a five-year period beginning in 1998/1999, achieving ultimate target shares per province in 2003/2004. As is shown below, the Western Cape's equitable share (target share) has been declining annually over the five-year period from 9,8% in 1999/2000 to 8,9% in 2003/04. In 2003/04 rands, although ostensibly a small percentage, that implies a shift of almost R1,2 billion to less well-off provinces, a not insignificant contribution in cash towards reaching regional equity, with particularly Gauteng, KwaZulu-Natal, Mpumalanga and Limpopo benefitting. The consistent decline in the equitable share of the Western Cape since 1999/2000 has caused some disruptions in allocations/budgets since considerable sacrifices had to be made in provincial departments like Health and Education, which have been struggling to provide acceptable levels of service in the face of continuously declining levels of funding relative to their counterparts in other provinces like KwaZulu-Natal, which has had a consistent increase of 0,2 percentage points in their target share over the five years phased-in process. Compared with other provinces, the Western Cape's equitable share weighting has decreased most (0,9 percentage points) from the base year to 2003/2004. Not only have service levels suffered, but capital and maintenance backlogs have inevitably escalated faster in the departments mentioned than those of their counterparts in other provinces. Although the need for equity is not disputed, one sometimes wonders if the delays have not had a detrimental effect on the country's overall quantum of social and infrastructure services.

The following table reflects the phasing in of the equitable share across the different provinces:

Table 5.4: Phasing in of the equitable share across the different provinces

Percentage	1999/00 base	2000/01	2001/02	2002/03	2003/04 target
Phasing	*Year 1*	*Year 2*	*Year 3*	*Year 4*	*Year 5*
Eastern Cape	17,6	17,4	17,3	17,2	17,0
Free State	6,8	6,8	6,7	6,7	6,6
Gauteng	14,9	15,1	15,2	15,3	15,4
KwaZulu-Natal	19,8	20,0	20,2	20,4	20,6
Mpumalanga	6,7	6,8	6,9	7,1	7,2
Northern Cape	2,4	2,4	2,4	2,4	2,4
Limpopo	13,3	13,4	13,5	13,5	13,6
North West	8,6	8,5	8,4	8,4	8,3
Western Cape	9,8	9,6	9,4	9,1	8,9
Total	**100,0**	**100,0**	**100,0**	**100,0**	**100,0**

Furthermore, a comparison between the nominal growth figures of the equitable share allocation of the Western Cape and those of provincial governments' global share proves to be significant. If the Western Cape's equitable share is compared with the latter in terms of its nominal growth over the period 1998/99 to 2000/01 and for the period beyond a very different scenario unfolds.

The following table shows the Western Cape's "equitable" share in terms of its growth, both in nominal and real terms:

Table 5.5(a)

WESTERN CAPE: FISCAL ENVELOPE 1998/1999 TO 2005/2006								
	Actuals			Esti-mated Actuals	Budget	MTEF		
R'000	1998/1999	1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
Revenue								
Own revenue	527 670	733 329	764 733	954 970	797 952	827 541	820 584	826 503
Equitable share (ES)	7 964 602	8 499 193	9 235 141	9 869 840	10 918 905	11 452 753	12 221 957	12 955 682
ES inflation adjustments (NT 16/10/2002)					191 720	465 203	547 261	588 735
Personnel					115 580	246 000	322 000	352 000
Social Security grants					46 788	127 000	126 000	133 000
General Inflation					29 352	92 203	99 261	103 735
Unforeseeable & unavoidable exp.					183 629	561 857	844 165	1 149 613
Conditional grants (CG) [18]	1 760 504	1 696 310	1 908 475	2 042 884	2 019 671	2 143 622	2 252 190	2 312 903
Total Revenue	**10 252 776**	**10 928 832**	**11 908 349**	**12 604 734**	**14 111 877**	**15 450 976**	**16 686 157**	**17 833 422**
Total national allocation (including conditional grants)	**9 725 106**	**10 195 503**	**11 143 616**	**11 912 724**	**13 313 925**	**14 623 435**	**15 865 573**	**17 006 933**
Total national allocation (excluding conditional grants)	**7 964 602**	**8 499 193**	**9 235 141**	**9 869 840**	**11 294 254**	**12 479 813**	**13 613 383**	**14 694 030**

Table 5.5(b)

	1998/1999	1999/2000	2000/2001	2001/2002	2002/2003	2003/2004	2004/2005	2005/2006
% Nominal growth in equitable national revenue transfers to Western Cape (excluding conditional grants)		6,7%	8,7%	6,9%	14,4%	10,5%	9,1%	7,9%
GDP inflation	7,0%	6,3%	7,0%	7,6%	9,3%	6,6%	5,1%	4,4%
% real growth in equitable National revenue transfers to Western Cape (excluding conditional grants)		0,4%	1,7%	-0,7%	5,1%	3,9%	4,0%	3,5%
	1998/1999	**1999/2000**	**2000/2001**	**2001/2002**	**2002/2003**	**2003/2004**	**2004/2005**	**2005/2006**
% nominal growth in equitable national revenue transfers to Western Cape (including conditional grants)		4,8%	9,3%	6,9%	11,8%	9,9%	8,5%	7,2%
GDP inflation	7,0%	6,3%	7,0%	7,6%	9,3%	6,6%	5,1%	4,4%
%real growth in equitable national revenue transfers to Western Cape (including conditional grants)		-1,5%	2,3%	-0,7%	2,5%	3,3%	3,4%	2,8%

%Growth in conditional grants		-3,6%	12,5%	7,0%	-1,1%	6,6%	4,9%	3,0%
GDP inflation	7,0%	6,3%	7,0%	7,6%	9,3%	6,6%	5,1%	4,4%
%real growth in conditional grants		-9,9%	5,5%	-0,6%	-10,4%	0,0%	-0,2%	-1,4%

Own revenue share of total	5,1%	6,7%	6,4%	5,5%	5,7%	5,4%	4,9%	4,6%
Equitable share portion of total	77,7%	77,8%	77,6%	78,3%	80,0%	80,8%	81,6%	82,4%
Conditional grant share of total	17,2%	15,5%	16,0%	16,2%	14,3%	13,9%	13,5%	13,0%
Total	100,00%	100,00%	100,00%	100,00%	100,00%	100,00%	100,00%	100,00%

[18] The 2002/03 amount includes inflation adjustments of R32,224 million and policy adjustments of R17,786 million. Partially own calculations by the Provincial Treasury in respect of the 2003/04 to 2005/06 MTEF using baseline conditional grant allocations as per the 2002 budget allocations and preliminary allocation letter from national Treasury dated 7 November 2002.

From 1998/99 to 1999/2000, the Western Cape's total national allocation (including conditional grants) showed a decline of 1,5% in real terms, using the GDP Inflator as a measure. During the period 1999/2000 to 2000/01 the Western Cape's total national allocation (including conditional grants) increased by 2,3% in real terms, while in the year there after a decline in real terms of 0,7% was realised. However, for the period 2001/02 to 2002/03 real growth of 2,5% is reflected, 3,3% for the period 2002/03 to 2003/04 and 3,4% for the period 2003/04 to 2004/05. As reflected in Table 6.5(b) above, from 2001/02 conditional grants in real terms decrease on average at a rate of 2,5% annually, whereas over the period 2001/02 to 2005/06 the Province's equitable share allocation increases on average at a rate of 2,3% annually. The latter increase could be ascribed to the possibility of conditional grants being incorporated into the equitable share portion. This increase in the equitable share, away from the conditional grant allocation, is a positive sign as it implies that the Province will have at its disposal more funds over which it can exercise its discretionary power.

However, what proves to be quite significant is a comparison of the Western Cape's total national allocation in nominal growth terms for the period 1998/99 to 2001/02, with 1998/99 as the base year, together with the period of 2001/02 to 2004/05, with 2001/02 as the base year, with those nominal growth figures applicable to provinces as a whole over the same periods. For the period 1998/99 to 2001/02 the Western Cape experienced total nominal growth in its total national allocation of 23,9% compared with 24,9% for provinces as a whole, with 1998/99 being the base year. Even when the period 2001/02 to 2004/05 is used, during which it is estimated that provinces as a whole will experience substantial nominal growth better than that of national, the nominal growth in the Western Cape's total national allocation is estimated at 37,9% compared with that of the provinces as a whole of 39,5%. It is therefore clear that the growth in the total national allocation of the Western Cape does not coincide with those growth figures applicable to the provinces on the whole. Clearly the decline in the Western Cape's equitable share could be seen as being part of national government's redistribution mechanisms. Although from the percentage year-on-year cited it is clear that there is significant variability requiring smoothing and unnecessary cash reserves.

Evolution of the equitable share formula: The introduction of the formula-driven equitable share allocations in 1997 has created some degree of certainty in the budgetary process. It has also provided a systematic and scientific method for the making of allocations within the framework of Cabinet's strategic priorities. The equitable share formula is a fairly flexible method to use to adjust to an ever-changing environment as it easily accommodates refinements of the different components, updates of the components with new data, small function shifts, adjusting the weightings of the components and adding new components to the formula. It also has a strong redistributive effect while creating some incentives for provinces to develop productive capacity and stimulate growth. However, in spite of the value that such a formula poses, it does have inherent weaknesses in its design. The following is indicative of these weaknesses:

- The specific weights of the different components are political decisions, thereby diluting the scientific nature such a formula should have. In other words, allocations to provinces can be manipulated through national political interventions to decide on an outcome and then amend the weights to suit the desired objective.
- The formula is based on inaccurate and outdated data, i.e. GGP data in the economic activity component which had not been updated since 1994.
- The formula does not take migration factors into consideration.
- It does not provide enough incentives for the more "wealthier" provinces to perform better.

Since its inception, the structure of the formula has been changed in the following manner:

- In 1999/2000 preliminary Census 96 data was replaced with the final census data, and the impact of this was to be phased over five years, ending in 2003/04. The basic component was also split to create a backlog component intended to capture variations in infrastructure backlogs across provinces.
- Gross geographic product data used in the economic activity component, which serves as a proxy for tax capacity, were replaced by remuneration data.
- Weights for the social services components have been increased in line with these functions share in total provincial expenditure. Most of the increases in the social services components have been compensated for, through reductions in the basic component. The increase in the welfare component in 2002/03 was compensated for by a decrease in the economic activity component. This is called "umraba-raba"[19].
- In 2002/03 the use of average education enrolments for the last three years was introduced instead of the most recent year's enrolment. By using averages, unexplained fluctuations in year-on-year enrolment figures were smoothed out, one of the better amendments to the formula providing some incentive to improve enrolment and throughput, particularly at secondary school level.

Table 5.6 below shows the current structure and distribution of the shares by component, and the target shares to be reached by 2003/04. The elements of the formula are not supposed to be indicative budgets nor guidelines as to how much should be spent on those functions, but the argument is intrinsically faulty because as budget pressures rise, more and more stakeholders are using the relative weights to determine whether they have received their "rightful" share. Rather, the components are weighted broadly in line with expenditure patterns to give an indication of relative need, although again faulty as argued under the distribution of

[19] Umraba-raba is the name of a game. It is played on a board which has a square diagram and another smaller square diagram within it. Cool drink `doppies' or neatly cut pieces of card board or even small wooden discs are used in playing the game. In this game the winner is the one who successfully closed up the movement of the opponent, just like in the game of draughts. In most instances, this is how people working in the mines are whiling away their time.

the vertical share. Gently put, it does not take account of national policy pressures, in a constructive way, but only perversely so.

Table 5.6: Distribution of shares by component per province

	Education	Health	Social Welfare	Basic	Backlog	Economic activity	Institutional	Total/ Target
Weighting	41,0%	19,0%	18,0%	7,0%	3,0%	7,0%	5,0%	100,0%
Eastern Cape	18,4%	17,0%	19,6%	15,5%	20,6%	6,5%	11,1%	17,0%
Free State	6,3%	6,5%	7,1%	6,5%	5,7%	5,3%	11,1%	6,6%
Gauteng	12,6%	14,7%	13,9%	18,1%	5,1%	41,6%	11,1%	15,4%
KwaZulu-Natal	22,0%	21,7%	19,6%	20,7%	22,9%	17,0%	11,1%	20,6%
Mpumalanga	7,3%	7,2%	6,5%	6,9%	8,5%	4,9%	11,1%	7,2%
Northern Cape	1,9%	2,0%	2,2%	2,1%	1,3%	1,7%	11,1%	2,4%
Limpopo	15,4%	13,3%	13,7%	12,1%	22,9%	3,0%	11,1%	13,6%
North West	8,0%	8,6%	8,7%	8,3%	9,4%	5,7%	11,1%	8,3%
Western Cape	8,0%	8,9%	8,8%	9,7%	3,7%	14,4%	11,1%	8,9%
Total	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**	**100,0%**

Other recent developments involve the in-principle approval on 17 July 2002[20] by the National Minister of Finance of inflation adjustments for the 2002/03 budget and the 2003 MTEF period with specific maximums for 2002/03 and 2003/04. These adjustments cover higher personnel costs, increases in social grants and an allowance for general inflation on budgets.

Table 5.7 below shows the inflation assumptions, as calculated by National Treasury, that were made at the time of the 2002 Budget and the latest inflation forecasts (based on data made on salary increases contained in the allocation letters to national departments and provinces.

Table 5.7

	2002/03	2003/04	2004/05	2005/06
CPIX				
Budget 2002	6,6%	5,5%	4,6%	
June forecasts	8,9%	5,2%	5,0%	4,7%
Salary increase				
Budget 2002 National	6,0%	6,0%	5,0%	
Budget 2002 Provincial	6,7%	6,1%	5,3%	
New forecast	9,0%	7,0%	6,0%	5,5%

Table 5.7.1 below gives an indication how these increases are allocated to the Western Cape Province.

[20] Budget Council Lekgotla: 21-24 August 2002, Appendix I1, page 1

Table 5.7.1 : Western Cape Inflation Adjustments for 2002/03 – 2005/06

R'000	2002/2003	2003/2004	2004/2005	2005/2006
Personnel adjustments[21]	115 580	246 000	322 000	352 000
Social grant adjustments[22]	46 788	127 000	126 000	133 000
General inflation adjustments[23]	29 352	92 203	99 261	103 735
Total	**191 720**	**465 203**	**547 261**	**589 735**

Status of the Western Cape Budget 2002 in relation to the equitable share: The total outlays[24] for all the provincial programmes, excluding direct charges, smoothing, contingent liabilities and unforeseen and unavoidable contingencies, are budgeted as follows:

- Financial year 2002/2003: R13,781 billion
- Financial year 2003/2004: R14,474 billion
- Financial year 2004/2005: R15,234 billion
- Financial year 2005/2006: R16,148 billion[25]

As already indicated the 2002/03 budget is 80,0% funded from the equitable share, 14,3% from conditional grants and the remaining 5,7% is funded from own revenue sources. In other words, the budget is highly dependent on nationally raised revenue which is in the order of 94,3%.

Table 5.8 below illustrates the comparison between allocations as per the national Treasury equitable share formula and allocations per sector in the Western Cape Budget 2002 for the financial years 2002/03 to 2004/05.

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[21] The additions to personnel budgets are based on the differential between budgeted increases in personnel expenditure at the time of the Budget 2002, and higher than budgeted personnel expenditure following the 2002 wage settlement and a forecast over the 2003 MTEF based on June data. Own calculations by the Provincial Treasury in respect of the 2003/04 to 2005/06 MTEF.

[22] The rationale behind the increases in the social grants will be explained under the conditional grants heading. Own calculations by the Provincial Treasury in respect of the 2003/04 to 2005/06 MTEF.

[23] The general inflation adjustment is made up of the remainder of the total proposed inflation adjustment, less personnel and social grant increases. It is distributed between the provinces by using the equitable share formula, or to be more specific, the different weightings. Own calculations by the Provincial Treasury in respect of the 2003/04 to 2005/06 MTEF.

[24] As per the 2002 main budget. Direct charges include salaries and remuneration of the members of the provincial parliament.

[25] Adjusted by adding 6% to the 2004/05 baseline.

Table 5.8

Comparison of national Treasury's formula with the Western Cape Budget 2002 2002/03								
Function	Formula allocation as per national Treasury		Actual allocation Western Cape Budget 2002		Revised formula allocation		Actual allocation, including Works and IT, distributed between different sectors	
	%	Amount R'000	Amount R'000	%	%	Amount R'000	Amount R'000	%
Education	**41,00**	**4 476 751** [a]	**4 485 976** [a]	**41,08**	**46,72**	**5 101 312** [a]	**4 670 281**	**42,77**
Basis	41,00	4 476 751	4 485 976		41,00	4 476 751	4 670 281	
Backlog					2,04	222 746		
Basic					3,68	401 816		
Health	**19,00**	**2 074 592** [a]	**2 253 836** [a]	**20,64**	**21,66**	**2 365 035** [a]	**2 378 361**	**21,78**
Basis	19,00	2 074 592	2 253 836		19,00	2 074 592	2 378 361	
Backlog					0,95	103 730		
Basic					1,71	186 713		
Social Services	**18,00**	**1 965 403** [a]	**2 714 388** [a]	**24,86**	**19,62**	**2 142 289** [a]	**2 751 188**	**25,20**
Basis	18,00	1 965 403	2 714 388		18,00	1 965 403	2 751 188	
Backlog					0,00			
Basic					1,62	176 886		
Total Social Sector allocation	**78,0**				**88,0**			**89,75**
Institutional (Including votes 1-3 & 12)	**5,00**	**545 945** [a]	**455 565** [a]	**4,17**	**5,00**	**545 945** [a]	**459 665**	**4,21**
Balance of Votes	**17,00**	**1 856 214** [b]	**1 009 140** [b]	**9,24**	**7,00**	**764 323** [b]	**659 410**	**6,04**
Economic	7,00	764 323			7,00	764 323		
Backlog	3,00	327 567			0,00			
Basic	7,00	764 323			0,00			
TOTAL	**100,00**	**10 918 905**	**10 918 905**	**100,00**	**100,00**	**10 918 905**	**10 918 905**	**100,00**

Comparison of national Treasury's formula with the Western Cape Budget 2002 2003/04								
Function	Formula allocation as per national Treasury		Actual allocation Western Cape Budget 2002		Revised formula allocation [c]		Actual allocation, including Works and IT, distributed between different sectors	
	%	Amount R'000	Amount R'000	%	%	Amount R'000	Amount R'000	%
Education	**41,00**	**4 695 598** [a]	**4 717 791** [a]	**41,19**	**46,72**	**5 350 691** [a]	**4 906 726**	**42,84**
Basis	41,00	4 695 598	4 717 791		41,00	4 695 598	4 906 726	
Backlog					2,04	233 635		
Basic					3,68	421 459		
Health	**19,00**	**2 176 009** [a]	**2 443 550** [a]	**21,34**	**21,66**	**2 480 650** [a]	**2 547 075**	**22,24**
Basis	19,00	2 176 009	2 443 550		19,00	2 176 009	2 547 075	
Backlog					0,95	108 800		
Basic					1,71	195 841		
Social Services	**18,00**	**2 061 482** [a]	**2 947 662** [a]	**25,74**	**19,62**	**2 247 015** [a]	**2 982 298**	**26,04**
Basis	18,00	2 061 482	2 947 662		18,00	2 061 482	2 982 298	
Backlog					0,00			
Basic					1,62	185 533		
Total Social Sector allocation	**78,0**				**88,0**			**91,12**
Institutional (Including votes 1-3 & 12)	**5,00**	**572 634** [a]	**450 682** [a]	**3,94**	**5,00**	**572 634** [a]	**453 304**	**3,96**
Balance of Votes	**17,00**	**1 946 955** [b]	**892 992** [b]	**7,80**	**7,00**	**801 687** [b]	**563 274**	**4,92**
Economic	7,00	801 687			7,00	801 687		
Backlog	3,00	343 580			0,00			
Basic	7,00	801 687			0,00			
TOTAL	**100,00**	**11 452 677**	**11 452 677**	**100,00**	**100,00**	**11 452 677**	**11 452 677**	**100,00**

a Excludes Works and Information Technology (IT) expenditure
b Includes all IT and Works expenditure
c Revised formula allocation allocates the backlog share weight in the equitable share to the weights of Education and Health in the same proportion as the national Treasury formula. It further allocates the basic share weight in equitable share to the weights of Education, Health and Social Services in the same proportion as the national Treasury formula.

Table 5.8 *(Continued)*

Comparison of national Treasury's formula with the Western Cape Budget 2002 2004/05								
Function	Formula allocation as per national Treasury		Actual allocation Western Cape Budget 2002		Revised formula allocation [c]		Actual allocation, including Works and IT, distributed between different sectors	
	%	Amount R'000	Amount R'000	%	%	Amount R'000	Amount R'000	%
Education	**41.00**	**5 010 741** [a]	**4 933 805** [a]	**40.37**	**46.72**	**5 709 800** [a]	**5 109 805**	**41.81**
Basis	41.00	5 010 741	4 933 805		41.00	5 010 741	5 109 805	
Backlog					2.04	249 315		
Basic					3.68	449 745		
Health	**19.00**	**2 322 051** [a]	**2 605 881** [a]	**21.32**	**21.66**	**2 647 138** [a]	**2 711 806**	**22.19**
Basis	19.00	2 322 051	2 605 881		19.00	2 322 051	2 711 806	
Backlog					0.95	116 103		
Basic					1.71	208 985		
Social Services	**18.00**	**2 199 837** [a]	**3 179 021** [a]	**26.01**	**19.62**	**2 397 823** [a]	**3 213 657**	**26.30**
Basis	18.00	2 199 837	3 179 021		18.00	2 199 837	3 213 657	
Backlog					0.00			
Basic					1.62	197 985		
Total Social Sector allocation	**78,0**				**88,0**			**90,3**
Institutional (Including votes 1-3 & 12)	**5.00**	**611 066** [a]	**467 356** [a]	**3.82**	**5.00**	**611 066** [a]	**469 978**	**3.85**
Balance of Votes	**17.00**	**2 077 624** [b]	**1 035 256** [b]	**8.47**	**7.00**	**855 492** [b]	**716 073**	**5.86**
Economic	7.00	855 492			7.00	855 492		
Backlog	3.00	366 640			0.00			
Basic	7.00	855 492			0.00			
TOTAL	**100.00**	**12 221 319**	**12 221 319**	**100.00**	**100.00**	**12 221 319**	**12 221 319**	**100.00**

a Excludes Works and Information Technology (IT) expenditure
b Includes all IT and Works expenditure
c Revised formula allocation allocates the backlog share weight in the equitable share to the weights of Education and Health in the same proportion as the National Treasury formula. It further allocates the basic share weight in equitable share to the weights of Education, Health and Social Services in the same proportion as the national Treasury formula.

