# 2011

# Local Government Budgets and Expenditure Review:

# 2006/07 – 2012/13

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# 2006/07 – 2012/13

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# Foreword

The *Local Government Budgets and Expenditure Review* is a valuable resource that assists analysts, policy makers, elected representatives, citizens, academics and practitioners in assessing the impact of government policies and the resources allocated to implement them. It supports Parliament, provincial legislatures and municipal councils in assessing progress made in implementing government programmes funded through the equitable share and conditional grants allocated to municipalities, as well as municipal own revenue raised from local communities. The *Review* will also assist political office bearers and all South Africans in evaluating future plans for critical municipal services such as water, sanitation, electricity, refuse removal, municipal transport, roads and community and recreational facilities. In this way, the *Review* serves as both an accountability and future planning document.

This *Review* contains both financial and non-financial information relating to key municipal functions. While it is evident that the ability of municipalities and municipal entities to collect financial data has improved, it must be acknowledged that a lot still needs to be done to improve local government non-financial data. Only when this is done will it be possible to evaluate the efficiency of spending with greater accuracy. Steps are already being taken in this regard.

The outcomes approach adopted by the Presidency to measure and monitor government performance and the collaborative effort among key government stakeholders to co-ordinate data collection across all spheres of government should contribute towards improving government's ability to collect, use and publish non-financial information on local government.

Revenue and expenditure trends in this *Review* show that local government expenditure continues growing strongly in real terms. Access to service delivery is accordingly improving, particularly in the metropolitan municipalities and other big cities. All this contributes significantly to supporting economic growth, delivering basic municipal services and creating jobs. The *Review* also identifies a range of challenges that will need to be addressed to ensure faster service delivery in the period ahead.

The compilation of this *Review* is a collaborative effort among officials of government. I wish to thank all of them for their contributions.

**Lungisa Fuzile**
**Director-General: National Treasury**

# Technical notes

The notes set out below are intended to assist readers, analysts and users by giving context to the information in the *Review*.

### *General notes on numbers*

Although the financial data in the *Review* covers a seven year horizon (i.e. 2006/07 to 2012/13), the data may not always be strictly comparable. The key reasons for this are as follows:

- The Municipal Budget and Reporting Regulations came into effect on 1 July 2009. These regulations made some changes to the functional and standard classification of municipal accounts. Good progress has been made with the implementation of the new budget formats, but it will take time to ensure complete alignment of accounting information with the new classifications. Indeed this process is only likely to be fully completed with the implementation of a standard chart of accounts for local government.
- As a result of the changes in the budget formats, some amounts recorded under certain items changed due to a change in accounting practice rather than real change in the substance of the transactions and the financial circumstances. This means that amounts were reclassified rather than changed due to the nature of the transactions. This exercise was undertaken by National Treasury and, in our opinion, this is the best set of financial information available given the circumstances. The aim was to prepare a set of numbers that will provide a high level comparison across all the 283 municipalities.
- With the phased implementation of the MFMA, the clause relating to preparation of consolidated financial statements was delayed for all municipalities, but the municipalities and entities were encouraged to adopt it early. This means that in some instances the data of municipal entities may be included in the consolidated numbers and in other instances this may not be the case.
- Since the abolishment of the RSC levies in 2006, the equitable share calculation includes the RSC replacement grant for metros and district municipalities. Equitable share figures may therefore seem inflated from 2006/07 onwards. And since 2009/10 the metros' share of the RSC levy grant has been removed as it has been replaced by the general fuel levy sharing with metros, which metros now report under 'other revenues' as it is an own revenue source.

### *Data sources and reliability*

The main sources of data for the *Review*, and the extent of their reliability, are as follows:

- The 2006/07 to 2008/09 numbers were obtained from the audited annual financial statements and, where applicable, the consolidated annual financial statements of the municipalities and municipal entities. Where available, the previous years' restated numbers from the annual financial statements were used as these take into account the adjustments required by the auditors. However, such restated numbers were not available in all instances, in which case the numbers applicable for that financial year were used. Every effort has been made to compile a reliable set of numbers, but there may still be some shortcomings in the dataset.
- 2009/10 numbers were obtained from two sources, namely (1) the audited annual financial statements of municipalities where they were available at the time of capturing and drafting of the publication and (2) the pre-audit in-year results submitted to councils and National Treasury as part of the monitoring on budget implementation where the annual financial statements have not been finalised. Whereas the reliability of the audited financial statements is high as mentioned above, the reliability of the in-year reports is moderate. This is expected to significantly improve with the new budget and in-year reporting formats and regulations and as the coverage is extended to all 283 municipalities.

