LOCAL GOVERNMENT

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New grants, more money

IN THE FIGHT AGAINST POVERTY

COMMUNITY LAW CENTRE
University of the Western Cape

Municipalities' share of the national pie

NEW GRANTS, MORE MONEY IN THE FIGHT AGAINST POVERTY

The Division of Revenue Bill of 2007 (the Bill), introduced by the Minister of Finance, Trevor Manuel, sets out the allocations local government will receive for the 2007/08 financial year. The Bill not only determines local government's equitable share of revenue raised by the national government, but it also contains a number of innovations. The most important are the new conditional grants – the Neighbourhood Development Partnership grant and the Water Services Bulk Infrastructure grant. Provision is also made for assisting host municipalities in their preparation for the FIFA World Cup in 2010.

The Bill and the accompanying Explanatory Memorandum as well as the National Treasury's *2007 Budget Review* give a comprehensive review of the financial allocation of funds to the three spheres of government. A few of the pertinent matters affecting local government are highlighted here.

Division process

At least ten months before the start of each financial year, the Financial and Fiscal Commission (FFC) must submit to the Minister of Finance recommendations for that financial year regarding an equitable division among the national, provincial and local spheres of government of revenue raised nationally. Having received the recommendations the Minister consulted the provinces in the Budget Council and Salga in the Budget Forum. An extended Cabinet meeting involving cabinet ministers, premiers and the chairperson of Salga was held on 18 October 2006 where agreement was reached on the final budget priorities and the division of revenue over the next three financial years. One of the core areas that the 2007 budget will support is housing delivery and the roll out of basic services, which require both municipal capacity-building and investment by the public and private sectors in improving the quality of life in poor neighbourhoods.

Local government's cut

Over the next three financial years, local government will slowly receive an increased percentage. While in the 2003/04 year, local government received only 4.1% of the revenue raised for

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division among the national, provincial and local governments, that percentage increased to 6.5% for 2006/07 and will stabilise at 7.8% in 2009/10. The increase in allocations to municipalities from R27.1 billion in 2006/07 to R45.6 in 2009/10 represents a 19% increase per year.

Provinces receive between 42% and 43% of the nationally raised revenue compared with local government's 7%. However, local government's allocations constitute only 15% of municipalities' income (the rest they collect themselves), while provinces are dependent on national allocations for 96.4% of their revenue.

Division of nationally raised revenue, 2006/07 to 2009/10 (R billion)

Level of government	2006/07	2007/08	2008/09	2009/10
National	213.5 (51.0%)	240.9 (50.4%)	252.1 (49.2%)	286.3 (48.8%)
Provincial	177.9 (42.5%)	202.8 (42.4%)	229.3 (43.0%)	254.4 (43.4%)
Local	27.1 (6.5%)	34.3 (7.2%)	41.8 (7.8%)	45.6 (7.8%)
Totals	R418.4 bn	R477.9 bn	R533.2 bn	R586.4 bn

The transfers to municipalities are composed of local government's equitable share and conditional grants. While expenditure against the equitable share allocation falls in the discretion of the municipalities, spending against conditional grants are governed by the terms of the grants. Of the R34.3 billion municipalities will receive in 2007/08, nearly 40% will be conditional grants.

Equitable share

The government retained the formula, introduced in 2006, to calculate the equitable share of each municipality. The formula consists of five components: (i) a basic service component to enable municipalities to provide water, sanitation, electricity, refuse removal and other basic services and free basic services to poor households; (ii) an institutional support component to enable particularly poor municipalities to fund the basic costs of administration and governance; (iii) a development component; (iv) a revenue-raising capacity correction; and (v) a correction and stabilisation factor to ensure that municipalities are given what they are promised in the two year budget projections. This formula was introduced in 2006/07 and is being phased in over two years, taking full effect in the 2007/08 financial year.

RSC/JSB levies

Since the 2006/07 budget, a grant was used as a replacement for the RSC/JSB levies that were abolished as from 1 July 2006. For 2007/08, R8 billion has been made available for this purpose (R9 billion for 2008/09 and R9 billion for 2009/10). The grant is, however, an interim measure and other options are to be explored. The National Treasury noted that any replacement option(s) should have limited negative economic impact, provide adequate revenue at acceptable rates and be easy to administer. Although options that increase local government's fiscal autonomy are preferred, such options should comply with the framework of local government's constitutional taxing powers.