In Table 5.8 above a comparison is made in the allocation of the welfare components of education, health and social services between National Treasury's formula and the Province's Budget 2002 for 2002/03, 2003/04 and 2004/05. It indicates that the Province foresees that it will allocate more funds to the afore-mentioned sectors than is expected and/or anticipated by National Treasury in its formula. In 2002/03 89,75% of the funds will be allocated to the relevant sectors as oppose to the National Treasury's guideline of 88%, while in 2003/04 and 2004/05 it is foreseen that respectively 91,12% and 90,3% of the funds will be allocated to the welfare sectors compared to the 88% guideline of the National Treasury. The crowding out effect that is caused by the aforementioned has an obvious detrimental effect on available resources of the other sectors and consequently on the levels of service delivery of these sectors. Also, although it is realised that spending on social services is captured in the equitable share, it is evident that they are not adequately captured in the current equitable share formula, calling into question the adequacy/

efficacy of the equitable share formula itself as means of equitable distributing the equitable share amongst provinces, which are relevant to the issue of inter-provincial equity in funding.

In addition, Table 5.9 below indicates the way in which funds will actually be allocated in 2002/03 to the social services sector compared to the revised allocation from the National Treasury in terms of the equitable share formula. While the allocation of the conditional grant and own revenue components are allocated in full to the social sector services, over-funding to the tune of R191,194 million is foreseen from the equitable share revenue source to this sector. However, this over-funding is covered by under-funding in the institutional sector (R87,276 million) as well as the balance of the votes (R103,917 million). The latter clearly illustrates the crowding-out effect that the social services sector has on the rest of the Votes in the Province.

Table 5.9

Analysis of own revenue deployment				
		2002/03 in R'000		
Social Services Sector		**Actual Allocation**	**Revised allocation E/Share formula**	**(Over)/ Under - funding**
Equitable share		9 799 830	9 608 636	(191 194)
Conditional Grants	a	1 509 621	1 509 621	
Own Revenue		110 556	110 556	
Net effect	b	**11 420 007**	**11 228 813**	**(191 194)**
		2002/03 in R'000		
Institutional (Votes 1,2,3&12)		**Actual Allocation**	**Revised allocation E/Share formula**	**(Over)/ Under - funding**
Equitable Share		459 665	545 945	86 280
Conditional Grants		16 500	16 500	
Own Revenue		166 977	167 973	996
Net effect	c	**643 142**	**730 418**	**87 276**
		2002/03 in R'000		
Balance of Votes (Votes 4,8,9,10,11,13&14)		**Actual Allocation**	**Revised allocation E/Share formula**	**(Over)/ Under - funding**
Equitable Share		659 410	764 323	104 913
Conditional Grants		435 183	435 183	
Own Revenue		520 419	519 423	(996)
Net effect	c	**1 615 012**	**1 718 929**	**103 917**

a Includes PIG and HRRP grants
b Funding from other sectors
c Funding to other sectors

Table 5.10 below depicts the Budget 2002 expenditure allocations per vote from 2002/03 to 2005/06 expressed as a percentage of total provincial revenue. From the table, it is evident that in "general", allocations to the different votes, as a percentage of total provincial revenue, remained more or less at the same levels, with marginal movement, since 2002/03 over the MTEF. On a pure superficial analysis of social sector spending (health, education, and welfare), it is found that this sector, in total, experienced consistent increased allocations[26] since 2002/03 over the MTEF. One tends to wonder what the driving forces behind these allocations trends are. ***With relatively less "new money"***, superficially, it appears that the some of the reasons might be the decision[27] to in general keep the social sector departments / allocations basically constant in real spending terms after adjusting for inflation, virements, function shifts, once off expenditures, earlier prioritization decisions, improvement of conditions of service agreement and accommodating the fall in the National Tertiary Services and Professional Training and Development grants. Added to this was to provide for the increased beneficiaries of the Child Support grant, with its raised limits, as well as those of other social security grants.

Table 5.10: Allocations per vote from 2002/03 to 2005/06 expressed as a % total provincial revenue

	VOTE	2002/03	2003/04	2004/05	2005/06
		% Allocated to Votes	% Allocated to Votes	% Allocated to Votes	% Allocated to Votes
	EXPENDITURE				
1	**Premier, Director-General and Corporate Services**	**2,55**	**2,51**	**2,49**	**2,51**
	IT	**1,74**	**1,63**	**1,56**	**1,57**
	Rest	**0,81**	**0,88**	**0,93**	**0,94**
2	**Provincial Parliament**	**0,17**	**0,17**	**0,17**	**0,17**
3	**Finance**	**0,44**	**0,43**	**0,43**	**0,44**
4	**Community Safety**	**0,86**	**0,95**	**0,94**	**0,95**
5	**Education**	**32,89**	**32,93**	**32,67**	**32,96**
	Public School Education	**26,18**	**26,23**	**26,03**	**26,25**
	Rest	**6,71**	**6,70**	**6,64**	**6,70**
6	**Health**	**27,15**	**27,34**	**27,29**	**27,53**
	Academic Health	**10,19**	**10,26**	**10,24**	**10,33**
	Rest	**16,95**	**17,08**	**17,04**	**17,19**
7	**Social Services and Poverty Alleviation**	**19,84**	**20,50**	**21,00**	**21,19**
	Social Security grants	**16,07**	**16,73**	**17,26**	**17,41**
	Rest	**3,78**	**3,77**	**3,74**	**3,78**

[26] Social Welfare sees a consistent increase; Health increases and then dips, with Education increasing marginally and only to see it dipping more substantially than Health. This is somewhat contrary to the philosophy that "the key to long term improvement in economic growth and in equity (via improved access to the labour market and greater economic opportunities) is improved education. From a fiscal perspective however, greater efficiency in the education system is needed, to counter the degree of drop-outs from especially the secondary school system. Before considering adjustment to future spending levels, a combination of assessing the efficacy of spending and demographics information is needed.

[27] Sequential Priority Framework, Chapter 7 (Proposals on future budget allocations over the MTEF period 2002-2005) Page 114, Western Cape Fiscal Policy 2002-2005.

Table 5.10 *(Continued)*

VOTE		2002/03	2003/04	2004/05	2005/06
		% Allocated to Votes	% Allocated to Votes	% Allocated to Votes	% Allocated to Votes
8	Housing	3,05	3,35	3,33	3,36
9	Environmental Affairs and Development Planning	0,80	0,79	0,78	0,79
10	Transport and Public Works	9,16	8,70	8,44	7,63
	Transport	5,28	4,91	4,73	4,25
	Public Works	3,67	3,56	3,46	3,14
	Rest	0,21	0,22	0,24	0,24
11	Agriculture	1,01	1,02	1,07	1,08
12	Local Government	0,47	0,31	0,29	0,30
13	Economic Development and Tourism	0,91	0,29	0,39	0,39
	Tourism	0,75	0,12	0,11	0,12
	Rest	0,16	0,17	0,28	0,28
14	Cultural Affairs and Sport	0,71	0,71	0,70	0,71
	Total Allocated to votes	100,00	100,00	100,00	100,00

From table 5.10 above, an observation, not necessarily worthy of praise is the accelerated growth in allocations in respect of the social sectors that have somehow been at the expense of the economic sector as the social sector allocations as a percentage of total provincial revenue increased whilst the economic sector in the same relation experienced a continued decease in its allocations. It is acknowledged that in preparing the budget, choices and trade-offs need to be made between objectives and goals, as available funds never suffice, given the plethora of needs. Provincial resource allocation occurs within the context of what occurs at the national and local government level, and thus therefore also has an effect on allocations to departments. However, if the underlying spirit of economic growth, pro-growth or rather anti-poverty in its true sense supports the budget, then serious introspection, with all due respect, is may be required in order to find a balance in allocations between the social and economic sectors.

A question which still remains unanswered, and indeed a challenge, is determining the value for money spending (cost effective service delivery through targeted spending by departments) which the Province achieves in making increased (might be substantive) allocations or adjustments in allocations to departments.

As can be deduced from current expenditure levels versus allocations as illustrated in Tables 5.8 to 5.10, the health, education and social services components (individually and combined) in the equitable share formula do not address the relative cost of delivery or demand for the service. The equitable share portion of the social services is therefore insufficient to cover the expenses related to them. One of the major contributors to the aforementioned problem is a very rapid take-up rate of social welfare services. For example, in November 2001, 103 537 children received the Child Support Grant, thus exceeding this nationally projected estimate of 90 000 as an upper limit. Estimates for November 2002 are in the region of 205 624 children, double the original upper limit, and this figure is projected to increase to at least 225 000 for the same period in the next two years. In respect of the latest proposed revision of the formula, the Budget Council[28] has indicated that the broad structure of the formula should be retained until the 2005 MTEF, when the new census data should be available. However, the Budget Council is of the opinion that a thorough review of data and component weights should be undertaken with a view to:

- Determining whether the weights in the formula (which should reflect policy priorities) are still equitable in view of changes in policy, demographic patterns and economic changes.
- Evaluating the data for the different components of the formula and advising the Budget Council and subsequently Cabinet on the possible updating of data in the formula.

The Budget Council is also of the opinion that consideration should be given to a fundamental review of the structure of the formula periodically (probably every five years) to provide certainty and to the extent necessary to allow for the phasing in of changes.

Although the welfare component has been increased to 18% as mentioned previously, the projected expenditure on welfare in the Western Cape is due to increase from 20% of total budget (also equitable share proportion, which is more relevant) in the current year to 22% in 2004/05 and even this might be an underestimation, with the latest projected overspending of some R286 million in the current year[29]. Furthermore, the equitable share does not take account of the fact that medical inflation is higher than CPIX inflation, thereby placing additional pressure on the health budget of the Province.

It must be realised that the Western Cape, like the rest of the country, also experiences socio-economic problems related to HIV/Aids, poverty and unemployment, although to a lesser degree. However, to maintain the current levels of health care, education standards, lower levels of poverty and consequently greater overall prosperity, the Western Cape will require sufficient funding, *inter alia* to address the needs pertaining to education, health, welfare and infrastructure. An equitable share portion with negative real growth, as in the case of the Western Cape, is not supportive of a pro-growth budget, given the high dependency of the budget on the equitable share portion. The Western Cape budget can therefore be in line with national government's objectives in terms of anti-poverty, reducing disparity and protecting the vulnerable only to the extent that it is allowed to do so in terms of its equitable share allocation. In other words, it should receive sufficient funding to perform its constitutional mandated basic services.

[28] Proposals on provincial equitable share formula, Budget Council Memorandum 11 August 2002: Paper by Ismail Momoniat
[29] Projections obtained from the August 2002 Early Warning System Report.

In summary, the increasing demands being made on the education, health and social services budgets in the Province require additional resources to be directed to these sectors so that they can continue providing a service of acceptable minimum standard. This implies that the current vertical share division will have to be drastically revised to compensate this Province and other provinces in a similar position (but on a different basis) for the cost of dealing with the current budget pressures which are in the main a result of national policy decisions. It will, however, not suffice simply to adjust the specific sector/component weightings of the horizontal share to ostensibly try and compensate for increased expenditure in a zero sum scenario that is non-sensical unless national policy directives directly mandate a cut in certain services – the vertical division itself will have to be revised to accommodate these extraordinary cost pressures emanating from the health, welfare and education sectors in the Province.

5.2.5 Conditional grants

Conditional grants are special purpose grants made from the National Budget[30] to the provincial and municipal spheres of government with specific conditions attached. They are determined by the national government and are earmarked for special priority programmes. Conditional grants are reflected in the annual Division of Revenue Act, which spells out the monitoring and reporting requirements for all conditional grants.

Conditional grants were introduced in 1998/1999 mainly to meet pressing needs, to expand the oversight role of national departments in policy areas shared concurrently with provinces and to support national priorities, particularly in the social services sectors (health, education and social security), and latterly (2001/02) for infrastructure. They are specifically used to –

- Provide for national priorities in provincial and local government budgets;
- Promote national norms and standards;
- Compensate provinces for cross-boundary flows and the provision of specialised services that have important cross-province externalities;
- Effect transition by supporting capacity building and organisational reforms (structural adjustments within recipient administrations);
- Address backlogs and regional disparities in social infrastructure.

There are broadly three categories of conditional grants, with different degrees of constitutionality attached:

- Block (assigned function) grants;
- Specific priority grants – infrastructure and recurrent grants;
- Transitional or special allocation grants.

The national Departments of Health and Housing and the national Treasury (although considerably less post-2001/02) administer the largest proportion of conditional grants to provinces. Table 5.11 sets out conditional grants for 1999/2000 and over the MTEF:

[30] It may be legally arguable that conditional grants are grants from the national share. They are sometime reflected as such (refer to Division of Revenue Act, 2002, Schedule 1, page 26)

Table 5.11: Conditional Grants: Western Cape: 1999/2000 – 2005/2006[31]

CONDITIONAL GRANTS: WESTERN CAPE: 1999/2000 – 2005/06								
Recipient votes in Province	Source (national department)	1999/2000 Actual transfer R'000	2000/2001 Actual transfer R'000	2001/2002 Actual transfer R'000	**2002/2003 Voted R'000**	2003/2004 Preliminary MTEF R'000	2004/2005 Preliminary MTEF R'000	2005/2006 Preliminary MTEF R'000
Vote 3: Finance								
Financial and personnel Management system support		4 230	8 666					
Contingency transfer: Debt relief		139 400						
Financial management: Internal audit								
Supplementary allocation		234 049	205 502	225 647				
Other		234 049	205 502	184 547				
Housing: capacity building				1 100				
Economic: National Land Transport Transition Act				1 000				
Health: Health management				16 000				
Finance: Implementation of Public Finance Management Act				5 000				
Provincial infrastructure: Flood damage [a]				18 000				
Vote 5: Education								
Financial management and quality enhancement	Education	15 168	15 168	17 827	**18 037**	18 519	19 630	20 777
Early childhood development	Education			1 659	**4 187**	6 952	0	0
HIV/Aids	Education		2 279	5 017	**11 376**	9 518	10 158	10 767
Vote 6: Health								
Central hospital		954 499	961 949					
National tertiary services [b]	Health			1 011 436	**1 047 438**	1 076 724	1 104 087	1 121 379
Professional training Development [c]	Health	278 382	292 326	308 776	**316 364**	314 696	327 210	323 278
Integrated nutrition programme	Health	33 734	28 789	28 789	**28 789**	34 653	40 727	44 632
HIV/Aids	Health		2 190	4 328	**11 713**	24 204	34 661	35 849
Hospital management improvement	Health				**19 000**	16 376	16 983	17 608
Vote 7: Social Services								
Financial management and improvement of social security system	Social Development	3 405	4 583	642	**1 200**			
Child support grant		2 000	2 000					
Victim empowerment		430						
Criminal justice system		1 888						
HIV/Aids	Social Development			1 000	**2 090**	2 900	3 088	3 273
Disaster relief grant				2 500				
Vote 8: Planning, Local Government and Housing								
Housing Fund	Housing		341 466	325 861	**378 860**	423 282	446 035	473 136
Capacity building		1 120	510					
Land development objectives				17 500				
Local government support	Provincial and Local Government	13 550	5 420		**16 500**	15 100	13 350	14 151
Provincial Consolidated Municipal Infrastructure Programme (CMIP)	Provincial and Local Government				**8 357**	8 858	9 390	9 953

[31] Partially own calculations by the Provincial Treasury in respect of the 2003/04 to 2005/06 MTEF using baseline conditional grant allocations as per the 2002 budget allocations and preliminary allocation letter from national Treasury dated 7 November 2002.

Table 5.11 *(Continued)*

CONDITIONAL GRANTS: WESTERN CAPE: 1999/2000 – 2005/06								
		1999/2000	2000/2001	2001/2002	**2002/2003**	2003/2004	2004/2005	2005/2006
Recipient votes in Province	**Source (national department)**	Actual transfer	Actual transfer	Actual transfer	**Voted**	Preliminary MTEF	Preliminary MTEF	Preliminary MTEF
		R'000	R'000	R'000	**R'000**	R'000	R'000	R'000
Hostel upgrading		3 750						
Human settlement	Housing		9 000	12 500	**13 250**	13 500	14 310	12 211
Vote 10: Transport and Public Works								
Provincial Infrastructure	National Treasury			49 524	**86 589**	130 671	161 397	171 570
Hospital revitalisation	Health	10 705	28 294	29 000	**45 000**	31 350	33 231	35 225
Vote 11: Economic Development, Tourism and Agriculture								
Provincial Infrastructure								
Poverty relief and Infrastructure development	Agriculture		315	878	**1 300**	1 800	0	0
Provincial Infrastructure	National Treasury				**9 621**	14 519	17 933	19 063
Contingency grant								
Total conditional grants		**1 696 310**	**1 908 457**	**2 042 884**	**2 019 671**	**2 143 622**	**2 252 190**	**2 312 903**

a - Reimbursement of expenditure incurred by (the old) Vote 10: Economic Development, Tourism and Agriculture for reconstruction of roads (infrastructure) in 2000/01.
b - Central Hospital grant until 2001/02.
c - Professional training research until 2001/02.

Although some conditional grants have been implemented successfully, others have experienced problems, especially with the flow and spending. The problem of spending relates to provinces that underspend their allocated grants owing to a lack of capacity (although to a lesser degree in the Western Cape) or to late allocations or the late finalisation of approval of business plans by national departments. Another factor that exacerbates the problem is the increase in the number of small grants in the system, which has increased the fragmentation of the funding and has placed an unnecessary additional administrative burden on provinces. Some of the small grants have, however, been amalgamated into the supplementary grant in 2001/02 and, subsequently, subsumed into the equitable share from 2002/03.

Inconsistent measures introduced through the various annual Division of Revenue Acts have progressively aimed at addressing some of these problems. However, the inconsistency of the measures has compelled provincial treasuries and departments to continue introducing new control and reporting measures. A challenge for national government would be to investigate the streamlining and consolidation of the remaining grants, incorporating them into the equitable share and introducing more effective measures to monitor their implementation. The national Treasury has recently met some of these challenges by addressing the problems surrounding the implementation of grants through the introduction of a provincial framework[32] for conditional grants which aims to:

- Limit the number of conditional grants to those terrains where the equitable share and norms and standards cannot appropriately fund specific programmes;

[32] "Conditional Grants Framework" prepared by National Treasury for the Budget Council Lekgotla, 4 - 7 July 2001

- Eliminate small conditional grants as they impose disproportionate administrative burdens;
- Provide tougher threshold criteria for national departments planning to introduce conditional grants, including more rigorous consultation with provincial treasuries and the approval of Cabinet. National departments which intend to introduce new conditional grants will be required to first demonstrate first of all why such objectives cannot be fulfilled through the equitable share and why the establishment of norms and standards within agreed funding levels cannot help to achieve such objectives;
- Incorporate conditional grants into the normal budget preparation process;
- Provide best practice in designing, planning and monitoring conditional grants; and
- Focus on outcomes rather than inputs when monitoring conditional grants.

Although it is realised that conditional grants only represents a relatively small portion of the total revenue envelope of a province, it is significant enough to enable the provision of public services within seven sectors which will be discussed in more detail below. In the Western Cape budget for 2002/03 conditional grants constitute in the region of 15% of total revenue (see Table 5.5). There is a very inconsistent trend in the funds allocated to the Western Cape in the form of conditional grants and it is projected that this trend will be continued over the MTEF years. As indicated in Table 5.5, conditional grants in real terms decreased by 9,9% from 1998/99 to 1999/2000, increased by 5,5% in the year thereafter, decreased by 0,6% in 2001/02 and will do so for the MTEF years as well when it will decrease by 10,4 in 2002/03, 0,2% in 2004/05 and 1,4% in 2005/06. It is acknowledged that some of the variability in the conditional grants could be ascribed to national Treasury's efforts to limit the number of conditional grants by incorporating them into the equitable share, as in the case of the supplementary grant allocation which was eliminated in 2002/03 and incorporated into the equitable share. Nevertheless, it does impact on fiscal planning, forcing the provincial Treasury to introduce measures to protect departments and service delivery efforts from fluctuating national revenue flows.

Conditional grants consist of the following components, with the allocations reflected in Table 5.11 categorised per sector:

- National Agriculture Department: It consists of a small grant aimed at degradation problems of natural resources and meant to improve the socio-economic status of rural communities.
- National Education Department: These grants consist of a Financial Management and Quality Enhancement, HIV/Aids and Early Childhood Development (ECD) grant. The first-mentioned grant was introduced in 1999/2000 and was supposed to be phased out by 2002/03, but the national Department of Education proposed that the grant should be retained to consolidate gains achieved over the last three years in improving education outcomes. The ECD grant was introduced in 2001/2002 and it is foreseen that it will be phased into the equitable share in 2003/04 over a period of ten years.