- The Medium Term Revenue and Expenditure Framework (MTREF) estimates are based on the budget and related documents of municipalities and their entities as approved by their respective municipal Councils and municipal entities' Boards. The quality of this data improved significantly with the implementation of the Municipal Budget and Reporting Regulations, but is still not of the desired standard as the multi-year planning and budgeting reforms are not yet sufficiently institutionalised in all municipalities. The budget reform programme continues to address this deficiency.
- Data from official publications of other government departments and state owned enterprises have been used. Key sources are the Budget Review (2010 and 2011), Stats SA Census 2001 and the 2007 Community Survey, the national spatial development strategy, latest Auditor–General reports, the provincial budget statements, South African Reserve Bank Quarterly Bulletins, the Department of Water Affairs' water resource strategy and other reports, Eskom's annual report; the National Energy Regulator of South Africa (NERSA), the national Department of Transport; Human Sciences Research Council and the Council for Scientific and Industrial Research. These data sources are generally very reliable.
- Non-government sources such as reports from the United Nations, the World Bank, HIS Global Insights, and the Bond Exchange of South Africa have also been used. These sources are usually secondary and reliability depends to some extent on the interpretations and judgements of the writers of these reports.

The data for the entire 2006/07 to 2012/13 period are based on the 283 municipalities and the municipal boundaries as they existed from 2006/07 to just prior to the municipal elections held on 18 May 2011.

### *Financial years*

A financial year for the municipalities and municipal entities starts from 1 July and ends on 30 June of the following year.

### *Per capita estimates*

Except for instances where it is stated otherwise, estimates of per capita spending are based on Census 2001 and 2007 Community Survey results. Such estimates will be different from those that are calculated using data from other sources.

### *Real growth rates*

When comparing monetary values from one year to another, it is common to adjust the growth rates for inflation. Real growth rates in this publication are calculated using the CPIX.

### *Rounding of numbers*

Appropriation of funds and reporting of expenditure is done in terms of Rand thousands. The majority of the tables in this publication are in Rand millions. As a result of rounding off, some minor deviations may occur, and in certain instances the rounded figures do not sum exactly to the total line.

### *Classification of municipalities*

To facilitate the analysis, the 283 municipalities are divided into groups according to the methodology adopted by the Department of Cooperative Governance, as developed by the Palmer Development Group (PDG). For further details see Chapter 12 Delivering municipal services in rural areas.

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# 1

# Introduction

## Introduction

Local government has a crucial role to play in the new growth path

To meet South Africa's development needs, government has developed a new growth path that has employment creation as its central focus. There is general agreement that job creation makes economic growth more inclusive, and facilitates faster poverty reduction and income redistribution. Local government has a crucial role to play in the new growth path and the realisation of many of government's recently articulated 12 outcomes.

Municipalities continue to face a number of challenges

The *2008 Local Government Budgets and Expenditure Review* highlighted the fact that municipalities faced a range of challenges arising from the high levels of economic growth and urbanisation that characterised the period 2001 to 2008. These challenges remain: the increased demand for economic infrastructure, ageing assets that require upgrading, rehabilitation or replacement, and changes in the location and nature of poverty. However, the economic and fiscal context to address these challenges has changed. Due to the recession, municipal revenues are growing slowly; which makes it all the more important to ensure that spending is prioritised appropriately, and implementation is effective and efficient. Good governance is critical in this regard.

While there are many examples of councils, mayors and municipal managers striving to provide effective leadership and making progress with strengthening governance, there are instances where serious governance shortcomings remain. The systems that are under greatest pressure are procurement, billing and revenue collection, staff appointments and the planning and zoning functions.

The period ahead will see continuing efforts to improve the effectiveness and efficiency of local government so as to ensure that the legislative and fiscal framework is appropriately structured to facilitate the functioning of municipalities in different contexts. While the current system does provide for significant differentiation in the fiscal arrangements of municipalities, these are being further strengthened to ensure that rural municipalities receive a greater share of the funds flowing to local government from the national revenue fund. A separate regulatory framework for urban municipalities is under consideration. The aim is to give them greater autonomy to plan, co-ordinate and manage urban development.

*Since 2008, National Treasury has taken further steps to improve the transparency, credibility, timeliness and usefulness of municipal financial information*

Since 2008, National Treasury has taken further steps to improve the transparency, credibility, timeliness and usefulness of municipal financial information. Key initiatives include the introduction of the Municipal Budget and Reporting Regulations, strengthening of the Section 71 quarterly financial reporting processes, improved monitoring and enforcement of the Division of Revenue Act and the publication of a wider range of municipal financial information on National Treasury's website. Collectively, these initiatives aim to help municipalities realise better value for money in the use of public resources. They also provide councils and communities with key information for holding their municipalities to account.