Conditional grants

The most important conditional grant is the Municipal Infrastructure Grant (MIG). In view of the FIFA World Cup in 2010, grants directed at that event will feature prominently in the next three financial years.

Municipal Infrastructure Grant

The MIG is to supplement municipal capital budgets to fund backlogs in municipal infrastructure required for the provision of basic services, primarily for poor households. A further aim of the grant is to stimulate local economic development and job creation through labour-intensive methods as prescribed by the expanded public works programme. The National Treasury has rejected the proposal by the FFC that the MIG should include operational and maintenance costs of the infrastructure as well, arguing that municipalities have a substantial revenue base which should fund such operation and maintenance costs. For 2007/08 and the two following years, the MIG will be R7.5 billion, R8.1 billion and R9.1 billion respectively.

FIFA World Cup 2010

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public transport infrastructure and the construction and renovation of stadiums.

Allocations to municipalities for FIFA World Cup 2010

	2007/08	2008/09	2009/10	Totals
Transport infrastructure	R1.2 bn	R3.2 bn	R2.3 bn	R6.7 bn
Stadium construction and renovation	R2.7 bn	R3.8 bn	R1.3 bn	R7.8 bn

The transport infrastructure grants will focus on establishing, constructing and improving new and existing public transport infrastructure, including commuter bus and rail transport. With regard to the building and renovation of stadiums, the National Treasury cautions that municipalities are required to plan and budget for them, taking into account their own revenue potential along with transfers from the national government. In short, the national government is not going to foot the entire bill.

Neighbourhood development partnership grant

An amount of R3.7 billion over the next three financial years will be made available to municipalities to provide both technical assistance and project funding to improve infrastructure in townships and informal settlements. The aim of the grant is to leverage increased private-sector investment by providing opportunities for retail, mixed-income housing, manufacturing and commercial projects in township nodes. The grant is to support high-quality developments in townships to overcome the spatial and economic distortions of the apartheid past. A key principle of developments is to retain and increase the buying power within townships.

Water services bulk infrastructure grant

A new water services bulk infrastructure grant has been introduced with the aim of improving bulk water supplies to enable municipalities to connect more households to their water and sanitation systems. For 2007/08, R300 million is allocated, an amount that will increase to R650 million in 2009/10.

Capacity building

In order to develop local government capability for sustained service delivery, the National Treasury plans to spend R1.4 billion over the next three financial years to modernise local government budgeting and financial management systems and to improve compliance with the Municipal Finance Management Act. An additional R742 million will be channelled during the next three financial years to

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municipalities through the Development Bank of Southern Africa's support programme called Siyenza Manje. The aim of the programme is to develop skills in engineering, planning and financial management in municipalities.

Review of financing local government

The National Treasury noted that it is continually exploring efficient options for financing local government with the ultimate aim to ensure that each municipality has a sufficient resource base for executing its constitutional mandate. The local government fiscal framework is thus being reviewed to ensure better alignment between powers and functions, on one hand, and revenue generation and allocations, on the other. Importantly, the manner in which local government exercises its taxing powers should not impact materially on national economic policy imperatives such as inflation targeting. The focus of the review is thus currently on assessing the impact and implementation of the new Municipal Property Rates Act, the alignment between functional and fiscal divisions between district and local municipalities, and the restructuring of the electricity distribution industry (the REDs).

Comment

Along with the general thrust of Minister Manuel's budget speech, local government's share of the revenue raised nationally reflects local government's critical role in addressing poverty. As the provider of basic services, and for free to poor households, municipalities should receive sufficient funds to meet their constitutional obligations. However, the increase in transfers from the national government should not hollow out local government's large measure of self-sufficiency. As point out above, municipalities on the whole collect 85% of their own revenue. This principle reinforces accountability of municipal councils to their community. It is thus important that in the development of new taxing powers to replace the RSC levies, the principle of local financial autonomy is maintained.

Prof Nico Steytler
Editor-in-Chief and Director
Community Law Centre, UWC