- National Health Department: The **health conditional grants** [National tertiary services (NTS), Health professional training development (HPTD), Hospital revitalisation, HIV/Aids, Integrated Nutrition Programme and Hospital Management Improvement grants] comprise 72% of the total conditional grants received by the Province, based on the 2002/03 allocations. The health sector's new framework for tertiary services and training constitutes a major reconfiguration of the three tertiary services and training grants and ostensibly improves equity between provinces. The new framework provides for the rationalisation of the three grants into two. This entails a redistribution of tertiary health care funds away from the Western Cape and Gauteng to other provinces, to be phased in over a period of five years starting in 2002/03. National Treasury expects the provinces concerned to fund any resulting shortfalls from their equitable shares or own revenue resources. The change to the structure of health conditional grants (NTS and HPTD) will result in an average real decrease of 4,4% over the period 2002/03 to 2005/06 for the Western Cape over the full four-year period.
- National Treasury: The Western Cape only receives the provincial infrastructure grant which is to be used to fund rehabilitation and construction of roads, schools and health facilities and to address infrastructure for rural development.
- National Provincial and Local Government Department: Two grants, namely the Local Government Support and Consolidated Municipal Infrastructure Programme grants are transferred to the Province. The first grant is aimed at capacity building at smaller local governments, and the second is allocated to provinces to provide technical and administrative support to enable municipalities to implement this infrastructure programmes.
- National Housing Department: This sector comprises two grants, namely the Housing Subsidy grant for low-income housing and the much smaller Human Settlement Redevelopment grant, which provides funds for urban pilot projects.
- National Social Development Department: Most of the social development grants have been phased out, with the Financial Management Grant also to be phased out in 2002/03. The HIV/Aids grant provides for community and home-based care.

Latest revision of grants structure: In the 2002 MTEF allocations, only the housing subsidy and HIV/Aids grants have undergone changes, and the supplementary finance grant has been incorporated into the equitable share, with effect from the 2002/03 financial year. However, changes are on the cards for some of the grants, particularly in health and housing. For instance, it is being considered to transfer the IPSN grant (part of the Integrated Nutrition Programme (INP)) to Education from the 2003/04 financial year. Policy considerations, for example, necessitated restructuring and rationalisation of health grants.

As already explained in paragraph 5.2.4, in-principle approval was granted by the national Minister of Finance on 17 July 2002[33] for inflation adjustments for the 2002/03 budget and the 2003 MTEF period, with specific maximums for 2002/03 and 2003/04, *inter alia* for social grants. The increases in the social grants are based on increases in old age and disability grants by R20 per month and the child support and foster grants by R10 per month from 1 October 2002, based on national projections of take-up rates from 2002/03 to 2005/06, which has been referred to earlier, out of kilter with reality.

5.2.6 Challenges facing the Western Cape province

The main challenge for the Western Cape is to build and maintain professional capacity within the Province to spend the total available resources of the nationally raised revenue in the most efficient, economic and effective manner to achieve national and provincial policy objectives, which ultimately will contribute towards economic growth and development or Ikapa elihlumayo . However, in meeting this challenge the Province will come across several sub-challenges, to be highlighted in more detail below.

Over the short term the Province needs to provide targeted fiscal transfers for social renewal, employment creation and poverty reduction, and over the medium to long term it must provide an institutional infrastructure and good public services to raise the potential growth rate of the economy and the income of the poor (reducing the gini-coeficient). This will require the Province to increase its capacity in order to implement policies for efficient and effective spending and to deliver a larger quantity and higher quality of public benefits, naturally within the boundaries of its allocated funds. In the long term the Province will have to focus on the following measures:

- Creating market and government procurement opportunities for the historically disadvantaged
- Developing small businesses
- Effecting land and agricultural reform to the benefit of small-scale farmers
- Increasing investment in quality social infrastructure (schools, hospitals, etc.)
- Deepening the skills base
- Increase focused and well considered infrastructure spending (roads, buildings, etc.) dynamically tied to economic development with both domestic and export growth potential
- Increasing education and overall sill levels (focus on mathematics and science)
- Taking steps to reduce unemployment and poverty levels
- Broadening the economic base, with the emphasis throughout the above measures on black economic empowerment.

[33] Budget Council Lekgotla: 21-24 August 2002, Appendix I1, page 1

With regard to the provision of quality social and economic infrastructure, it should be realised that this forms one of the most fundamental preconditions for economic growth, job creation and accelerated service delivery, with political stability and indeed a better life for all.

In the process of addressing the aforesaid, the Province will have to play an active role in reducing the barriers to economic growth, ensuring that regulatory frameworks are conducive to investment, employment and continuous learning. Although the regulation of economic activity does help to provide a supportive environment, regulation should also take account of the economic costs of compliance. Also, on the one hand policies should recognise institutional capacity constraints and on the other the costs of new and existing regulations should be justified by their benefits.

5.3 Total revenue and expenditure of the Province

To conclude this chapter on the fiscal envelope for the Province, the table below illustrates the various components making up the total revenue and expenditure budget of the Province available for distribution over the MTEF 2003/04 to 2005/2006 as at the end of September 2002, before allocations to departments are made. It includes provisional additional allocations from national Treasury in respect of inflation adjustment for personnel and welfare and an additional allocation to provinces based on each one's target share.

Table 5.12

Provincial Budget Summary									
Provincial Department	1999/2000 Actual R'000	2000/01 Actual R'000	2001/02 Actual R'000	2002/03 Budget R'000	2002/03 Est. Actual R'000	2003/04 MTEF R'000	% Change Voted to Est. Actual	2004/05 MTEF R'000	2005/06 MTEF R'000
National transfers	10 195 503	11 143 616	11 912 724	12 880 209	13 313 925	14 623 435	9,8	15 865 573	17 006 933
Equitable share	8 499 193	9 235 141	9 869 840	10 918 905	10 918 905	11 452 753	4,9	12 221 957	12 955 682
Plus: Inflation adjustments					191 720	465 203	142,6	547 261	588 735
Policy adjustments "New Money" (NT 16/10/2002)					183 629	561 857		844 165	1 149 613
Adjusted Equitable share	8 499 193	9 235 141	9 869 840	10 918 905	11 294 254	12 479 813	147,5	13 613 383	14 694 030
Conditional grants	1 696 310	1 908 475	2 042 884	1 961 304	1 961 304	2 072 245	5,7	2 153 130	2 153 130
Plus: Inlation adjustments and Policy adjustments					50 010	71 377		99 060	159 773
Adjusted Conditional grants	1 696 310	1 908 475	2 042 884	1 961 304	2 019 671	2 143 622	0	2 252 190	2 312 903
Own Revenue	733 329	764 733	954 970	797 952	797 952	827 541	3,7	820 584	826 489
Total revenue	10 928 832	11 908 349	12 867 694	13 678 161	14 111 877	15 450 976	9,5	16 686 157	17 833 422
Current outlays	7 494 595	7 868 888	8 584 844	9 226 492	9 226 492	9 729 468	5,45	10 213 319	10 213 319
Capital outlays	219 622	551 778	815 606	840 000	840 000	802 930	-4,41	817 181	817 181
Transfer payments	2 682 365	3 092 590	3 394 105	3 727 076	3 727 076	3 956 098	6,14	4 219 014	4 219 014
Expected increased expenditure					433 716	1 082 986	149,70	1 476 065	2 623 330
Sub Total	10 396 582	11 513 256	12 794 555	13 793 568	14 227 284	15 571 482	9,45	16 725 579	17 872 844
Smoothing				81 286	81 286	-61 681		-19 605	-19 605
Contingent liabilities				52 750	52 750	55 335		58 267	58 267
Unforeseen and unavoidable contingencies				50 100	50 100	52 499		54 821	54 821
Total expenditure	10 396 582	11 513 256	12 794 555	13 977 704	14 411 420	15 617 635	8,37	16 819 062	17 966 327
Surplus/ (deficit)	532 250	395 093	-189 821	-299 543	-299 543	-166 659		-132 905	-132 905

5.4 Provincial borrowing

In terms of section 230 of the Constitution, provincial governments may borrow money for bridging finance and to fund capital projects such as investments in infrastructure. It further states that provincial borrowing must be "in accordance with reasonable conditions determined by national legislation." The proviso "reasonable conditions determined by" the latest Constitutional amendments enacted, was amended and are only allowed within the framework of national legislation. Moreover, section 215 of the Constitution states that budgets in each sphere of government must indicate proposals for financing anticipated deficits, and intentions regarding borrowing and other forms of public liability that will increase the public debt. Currently the Borrowing Powers of Provincial Governments Act of 1996 regulates provincial borrowing. This Act establishes a loan-coordinating committee ("LCC") with membership identical to the Budget Council, and details the borrowing powers of provinces. The responsibilities of the LCC are to coordinate provincial borrowing, taking into account the overall demand for capital market funds, the total debt of each province and its associate institutions, any contingent liabilities, and the ability of provinces to service debt. Key provisions include prohibiting foreign borrowing, permitting domestic borrowing to be undertaken only by the MEC for Finance, and allowing the national Minister of Finance to effectively control borrowing by specifying the permissible ratio of interest repayments to current revenue.

Borrowing enables a government to finance the initial cost immediately, but repayment must be budgeted over time as benefits from the investment are generated. Spreading the burden of the investment ensures that the current taxpayer does not fund the entire cost of a project that will render benefits to future generations. Debt financing also allows a government to undertake more projects, and sooner, than would have been possible from tax revenue alone.

The Borrowing Powers of Provincial Governments Act was enacted before the provinces received their current level of autonomy with regard to budgeting and before current intergovernmental fiscal relations took shape (without any regulation being issued, based on the Interim Constitution of South Africa). Despite the Constitutional autonomy and independence of the provinces, the market often views national government as a guarantor of provincial debt. As a consequence and to counter this perception and foster provincial independence, the Budget Council agreed in 1997 that provinces should not borrow funds until a clearer framework emerged that complied with the final Constitution. This was mainly intended to prohibit borrowing for operating, except for short-term bridging loans in anticipation of revenue or capital expenditure. Some legal ambiguities existed in provinces in the interpretation on the use of bridging finance. The Provincial Borrowing Powers Act defines bridging finance as funds raised during a financial year to fund current expenditure in anticipation of the receipt of current revenue within that financial year, whilst the 1996 Constitution initially stated that bridging finance must be redeemed within twelve months. The difference in wording of these two provisions gave rise to contradictory interpretations and consequently the Constitution was amended in 2001 by eliminating the provision that loans for current expenditure must be repaid within a period of twelve months.

The current legal framework has not been particularly effective, primarily because it has never been fully implemented. The decision of the "no borrowing" taken by the Budget Council seems to have had two effects, namely:

- The national Treasury did not institute a programme for monitoring provincial borrowing;
- No regulations were issued in terms of the Borrowing Powers of Provincial Governments Act.

This resulted in uncertainty as to what exactly the law permits and what role the LCC should play.

Further development in respect of provincial borrowing is that the provincial borrowing framework was reassessed at the Budget Council Legotla in 2001. The result was a resolution that called for the Budget Council's Technical Committee for Finance (TCF) to take a consultative approach in developing a borrowing framework that considers the full range of provincial capacities and borrowing options, for national Treasury to provide provincial staff with borrowing-related training and technical assistance, and for a policy of no provincial borrowing for capital projects during the 2002/03 financial year. The Technical Committee on Finance in April 2002 requested that a task team be formed that would present a way forward on the borrowing framework to the TCF. This Province is also represented on the task team. The Budget Council, at its meeting of 17 May, was presented with a detailed work plan, indicating the timeframes, for the completion of a borrowing framework.

If one should explore the way forward in respect of provincial borrowing powers, there is some merit in permitting sub-national borrowing as long as it increases the efficiency of public resource use and transfers risk to the private sector. It is unlikely, however, that market discipline alone will offer a viable regulatory environment in the medium term and a strong oversight role for national Treasury is therefore necessary. It is conceded that national government retains responsibility for overall debt management, and therefore it must coordinate and regulate provincial borrowing within a rule-based framework. The framework should detail the ability of the national government to impose financing limits on the provinces, improve disclosure requirements, prohibit foreign borrowing, and incorporate clear rules on deficit management. It should further seek to maximise provinces' ability to use debt efficiently without compromising the national government's ability to manage the aggregate debt or increasing its indirect risks. A framework for monitoring and managing provincial borrowing is necessary, irrespective of the overall financing limit. Indeed, an integrated borrowing framework is unlikely to lead to a substantial increase in provincial borrowing over the medium term as most provinces are unable to support a significant increase in debt-servicing costs, which limits their ability to borrow. At present most provinces do not generate sufficient information for monitoring and managing the capital they deploy (assessing the productivity of existing and potential new assets, the risk of financing those assets and the indirect risk to national government). Available information on assets and liabilities which includes projects with significant future financial commitments, the present value of existing assets, etc will have to be more disaggregated. Improved disclosure will promote transparency, accountability and a better evaluation of financial exposure, including the efficiencies of projects for which funds are to be borrowed and the attendant financial risks.

Developing the required capacity at provincial level to manage provincial borrowing effectively remains a challenge to provinces and is likely to take time. In this Province the expertise in making effective and appropriate decisions to manage this portfolio has to be developed urgently in the next year for the Province to be able to effectively utilise the anticipated lifting of embargos on provincial borrowing once the framework has been finalised, which is scheduled to be at the end of the 2003/04 financial year.

5.5 Own revenue overview and trends

Present own revenue sources of the Province are fairly limited, consisting mainly of motor vehicle licence fees, hospital fees, interest revenue and gambling and betting taxes. However, they do remain an important source of marginal funding. In this Province, own revenue formed 7,42% of the total provincial revenue envelope in 2001/02, being 1,0 percentage point higher than in 2000/01 and thus by far exceeding the national average[34] of approximately 4%. As the current sources have upper limits, it is projected that own revenue, as a percentage of total provincial revenue, will fluctuate between 4% and 6% over the MTEF. The trends in own revenue collection since 1999/2000 and MTEF projections are captured in some more detail in Table 5.13 below.

Table 5.13: Provincial revenue envelope

		1999/00		2000/01		2001/02		2002/03		2003/04		2004/05		2005/06	
		R'000	%	R'000	%	R'000	%	R'000	%	R'000	%	R'000	%	R'000	%
OWN REVENUE SOURCES	Motor vehicle licences	299,072	40.78	344,128	45.00	461,437	48.32	491,519	61.60	583,000	70.45	583,000	71.05	583,000	66,89
	Hospital fees	61,679	8.41	70,451	9.21	88,895	9.31	70,721	8.86	79,075	9.56	83,413	10.17	87,368	9,44
	Betting	29,773	4.06	27,733	3.63	24,795	2.60	15,5000	1.94	13,500	1.63	13,500	1.65	13,500	1,85
	Gambling	-	-	21,654	2.83	85,630	8.97	84,000	10.53	51,000	6.16	51,000	6.22	51,000	10,05
	Liquor licences	-	-	2,690	0.35	3,299	0.35	3,388	0.42	3,450	0.42	3,440	0.40	3,440	0,40
	Casino Bid Fees	135,000	18.41	11,400	1.49	-	-	-	-	-	0.00	-	0.00	-	-
	Interest	86,962	11.86	149,722	19.58	184,826	19.35	69,776	8.74	35,892	4.34	22,966	2.80	22,966	2,75
	Property income	16,877	2.30	15,740	2.06	17,902	1.87	9,963	1.25	12,736	1.54	12,864	1.57	12,938	1,23
	Other	103,966	14.18	121,215	15.85	88,186	9.23	53,085	6.65	48,888	5.91	50,401	6.14	52,277	7,38
	Total	**733,329**	100	**764,733**	100	**954,970**	100	**797,952**	100	**827,541**	100	**820,584**	100	**826,489**	100
NATIONAL TRANSFERS	Equitable share	8,499,192		9,235,141		9,869,840		11,294,254		12,479,813		13,613,383		14,694,030	
	Conditional grants	1,696,310		1,908,475		2,042,884		2,019,671		2,143,622		2,252,190		2,312,903	
	Total national transfers	10,195,502		11,143,616		11,912,724		13,313,925		14,623,435		15,865,573		17,006,933	
	Total provincial revenue	10,928,831		11,908,349		12,867,694		14,111,926		15,450,976		16,686,157		17,833,422	

Consistent growth in own revenue has since 1999/2000 to 2001/02 been to the tune of 38,97%, 4.28% and 24,88% respectively, considerably more than the growth of 3,76%, 9,3% and 6,9% in national transfers over the same period. Over this period the main contributors to the growth in provincial own revenue were motor vehicle licence fees, hospital fees, gambling taxes and interest revenue. Own revenue as a percentage of total provincial revenue has also increased from 6,71% in 1999/2000 to 6,42% and 7,42% in 2000/01 and 2001/02 respectively, mainly from the

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[34] National Treasury Own revenue project: 2002 Paper by K. Brown - TCF 19 September 2002

aforementioned sources. Although own revenue for 2002/03 is projected to decline, if compared to the previous year's actual collection, it is projected that own revenue as a percentage of gross provincial revenue will vary between 5,65% in 2002/03 and 5,36%, 4,92% and 4,63% in 2003/04, 2004/05 and 2005/06 respectively. The Western Cape has so far maintained consistent growth in own revenue collections, but the challenge now remains not only to maintain, but also to continuously improve on these growth trends over the MTEF. In 2003/04 it is estimated that revenue will grow by 3,71%, if compared with 2002/03, but a slight decline in projections is shown for 2004/05 which is mainly due to no provision being made at this stage for increases in motor vehicle licence fees.

Table 5.14 depicts and illustrates the actual revenue performance against budgeted revenue per department from 1999/2000 to 2001/02, the difference being over/(under) collection as well as the percentage difference between the budget and actual collections. Some inefficiency in administering revenue sources coupled with some poor projections resulted in the true picture of the total own revenue performance not being reflected in the budget estimates.

It can thus be quite easily deduced that departments continue to budget too conservatively for own revenue. During the period 1999/2000 to 2001/02 total overcollection, or alternatively one might argue that under-budgeting, amounted to R290,069 million, R248,194 million and R264,095 million respectively. This represented a 65,4%, 48% and 38,2% overcollection above budgeted targets. Although this shows a declining trend, it remains to be said that current departmental projections over the MTEF in general appear not to be credible but "highly" conservative. It is evident that from 1999/2000 to 2002/03, budgeted own revenue for the next year was always below the actual collections for the previous financial year.

Table 5.14: Budgeted revenue vs actual revenue per department between 1999/2000 and 2001/02 and MTEF Projections

Departments	1999/2000		2000/01		2001/02		2002/03	2003/04	2004/05	2005/06
	Budget R'000	Actual R'000	Budget R'000	Actual R'000	Budget R'000	Actual R'000	Budget R'000	Medium-term estimate R'000		
Premier, Director-General & Corporate Services	3,752	1,740	1,132	1,386	674	742	468	468	468	468
Provincial Parliament		28		222		164				
Finance	36,992	257,176	26,760	214,794	112,791	298,442	166,505	97,707	84,774	84,774
Community Safety	10	2,131	560	505	571	472	567	367	367	367
Education	19,850	21,840	21,939	21,857	8,768	17,550	13,940	13,440	13,440	13,440
Health	84,789	84,263	82,316	98,781	87,132	117,194	92,035	101,676	107,370	113,383
Social Services	1,322	10,607	1,454	5,511	1,567	5,694	4,581	3,572	3,572	3,572
Planning, Local Government & Housing	596	909	722	665	267	400	217	194	108	
Environmental and Cultural Affairs and Sport	5,359	6,253	6,211	5,733	1,038	1,942	1,253	1,888	2,092	2,092
Transport and Public Works	273,252	339,119	357,919	402,496	461,263	498,546	501,888	594,165	594,165	594,165
Economic Affairs, Agriculture and Tourism	17,338	9,263	17,526	12,783	16,804	13,824	16,498	14,064	14,228	14,228
Total	**443,260**	**733,329**	**516,539**	**764,733**	**690,875**	**954,970**	**797,952**	**827,541**	**820,584**	**826,489**
Percentage difference between budget and actual										
Premier, Director-General & Corporate Services		-53.6%	-34.9%	22.4%	-51.4%	10.1%	-36.9%	0.0%	0.0%	0.0%
Provincial Parliament										
Finance		595.2%	-89.6%	702.7%	-47.5%	164.6%	-44.2%	-41.3%	-13.2%	0.0%
Community Safety		21210.0%	-73.7%	-9.8%	13.1%	-17.3%	20.1%	-35.3%	0.0%	0.0%
Education		10.0%	0.5%	-0.4%	-59.9%	100.2%	-20.6%	-3.6%	0.0%	0.0
Health		-0.6%	-2.3%	20.0%	-11.8%	34.5%	-21.5%	10.5%	5.6%	5.6%
Social Services		702.3%	-86.3%	279.0%	-71.6%	263.4%	-19.5%	-22.0%	0.0%	0.0%
Local Government, Housing & Planning		52.5%	-20.6%	-7.9%	-59.8%	49.8%	-45.8%	-10.6%	-44.3%	-100.0%
Environmental and Cultural Affairs and Sport		16.7%	-0.7%	-7.7%	-81.9%	87.1%	-35.5%	50.7%	10.8%	0.0%
Transport and Public Works		24.1%	5.5%	12.5%	14.6%	8.1%	0.7%	18.4%	0.0%	0.0%
Economic Affairs, Agriculture and Tourism		-46.6%	89.2%	-27.1%	31.5%	-17.7%	19.3%	-14.8%	1.2%	0.0%
Total		**65.4%**	**-29.6%**	**48.0%**	**-9.7%**	**38.2%**	**-16.4%**	**3.7%**	**-0.8%**	**0.7%**

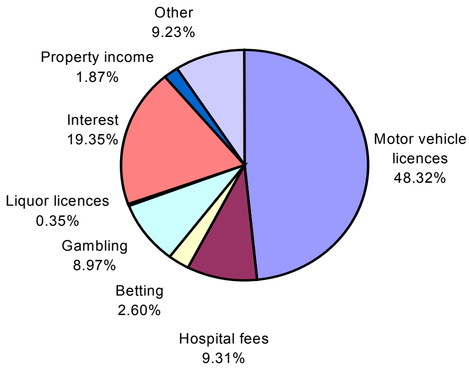
Names of Departments are those prior to 1 August 2002, i.e before the departmentalisation model came into play

Whilst it is conceded that overcollection may be attributable to improved revenue collection and administration mechanisms, it is to a great extent due to conservative revenue estimation. It is also acknowledged that collection in respect of some revenue sources is unpredictable by nature, which makes forecasting difficult and complicates the budgeting and planning processes. However, it remains a challenge for the Treasury and departments to develop mechanisms to address the continuing trends of conservative budgeting, which results in unacceptably high levels of overcollection.