### Uses of this publication

The main target audiences for this *Review* are people in local government: councillors, practitioners and citizens. The *Review* should help them form an aggregate picture of local government and to situate them in the context of the developmental role that this sphere of government is expected to play. Given the timing of the release of the *Review*, it will assist the new councillors elected on 18 May 2011 to get to grips with many of the challenges confronting them. Policy-makers in other spheres of government will also find the information and analysis useful. Provincial and national legislatures will be able to use the information to strengthen their oversight of government at all levels, through the comparative and historical data on financial performance and, where possible, associated outputs. National and provincial departments sharing functional concurrency with the local government sphere could enjoy similar benefits. Researchers, analysts and investors will find a wealth of information on individual municipalities, categories of municipalities and the sphere as a whole.

## Objectives of this publication

*This Review explores some of the key context differences between rural and urban municipalities*

The 2011 *Local Government Budgets and Expenditure Review* is National Treasury's third publication dedicated to local government financial and fiscal matters. The 2006 *Review* described the basic fiscal and financial position of the local government system, based on the limited data available at the time. The *2008 Review* focused largely on the impact of municipalities on their socio-economic environments – given that municipalities are institutions of democratic local governance that exist to provide basic services to the communities that are living and working in these environments. This *Review* explores some of the key context differences between rural and urban municipalities – highlighting the different kinds of developmental challenges they face, and the need for the regulatory and fiscal frameworks to respond to these differences.

### Data issues

Since the *2008 Review*, there have been a number of key improvements in the scope and detail of data available on local government – primarily driven by the coming into operation of the Municipal Budget and Reporting Regulations. However, it is still going to take a number of years for the benefits afforded by these regulations to flow through to provide a consistent multi-year local government financial dataset. Indeed, the full benefits will only be realised when the standard chart of accounts for local government gets introduced. Nevertheless the improvements that have occurred have facilitated better analysis of municipalities' finances.

*National Treasury now routinely publishes on its website municipalities' adopted budgets, Section 71 quarterly financial information and their annual financial statements*

National Treasury routinely publishes on its website municipalities' adopted budgets, Section 71 quarterly financial information and their annual financial statements. The logistics of managing data from 283 municipalities are very challenging – but gradually municipalities are beginning to take these reporting processes seriously. The aim continues to be that this should be part of a broader exercise to improve the quality of data available on local government and rationalise the number of data requests that are sent to municipalities. In addition, it is hoped that this will encourage empirically driven public interest analysis and debate on issues in local governance and basic service delivery. For more information on the different data sources used and their reliability, please refer to the Technical Notes at the beginning of this *Review*.

## Main themes for the 2011 *Review*

This *Review* focuses on the role municipalities need to play in supporting the new economic growth path and the realisation of government's outcomes through exploring three main themes:

*What is the performance of local government in supporting economic growth?*

First, the *Review* investigates the performance of local government in supporting economic growth. It updates previous information on the growth in demand for municipal infrastructure. It assesses the extent to which municipalities have used the opportunity afforded by the recent slower economic growth to address some of the infrastructure backlogs that had arisen and whether municipal infrastructure plans and the quality of services provided is adequate to meet the needs of the new growth path. It analyses trends in municipal capital spending relative to these priorities and provides an initial assessment of a range of services that are important to supporting economic growth.

*What are the different development challenges facing rural and urban municipalities when it comes to fulfilling their development roles?*

Second, the *Review* highlights the different development challenges facing rural and urban municipalities when it comes to fulfilling their development roles – particularly the provision of basic services in support of the government's outcomes. It explores the very different contexts within which rural and urban municipalities operate, and how these different contexts impact upon the finances of rural and urban municipalities, the kinds of service delivery challenges they face, and the choice of technology and service levels appropriate to the rural and urban contexts. This analysis highlights the need to provide for greater differentiation in the design of the local government fiscal framework, and the need for a differentiated approach to the assignment of functions to municipalities, based on their individual capacity to effectively manage them.

*Good governance and accountability are critical to ensuring the effective and efficient stewardship of municipal resources*

Third, the *Review* focuses on the importance of good governance and accountability in ensuring the effective and efficient stewardship of municipal resources, and the ongoing challenges of ensuring that proper and ethical standards of governance and administration are upheld. It highlights the further steps taken to improve the quality and usefulness of municipal financial information. It also re-emphasises the significant challenges that exist with the capacity of municipal Budget and Treasury Offices, and the importance of stabilising the senior managements of municipalities.

## Key issues identified

This *Review* identifies the following trends that are impacting on the performance of municipalities in combating poverty and supporting economic growth:

*The quality of leadership and governance is critical to how a municipality performs*

First, the quality of leadership and governance is critical to how a municipality performs. Effective leadership and good governance contribute enormously to ensuring a municipality makes positive progress in delivering services and extending infrastructure. To improve the capacity of municipalities to perform their functions, there is an urgent need to stabilise the senior management cadre of municipalities. Appropriate technical skills need to be in place.

*The municipal budget must be funded in accordance with legal requirements to ensure it remains a going concern able to sustain and extend services*

Second, to ensure municipalities remain going concerns, able to sustain existing services and progressively extend services, they need to ensure that the municipal budget is funded in accordance with the legal requirements set out in the Municipal Finance Management Act (2003). If a municipal budget is unfunded, it is not a credible budget – either the revenue projections are unrealistic, the operating expenditures are too high, or the capital budget is too ambitious. In most instances there are problems in all three areas. Correcting these problems involves going back to basics – and ensuring that the municipality only budgets to spend what it will realistically collect in revenue, eliminates all non-priority spending and has adequate cash reserves to back its existing obligations.

*A major part of the challenge is to get the basics of cash management and revenue management right*

A major part of the challenge is to get the basics of cash management and revenue management right. This means understanding the relationship between financial planning and effectively managing municipal cash resources and ensuring regular bank reconciliations of municipal accounts are undertaken. In respect of revenue management it means paying attention to the integrity of billing information, the accuracy of bills and having dedicated managers able to build administrative implementation systems that integrate each component of the revenue value chain. In addition, a careful balance will need to be struck between adjusting taxes and tariffs to cover the full, long term costs of service delivery and improved expenditure efficiencies.

Managing necessary price increases will require a long term view (based on new tariff setting models) and sensitivity to growing pressures on household budgets. Such increases will also need to be mitigated by improved expenditure efficiencies that increase productivity in all services.

Third, there is an urgent need for all municipalities to pay greater attention to maintaining their existing assets. Systems of asset management and levels of spending on repairs and maintenance need to be improved. To assist in financing this spending it is important that tariffs for the trading services are cost reflective, incorporating all the input costs associated with the production of those services. The clarification of the institutional responsibility for electricity distribution should lay the foundation for improved management of electricity assets.

*All municipalities need to pay greater attention to maintaining their existing assets*

Fourth, municipalities need to revisit how they fund their capital budgets. Generally, national capital grants are intended to finance the rollout of infrastructure for addressing service delivery backlogs and extending access to basic services. Municipalities are still expected to fund the on-going development and extension of infrastructure related to the economic and trading services for which they are responsible. To do so, municipalities need to examine the balance between their operating budgets and capital budgets, and ensure they structure their operating budgets so as to generate the surpluses required to fund infrastructure. Also, creditworthy municipalities need to explore opportunities for leveraging private finance for the expansion and delivery of services, especially those that support local economic development. There is considerable scope for expanding the use of development charges to finance infrastructure investment, based on the principle that direct beneficiaries of services should shoulder the associated costs.

*Municipalities need to revisit how they fund their capital budgets*

Fifth, in order to combat poverty more effectively, municipalities need to reconceptualise their current programmes to ensure greater access to basic infrastructure and services. Here, effective spatial planning and land use regulations governing development are crucial. While improving the access of poor households to the urban economy requires better use of strategically located urban land, municipal infrastructure investment decisions can be used creatively to provide appropriate incentives to the private sector. For example, the location of bulk infrastructure obviously influences the private sector's decisions about where to invest and set up their businesses within a municipal jurisdiction. However, municipalities will only be able to guide private sector investments towards efficient and pro-poor development outcomes if they are able to spatially co-ordinate public investments across housing and infrastructure sectors. This needs to be done in ways that improve the access of poor households to economic opportunities as well as public services. It is within this context that the devolution of the housing and public transport functions to municipalities is very important.

*Municipalities need to reconceptualise their current programmes for combating poverty*

There is also considerable scope for municipalities to generate more employment through their activities. A range of opportunities for labour intensive programmes and service delivery practices have not

*Municipalities need to generate more employment* been adequately explored. Domestic solid waste and public cleansing activities, in particular, seem to provide good opportunities for using comparatively unskilled labour. This could contribute significantly to government's job creation objectives without undermining the financial position of municipalities.