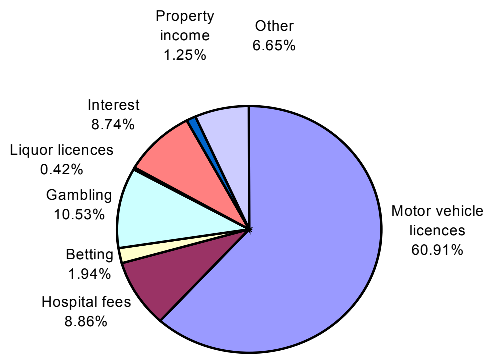
Composition of own revenue

The composition of own revenue collected during 2001/02 and projected revenue for 2002/03 is provided in Graphs 5.1 and 5.2:

Graph 5.1 - Actual 2001/02



Graph 5.2 - Budget 2002/03



Motor vehicle licence fees remains the largest source of own revenue, contributing 48,32% in 2001/02. Fees collected have increased from R299,072 million to R344,128 million and R461,437 million over the period 1999/2000 to 2001/02.

Interest on bank balances and investments constituted 19,35% of own revenue for 2001/02, with consistent growth since 1999/2000, from R86,962 million to R149,722 million in 2000/01 and R184,826 million in 2001/02. For the financial years 2002/03 to 2005/06, falling investment interest is projected, mainly because of the lowering of liquidity levels of the Provincial Revenue Fund as reserves are increasingly drawn down to fund infrastructure projects and cash management is increasingly refined to operate within narrower margins.

Hospital patient fees constituted 9,31% of own revenue in 2001/02 and is estimated to remain at more or less the same levels over the MTEF. Although hospital fees are adjusted annually to keep tread with inflation, actual collections show negative real growth, resulting in a real decrease in this revenue source.

Gambling (8,97%) and Betting (2,6%) revenues are made up mainly of taxes on casinos and horseracing and constituted 11,57% of total own revenue in 2001/02. It is expected that betting taxes will decline by 0,66 percentage points over the MTEF whereas gambling taxes will increase to the extent that it is projected to constitute 10,53% in 2003/04, decreasing to 6,22% of total own revenue over the MTEF. However, this might change if current rates are adjusted for inflation creep and to allow greater return to investors in the gambling industry, particularly to empowerment groups.

The remaining revenue categorised as “other” revenue (9,23%), liquor licences (0.35%) and property income (1,87%) represented 11,45% of the total own revenue in 2001/02 and is estimated to remain at more or less the same levels over the MTEF. This revenue includes mainly liquor licence fees, property sales and rentals, user charges and fees such as abnormal load permits, commission on insurance paid by insurance companies, examination and tuition fees, board and lodging, services, sales, stale cheques[35] and contributions by universities towards expenditure incurred by provincial academic hospitals. Another portion of other revenue is “miscellaneous” revenue, which consists mainly of once–off receipts such as refunds from previous years and donations.

5.5.1 Major revenue sources

5.5.1.1 Motor vehicle licences

The Constitution, Schedule 4, assigns concurrent national and provincial legislative competence for vehicle licensing. Section 92 of the National Road Traffic Act, 1989 (Act 29 of 1989) determines in this regard that “fees payable shall be as provided by the laws of the province” concerned. The Western Cape Road Traffic Act, 1998, which became effective on 18 December 2000, is a provincial Act in terms of which this Province, through the provincial minister responsible for transport may issue regulations determining motor vehicle licence fees and other related fees and tariffs.

In line with national trends, this source of revenue currently represents the biggest single source of provincial own revenue in the Province. For the years 1998/99 to 2001/02, these fees represented on average 45% of total provincial revenue. Table 5.15 below depicts the trend of revenue from motor vehicle licence fees collected from 1997/98 to 2001/02, and it is evident from the table that the Department of Transport and Public Works has maintained consistent growth in revenue from this source since 1997/98 and will do so over the MTEF. In 1999/2000, revenue collection escalated by 18,92% although fees were only increased by 15%. The additional growth of 3,9 percentage points came mainly from the increase in the vehicle population and some concerted initiatives in respect of motor vehicle licence fee collections. The Province made full use of the powers assigned to the Minister of Transport by implementing a 25% increase from 1 April 2001 and further increases

[35] On rapidly declining trend due to Electronic Fund Transfers (EFT’s)

of 10% over the MTEF after undertaking an extensive investigation into the fee structure of motor vehicle licences. The 25% increase resulted in R461,438 million in revenue in 2001/02, yielding R32,697 million above the 2001/02 Budget. The rationale behind this increase was to supplement the funding voted for the maintenance of provincial road infrastructure so as to address some of the backlogs which could not be afforded/funded through normal national budget allocations.

Table 5.15: Revenue collection of motor vehicle licence fees between 1997/98 and 2001/02 and MTEF projections

Revenue	Actual					Budget	Medium-term estimate		
	1997/98 R'000	1998/99 R'000	1999/00 R'000	2000/01 R'000	2001/02 R'000	2002/03 R'000	2003/04 R'000	2004/05 R'000	2005/06 R'000
Motor vehicle licence fees	226,495	251,497	299,072	344,128	461,437	486,049	583,000	583,000	583,000
% growth		11.04%	18.92%	15.07%	34.09%	5.33%	19.95	0.00%	0.00
Share of own revenue	40.10%	47.66%	40.78%	45.00%	48.32%	60.91%	70.45	71.05	70.54

It is important to note that the full amount of licence fees actually collected is retained by the responsible department for use on roads infrastructure.

It is expected that the annual increase in motor vehicle licence fees over the MTEF should continue at least at the rate of infrastructure inflation unless an upsurge in road maintenance and construction costs necessitates a higher increase. This approach will lead to some fee stability with excessive fee increases, which might not be defendable or not being transferred to the consumer vis-à-vis excessive infrastructure inflation increases or not being passed back to the Provincial Government, albeit still providing insufficient funding for road infrastructure maintenance and upgrades. Although to a lesser extent reasonable increases on an annual basis will also address the migration of vehicles (particularly heavy vehicles) to other provinces where licence fees are much lower, mainly because they have not been revised regularly. The regulation of the migration of motor vehicles between provinces (with the cost of the licence as deciding factor) remains a challenge to the transport department.

The responsibility for collecting motor vehicle licence fees rests with local authorities in the Province. Although no service level agreements have been concluded in this regard, local authorities are paid a commission of 12% on licence fee collections, which is deemed to be a proxy for collection costs incurred by them. The commission structure used is of an historical nature, and the question whether the commission currently paid relates to the services rendered, still remains to be settled. In addition to the commission, local authorities may retain revenue collected from drivers licences, registration fees and permits.

In 1999/2000, collection costs amounted to R53,989 million, increasing to R63,089 million in 2000/01 and R83,097 million in 2001/02. This represents a constant 18% of total motor vehicle licence fees collected annually over the period.

The absence of a service level agreement between the provincial government and the local authorities concerned in itself poses a risk to provincial revenue as no mechanism currently exists to deal with possible inefficiencies (slow pay-over rate and even non-payment of revenue collected and the reconciliation of these revenues) at local government level. Initial indications from the responsible Department are that a consultant is in the process of being appointed to determine a feasible/realistic fee structure and to facilitate the conclusion of an agreement to mitigate some of the risks identified above.

The success rate of motor vehicle licence fee collection has improved slightly from 2000/01 to 2001/02. In 2000/01, 3,95% of vehicle licences remained unpaid but decreased to 3,79% in 2001/02. This was mainly as a result of a pilot project of appointing debt collectors, undertaken between July 2000 and August 2001 either to collect unpaid licence fees or to rectify outdated motor vehicle records. This pilot project proved to be successful and consequently a financial inspectorate in the transport division was established to execute this function. A challenge remains, however, and that is the collection of all revenue due to the fiscus, thereby effectively maximising revenue potential.

5.5.1.2 Hospital patient fees

Hospital patient fees are generated in the main from sales of services to external or private patients in a competitive market and therefore cannot be classified as a compulsory fee. The provision of health services for subsidised patients is constitutionally mandated and is provided to patients who may also pay only a portion of the tariff, or alternatively, receive services free of charge. Given the public nature and substantial government funding related to the health sector, one can argue that public health services are not rendered in a true open-market system, which is based on the economic price theory principles of supply and demand, assuming there is no monopolising of services.

A consistent downward trend in revenue from patient fees occurred from 1997/98 up to 1999/2000, which in this Province in particular was even faster than the national average[36]. According to national evidence[37] the main reasons for this decline in hospital revenue were the decrease in the number of paying patients using private sector facilities, the loss of medical aid patients to the private sector and the effect of the national policy of providing free health care for children under the age of six and pregnant mothers and the elimination of user fees at primary health care clinics.

[36] Provincial Government Western Cape: Provincial Treasury – Western Cape Fiscal Policy 2002-2005, Chapter 3 – Page 21
[37] Equity Project: An assessment of revenue retention pilots in the South African Department of Health: June 2001

These policy amendments and an increasing culture of non-payment for services had a negative influence on revenue collection at public hospitals.

As reflected in Table 5.16 below, the Department of Health has managed to reverse the downward trend in hospital fee collections since 2000/01, making good progress in increasing revenue collections. In the main this can be attributed to improved administration in the collection of outstanding accounts, increased tariffs and the collection of overdue accounts by a private debt collector. Revenue collected during 2000/01, compared with 1999/2000, increased by 14,22%, which is substantially higher than the average patient fee increase of 8% during the same period. The implementation of revenue-generating schemes such as private wards at public hospitals, preferred provider agreements[38] with medical schemes, the settling of accounts by government institutions and the appointment of additional personnel have, in addition to the measures implemented during the previous years, contributed to a further growth of 26,18% in revenue collections during 2001/02. Nonetheless, it has been projected that revenue will decrease by 20,44% in 2002/03 to even lower than 1997/98 levels. Compared with 2001/02, the projection at this stage appears to be an underestimation of the revenue budget, or rather overly conservative budgeting.

The MTEF projections, which are all lower than actual collections in 2001/02, appear to be running contrary to the revenue-generation initiatives already implemented during the last couple of years, coupled with the improvement of provincial facilities.

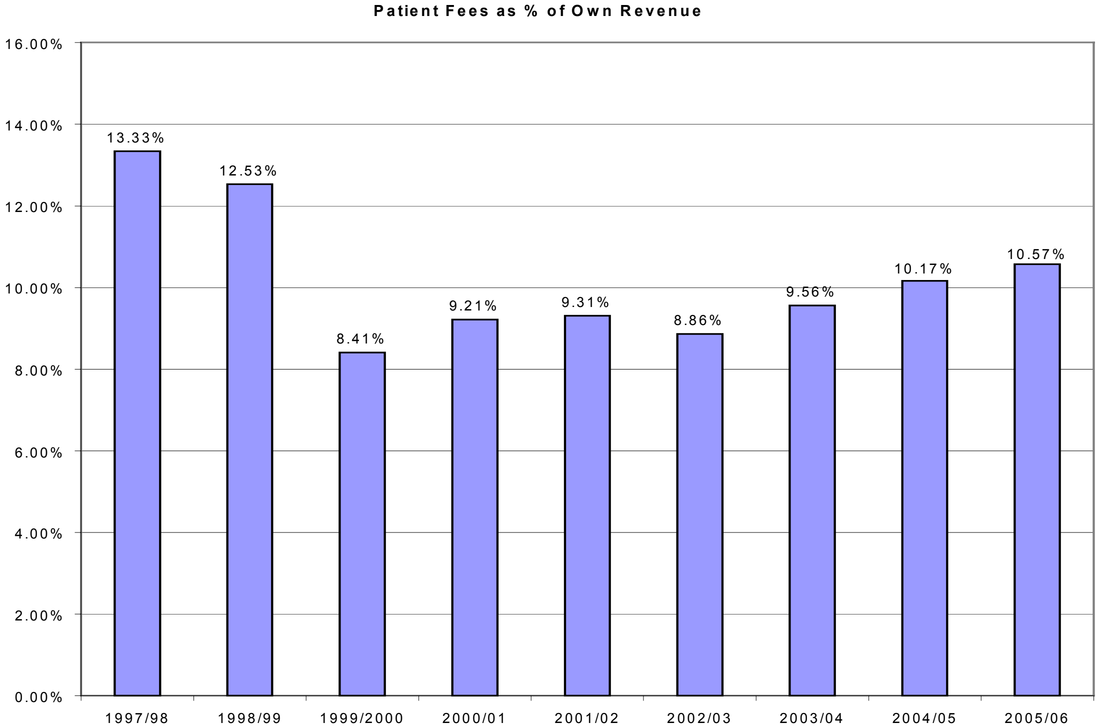
Hospital fees declined between 1997/98 and 1999/2000, both as a share of provincial own revenue and in real terms but appears to be stabilising around 10% of overall own revenue, as depicted in Table 5.16 and Graph 5.3 below.

Table 5.16: Revenue generated from hospital patient fees between 1997/98 and 2001/02 and MTEF projections

Revenue	Actual					Budget	Medium-term estimate		
	1997/98 R'000	1998/99 R'000	1999/00 R'000	2000/01 R'000	2001/02 R'000	2002/03 R'000	2003/04 R'000	2004/05 R'000	2005/06 R'000
Patient fees	75 312	66 098	61 679	70 451	88 895	70 721	79 075	83 413	87 368
% growth		-12,23%	-6,68%	14,22%	26,18%	-20,44%	11,81%	5,49%	4,74%
Share of own revenue	13,33%	12,53%	8,41%	9,21%	9,31%	8,86%	9,56%	10,17%	10,57%

[38] Preferred provider agreement: An agreement between the Province and medical schemes to secure the exclusive use of facilities for the members of the medical scheme involved.

Graph 5.3



To ensure that growth in hospital fees are maintained over the MTEF the Department of Health is busy implementing improved billing systems which will pave the way for the implementation of the Uniform Patient Fees Schedule ("UPFS"), i.e. tariffs based on health care activities, providing for more effective billing based on a professional and facility fee. The intention of the UPFS fees is to reduce the amount of items that appear on bills but to still reflect the value of the services rendered. The Department of Health, in collaboration with its national and provincial counterparts, is part of a process to finalise UPFS fees to be paid by subsidised patients based on their ability to pay.

Implementation of the UPFS fees needs to be supported by adequate information systems, administrative procedures and the training of personnel. Research by the National Treasury[39] established that some of the following generic factors in the provincial health departments may impede the efficiency of revenue collection:

- The focus in some health departments remains on expenditure whilst revenue collection is secondary.
- Capacity remains a problem in health departments, especially in sections responsible for revenue collection.

[39] National Treasury Own revenue project: 2002 Paper by K. Brown - TCF 19 September 2002

- Lack of will and commitment to do the basics right, also perhaps due to a lack of support from senior personnel.

- Hospitals fail to adopt an admission strategy that would speed up the admission process and ensure that patient details are accurate.

- All parties involved in the billing chain fail to capture services rendered and medicines dispensed, onto the health information system.

- The billing system is fraught with inefficiencies such as incomplete itemising of services rendered, inaccurate or incomplete patient details, late rendering of accounts and long time-lags between services rendered to medical aid patients and payments being received.

The hope is expressed that once the UPFS fees and the necessary support and capacity are in place to issue hospital accounts (the engine behind revenue collection and administration), it will be possible to manage hospital fees more effectively and undertake meaningful institutional and interprovincial benchmarking. Given the constraints the public health industry is facing, improved collection and administration of revenue, will be to the benefit of both the public and private sectors.

5.5.1.3 Gambling and Betting

Prior to the promulgation of the Interim Constitution of the Republic of South Africa ("the Interim Constitution") in 1994, tax on betting activities was the sole source of gambling revenue for the Province. At that stage all other forms of gambling were prohibited in terms of the then National Gambling Act.

The introduction of the Interim Constitution, however, significantly broadened the Province's potential tax base by authorising Provincial Legislatures to legislate on casinos, racing gambling and wagering, excluding lotteries. This paved the way for the introduction of the Western Cape Gambling and Racing Law, 1996 (Law 4 of 1996), as amended, ("the Law") which is the regulatory framework that regulates gambling and racing and activities incidental thereto in the Province. The Law, *inter alia*, provides for:

(a) the establishment of the Western Cape Gambling and Racing Board ("the Board");

(b) the introduction of casinos, limited gambling machines and bingo, while at the same time incorporating horse racing and betting under the same regulatory regime;

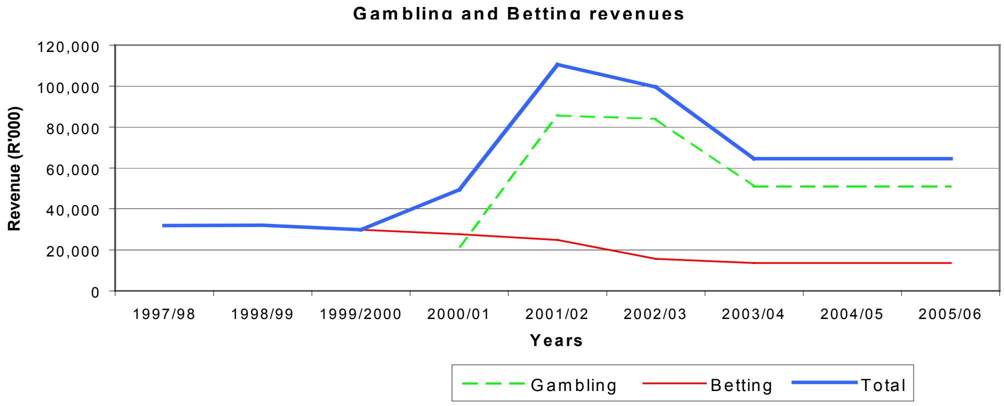
(c) the introduction of various licence types, licence and investigation fees, bid and exclusivity fees and gambling taxes.

The Province's revenue from betting taxes on horseracing amounted to R32,008 million in 1998/99 and has consistently decreased to such an extent that only R13,5 million is projected over the MTEF. This decrease is mainly due to the advent of other legal forms of gambling as well as a proposed amendment to the Law which will inevitably have a negative impact on betting taxes. The introduction of legal casino gambling in October 2000 generated revenue of R21,654 million for the 2000/01 financial year. In 2001/02 gambling taxes of R85,630 million were collected when the three new casinos were in full operation. It is projected that gambling taxes from the three casinos currently in operation will peak and then decrease in 2002/03, but that gambling taxes from the proposed Southern Cape casino will compensate to some extent for the aforementioned decrease, thereby resulting in maintaining the budget figure of R51 million for 2002/03 and over the MTEF. This major decline in gambling revenue is primarily as a result of a budget adjustment compensating for the risk of a possible future claim by the Western Cape casinos relating to the manner in which gambling taxes are currently being calculated, and a simultaneous request for the current rates of taxation to be adjusted to allow for tax indexation or inflation adjustments both resulting into gambling taxes being reduced by approximately R33 million per annum in 2003/04 and over the MTEF. Another reasoning behind the aforesaid expected decrease is mainly due to the novelty or the latent demand for gambling, which is expected to wear off over time. Taking cognisance of the above, gambling tax revenue is expected to settle around R50–odd million per year, in the absence of any adjustments, internal macroeconomic shocks or other changes to net disposable incomes of households. If the above claim by the casino industry is to be unsuccessful and their request not being entertained, gambling tax revenue is expected to settle around R80-odd million per year, *ceteris paribus*. The trends in actual tax revenue collected from gambling and betting from 1997/98 and projections over the MTEF are presented in Table 5.17 and Graph 5.4 below.

Table 5.17: Revenue generated by gambling and betting between 1997/98 and 2001/02 and MTEF projections

Revenue	Actual					Budget	Medium-term estimate		
	1997/98 R'000	1998/99 R'000	1999/00 R'000	2000/01 R'000	2001/02 R'000	2002/03 R'000	2003/04 R'000	2004/05 R'000	2005/06 R'000
Gambling				21 654	85 630	84 000	51 000	51 000	51 000
Betting	31 806	32 008	29 773	27 733	24 795	15 500	13 500	13 500	13 500
Total	31 806	32 008	29 773	49 387	110 425	99 500	64 500	64 500	64 500
% growth		0,64%	-6,98%	65,88%	123,59%	-9,89%	-35,18%	0,00%	0,00%
Share of own revenue	5,63%	6,07%	4,06%	6,46%	11,56%	12,47%	7,79%	7,86%	7,80%

Graph 5.4



The gaming industry is monitored and controlled by the Western Cape Gambling and Racing Board, a provincial public entity,[40] and responsible to the assigned Executive Authority. The Board is funded primarily by the Industry, in the form of exclusivity fees, application fees and investigation fees. Since the Industry is still in the process of being implemented, the Board has, to date, been unable to generate adequate revenue to be self-sufficient and therefore, in the interim, relies on the Provincial Government for bridging financing. However, it is anticipated that this situation should change with the implementation of the limited gambling machine industry, anticipated to be within the next two years.