*More inputs are required from national government to improve municipal capacity*

Sixth, more inputs are also required from national government to contribute to the improvement of municipal capacity. The following technical functions require particular attention: sewerage and water treatment plant operators, road maintenance supervisors, health inspectors and planning and project managers. In particular, there needs to be better co-ordination between policy instruments. For example, grants may be squeezing out borrowing and community/user contributions and undermining sound asset management practices. Greater emphasis needs to be placed on the self-financing of the trading services, the transparent operation of subsidies and clear incentives for municipal performance. It is hoped that the steps that national government has taken to restructure the capacity support programmes to local government will ensure better targeting of support.

Finally, ways of extending the differentiated approach to the local government fiscal framework need to be pursued so that the more capable municipalities are able to exercise greater discretion in the way they pursue their developmental mandates, and municipalities with low fiscal capacity are equitably supported.

## A summary of the chapters

The 2011 *Review* is made up of thirteen chapters that are divided into four parts. The first part of the *Review* looks at the context for local governance, the second part considers the financing of local government and key financial management issues, the third part investigates trends within the major services provided by municipalities and the final part looks at the contextual and developmental differences between rural and urban municipalities, and the need to adopt a differentiated approach to the local government fiscal framework in respect of these municipalities.

The first part consists of two chapters. *Chapter 2 The socio-economic and fiscal context for local government*, highlights the wide variation in social and economic contexts among South Africa's 283 municipalities. It outlines the key components of national government's fiscal policy stance that address the major social and economic trends, highlights the importance of adopting differentiated policies to local government and the importance of getting municipal governance right to ensure greater effectiveness. *Chapter 3 Intergovernmental relations and the local government fiscal framework* explains local government's position and role within South Africa's system of intergovernmental relations, describes the key elements of the local government fiscal framework and how it relates to municipalities' service delivery responsibilities, and highlights the important role municipal councils play in ensuring the effective management of municipal resources.

The second part consists of four chapters that look at the financing of local government and key financial management issues. *Chapter 4 Revenue and expenditure trends in local government* provides a broad overview of intergovernmental transfers and the financial performance of municipalities. It highlights five issues – the need to get the basics right in relation to revenue management and the collection of consumer debtors, under-pricing of services, inadequate maintenance expenditures by municipalities and the need to curb spending on non-priorities. *Chapter 5 Financial management and MFMA implementation* focuses on continuing initiatives to reform municipal financial management, particularly measures to strengthen the framework for aligning municipal plans and budgets, initiatives to strengthen oversight through improved transparency and reporting practices, and national government programmes to support institutional strengthening and capacity building. *Chapter 6 Leveraging private finance* notes the huge demands placed on municipalities for responding to local social and economic needs. It highlights initiatives to strengthen the municipal borrowing markets, including the bond market and the opportunities afforded by development charges, land leases and public private partnerships. *Chapter 7 Managing municipal personnel* considers trends in municipal employment. It highlights the modest contribution that municipalities make to overall employment. Personnel expenditure has been growing strongly, but with little noticeable impact on services. This raises questions about the effectiveness of municipal performance management systems.

The third part investigates municipal performance in the delivery of major services. *Chapter 8 Water and sanitation* highlights emerging challenges in the water and sanitation sector, specifically those related to system losses arising from inadequate maintenance. Importantly, it highlights emerging problems in the pricing of water services. *Chapter 9 Electricity* outlines the structure of the electricity sector in South Africa and some of the challenges it is facing. Again, issues of asset maintenance and pricing are highlighted as key challenges facing the electricity distribution industry. *Chapter 10 Roads* considers the current demand for municipal investment in roads in the context of limited public expenditure on the sector and an environment of institutional overlap and uncertainty. *Chapter 11 Solid waste services* provides an overview of institutional arrangements and financing for the provision of solid waste services, access to solid waste services and the challenge of waste minimisation, recycling and energy recovery.

The final part consists of two chapters that explore the service delivery contexts of smaller municipalities versus those of the metros and the secondary cities. *Chapter 12 Delivering municipal services in rural areas* explores the distinguishing features of rural municipalities and some of the specific challenges they face when delivering services and raising own revenues. *Chapter 13 Cities and the management of the built environment* reviews the demographic, economic and spatial challenges that confront South African cities and the challenges in current fiscal and institutional arrangements that complicate the ability of city administrations to manage the built environment. It also reviews public expenditure on public transport, housing and community assets.

## Conclusion

The environments in which South Africa's 283 municipalities operate differ considerably. The varied demographic and social trends and the varying spatial implications of national fiscal policy will all require vastly different policy responses from individual municipalities.

All municipalities must reconcile the need to fund service improvements, through price increases, with the imperative of ensuring that household bills remain affordable. Short term price increases seem to be unavoidable for the major municipal services. Over the medium term, however, municipalities will need to consider mechanisms to improve the efficiency of their expenditures. This will not only support local economic development, but also provide scope for more aggressive programmes to combat poverty.

National fiscal policy gives municipalities the space to respond appropriately to this challenge. Increased grant resources can fund the cost of necessary institutional reforms to improve expenditure efficiencies of municipal services. Exploring alternative funding mechanisms will enable municipalities to leverage their development potential and facilitate more rapid expansion of services.

The ability of municipalities to rise to these challenges will ultimately be determined by the quality of their governance and administrative practices. Stronger, more participatory governance practices will, however, only have a meaningful effect if municipalities provide stable and attractive work environments. Ultimately, councils must ensure that they have the right people in the right places to lead their municipal administrations and provide the technical expertise required to deliver services.

# 2

# The socio-economic and fiscal context of local government

## Introduction

South Africa's municipalities operate in a wide range of geographical, economic and social contexts. This was highlighted in the *2008 Local Government Budgets and Expenditure Review* using mainly information from the 2007 Community Survey undertaken by Statistics South Africa. The national census being planned by Statistics South Africa for October 2011 will provide a valuable update on municipalities' differing contexts – particularly the demographic trends over the last number of years. It is envisaged that this new information will greatly assist the refinement of policies and fiscal arrangements for local government, as well as facilitate better municipal planning.

*The economic recession affected some municipalities more than others due to the particular characteristics of their local economies*

While the economic recession in 2009 has affected all municipalities, some have been more affected than others due to the particular characteristics of their local economies. Those municipalities whose economies are predominantly trade and manufacturing based tended to be most affected, as job losses were concentrated in these sectors. The decline in employment has placed pressure on households' ability to pay municipal accounts; businesses have also been scaling back on the consumption of municipal services to save costs. Both these factors have placed pressure on municipal own revenues.

While the 2010 FIFA World Cup provided some relief from the recession, it is appropriate to review the lessons learned with a view to strengthening the country's ability to address the key development challenges facing it.

The economy is recovering, but employment growth remains very low. Consequently, municipal own revenues remain under pressure. The national fiscal framework also remains constrained. Despite this, national government has sought to minimise the impact on national transfers to local government, which have continued to grow more rapidly than general government expenditure.

*The local government fiscal framework needs to be progressively reformed to better reflect the different fiscal capacity of municipalities*

A key challenge going forward is to ensure that the local government fiscal framework is progressively reformed to better reflect the different fiscal capacities of municipalities. This will entail re-examining the different revenue streams available to municipalities and ensuring that the division of the local government equitable share targets the poorest municipalities. It will also be important to re-examine the design of conditional grants with a view to putting in place appropriate incentives to ensure that they are spent effectively.

However, the greatest challenge facing local government is the decline in public trust in municipalities. This is being reflected in various ways: increased public protests, more militant ratepayer associations, as well as in public opinion surveys. There is growing public frustration with poor governance and corruption, resulting in poor service delivery in many municipalities.

This chapter gives an overview of:

- socio-economic trends and local government
- the economic outlook and local government
- national fiscal policy and local government
- applying the differentiated approach to local government
- governance: the key to effective municipalities.

## Socio-economic trends and local government

Since the *2008 Local Government Budgets and Expenditure Review* was released, there have been a number of significant developments in the socio-economic context of local government, such as the economic recession, rising unemployment and the 2010 FIFA World Cup. There is also strong evidence of ongoing rural-urban migration – although the exact extent is unknown.

### Demographic trends

It was noted in the *2008 Review* that the prevailing trends of rapid urbanisation and a reduction in the average size of households are reshaping the contexts for service delivery and governance in most municipalities in strikingly different ways.

In more rural jurisdictions, the out-migration of individuals to urban areas has been accompanied by falling average household sizes. This reduces the number of persons reached by each household service connection, while simultaneously adding to backlogs in the urban centres. In larger urban areas, the process of rapid population growth and falling household size extend the service delivery challenge facing these municipalities. In addition, HIV and AIDS continues to fundamentally alter the definition of household units, with an increased prevalence of child-headed and multi-family units that have lost their primary income earners to illness or death. Most directly, this presents municipalities with more of a challenge when it comes to implementing their indigent policies and generating revenue.