In addition to generating more than R85 million in gambling taxes in the 2001/02 financial year, the casino industry, including the casino currently under construction in the Southern Cape, will have contributed more than R2 billion in infrastructure expenditure in the Western Cape once the latter casino development has been completed. These developments have focused on the creation or augmentation of tourist infrastructure throughout the Western Cape.

SunWest, the Cape Town metropolitan casino operator, developed a R1,7 billion casino and entertainment world on the dilapidated Goodwood showground site and contributed a further R140 million towards the development of the Cape Town Convention Centre currently under construction, over and above the payment of a bid fee of R135 million. SunWest is also the biggest contributor to gambling revenue and currently generate gambling taxes in the region of R78 million on an annual basis. Both the West Coast and Overberg licences were used to revive existing tourist attractions in the form of the Mykonos Holiday Resort and the Overberger Hotel and Spa. Both these two casinos currently generate gambling tax revenue in the region of R3 million each. It is expected that this trend will be maintained for the MTEF years. The fourth casino development will introduce a new hotel and golf

[40] As defined in the PFMA, 1999 (Chapter 1, Section 1 as listed in Schedule 3 Part C of the said Act)

estate in Mossel Bay. A bid fee to the amount of R6,124 million was received in 2002/03 from this casino, which is expected to open its doors during December 2002. It is expected that the casino in Mossel Bay will generate gambling tax revenue similar to that generated by the Caledon and West Coast casino of approximately R3 million annually, not taking into account the risks and requests mentioned earlier.

However, the introduction of these new forms of gambling has dealt the already struggling horse racing industry another telling blow. A significant portion of the gambling rand previously wagered on horse racing has now been channelled towards casinos, the lottery and even cellular telephones. The reduced turnover (on average approximately 10% per annum for the past three years) could result in significant job losses in the Industry, the economic effect of which could far exceed the tax benefits to the provincial fiscus derived from it. This will inevitably necessitate a reduction in the tax rate applicable to the totalisator in order to augment the cash flow of the racing club. The Provincial Legislature has recently approved an amendment to the Law which reduces totalisator taxes from 10% to 6%, bookmakers taxes from 6% to 3%, and created a betting levy of 3% which will be channelled to the holder of the totalisator operator licence. The result is that horseracing taxes (totalisator and bookmakers) will not decrease with approximately R11,6 million to approximately R13,5 million per annum. The reduction has already been provided for in the MTEF. During the 2001/02 financial year the 25 licensed bookmakers generated R16 million in betting taxes while the 44 totalisator outlets added another R9 million to the provincial fiscus

As indicated above, it is not foreseen that the limited gambling machine industry will be introduced within the next financial year and therefore no revenue emanating from this source has been budgeted for.

5.5.1.4 Other revenue

The residual category of revenue, namely other revenue, represented 11,45% of provincial own revenue in 2001/02, of which R184,826 million (62,82% of total “other revenue”) R35,104 million or 23,45% more than in 2000/01, consisted of interest from committed funds not spent as yet, but more specifically from improved cash and investment management policies in the Province. Interest income, as indicated in Table 6.18 below was relatively high in 1997/98 but will decline forward as a result of the draw-down of surpluses for infrastructure projects and settle at around R23 million to provide liquidity within the system.

Table 5.18: Interest revenue between 1997/98 and 2001/02 and MTEF projections

Revenue	Actual					Budget	Medium-term estimate		
	1997/98 R'000	1998/99 R'000	1999/00 R'000	2000/01 R'000	2001/02 R'000	2002/03 R'000	2003/04 R'000	2004/05 R'000	2005/06 R'000
Interest	96,339	63,815	86,962	149,722	184,826	69,776	35,892	22,966	22,966
% growth		-33.76%	36.27%	72.17%	23.45%	-62.25%	-48.56%	-36.01%	0.00%
Share of own revenue	17.06%	12.09%	11.86%	19.58%	19.35%	8.74%	4.34%	2.80%	2.78%

To date, interest on bank balances and investments has become an important source of capital accumulation in the Province. Concerns about increased so-called interest revenues were sighted by national Treasury[41] and the following generic reasons applicable to all provinces were identified as some of the main contributors:

- Slow spending in capital projects as provinces are only starting to build institutional capacity to spend on these projects and decrease the lead time to implement these projects;
- Continuous slow spending in respect of some conditional grants and the tendency of national departments not to delay or withhold funds in cases where the rate of spending tends to be slow;
- Late payment of creditors as some provinces take longer than 30 days to settle their outstanding debts;
- Increased growth in departmental allocations that has resulted in increases in the payment schedule amounts, without surpluses of the previous year and positive balances of provinces at the start of the new financial year being taken into account;
- The mismatch between the financial needs of provinces versus the actual national transfers effected;
- The cash flow needs of departments have not been thoroughly assessed and aligned to the payment schedule.

However, although there is a positive mismatch between revenue received and actual expenditure, and quite correctly so, the accumulation in the Western Cape is the result of purposeful investment strategy allowing over R600 million to be directed to major tourism and economic infrastructure spending from 2002/03 to 2003/04. Further augmentation is under consideration provided the necessary synergy can be

[41] National Treasury Own revenue project: 2002 Paper by K. Brown - TCF 19 September 2002

established with other economic stimulatory initiatives in line with our intention to grow and develop the (Western) Cape as "Ikapa elihlumayo".

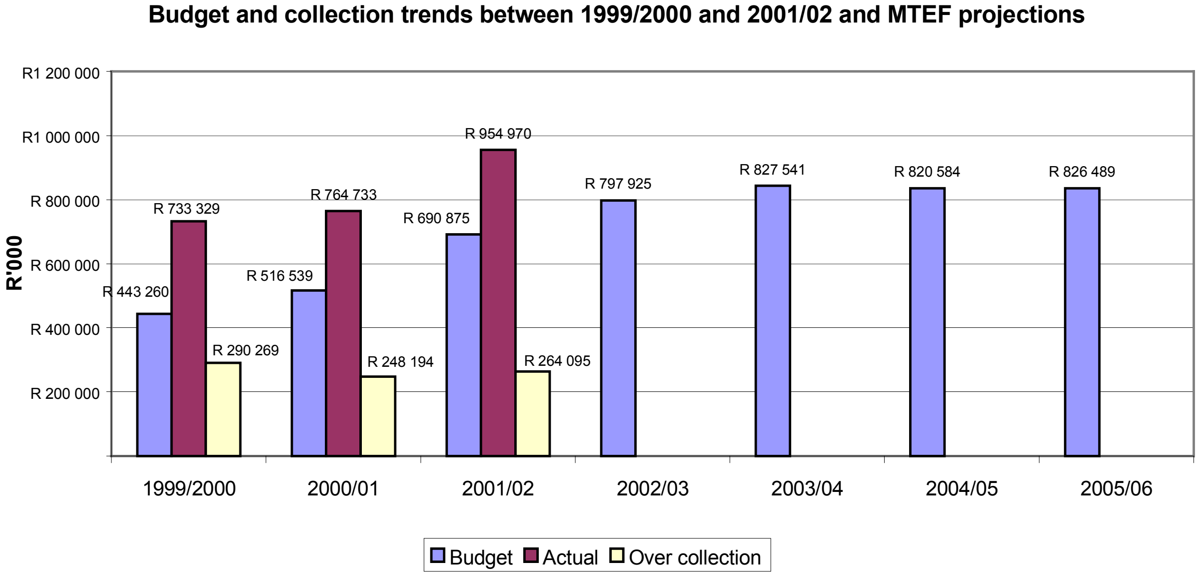
The remainder in "other revenue" is represented by revenue received from sources such as profits on trade accounts, board and lodging, contributions by universities, administration fees paid on insurance premiums and tuition and examination fees. The fee structures of user charges, which are revised annually by accounting officers of departments in terms of the national Treasury Regulations, are based on the cost-recovery principle. User charges are regarded as an efficient way whereby costs are recovered of publicly provided goods and services and whereby incentives are provided for improving the quality of service delivery. A further advantage of the regular revision of user charges is that it 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 the so-called "miscellaneous" revenue, which is very small in nature, and accordingly does not receive the necessary attention in this document. However, the sum of these revenues can be significant, although they rise and fall in no discernible pattern, implying that they are mainly once-off receipts. The unpredictable nature of these revenues, albeit relatively small in quantum, makes projections very difficult.

The national Treasury[42], in an analysis of provincial own revenue budgets, established that the understatement of budgets across provinces appears to be a major problem. This also occurred in the Western Cape province as illustrated in Graph 5.5 below:

[42] National Treasury Own revenue project: 2002 Paper by K. Brown - TCF 19 September 2001

Graph 5.5



Although gradually declining from 65,1% of the own revenue budget for 1999/2000 to 38,2% in 2001/02, the overcollection has a negative effect on the credibility of own revenue budgets, resulting in an understatement of funding available for service delivery. A major cause, apart from the reasons furnished earlier, appears to be the own revenue incentive scheme introduced a number of years ago. It is therefore imperative that the own revenue budget should be estimated as accurately as possible to secure the credibility of the budget and present the full extent of funding available from own revenue sources. It is, however, acknowledged that the collection of some revenue from some sources is unpredictable by nature since these sources are not rendered in an open-market system, which makes projections difficult and complicates the budget management process. Some degree of risk is therefore acknowledged and should be built into the budgeting system, but needs to be identified, calculated and managed during the budget estimation and implementation processes.

5.5.2 Revenue generation incentives

In order to implement revenue-generating strategies successfully, it is vital that departments should be given sufficient incentives to do so. One of the incentives can be to allow departments to retain or access their revenue collected above revenue targets.

In this regard, a revenue retention policy was approved by Cabinet during 1998 and reaffirmed during 2000. In terms of this policy, all departments are allowed to retain 50% of additional revenue collected above budget estimates except the former Department of Economic Affairs, Agriculture and Tourism, which may retain 100%.

The aim of the revenue retention policy was to return to departments additional revenue, or part thereof, collected in excess of budget estimates resulting from the improvement of own revenue management. In the provincial Treasury's analysis this caused a perverse incentive and accentuated underbudgeting of revenue. This contributed to the lack of credibility of budget estimates and was furthermore not in the spirit of the revenue retention policy. At the time of laying down this policy it was noted that the determination of credible budget estimates proved to be very difficult. A lack of management focus on revenue issues also resulted in a lack of management information, which caused departments to understate their budget estimates. However, it is now time to move on to better fiscal management of revenues.

One cannot deny that it is imperative to incentify departments so that they will make a concerted effort to improve revenue collection management. As an incentive, and to prevent underbudgeting, unnecessary delays in spending (with concomitant cost inflation) and cash accumulation, departments have been exhorted to make accurately revenue forecasts which will then be used to augment their base-line allocations over the new MTEF. This change in stance should foster more appropriate revenue budgeting and collection and facilitate quicker and more efficient spending. Allowing departments to rather increase their expenditure budgets on the baselines, i.e. equal to the difference in original MTEF projections and credible new revised estimates, provides greater certainty in the overall revenue envelope for spending. There is some risk, and this encouraged, in rather so for slightly more optimistic revenue forecasts that own revenue forecasts will not be achieved. If this does come about, the expenditure budget will be decreased by the same amount at no real loss to the department. It is thus clear that revenue from once-off receipts, and preferably non-manageable items, should be removed from the increased allocations in expenditure. Risks associated with revenue collection should therefore be calculated to ensure stable revenue flows.

5.5.3 Exclusions from the Provincial Revenue Fund

In terms of section 22 of the PFMA, all money received by a provincial government must be paid into the Provincial Revenue Fund ("PRF") except money received by the provincial legislature, public entities, donor funding payable to the Reconstruction and Development Program Fund, trading entities and trusts operated by a provincial department, exemptions in terms of the Division of Revenue Act and school fees, which are covered in terms of the SA Schools Act[43].

In the Province the main sources of revenue excluded from the Provincial Revenue Fund are revenue received by the provincial legislature, public entities and school fees. The main exclusion is school fees to be collected by public schools, which is estimated to amount to R462,735 million in 2002/03, increasing to R488,185 million in 2003/04 and R515,036 million in 2004/05. This represents a substantial amount of funding managed by school governing bodies in terms of the SA Schools Act, and in terms of its distribution raises the question of equity between well-off and less well-off schools in the Province. Accountability for these funds resides with the head of the institution or schoolmaster, whereas school boards, in particular the chairperson, is responsible for outcomes delivered by the school or institution.

Provincial public entities[44] are responsible for collecting an estimated R92,997 million in 2002/03, which is projected to increase to R98,721 million in 2003/04 and R102,795 million in 2004/05. The public entities were established to function autonomously and provide more efficient services outside the perceived constraints of the government environment whilst remaining under the auspices of political and some administrative control of the provincial government. Whether this is true for all public entities is questionable, however.

Revenue received by the provincial parliament is excluded from the Provincial Revenue Fund in terms of section 22(1) of the PFMA and therefore deposited into a separate bank account. Revenue collected in 2000/01 and 2001/02 was R222,000 and R164,000 respectively. It was proposed[45] that the annual budgets of the provincial parliament's expenditure requirements should be submitted to the Treasury after revenue projections have been taken into consideration (only nett expenditure to be funded).

5.5.4 New provincial taxes

Prior to finalisation of the Provincial Tax Regulation Process Bill, the invitation of comments, suggestions and other inputs into the process resulted in its being amended, taking cognisance of the inputs made by some provinces. In keeping with the principle of cooperative governance, the Western Cape province was one of

[43] South African Schools Act, 1996 (Act 84 of 1996)
[44] As defined in the PFMA, 1999 (Chapter 1, Section 1 as listed in Schedule 3 Part C of the said Act)
[45] TCF Memorandum dated 9 May 2002: N du Plessis (National Treasury)

those provinces to submit valid arguments that led to some meaningful amendments being effected. The amended version of the Bill was eventually supported by the National Council of Provinces and the National Parliament, thereby culminating in the State President assenting to the Provincial Tax Regulation Process Act ("PTRPA") [46]' on 4 December 2001, with an effective date of 1 June 2002 for implementation.

The declining trend of province sourced revenue, as was projected in the Medium Term Expenditure Framework ("MTEF"), has focused provincial Treasury efforts primarily to improve provincial tax and revenue administration and at the same time to systematically explore the possibilities of supplementing provincial discretionary funds.

In respect of the primary focal effort, the Treasury, in collaboration with the Department of Economic Development and Tourism, has investigated the processes and procedures relating to the current system of administration in respect of liquor licence fee collections in the Western Cape province. It is anticipated that the proposed refinements to this system will pave the way for effective and efficient future administration of taxes in the Province. The degree of success of this intervention may only be quantified after the proposed amendments have been accepted and implemented.

Although it is a statistic not worthy of praise, the Western Cape province has at April 2001 a backlog, increasing at an accelerating pace, of approximately R1,2 billion[47] in its road maintenance programme, which in the main is attributable to the general paucity of national revenue transfers. The diminishing trend in provincial discretionary funds over the medium-term framework will exacerbate this unenviable situation, which in effect has a snowball effect on the backlog of funds required for this programme due to constant road maintenance requirements.

The required sustained increase in funds to keep pace will consequently escalate the road maintenance needs to such an extent that it will be impossible to manage without substantial alternative funding resources. To circumvent this situation, the Western Cape province has embarked on avenues which will potentially augment its discretionary funds to facilitate the conservation of its road infrastructure. It must be accepted that this asset is undoubtedly the economic backbone of the province. It is the backbone in various ways, e.g. its role in supporting the promotion of provincial tourism, providing a road network conducive to cross-border transport operations allowing access to economic opportunities, and relieving the serious traffic congestion problems for local residents, all of which have far-reaching economic implications. In this regard, the Minister of Finance and Economic Development in the Western Cape indicated in his main Budget Speech in 2002 that a particular avenue of current focus identified by the Treasury will be the exploration of the

[46] Provincial Tax Regulation Process Act 2001 (Act 53 of 2001)
[47] Provincial Government Western Cape: Provincial Treasury – Western Cape Fiscal Policy 2002-2005, Chapter 4 – Page 55

viability of introducing a provincial fuel levy in the MTEF for the proactive augmentation of funding for road maintenance programmes and backlogs. The business sector has generally come out in support of this initiative. The initiation of this endeavour has lead the Treasury to engage in discussions with and invite proposals from economists and tax experts with a view to procuring the services of a team of research consultants and economic advisors to undertake research and investigations in concert with the Treasury. The level at which such a particular tax form of the tax base, relief measures, interprovincial implications and other requirements of the PTRPA will similarly be researched and investigated by the applicable expert analysts and the Treasury in addition to appropriate consultation prior to any recommendation to the provincial Cabinet and the national Minister of Finance. This exercise will enhance the Province's required fiscal capacity and expertise and also promote provincial fiscal accountability.

Whilst it is envisaged that such a tax may only be implemented during the 2004/05 financial year, timely interventions are essential for all the necessary steps to be followed that will culminate in the required submissions being framed for consideration.

5.6 Conclusion

Transfers from the national budget will continue to dominate provincial budgets, at least over the MTEF period, owing to intergovernmental fiscal system which is based on a revenue-sharing model complemented by limited taxation and borrowing powers to Provincial Government. Based on the trends and observations elaborated on in this chapter, a number of fiscal challenges face the Western Cape province in respect of the fiscal envelope, the fiscal foundation of provincial service delivery. For ease of reference these challenges are summarised below.

5.6.1 Western Cape Expenditure Budget Allocations

A perceived "mismatch" in expenditure allocation (see page16-20) in the sense that serious introspection may be required in order to find a balance in allocations between the social and economic sectors in order to support the broad principals of economic growth and development in the province, the concept which is underpinned by our proposed Budget 2003 theme of "Ikapa Elihlumayo".

A question which still remains unanswered, and indeed a challenge, is determining the value for money spending (cost effective service delivery through targeted spending by departments) which the Province achieves in making increased (might be substantive) allocations or adjustments in allocations to departments.

5.6.2 Vertical division of revenue

The Constitution entrenches “co-operative governance”, obliging the three spheres of government to cooperate and to negotiate political and budgeting issues between them. It is high time for serious introspection and objective analysis of the vertical division decision-making process as it needs to be reviewed so as to reflect from the outset a greater, more forceful and better articulated prior provincial presence in policy-making to counter the current *ex post facto* consultation of provinces in the budget process.

Vertical division must coincide with other national policy spending decisions that are implemented at provincial and even local government level.

Vertical division must shield provincial and local governments from nationally driven policy decision shocks, e.g. social security spending vs allocations. Clear distinctions between trade-offs are needed to absorb any implications of such new initiatives.

Vertical division needs urgent adjustment to create some room in the equitable share formula to:

- Address current vertical imbalances of allocations between the three spheres;
- Counter the current mode of forced reprioritisation at provincial government level;
- Stop the current crowding out of other equally important services at provincial level;
- Not simply adjust the pressure points within the equitable share, as is currently the practice, resulting in a zero sum game – “mraba raba”

5.6.3 Horizontal division of revenue (equitable share formula)

Adjustments within the equitable share formula are deemed secondary, whilst adjustments to the vertical division are a primary concern for some of the reasons mentioned earlier. If the vertical imbalances of allocations between the three spheres are adequately accommodated, then adjustments to the equitable share should be accommodated as follows:

- Equitable share formula should fully recognise the cost drivers at provincial level, e.g.:

  - the health component in the equitable share formula does not address the relative cost of delivery or demand issues, being based simply on a weighted average of number of persons with and without medical aid (impact of HN);
  - the welfare component does not, through it means testing mechanism, fully capture this Province’s responsibility for social security grants as data appears to be outdated. This information is drawn from 1995 Income and Expenditure

surveys, which have not been updated. The impact on the demand for social welfare services needs to be accommodated;
- Migration factors should be accommodated the formula (the education component already accommodates migration to some extent, but not the other components, especially the health and welfare components); and
- Sufficient incentives for accelerated economic development should be provided for the "wealthier" provinces, and should not be penalised in favour of the social services sectors as currently the practice.

5.6.4 Conditional grants

National Treasury should be engaged in dialogue to:

- reduce the many small grants in the system, which increase the fragmentation of the funding and place unnecessary additional administrative burdens on the Province;
- convince them that the need for conditional grants has diminished, emphasising that conditional grants should be incorporated into the normal equitable share allocation process, at least after the MTEF, with at least an equal adjustment to the equitable share per province, and
- debate that a shift is needed in line with the agent-for-change concept, in that conditional grants in respect of its monitoring should focus on outcomes rather than inputs.

5.6.5 Provincial borrowing

- There is a need in this Province to develop the required capacity to effectively manage and accept full liability for provincial borrowing, i.e. sourcing the required skills to access additional sources of funding through the various borrowing instruments available on the capital market.

- Before provincial borrowing is considered, the existing own revenue base has to be improved in terms of both estimation and collection before venturing into more complex methods of financing like borrowing.