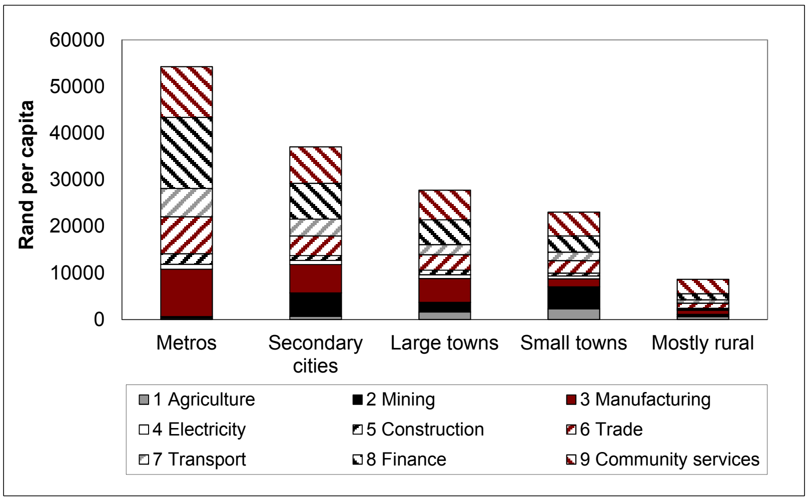
These trends highlight the importance of the national census being planned by Statistics South Africa for October 2011. It is envisaged that by using geographical mapping technologies to plot the dwelling point information gathered through the census, municipalities will have a valuable tool for analysing and understanding their differing contexts – particularly the demographic trends over the last number of years. It is envisaged that this tool will greatly facilitate municipalities' spatial planning – assisting them to deliberately plan to shift the existing apartheid settlement patterns towards more inclusive human settlements.

*The national census in October 2011 will provide municipalities with a valuable tool for analysing and understanding their differing contexts*

### Economic activity

There is significant variation in the level and nature of economic activity across municipalities. The following table shows gross value added (GVA) by type of municipality.

**Figure 2.1 GVA per capita by type of municipality, 2009**



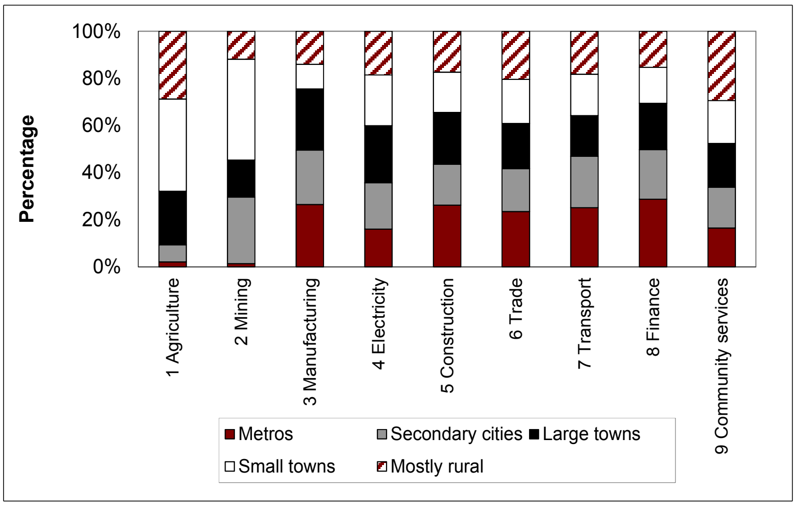

*Source: HIS Global Insight, September 2010*

Figure 2.1 shows the strong bias in most economic sectors towards larger, more urban municipalities and the contrasting weak economic base of mostly rural municipalities. This highlights the need for the local government fiscal framework to differentiate between urban and rural municipalities in the allocation of taxing powers and the design and targeting of transfers from national government.

Figure 2.2 shows that mostly rural municipalities and small towns are predictably reliant on agriculture, fishing and forestry activities, while the secondary and tertiary economic sectors are more dominant in metropolitan areas. The mining and quarrying sector is most dominant in secondary cities, reflecting both the location of these activities and their significant contribution to the development of these regions. These differences underscore the need for individual municipalities to pursue vastly different infrastructure investment and service delivery strategies. Declines in the dominant sectors of a local economy can have knock-on effects for household spending, which ultimately impacts on municipal revenues.

*Because of the differences in their local economies, different municipality types need to pursue different infrastructure investment and service delivery strategies*

**Figure 2.2 Share of economic sector by type of municipality, 2009**




*Source: HIS Global Insight, September 2010*

### Trends in unemployment

Total employment declined by more than one million jobs (8 per cent) between the fourth quarter of 2008 and the second quarter of 2010. Job losses were concentrated in the trade, manufacturing and construction sectors. The official unemployment rate at the end of August 2010 reached 25.3 per cent, and labour force participation (the percentage of working age adults with work or actively seeking work) fell sharply, because many people were discouraged and stopped looking for work.