5.6.6 Own revenue

In terms of the PFMA, it is incumbent upon the provincial treasury to promote and enforce transparent and effective management of revenue. In essence this review of provincial own revenue illustrates that the collection of own revenue, given the imperative to use it as marginal funding, requires a concerted effort to shift the current management focus towards revenue management. This year, the Treasury and the Departments in concert will, *inter alia*, pursue the following challenges to increase the efficacy of own revenue:

- Stability in revenue collection through improved forecasting and the tabling of sustainable credible revenue estimates;

- Improved administrative efficiency, which includes improving human resource capacity and supportive infrastructure;
- Enhanced information technology systems, specifically in the Departments of Health and Transport and Public Works;
- Reduction of the differences, interdepartmental and between provinces, in user fee charges and tax variances through sectoral interdepartmental and interprovincial cooperation;
- Development and implementation of a clear revenue generation incentive policy in cooperation with departments, which will provide for departments' base-line allocations to be augmented by amounts that are equal to the difference between original MTEF projections and credible new revised estimates, taking into account any associated risks;
- Maximisation of provincial own revenue through the implementation of new provincial taxes, with specific focus on introducing a provincial fuel levy over the MTEF earmarked specifically for road infrastructure spending.

6

CONCLUSIONS AND KEY PRIORITY AREAS

Conclusions

Introduction

This section consolidates the main points from all other chapters, including those from the Expenditure Review 2002. These inherently propose a number of departure points that will begin to give more substantive shape to the provincial government's objectives and thus provide a reference for informing the relative allocations to the different votes from 1 April 2003 onward over the new MTEF.

These proposals build on the 2002-2005 Fiscal Policy, the Provincial and National Governments' Policy Frameworks. Fiscal policy in simple terms has to be backed by a solid grasp of economic realities and circumstances, and then using the budget as a tool, try not only to ameliorate adverse socio-economic conditions but over time to contribute systematically to wealth creation over the entire spectrum, substantively narrowing the income gap between the upper and lower income deciles of the population.

Economic analytic framework

The Province operates in an economic environment that is not only exceedingly complex, but also subject to a host of external factors, both domestic and international. The challenges are patently immense, albeit imperfectly understood owing to the rather limited analysis of regional economic forces and the dynamic relationship between these variables. Changes in fiscal policy are also very difficult to implement because of the limited resources and fiscal tools at the Province's disposal.

As a strategy, to overcome gaps in the Province's delivery efficacy, the following steps have been initiated by the provincial Treasury, due be to increasingly evolved together with key departments and other role players over the next four to five years:
Firstly, determine and evaluate both the regional macroeconomic framework and socio-economic needs that exist in the Province; simultaneously develop key service delivery outcome indicators for the provincial departments; then determine the gap between service delivery performance versus the macro- and socio-economic imperatives that the Province can impact on. From this determine and propose spending priorities for the provincial government, and so the cycle continues with intended increasing sophistication and greater efficacy.

Secondly, enhance synergy with all role players within the Province and other spheres of government to facilitate both good and integrated governance.
Thirdly, it must be accepted that the available database to analyse and make meaningful recommendations on the socio-economic and macroeconomic variables has to be improved as matter of urgency. This will place the provincial government in a more informed position to make better decisions and ensure better allocative efficiency.
Fourthly, notwithstanding its limited capacity to bring about change, the Province must accept the challenge to stimulate economic growth and reduce poverty and inequalities in the medium to longer term. This should be driven forward within a realistic framework that is affordable and attainable over time.
Fifthly, it must also be accepted that in achieving success, tough decisions might have to be taken now if a better future for the Province and its population is envisaged in the longer run.

Expenditure review

Expenditure quality and quantity

So far the elusive goal to be attained, is that of allocative efficiency. This can be defined as the capacity to distribute resources on the basis of the effectiveness of public programmes in meeting government's strategic objectives[1]. This definition allows the Treasury to determine its role with regard to the allocation or distribution of provincial resources between departments and poses a real challenge to the Treasury to adequately develop its capacity so as to give effect to this definition.

Presently, the focus of fiscal policy analysis is primarily on financial information, but a beginning has been made with non-financial or delivery assessment for some of the votes (Community Safety, Education, Health, Transport and Public Works, Agriculture and Economic Development and Tourism).

Another challenge facing the Province is to deepen the knowledge base without necessarily increasing the number of personnel. The improved ratio of personnel expenditure *vis-à-vis* other arising from the major restructurings post-1997/1998 and the social sector *vis-à-vis* other are under pressure because of the 9 % ICS increases and the steeply rising expenditure of social security.

Although there has been a physical infrastructure spending recovery, the current level, for all intents and purposes, is still inadequate either to address the backlogs that have accumulated, or to counter the depreciation or deterioration rate. The Province will have to work closely with the local sphere and give their full cooperation with regard to the municipal-based integrated development planning (IDP) process to maximise efficiency in both fixed capital and other spending.

Clusters (e.g. Social and Economic) were recently formed to ensure efficiency gains and synergy with national clusters and policies. Likewise the greater synergy necessitated by

1 Cf. Schick, A. *A Contemporary Approach to Public Expenditure Management*, World Bank Institute 1999, p89f.

the IDP process, should over time contribute to greater efficacies. In general, while acknowledging that there could be constraints limiting effective coordination between and even within departments, it could be argued that there is a greater need than ever before for interactivity between provincial departments to ensure efficiency gains.

There is also a lack of proper performance indicators (benchmarks) to measure performance against spending i.e. non-financial indicators. Infrastructure needs should be aligned with and integrated into strategic plans and budgets of department(s), based on technical, economic, socio-economic and demographic factors. Further work in this regard is thus essential for the measurement of progress over time.

In closing, before moving to short assessments of the various votes, departments should not enter into national policy agreements that could impact on the provincial budget until the financial implications have been spelt out and the funding arrangements secured. The tendency of wanting to comply has led to severe strains on provincial fiscal arrangements, with negative implications for provincial governance. Any new policy contemplated has to be properly costed first and adequately debated between the national and provincial line functions, together with the national and provincial treasuries. This must then lead to a joint decision on relative priorities and eventual funding arrangements before any agreement on implementation can be reached.

Premier, Director-General and Corporate Services

The growth from 2001/02 to 2002/03 is mainly due to the growth of IT capital projects. The intended decentralisation of Internal Audit (function and committees, excluding Forensic Audit) requires financial resource investment to yield a multiplier return in efficiency gains through the application of the full spectrum of work attached to the internal audit function.

Taking the nature of IT services into account, they will continue to be subjected to external inflation and foreign exchange rate fluctuations. The challenge is to yield significant efficiency gains on the investment in IT services through innovative procurement practices, prudent contract management and the optimal use of systems.

The envisaged internal restructuring and the apparent adequate level of financial resources available to the Department will require the appropriate allocative mix between programmes for the optimal utilisation of the resources and the attainment of efficacy in spending. In summary it appears as if the Department has reached maturity regarding the allocation of resources over the MTEF period.

Provincial Parliament

The provincial parliament's allocations grow at a moderate rate, continuously contributing to its constitutionally mandated proficiency. It has demonstrated that it has the capacity to spend the resources allocated. The provincial parliament as the legislative authority in the Province requires to be adequately funded to enhance the effectiveness of its legislative and oversight processes. Indications are that the staff establishment, improvement of conditions of service of staff, public participation, communication, catering services and employees contributions related to members benefits will require strengthening over the medium term.

Finance (provincial Treasury)

Over the medium term the allocations remain fairly constant in nominal terms, but decline in real terms. Although the Department intends to restructure within its current resource envelope to promote and enforce the attainment of transparent and effective financial governance, it is questioned whether the current funding level will match the envisaged roll of a provincial Treasury.

Community safety

Given the growth in budget allocations from a very low base in 1997/98 to a significant spending level in 2002/03, the department has most likely reached a degree of consolidation and stability. The Phillipi College poses a financial management problem of underutilisation and a resultant higher unit cost per student plus underspending with consequences of non-optimal utilisation of allocated funds. The merging of the Gene Louw and Phillipi Colleges may be a viable option. However, further work must be done on the sustainability and management of Municipal Policing Services. A further risk related to the past endeavours of community patrol officers has to be accurately costed.

Given the evolvement of the efficacy of traffic law enforcement, the department may experience some budget pressures, but because of the significant real increases in budget allocations over the medium term it should be able to accommodate these pressures through internal reprioritisation/choices to achieve the optimal utilisation of their available funds. Notwithstanding the aforementioned, the evolvement of effective traffic law enforcement may put pressure on the infrastructure budget. Work needs to be done in this regard through the five year departmental accommodation plans launched by the Department of Transport and Public Works. Related to this and in order to relieve the financial investment in maintaining roads, the efficacy of weighbridges must be strengthened substantially and its policing capability secured.

With reference to Chapter 2, the question can be raised whether the departmental programmes are appropriately structured to act more efficiently as a positive change agent on issues causal to crime.

Education

The department received fewer funds in real terms in 2002/03 than they had spent in 2001/02. Furthermore, the allocations drop slightly in real terms over the medium term. Personnel expenditure constitutes about 87% of total expenditure (2001/02). Thus, calculated risks related to the management of personnel expenditure need to be carefully monitored to prevent budget overruns, as manoeuvrability within non-personnel expenditure is limited.

Given the important role that education plays in a developing country, the department's allocation over the medium term should ideally be augmented to at least remain constant in real terms on condition that clear benchmarks/indicators, against which they can be measured over time, are provided on how the quality of education will be improved. To the extent that this proves possible, an appropriate proportion of the increase in the vertical split should find its way to provincial education budgets.

The challenge to the department is to attain efficiency gains in the education system. A further major challenge is to improve the "pass-through rate of pupils", particularly in secondary schools and the quality of education as a whole over time.

Health

Public health funding has increased since 1998 but is projected to grow negatively over the MTEF in real terms. Among others, the high salary bill necessitated rapid restructuring in the hospital sector. The result was a reduction in health workers and hospital beds since 1997/98. Despite evidence of improved quality of primary health care services, many problems and inequities remain. Early budget estimates show that the overall allocation to primary care (district hospital services) is set to decline in real terms over the next three years. Further investigation and monitoring is needed to ensure that funds are aligned with policy priorities.

The HIV/Aids epidemic means that real growth in health budgets may not be adequate to deal with the increase in demand for services and the impact of the disease on resources in the health sector.

Reconfiguration of public health services is needed, taking into account that, for the sake of achieving provincial equity, the Tertiary Hospital and Training and Development grants for the Western Cape have been cut by the national government, by approximately R230 million over five years (2002/03 – 2006/07) in 2001 rand terms. With regard to the National Tertiary Service Grant, further work needs to be done by the national and provincial Health Departments to reach agreement on the particular services to be rendered and costs related to such services.

To enhance hospital efficiency and quality, issues in the sector include finalising the Integrated National Planning Framework, revenue retention, governance reform, management decentralisation in hospitals and an appropriate staff mix, human resource development and training strategies. The replacement of outdated equipment needs to be stepped up to facilitate cost-effectiveness within the health system.

Strategies to deal with the declining health budget which are in line with national policies with regard to reorganising support services and shifting the focus from higher to lower levels of health care are, *inter alia*:

- Increased efficiency in the hospital services (through improved referral systems, day surgery and the strenghthening of capacity at secondary and primary levels of care).
- Consolidated tertiary and highly specialised services, the development of an essential core package of tertiary services and ensuring optimum use of scarce resources.

- Greater efficiency and cost-effectiveness with regard to non-clinical support services.

Given the Department's exposure to patient growth and inflationary pressures combined with exchange rate fluctuations, stark choices need to be made if the health budget is to remain constant in real terms and to absorb the aforementioned pressures. Alternatively the services need to be run down.

Social Services and Poverty Alleviation

Present growth rates in Child Support Grant and Disability Grant beneficiary numbers will pose a crowding-out problem to other welfare services, as it has already done to the social services sector as a whole, particularly Education and, to a lesser extent, Health.

Extending the validation processes to make doubly sure that only those who legitimately qualify receive the grants can only partially contain growth in beneficiary numbers. Greater impact will only be possible by better management of external factors such as national policy shifts and the introduction of a gatekeeper function for better assessment of the appropriateness of disability grants. In addition, only an adequate shift in the vertical split of revenue collected nationally in favour of the Province and provinces generally would allow both efficient take-up rates in social security grants and appropriate investment in economic and other social infrastructure. This would make possible the further rollout of developmental social service delivery, contributing to the department's vision of a self-reliant society.

The national department responsible for the management of the SOCPEN (security grant) system also needs to be encouraged to improve the efficiency of the system.

The department is in the process of instituting various cost-saving initiatives and is continually improving on the accuracy of future social security cost projections. Although final amounts must still be determined, the impact of savings and other efficiencies to be realised will perhaps be relatively marginal given the overall scope of the cost problem. Taken as a whole, the likelihood of a significant shift of provincial revenues to social security will prove inevitable.

Housing

This is the first of the refocused departments in terms of the departmentalisation model that came into effect on 1 August 2002. The challenge is to find a solution to augment the national Housing Subsidy grant to address the housing backlogs and to develop alternative delivery and perhaps more efficient programmes for a better response to urgent housing requirements. In this vein, a great challenge for Province, in liaison with municipalities, is to deliver housing in an integrated manner, i.e. inclusive of services such as Health, Education, Municipal Policing and Transport and to ensure that municipal integrated development plans reflect such services properly. Further work needs to be done on the burdens (financial) that delivered housing places on ownership, society and government and how to address these.

Environmental Affairs and Development Planning

This is also a reshaped department in terms of the departmentalisation model that came into effect on 1 August 2002, requiring restructuring and a phase of consolidation. The Western Cape Nature Conservation Board (WCNCB) is the biggest cost driver, but the financial assistance from the Department is decreasing in real terms. Although the overall Vote received higher than inflation adjustments up to 2002/03, the same sort of increase is not reflected in the allocations to the WCNCB. Unless the latter's revenue streams show a consistent upturn, funding of the public entity should at least be kept constant in real terms.

The department is faced with a number of liabilities in the form of compensation claims/legal fees, mainly in the development planning and nature conversation environment. National legislation in the making could have a negative impact on the department's budget. However, national policy imposing pressure on the provincial budget must be financed through a shift in the vertical split of revenue collected nationally in favour of the Province.

Transport and Public Works

In order for this department to make real inroads into infrastructure backlogs, both in terms of maintenance and new demands, its budget allocation will need to increase substantially in real terms. However, such increases as might be possible have to be targeted in a manner that would stimulate economic activity in the Province, with concomitant increases in job opportunities and beneficial results for poverty reduction over the medium to long term.

This would require future resource allocation to road infrastructure to be underpinned by a technical, economic and socio-economic analysis of the road network or extension thereof in order to direct funds appropriately. The roads allocation should be utilised to encompass and integrate economic development and tourism so as to regenerate/stimulate economic growth, create sustainable employment opportunities and address black economic empowerment and economic inequalities.

With regard to Public Works, it is imperative that consolidated departmental five year integrated accommodation plans should be compiled as a matter of urgency in order to determine realistic expenditure levels – demographic factors and spatial distribution in the Province and in particular the Cape Metropole need to be taken in account in this endeavour. The provincial accommodation plan should ultimately ensure efficiency gains for the Province in terms of utilising resources optimally.

Agriculture

This is another "new" department in terms of the departmentalisation model that came into effect on 1 August 2002, requiring some restructuring and subsequent consolidation. Personnel expenditure constitutes about 56% of total expenditure for 2002/03 and 58% for 2001/02. Calculated risks related to the management of personnel expenditure need to be clearly substantiated to prevent budget overruns, as manoeuvrability with non-personnel expenditure is limited.

The department enjoyed substantial real growth in expenditure up to 2001/2002 and this trend continues in the budget provisions over the medium term. Notwithstanding these positive funding trends, there is substantial pressure on the department to fulfil its commitments in relation to supporting the Land Redistribution for Agriculture Programme. The pressures relate to small farmer settlement, water engineering services, technology transfer and training.

Further pressures relate to keeping the Western Cape agricultural sector competitive in the global environment through adequate delivery of veterinary services that conform to global standards, research and information and technology transfer and the development of farm workers.

Further work on proper output-related benchmarks, such as, increase in jobs created, farmers settled and students trained, is necessary in order to measure progress with resource use over time.

Local Government

This is another department in terms of the departmentalisation model, but with an emphasis on purely local government issues as from 1 August 2002. Consequently it is also subject to restructuring and consolidation.

The process of approving business plans required in terms of national conditional grants needs to be streamlined to prevent underspending. Although the Department underspent in the past, the important role it fulfils in supporting municipalities needs to be acknowledged and promoted. The implementation of the envisaged Municipal Finance Management Act, once enacted, will have an effect on the resources of the department, and also on the provincial Treasury. However, the full effect will only be known over the next couple of months as and when the Act evolves into practical implementation.

Economic Development and Tourism

In terms of the departmentalisation model this has been a “new” department from 1 August 2002 and is subject to appropriate restructuring and consolidation.

Investment in tourism should be an obvious key consideration for resource allocation as it can make a substantial difference in the lives of the poor. However, the targeting of such an investment requires further interaction between the department and the Treasury. In addition, the latter needs to gain a deeper understanding of the department’s endeavours associated with industry development and economic development co-ordination issues.

Although a number of key initiatives have been launched by the department, further work is necessary to reflect potential areas of economic development, proper output-related and measurable benchmarks such as skills gap, employment opportunities, contribution to GGP, growth rates, export potential, synergies, black economic empowerment and business opportunities for small, medium and micro enterprises. It goes without saying that initiatives launched by this department have to be synchronised with those of Transport and Public Works and Agriculture to achieve complementary and optimal gains.

Cultural Affairs and Sport

This is the last of the departments to emanate from the departmentalisation model that came into effect on 1 August 2002, and is also subject to restructuring and consolidation to achieve efficiency gains.

Over time the department has made a strong case for tourism-oriented further investment in culture and sport (contributing to both economic and social investment), which should be a key consideration for resource allocation. Similarly, the demand for literary material is insatiable. Apart from the limited provision for such material, the funding is partially consumed by inflation and foreign exchange rate fluctuations.

Local Government

As a sphere of government, municipalities collectively as a co-deliverer of services with a direct impact on poor and less poor alike, have perhaps not been co-partnered with the other two spheres to the degree that delivery efficiency objectives would have desired. Part of this can be ascribed to the delayed transformation of the local government sphere and the incompleteness of the legal framework regulating both that sphere and its interaction with the other two spheres. Perhaps the most important of the outstanding legislation is the new Municipal Finance Management Act that is still before Parliament as a Bill.

Municipal Finance Management Bill (MFMB)

The ambitious competencies that the envisaged Municipal Finance Management Act (MFMA) intends granting provincial governments will strain the resources of provincial governments. In practice, the level of readiness of provincial governments to deal with this in a constructive and coherent manner is an area requiring a considerable amount of additional work. Although the provincial Treasury, after restructuring, should be robust enough to shoulder its share of the burden, successful delivery would be jeopardised without the assistance of national Treasury and the partnership of the provincial Department of Local Government. Assistance will have to come in the form of financial resources, human resources, guidance, training and infrastructure.

Steps should be taken to ensure that the MFMA is properly costed to obviate the imposing of a possible unfunded mandate by the national government on the provincial government, as this is nothing else than a function shift from the national Treasury via the delegation route. Thus the usual funds–follow–function principle, should be applicable.

Provincial departments generally, and not only the provincial Treasury and Local Government, need to incorporate the envisaged Municipal Finance Management Act into their strategic planning to position themselves for implementation of the legislation. Likewise municipalities, as the main "beneficiaries" of the MFMA, should prepare themselves for the implementation of this legislation. By the same token the national Treasury and Department of Provincial and Local Government (DPLG) must be persuaded to develop implementation plans in conjunction with provincial treasuries and local government departments.

Transfer of functions and powers

Disciplined effect should be given to the various requirements of the 1996 Constitution and related legislation so as to properly formalise the Province's relationship with municipalities to determine the proper role of each in delivering functions of concurrent and exclusive provincial competence.

A position paper is currently being compiled titled *The Western Cape perspective on the transfer of functions and powers between the provincial and local spheres of governments* which will inform the framework. The position paper will include, amongst others:

- The identification, and compilation of an inventory, of relevant legislation governing the **mechanisms available** for the transfer of powers and functions and the assessment thereof;
- The identification, and compilation of an inventory, of applicable legislative provisions governing the **performance of the functions/services** concerned and the assessment thereof;
- The identification, and compilation of on inventory, of applicable legislative provisions governing the **funding arrangements** for the transfer of powers and functions and the assessment thereof;
- The range and inventory of affected functions/services at provincial government level and an assessment thereof;
- The range and inventory of affected functions/services at local government level and an assessment thereof;
- Intergovernmental financial and fiscal arrangements and an assessment thereof;
- Strategic, economic and institutional considerations;
- The current status and assessment of service relationships (agreements) between the provincial government/provincial departments and individual municipalities.
- A *practical and sustainable framework* to govern the transfer of functions and powers needs to be compiled. The framework will articulate provincial interests, prescribe mechanisms for efficient and effective service delivery and promote democratic accountability, such as legal guidelines and implementation processes, financial and fiscal guidelines, assessment criteria for provincial departments to transfer functions and powers, process guidelines for approving transfers, assessment criteria for municipalities receiving functions and powers from provincial departments, assessment criteria for institutional capacity; and pro forma agreements as contemplated in relevant legislation.

The position paper and framework need to be consulted with the affected departments and organised local government during the compilation and editing phases and eventually submitted to the respective authorities for endorsement.

In view of the nature and transfer of the particular service, further work/research is necessary to determine appropriate funding mechanisms such as shifts in the vertical division of revenue collected nationally, grant funding (conditional), co-funding and matching grants (50:50).

When a *practical and sustainable framework* has been established, provincial departments will be requested to compile a detailed report on the affected functions and powers which should deal with aspects such as composition of affected functions, historical overview, applicable national and provincial legislation (legislative framework), current financial arrangements, and proposed future financial arrangements.

Until such time as the position paper has been finalised and sufficiently accepted, the contemplated Memorandum of Understanding, currently being driven by the Department of Local Government, would serve as an interim arrangement between the province and municipalities. This is to ensure continued service delivery by municipalities within the Western Cape province, to strengthen a relationship of cooperative governance and to ensure fiscal stability.

Integrated development plans (IDPs)

The current intergovernmental coordination, which includes planning processes and fiscal allocations, has to be reviewed with the establishment of mechanisms to elicit greater synergy between planning processes undertaken by the different spheres of government. Maximum senior management support of and involvement in all government spheres has to be fostered so that, where applicable, both national and provincial departments can participate more meaningfully in the formulation and implementation of IDPs.

Intergovernmental relations

A particular facet to be taken forward is the necessity to improve the working relationship and cohesion between provincial and local government. Apart from the issues referred to earlier (organisation of services, funding arrangements, legal framework, IDPs, etc.), such an endeavour will also have to deal with skills, perception and information gaps wherever they occur.

Financial management issues

Imperatives towards greater efficiency

What this section and actually the whole chapter purports to do, is to promote the concept of efficiency in resource use, assuming that resources have been allocated effectively in the first place. However, whether the latter is true or not does not take away from the necessity to improve significantly on the efficiency of resource use, as that is what has been entrusted to a department or a unit in a department and, more specifically, to an accounting officer and other managers and individuals.

The key elements are perfecting, and complying with, the basics or established rules (irrespective of origin), due diligence and, in the spirit of the Public Finance Management Act, the development and implementation of appropriate operational and management frameworks to identify risk, prevent losses and fraud, and ensure timely and appropriate delivery of resources to the points of consumption. In a nutshell this is what accountability is all about, and definitely not mere nominal compliance with rules, although the value of rules should not be underestimated, provided they are assessed and revised periodically and also understood that efficiency has to be driving force, not rules per se.

Compliance with the national and provincial norms and standards will contribute to sound financial management through the effective and efficient utilisation of resources. These benefits, however, are mainly dependent on the will and ability of accounting officers/authorities, together with the combined successes of the various oversight bodies. Internal reflection is indeed necessary by the latter bodies on their actual successes to date in improving service delivery and efficiencies.

Without taking anything away from normal line managers, an essential requisite for accounting officers/authorities, allowing them to comply more fully with the plethora of increasingly sophisticated governance norms and standards, is a properly qualified chief financial officer (CFO) with an adequate CFO support structure, staffed by competent individuals.

A third leg in promoting efficiency relates to those transversal financial systems within the ambit of the provincial Treasury's sphere of influence, as the key instrument for capturing most of the financial transactions attributable to provincial service activities. A number of developments are underway, notably the imminent replacement of FMS[2] in the Province by BAS[3] (before 1 April 2004), the further rollout of LOGIS[4], the searching for an integrated financial system solution by the national Treasury, and other value additions. However, notwithstanding the shortcomings of the current financial administration systems in complying fully with Generally Recognised Accounting Practice (GRAP) and asset management, the optimal utilisation of these can go a long way in assisting accounting officers to execute their responsibilities more effectively. Accounting officers should take more advantage of whatever residual untapped potential.

The introduction of supply chain management (SCM) will transform the existing bureaucratic rule-driven and fragmented way in which provisioning and procurement are currently dealt with. SCM will primarily focus on achieving value for money and effective and efficient use of available resources, and assist with sound financial and economic decision-making. Instrumental to SCM will be the meaningful and sustainable empowerment of those historically disadvantaged.

[2] Financial management system
[3] Basic accounting system
[4] Logistical information system

The recovery of outstanding debts has to receive urgent attention by accounting officers as the overall amount reflected in the Province's accounts is unacceptably big. Particularly worrying is the upward trend, necessitating remedial action by accounting officers and CFOs. Both the provincial Treasury and SCOPA will closely monitor progress in the recovery of debts.

Another component in the drive to effect greater efficiency was the move to create more focused departments with the departmentalisation model implemented on 1 August 2002.

As the key regulatory framework underpinning the whole philosophy of efficiency in spending is the PFMA, both Provincial Treasury and accounting officers are required to prioritise and champion the substantive implementation of the PFMA more dynamically. Adequately funded Internal Audit units at the three to four bigger departments, a cash positive position as an imperative for departments, and expediting the setting of standards of GRAP by the Accounting Standard Board (ASB) all merit special attention.

Cash management

The main objective is the further improvement of cash flow management within the Province. The positive spin-off of endeavours in this regard will be the placing of investments at various financial institutions according to an approved investment policy, resulting in a balanced trade-off between risk and receipt of maximum interest gains. Depending on revenue flows to the Province and committed outflows, constant capitalisation of interest will result in accumulating capital with which to finance major infrastructure projects. Part of this hinges on maintaining minimal departmental cash and bank balances, so there is some risk of an overdrawn position requiring innovative steps to remain both cash positive and a net accumulator of capital.

Contingent liabilities

The provincial government has to identify and record contingent liabilities, disclose pertinent information about its exposure to risks pertaining to contingent liabilities, give sufficient attention to contingent liabilities and reform its analytical policy and institutional public finance frameworks to address all major fiscal risks.

From the definitions it is evident that there is some difference between approaches from an accounting or a fiscal adjustment/budgeting perspective. The apparent inconsistencies require further engagement through debate and investigation to be able to give clear guidelines on definitions to managers. Nonetheless, complete information with regard to contingent liabilities has to be captured in the annual reports of provincial departments. An assessment of the 2001/02 annual reports reveals that a desired state has not been attained as yet. On aggregate only the following items were presented:

	R'Million
Housing guarantees	189,489
Guarantees motor vehicle	0,280
Capital commitment in respect of Health Information System project	63,239
Legal claims	45,374
Other	0,535
Total	**298,917**

Based on the magnitude and scope of operations of the Western Cape 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 Province'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 provincial Treasury need to engage in order to establish both institutional capacity and clear guidelines to achieve these objectives and to prevent ambiguities.

Given the very tight budget over the MTEF requires a rethink about the amount of reserves to be set aside for unknown or (un)expected fiscal risks (including major natural disasters and major unforeseen and unavoidable events). Currently, an amount of R300 million in real terms over the MTEF has been tied up for this purpose. On re-evaluation a once-only amount of R100 million (topped up as necessary in outer years to keep the amount constant in real terms) is to be set aside as provision for mostly unforeseeable and unavoidable expenditure, and the balance for other essential contingencies. Any draw-down will be accommodated via the normal process underpinning the annual adjustment estimates.

Fiscal envelope

Transfers from the national budget continue to dominate provincial budgets and will do so for the foreseeable future as the intergovernmental fiscal system is constitutionally based on a national revenue-sharing model. A number of fiscal challenges face the Western Cape province in respect of the available fiscal envelope, which is the fiscal foundation for provincial service delivery.

Vertical division of revenue

The Constitution entrenches "co-operative governance", obliging the three spheres of government to cooperate and to negotiate political and budgeting issues between them. It is high time for serious introspection and objective analysis of the vertical division decision-making process as provinces generally play the role of junior partner, obligated to pick up the national policy-making tab without sufficient resources to do the job properly and tending to set themselves up for failure due to this. Although provinces are not exactly blameless in the sense that standards of services can be considerably improved, national departments more often than not are really in a position to criticise.

On balance people tend to forget that South Africa is in an important development stage of its history, necessitating due attention to be paid to capacity building, rather than simply continuously finding fault with provincial service delivery.

In this light, provinces collectively have to have a more forceful, innovative and better articulated provincial presence throughout the policy-making process to counter the current *ex post facto* consultation of provinces in the final budget decision-making process or, in slang terms, the “beggar thy boss” syndrome. The vertical division must then correlate with national policy spending decisions that are implemented at provincial and even local government level.

The vertical division must either shield provincial and local governments from nationally driven policy decision shocks, e.g. social security spending imperatives versus relative lesser allocations, or alternatively clear agreement has to be reached between the two spheres on the trade-offs to be achieved prior to any implementation, so as to deal with the implications of such new initiatives in an effective and responsible manner.

The vertical division needs urgent adjustment to create some allocation room in the equitable share formula to:

- Address current vertical imbalances in allocations between the three spheres;
- Counter the current mode of forced reprioritisation at provincial government level;
- Stop the current crowding out of other equally important services at provincial level;
- Deal more satisfactorily with the pressure points than simply adjusting them within the equitable share, as is currently the practice, resulting in a zero sum game – “*mraba raba*”.

It is to the credit of the national Treasury that most of these principles have been incorporated into the proposed vertical division for the forthcoming MTEF and have been accepted as such by the national Cabinet.

Horizontal division of revenue (equitable share formula)

Adjustments within the equitable share formula are deemed secondary, whereas the adjustment to vertical division is a primary concern owing to the factors referred to above. If the vertical imbalances in allocations to the three spheres are adequately accommodated, then adjustments to the equitable share should fully recognise the cost drivers at provincial levels, e.g.:

- The health component in the equitable share formula does not address the relative cost of delivery or demand issues, being based simply on a weighted average of number of persons with and without medical aid;
- The welfare component does not, through the means testing mechanism, fully capture this Province’s responsibility for social security grants, as data appears to be outdated. The latter information is drawn from the 1995 Income and Expenditure Survey. In addition the demand for non-social security services needs to be accommodated;

- Migration factors should be accommodated within the formula (education component already accommodates migration to some extent, but not the other components, especially the health and welfare components);
- Sufficient incentives for accelerated economic development should be provided for the "wealthier" provinces and they should not be "penalised" in favour of the social services sector, as is currently the practice.

Conditional grants

The national Treasury and likewise the respective national departments should be engaged to reduce the many small grants in the system, which simply increase the fragmentation of funding, without adding any real value and placing unnecessary administrative burdens on all parties. As an underlying principle the parties concerned have to accept that the need for conditional grants has diminished with the overall improvement in provincial governance and that they should rather be incorporated into the normal equitable share allocation process. In any case, whatever conditional grants remain must focus on outcomes rather than inputs.

Provincial borrowing

The backlogs in physical infrastructure together with the Province's economic potential obligates the Province to develop the required capacity to effectively manage and accept full liability for provincial capex borrowing, i.e. sourcing the required skills to access additional financing through the various borrowing instruments available on the capital market. However, there are caveats. The first requires the capability to unambiguously derive various rates of return from alternative infrastructure projects, as well as alternative delivery models, and to weigh these up against the cost of capital in economic terms. The second caveat is that the existing own revenue base has to be improved both in terms of estimation and collection before venturing into more complex methods of financing.

Own revenue

In terms of the Public Finance Management Act it is incumbent upon the provincial Treasury to promote and enforce transparent and effective management of revenue. In essence a review of provincial own revenue illustrates that the collection of own revenue requires a concerted effort in shifting the focus towards more active revenue management. The Treasury, in conjunction with departments, will *inter alia* pursue the following avenues to increase the efficacy of own revenue:

- Stability in revenue collection through improved forecasting and the tabling of sustainable credible revenue estimates;
- Improved administrative efficiency, which includes improving human resource capacity and supportive infrastructure;
- Enhanced information technology systems, specifically in the Departments of Health and Transport and Public Works;
- Reduction of the differences, interdepartmental and between provinces, in user fee charges and tax variances through sectoral interdepartmental and interprovincial cooperation;

- Development and implementation of a clear revenue generation incentive policy in conjunction with departments, which will provide for departments' base-line allocations to be augmented by amounts that are equal to the difference between original MTEF projections and credible new revised estimates, taking into account any associated risks;
- Maximisation of provincial own revenue through the implementation of new provincial taxes, with specific focus on introducing a provincial fuel levy over the MTEF earmarked for road infrastructure spending.

Key priority areas

Introduction

This section does not dilute any of the conclusions summarised previously, but attempts to concentrate the attention on the main drivers informing the allocations for the new MTEF. Although the demands are infinite, the overall fiscal envelope is very tight given the extrapolation of current budget pressures forward into the new financial year. What makes matters worse is that the 2003/2004 financial year ushers in the final phasing in of the equitable share formula, as it is currently constituted. What effect the 2001 Census will have on future years is anybody's guess. By the same token both the replacement, if any, for the present equitable share formulation and the question whether that will contain incentives or disincentives for provincial growth strategies are uncertain. Although this is a matter for future negotiations with the national government, the latter has become important because it does not make a great deal of sense, nor will it attract investors if successful provincial economic growth endeavours are willy-nilly rewarded by lesser fiscal transfers to it.

National policy guidelines

Before moving to specific provincial issues it is worthwhile to bear in mind that, in adjusting the vertical share of national revenue funds in favour of provinces and local government for the next MTEF, provinces were implicitly invited to agree that the augmentation would be used to fund mainly:

- Learner support materials and other non-personnel non-capital budgets in education;
- Medicines, drugs (including antiretroviral drugs), equipment, medical supplies and other non-personnel non-capital budgets in health;
- Restructuring and improving pay packages for scarce health personnel;
- Social security grants, implementation of norms and standards, and welfare services including the implementation of the Child Justice Bill in Social Development;
- Roads, agriculture and other economic infrastructure and rural development programmes.

On further analysis of the national recommendations the impression is gained that for the foreseeable future some amicable balance has to be achieved between social and economic infrastructure spending, without any overt thrust in any particular direction. While that is probably relevant for the country as a whole, one could argue that a more stimulatory or growth and development budget would be better applicable for the Western Cape, given the slow improvement in per capita incomes and stubbornly wide disparities in income levels between communities, genders and races.

The basis of such argumentation could be the contention that, over the last five to eight years, substantive shifts have occurred to improve in-kind disparities, including improved access to social and other services by historically disadvantaged individuals. These shifts, so the argument goes, were in recent years, particularly the last 18 months or so, complemented by significant increases in unrequited transfers through the social security system. This then requires a shift of available funds to the economic sector.

The problem is that a contention like this is extremely difficult to substantiate with good empirical evidence. The evidence that does exist seems to suggest that consolidation in the social services sector together with efficiency improvements would result in the improvements in social equity achieved over the last eight years at least being maintained. However, the fact that increasing relative poverty and deprivation asks for greater unrequited cash transfers, mitigates against even thinking of holding social security transfers constant in real terms. However, taken to the extreme, this approach in itself can cause an unsustainable fiscal environment, as relatively little government funds go to productive economic investments.

The challenge then is to strike a balance between what at first glance seems, to be opposing choices but in reality, provided the right combination can be found, is in fact complementary to a growth and development goal. The extent to which this will be possible would depend on the overall envelope and the necessity to deal with relatively fixed costs in this context versus discretionary amounts.

Efficiency gains

Whatever the final envelope, as was argued earlier, much greater effort has to be put into improving efficiency overall and specifically in the area of non-personnel expenditures, if the assumption holds that the reductions in personnel numbers during 1997/1998 and subsequently indirectly contributed to enhanced productivity without damage to service delivery. What is implicitly presumed is that departments have improved on their personnel utilisation, as overall service delivery numbers on average appear to have either increased or at least remained relatively constant.

Supply chain management

The key problem area relates to the concept of supply chain management recently introduced into government, whether in the procurement or actual supply of services to the general public and all the steps in between or subsequent to these two finite actions. Based on evidence supplied by departments and on information obtained from the Auditor-General reports and Internal Audit, most of these processes still leave much to be desired. The net effect of all of this is that the Province ends up by paying more for services or other obligations on a unit cost or global basis than really necessary. Therefore accounting officers and their executive authorities (as applicable), assisted by the provincial Treasury and even Legal Services, will have to give this facet close attention over the new MTEF so as to stretch the available rand further and prevent unnecessary leakages or exorbitant prices.

Principle areas deserving of attention are Health (equipment and a broad range of consumables), Education (learner transport and learner supply materials), Transport and Public Works (capital projects and property management), Premier, Director-General and Corporate Services (IT and ICT) and Social Services and Poverty Alleviation (social security). However, other departments are no less deserving of attention as they, because of their smaller bulk, could show the way with more innovative supply chain enhancements.

Part of this thrust has to incorporate making greater use of private-public-partnerships to spread risk, but also to introduce both greater efficiency in procuring goods and services (movable or immovable) and better local investment possibilities with economic growth spin-offs.

Improvement in personnel utilisation

PSCBC[5] Resolution 7 of 2002 provides another opportunity to utilise personnel to their fullest potential by the rearrangement of staffing structures and supportive retraining to best meet strategic goals of departments. Probably the most intensive exercise will be in the Department of Health, which will most certainly extend beyond the final d-date set for ending the formal process. Government really needs employees who are committed to the goals of government. Difficult as it may be, serious consideration has to be given to weeding out old wood or square pegs in round holes and other measures that would contribute to greater efficiency in service delivery.

Financial management improvements

A range of actions have been dealt with fairly exhaustively in this Fiscal Policy which includes, apart from effective supply chain management, strengthening the oversight role in respect of accountability, more purposeful and systematic capacity building of finance personnel, a switchover from the outdated FMS batch-oriented financial system to the more modern real-time BAS system before 1 April 2004, extending the rollout of LOGIS where the advantages of doing so outweigh any downsides, further improvements in cash management and accounting processes and standards, the creation of Internal Audit Units within Health, Education and Social Services from 1 April 2003, standardisation of chief financial officer requirements and structures, and a better grasp of contingent liabilities.

The costs to be incurred are relatively low, with the provincial Parliament requiring a bit of strengthening, three new Internal Audit Units, once-off capital costs for BAS and subsequent higher running costs than with FMS and so on, most of which will be doubly compensated for by efficiency gains over time. Most of these issues require further work on detail in liaison with accounting officers, to be performed in direct relation to benefits perceived and in time for the new financial year.

Departmentalisation

A number of departments have been subdivided to enhance efficiency and service delivery. This exercise also provides the opportunity to rectify both the Human Resource (HR) and Financial (Chief Financial Officer) Management components and so set a standard for the Province that would allow the new heads of these departments to deal

[5] Public Sector Central Bargaining Chamber

fully with the scope and breadth of both HR and public financial management requirements. In public finance parlance that would facilitate substantive compliance with both the letter and spirit of the Public Finance Management Act, which so far has proved to be elusive. At the same time, alignment with the national Treasury's normative financial standards might then also be feasible. These departments would then become the test bed for new innovations in financial management to be rolled out to the other departments over time.

Cost implications of the "new" departments are still uncertain, with most of the Organisation and Development reports still to be delivered to the provincial Treasury for assessment.

Own revenue improvements

The first objective has to be a systematic reduction in outstanding debt to the Province and clearing of nominal (non-substantive) amounts. With the budget as tight as it is, there is no excuse for insufficient and lack of attention to these long outstanding and increasing amounts. As an incentive, the provincial Treasury is quite prepared to consider enhancing baseline allocations of the affected departments equal to the real debt outstanding as at 1 April 2003 as a once-off concession. The flip side to this is that any remaining long-outstanding amounts subsequent to 31 December 2003 will be set off against future allocations as a censure for not delivering on their revenue potential to the detriment of service delivery. This brings revenue management in the Province in line with the approach applicable to expenditure management.

The second objective has to do with maximising revenue potential and in this endeavour the provincial Treasury will work very closely with departments to achieve the desired state. The same incentive and "penalty" will *mutatis mutandis"* apply as for outstanding debt, although non-collected revenue could result in equivalent downward baseline adjustments in the same financial year, but only where such revenue is linked to expenditure estimates for that department in that year.

The third objective relates to the development of new revenue sources, of which the most substantive would be the envisaged fuel levy. However, these processes take a long time to see through to fruition, given the requirements of legislation to determine the net economic and tax (where applicable) incidence effects. To accomplish this result, the provincial Treasury will drive the project in liaison with any initiating or partner departments.

Otherwise, own revenue projections over the new MTEF unfortunately do not add any joy, as they show a weakening trend, in part due to already relatively high user charge or tax rates in comparison with other provinces. As yet forecasting on new sources expanded on earlier has not proved to be possible with a sufficient degree of certainty to be taken up in budget estimates for the future.

Underlying theme: Ikapa elihlumayo

Perhaps in spite of what has been said so far, an imperative rests on the shoulders of government generally not only to grow the economy at a significantly faster rate than the population growth rate, but also to ensure greater and equitable participation in the fruits of any successes. This is particularly relevant for our country with its large income disparities and low growth rates and the earlier systematic exclusion of the greater share of the population from economic opportunities. The Province has no less a responsibility in this context, and has to initiate those actions that would contribute to the unlocking of any untapped potential within the Western Cape as well as grow the capacity for growth over time. The general perception is that people have become despondent about the potential for economic participation, possibly more so amongst the youth as the new labour market entrants.

Thus it is suggested that the executive and accounting officers embrace the concept of *ikapa elihlumayo*, meaning growing and developing the Cape. Although planning in this respect is still in its infancy, it has become important to convey the intention of the Province to do so as it informs the underlying principles of the budget, its desired deliverables and the allocation of resources. Driving this concept has to be the necessity to lower poverty levels, which is only possible via increased wage employment opportunities, which in turn is dependent on economic growth.

Suffice it to say that some work towards this ideal has already commenced in liaison with the Departments of Economic Development and Tourism and Transport and Public Works who have their own laudable initiatives. Further expansion on *ikapa elihlumayo* is included in Appendix A, with due credit given to Economic Development and Tourism who provided most of the inputs. Hopefully this will serve as a useful discussion document to take the idea forward. Various inputs in different stages of completeness have been received and the daunting challenge now is to put together a coherent framework. That is a no easy matter and although the underlying ideal is clear, a great deal of research lies ahead to ensure an adequate return on investment, appropriate targeting, crowding in of private sector and perhaps even foreign direct investment and, lastly, proper synergy with other delivery partners, especially provincial public entities, national and local government and state-owned enterprises. Conceptually the idea hinges around a flagship (combination or single) physical infrastructure investment to which all other initiatives are linked in synergistic manner. A tall order, perhaps, but any other alternative is likely to be a continuation of the current piecemeal approach, diluting possible advantages and lowering the impact on employment creation.

The main thing about the *ikapa elihlumayo* concept is that it begins to concentrate the mind at a time when provincial and local government spheres in the Western Cape are amenable to the idea and prepared to make the required trade-offs in the interest of long-run benefits. This would most probably also coincide with national government initiatives of which NEPAD is only one. However, two key constraints are the low skills levels in the country (a mere 2.5% of all adults between the ages of 26 and 30 years have a tertiary degree or more and 29.4% a grade 12 qualification)[6] and the competitive and other vagaries that a small open economy like South Africa is subject to.

Also underlying the *ikapa elihlumayo* concept is the further promotion of black economic empowerment, supported by the initiatives already underway in support of preferential procurement and the successes achieved in this context over the past year.

Service delivery improvements

From the analysis per provincial department and from national policy guidelines it should be fairly clear what provincial fiscal policy should ideally be. However, being on the receiving end of an equitable share formula, indexed to relative poverty and other indices, on the one hand, and, on the other hand, perhaps being too efficient or compassionate in social security management, limit the Province's budget manoeuvrability.

Before moving on to specific proposals, a summary of the possible additional available amount from the national revenue fund is deducible from the Medium Term Budget Policy Statement 2002, as tabled by the national Minister of Finance in Parliament on 29 October 2002, and further elaborated on in Chapter 5 of this Policy. Quite obvious are the substantive additions to provincial baselines over the next three financial years, resulting in a restitution of the vertical share proportion going to provinces. What is perhaps not so obvious is that the greatest proportion of the augmentation caters for "new money" and the balance for inflationary cost pressures.

The major problem with additions to deal with current cost pressures, is the linkage to a general GDP inflator which, although appropriate for national budgetary purposes, is rather less than the actual cost pressures felt at point of purchase and also differs from sector to sector. But then, expectations and poor supply chain management also drive inflation, with the latter elaborated on earlier.

The main cost driver in the Province is Social Security and, owing to its compelling characteristics and the driving forces behind it, mainly the high incidence of abject poverty, which has to be funded first out of "new money" or, in national government speak, "policy adjustments". Based on current growth or accumulation rates of registered beneficiaries and future projections, mainly depending on national Treasury calculations (the projections of Social Security and Poverty Alleviation vary from slightly lower to much higher), all new money via the equitable share contribution will have to be used for this purpose, i.e. growth in social pension beneficiaries, chiefly the Child Support and Disability Grants. However, the projections are based on questionable assumptions requiring reassessment in the course of next year which would hopefully allow for downward adjustment, that is to say if the measures introduced by Social Services and Poverty Alleviation have the desired effects. Another dynamic not factored in is the Masava case against government and the in-principle decision by the national Cabinet to create a National Agency which, in future, will manage social security grants. What

[6] Van der Berg, Outlook on the South African Economy, BER, 2001

provinces have to be very wary of is how this transition will be managed, as some approaches could have deleterious and even perverse results.

That leaves the balance of the equitable share available to maintain all other services and also to provide for cost pressures of which there are essentially two categories, namely salary (ICS[7]) and procurement-related cost increases. Discounting the additional funding for Social Security, macroanalytically it would appear that the Province would just be able to maintain a constant real growth overall on all other services over the next MTEF.

Part of the problem for the limited budget lies in the national government allocation process and the division of cost pressures between equitable and conditional grants. Two main points arise, the **first** being that it creates distortions in funding mechanisms, and, **secondly**, the way that personnel cost adjustments are made. Although the Province is heavily dependent on conditional grants (over R2 billion in 2002/03), particularly those funding the academic hospitals, all adjustments related to personnel are made via the equitable grant mechanism which, due to its redistributive nature, might not be a true reflection of the actual personnel cost of running these facilities.

The national Treasury has made selective adjustments to conditional grants for the next MTEF, but apparently only for non-personnel-related cost inflation, together with policy adjustment boosts for HIV/Aids (mostly mother-to-child prevention), Hospital Revitalisation and the Integrated Nutrition Programme. Calculations based on the 2002/2003 experience have been made as to the possible quantum of these grants due to be distributed to the Province, and although somewhat speculative, as equity also plays a role, they do not add substantive additions to baseline. Nonetheless, it will provide some relief and allow greater focus on the designated policy areas, although measures will have to be introduced to improve the disbursement of the Integrated Nutrition Grant.

However, after discounting conditional grants with no personnel component and making assumptions about the proportions of conditional grants that should flow to the Province, double-checking against the individual votes points towards a degree of flexibility in the revenue envelope. This should allow attention, even if imperfectly, to be given to the various conclusions taken from the Expenditure Review and others as enumerated in the previous section. As the latter and the national policy guidelines closely coincide, this would appear to allow some scope, albeit limited, to incorporate these into the final allocations. Nonetheless, as the 2003/2004 is the target year for full attainment of equity, this year would require smoothing from future expected revenues to cover a deficit between expenditure and revenue, in the absence of other measures.

Abolishing the present provision for contingent liabilities from revenue in 2003/04 and beyond should provide sufficient space to cater for reasoned departmentalisation costs as well as other requirements in the economic sector, particularly Agriculture [to further promote Farmer Settlement as an extension of the Land Redistribution for Agricultural Development (LRAD)], Tourism, school sport and selected industrial sector

[7] Improvements in conditions of service

developmental initiatives provided adequate analysis can be finalised within a broad integrated approach to gauge returns on any proposed intervention. The latter combination will begin to lay the basis for the *ikapa elihlumayo* drive.

All of this implies the necessity for greater efficiency in resource use, but also the much sharper redeployment of services to give effect to the Executive's priority framework, as further expanded on by the provincial Treasury in its 2002 expenditure goals[8].

Additional capital expenditure

All capital spending as originally provided in the 2002-2005 MTEF remains as is, save for adjustments for inflation as expanded on previously. Unfortunately, the national Treasury elected to keep the Provincial Infrastructure Grant more or less the same in nominal terms for the new MTEF, resulting in an overall real decrease in the national transfers available for physical infrastructure. Although the Hospital Revitalisation Grant has been significantly adjusted upwards overall, actual amounts also expected to flow to this Province would probably be relatively small.

Still included in the provision for capital spending are the remaining balances from cash reserves (R320 million) to cater for the outstanding payments to the convention centre in Cape Town and transport and public works projects during 2003/2004 and 2004/2005. As a result of further improvements in cash management and a purposeful goal of capital formation and depending on progress made in giving substance to the *ikapa elihlumayo*, further dividends from cash management activities (at least R300 million over the MTEF) might be allocated for this purpose eventually.

The gross total would depend on the efficiency of money management operations and exogenous factors like interest rates, the national Treasury's cash policy framework and what arrangement the Province can come to with the national Treasury in dealing with the long outstanding 1994/1995 and earlier expenditures that were inherited into the books of the Western Cape. In line with earlier conclusions, it is intended to augment these capital provisions by entering into loan agreements, provided the return on such economic infrastructure is in excess of the cost of capital.

It is also proposed to make a significant dent in the equipment backlogs in Health over the next two financial years (in the vicinity of R120 million over the next two years). However, this would be dependent on prior assessment of Health's supply chain management system in liaison with the Auditor-General and appropriate remedial steps, where indicated.

Remaining balances in the capital "fund" will be used to top up to R100 million (in real terms) the unused provision for contingencies provided for in 2002/03 and rolled forward into 2003/04, and secondly, to possibly, depending on future revenue forecasts, bridge the shortfall between expenditure and revenue in the 2003/04 period.

[8] 2002 Budget Speech of the Minister of Finance and Economic Development

The overall strategy is not without risk as the liquidity buffer in the Provincial Exchequer would be rather stretched, and secondly, borrowing implies ceding an own revenue stream to the lender, which in effect reduces the primary revenue envelope. Thirdly, the entire approach is premised on the condition that no department will overspend, because if that happens and the monies referred to have already been tied up, there would be no bridging finance available within the Province's coffers, requiring an approach to the Corporation for Public Deposits (national Treasury) for assistance. The possibility of such an eventuality could affect the Province's risk profile, attracting less favourable lending rates.

Conclusion

What all of this boils down to is a fairly comfortable, although tight, holding budget forecast for the next MTEF, with room for manoeuvring to begin to lay a basis for growth, even if modest. The proviso quite naturally is subject to an unambiguous commitment, firstly to sound governance within each department's resource limits and secondly, to *ikapa elihlumayo*.

This scenario sketched would not have been possible without the national government's beneficence and acknowledgement of the important role that provinces generally fulfil in the delivery of social and economic infrastructure and developmental services. It provides an opportunity for careful reflection on the road to be taken for the future, building on achievements to date, coming to grips with both our weaknesses and strengths and using our resources optimally and sensitively to reward those dependent on the provincial government for the trust placed in it as an institution of change.

The key to this process has to be the substance of *ikapa elihlumayoi*, so that the net result is a systematic improvement in per capita income levels and income disparity brought about by economic growth, broadening of the economic base participation, appropriate skilling, significantly higher and sustainable wage employment and investment opportunities in the business sector. The only two tools that government has are the budget, which is the primary tool, and the human capital capacity intrinsic to the Province. These have to be used wisely with full support and buy-in of both investors and the public at large: a tough challenge, but necessary to give hope for the future!

ANNEXURE A

IKAPA ELIHLUMAYO
Conceptual Framework for discussion

Introduction

“Ikapa elihlumayo”, the Xhosa name for a Growing Cape, is the underlying concept for the Province’s Budget theme for 2003/04 and beyond. Growth has two different meanings in Xhosa, namely “khula” and “hluma”. The first literally meaning growth, or “groei” in Afrikaans, while the latter has a profound and more proverbial meaning.

“Elihlumayo” means growth for the Province in a holistic sense. This follows that harmonious growth should be perceived as growth in all sectors and regions, benefiting the poorest to the richest. The symbiotic interpretation of the word must also be emphasised, as the growth of the different parts or sectors should benefit each other in a mutually advantageous manner whereby the desired results or outcomes are at a higher level together than what would have been the case in isolation.

Just as the Winter rains bring growth and new strength to all the plants in the Western Cape before Spring emerges, whether it is the wheat to be harvested to feed a nation, the indigenous flora of the Province, or even the unwanted wild plants that also prosper from nature’s unconditional abundance, “Ikapa Elihlumayo” will prosper the Province.

“Ikapha Elihlumayo” directs our efforts to a holistic approach where we all take up the challenge to see the Province grow, to the best benefit of its people, both individually, and collectively. The ultimate challenge is thus for all to do their best so we can all grow together, even if progress brings with it inevitable obstacles before we reach our desires.

Cape Town, as the oldest city in South Africa, has built a reputation for high-quality skills and infrastructure and attracts an increasing amount of tourists, residents and refugees. Fortunately the Western Cape economy is broad based, with manufacturing accounting for 24%, financial services 16%, Government 14%, tourism 9% and agriculture 6%, of Gross Geographic Product (GGP).

The Western Cape government therefore realises the need for economic growth and development and has to make use of the opportunities that are available to boost the local economy, especially the improved nationally negotiated trade agreements, exports of agricultural products, high-quality clothing, automotive components, boat-building, information communication technology (ICT) services, etc.

The new Western Cape economic approach will be to:

- Grow our strengths rapidly;
- Tackle our weaknesses systematically;

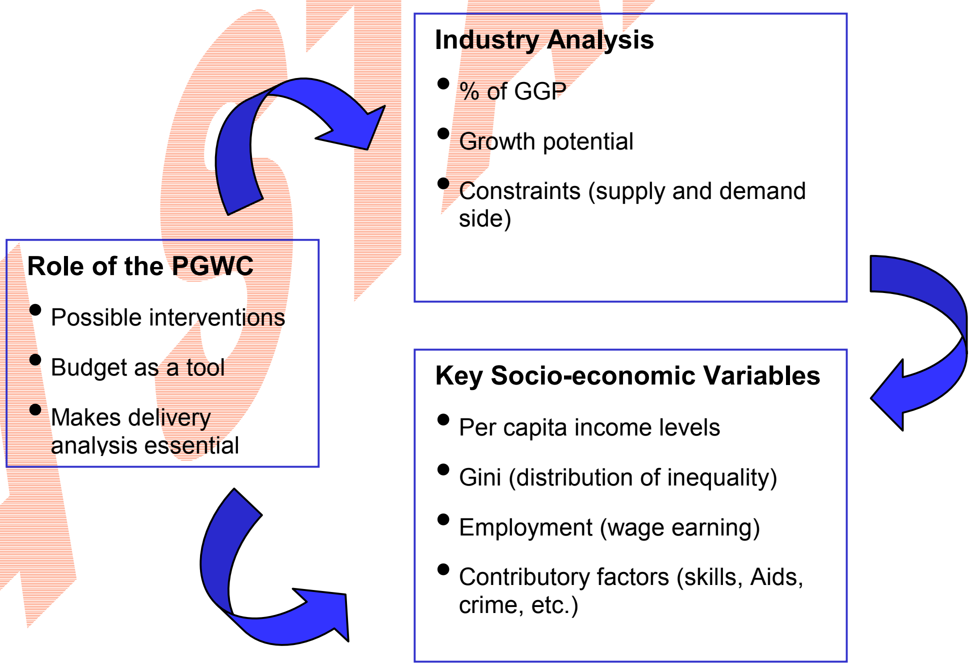
- Promote our opportunities locally and internationally; and
- Manage any threats to us wisely.

With the Western Cape focus on economic growth, in conjunction with the alleviation of poverty and black economic empowerment (BEE), this approach requires targeted interventions in the regional economy. These interventions are to be aligned with national government's programmes for macroeconomic stability and micro-economic reform.

The key to success for the Provincial Government of the Western Cape (PGWC) is to have adequate capacity to create a favourable environment for the private sector. Industry analysis and an understanding of the dynamics of the Western Cape's sectoral economy, socio-economic variables and constraints are of utmost importance.

Industry analysis will have to be broken down by sector and region to determine the contribution of each economic sector to the GGP, the growth potential of each sector or sub-sector and the constraints on both the supply and demand side so that these can be eliminated to give impetus to a virtuous and sustainable cycle of growth.

The three key macro/socio-economic variables that will have to be determined per sub-region and for the Province as a whole are per capita income level, inequality and employment. Although these key factors need to be complemented by other variables as well, they are the key variables to measure the attainment success of economic growth in the Province.



To alleviate poverty and empower historically disadvantaged people, considerable human and financial resources will be deployed over the next three years by the Western Cape Provincial Government to promote economic growth in targeted areas where the ownership base of the regional economy will be broadened.

Building cumulative strength

The growth of national and regional economies is highly dependent on the growth of the economic sectors present in those geographic areas. Thus building cumulative strengths is a combination of building on natural comparative advantages of geographic position, natural resources, environmental beauty plus human resource skills, institutional capacity and good governance.

The challenge is to bring historically disadvantaged people into these growing sectors through explicit programmes of support.

Growing sectors with potential for absorbing more players of colour and women have been identified.

Micro-economic reform

The integrated development planning (IDP) process can be linked to delivery programmes in order to deliver local economic development (LED).

Small, Medium and Micro Enterprises (SMMEs), like other businesses, will only thrive in growing sectors, with access to finance and mentoring.

A human resource strategy to build a culture of learning in the Province is one of the most critical areas to receive attention: not just to provide the people with skills required for jobs, but for empowerment and growth.

Areas of intervention by sector are Research and Development (R&D), where the Western Cape's tertiary institutions should play an active role. The national Departments of Science and Technology (DST) and Arts and Culture (DAC), which support the Biotechnology and Craft sectors, respectively, are valuable examples for others to follow.

Cluster development

Cluster development, through government intervention, where a critical mass of services, pools of knowledge, suppliers and institutions are woven together, is a strategy which brings real benefits in terms of expansion, new firms, employment and growth, but will only be realised over the medium to long-term.

Sector selection for intervention depends on the objectives of government and the mix of industries within a region. The approach of the Western Cape government has been to select a portfolio of sectors with a range of characteristics and imperatives, many of which have been identified nationally as key sectors, namely:

- The employment sectors: Clothing, agricultural-processing and tourism.
- Sectors with high growth potential: Oil and gas supply industry, organics and call centres.
- High-technology sectors: Information, communications and technology, biotechnology and materials.
- Manufacturing sector: Machinery, footwear, food processing and metal fabrication.
- The profile sector: Film and wine.
- Traditional slow-growth sectors such as printing and publishing, financial services, retail or domestically focused services sectors, which largely depend on the growth in local demand arising from other sectors.

The growth in exports is seen as vital to the success of a sector and should be viewed as a key objective in all clusters.

Workshops and seminars can be an effective medium to share information about entering new markets and partnerships between firms, trading houses can provide marketing and logistics expertise to small firms, and trade missions can assist firms in understanding foreign markets. A cluster can assist companies in benchmarking themselves against each other and against the world's best to ensure that they are meeting the requirements and techniques necessary to compete globally. Clusters should thus assist firms in sharing knowledge through factory visits, international conferences, inviting international leaders and other means.

Clusters are ideal vehicles for facilitating the expansion and development of SMMEs and start-up companies. Clusters must have explicit aims to facilitate the entrance of firms owned by historically disadvantaged individuals (HDI) into the mainstream. Active interventions are required to encourage partnerships between larger firms and HDIs or linkages built into supplier/buyer procurement relationships. Therefore it is of utmost importance that boards should have black representation.

Communication

The action required to grow the regional economy from its current position and to build on its cumulative advantages has been detailed above, but equally important is to communicate with and inspire a somewhat mixed array of people who live in the Western Cape, to turn them from being rather uninvolved bystanders, into proud South African contributors to economic growth.

Delivery

The institutional architecture to deliver on the above proposals requires to be transformed. Government (according to the White Papers) should focus primarily on development – mainly skills and infrastructure. Agencies in partnership with the private sector should focus on generic promotion of opportunities, support and the achievement of goals set by government.

Joint Marketing Strategy

One of the primary aims of the joint marketing strategy (JMS) in the Western Cape is to exploit opportunities linked to comparative advantages through synergistic marketing and, in so doing, realise economic policy objectives such as poverty alleviation, improved equity and sustainable development. It recognises the need for focused and well-coordinated marketing to achieve success in unlocking the potential of the Western Cape as the Province competes in an increasingly global market. The JMS will align all marketing efforts, including the linking of agencies that promote tourism, trade, investment, events and film, to give birth to a single-minded public private partnership (PPP) that will focus on promoting the city and regions.

Successful PPPs, such as the one contemplated for the Cape Town Convention Centre, draw on the respective strengths of the public and private sectors and, in so doing, bring greater skills and resources to bear on developmental challenges and leverage higher levels of investment.

Linking the marketing of tourism to trade and investment can only add impetus to initiatives to attract more business travellers.

Business will benefit from the JMS by increased exposure through more focused and integrated marketing and cross-sectoral marketing opportunities. Being highly web-leveraged will further ease interaction between business and the joint marketing initiative, making it easier to link companies to opportunities and make better use of electronic business databases.

Between 1980 and 2000, the manufacturing, trade and catering (including tourism) and finance and real estate sectors experienced the highest levels of growth in the Cape Town economy. For the economy to continue growing, however, it needs to remain dynamic and undergo necessary structural changes. Future growth in the Western Cape is expected to come from increased adding of value in the five broad sectors (ICT and technology, tourism and leisure, agriculture, smart manufacturing and clothing and textile) outlined in the Investment Promotion Sector Marketing Strategy forming part of the JMS.

Agriculture

The Western Cape is responsible for 22% of the total value of agricultural production of South Africa and supplies 50-60% of all agricultural exports. This sector supports approximately 14 000 farmers (of whom 2 500 are from previously disadvantaged communities) and 250 000 farm workers with 1,5 million dependants. It has been found that for every R1 million increase in disposable income received by the lower income groups, 53,9 job opportunities are created in the economy of the Western Cape. Agriculture therefore needs to play a significant role in a growth strategy for the Province.

The political directive to distribute 30% of commercial agricultural land in the country within the next 15 years is the guiding force behind the land reform strategy in its broad context and commercial farmer settlement within the context of the Land Redistribution for Agricultural Development (LRAD) programme. The LRAD will address agricultural land needs for productive purposes among the black people of the Western Cape.

Producers in the Western Cape will also have to adapt to the changing environment due to globalisation if they wish to stay competitive. Local consumers want for low-cost commodity-type products, whereas the export market consumers are more sophisticated and want quality, traceability and safety as far as their food is concerned. For such products they are willing to pay more. These are the sort of market characteristics that producers will have to be aware of to get a competitive advantage. For every R1 million increase in demand for agricultural products, more than 80 jobs are created, in contrast to the industrial sector's figure of 29 jobs. To boost the sector and region, cooperation is also essential, for example the beneficial interrelationship between the wine route, restaurants, local arts, crafts and curio shops, farms, tourism, agri-tourism, agricultural labour and job opportunities, local cheese makers and olive growers.

This annexure, together with one or two additions, has been condensed by the provincial Treasury from the original document, titled IKapa Elihlumayo: Growing and Developing the Cape, Draft 3, October 2002, by Dr Laurine Platzky, Department of Economic Development and Tourism, and extracts from the Department of Agriculture's Submission for Budget Increase inputs.