*The decline in employment has a direct impact on the affected households' ability to pay municipal bills*

The decline in employment has a direct impact on the affected households' ability to pay municipal bills. In June 2008, outstanding debtors stood at R37 billion or 39 per cent of municipal own revenue. In December 2010, outstanding debtors stood at R62 billion or 30 per cent of own revenue. So while there has been an increase in the level of debtors, there has been a decline in debtors as a percentage of own revenues. Part of this can be attributed to the rapid increase in own revenues due to the increase in electricity tariffs, as well as to debt write-offs. In addition, certain municipalities have been paying greater attention to revenue management.

Government's new growth path aims to substantially increase the number of jobs created through economic growth. However, it is likely to take some time before these initiatives begin to bear fruit. In the interim, employment is expected to rise gradually as growth accelerates. As a result, households' ability to pay for municipal services is unlikely to recover at the same rate as the recovery in economic growth – and so municipal own revenues will remain under pressure for some time.

### Legacy of the 2010 FIFA World Cup

From the outset, national government viewed the hosting of the 2010 FIFA World Cup as a catalyst for investments in both sport and economic infrastructure, as well as for skills development and employment creation, rather than just a once-off event. To this end, 24 priority initiatives were identified between 2005/06 and 2010/11, and national government allocated R33.4 billion to these initiatives. Projects included the stadiums and training venues, upgrading of airports and rail-links, rapid bus transit systems, telecommunications and safety and security services.

The plans that the nine host cities developed to host the event included stadium development, transport improvements, electrical reticulation upgrades, health facilities, disaster management, city beautification, marketing and operational plans. National government departments, through a series of bilateral meetings with the host cities and the use of conditional grant instruments, assisted with funds to implement the plans. The host cities funded any shortfall from their own resources.

*The World Cup's greatest legacy lies in the way it changed the world's perceptions about South Africa*

The World Cup's greatest legacy probably lies in the way it changed the world's perceptions about South Africa, and South Africans' own perceptions of themselves. The impact this will have on future business investment decisions, tourism and how the country manages its development challenges can only be guessed at this point, but it is likely to be significant.

*The hosting of the event provides municipalities with important lessons to be learnt*

While there are many lessons to be learnt from the hosting of the event, key lessons relevant to addressing the country's development and service delivery challenges include:

- Success depends on hiring the best – people with advanced conceptual, project management and project execution skills are required to increase the pace of service delivery.
- Core 'anchor management tools' are required to focus and instil discipline on the institutions involved in service delivery projects.
- A forward-thinking approach to risk management needs to be adopted so that early remedial action can be taken.
- Ring-fenced bank accounts for managing very large projects to control costs and prevent leakage need to be used.
- Detailed cash-flow planning and complete transparency on all contract payments are essential.
- A specialist oversight team which is capable of making strategic, solution oriented interventions to ensure completion of the project needs to be established.

These lessons apply to all spheres of government. However, they are particularly relevant to municipalities.

## The economic outlook and local government

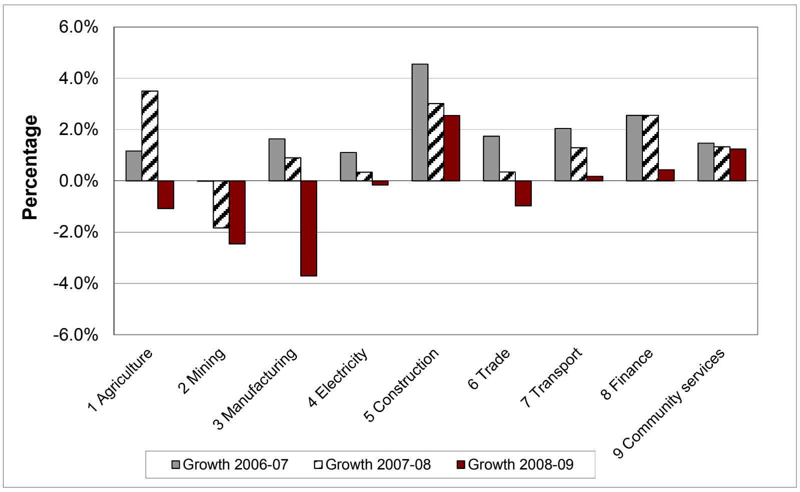
The 2011 Budget Review provides a more detailed analysis of the current economic outlook. It notes that the recovery in global demand has benefited South Africa by supporting higher prices for the country's major commodities. The domestic economy grew by an estimated 2.7 per cent in 2010 as household demand strengthened, supported by expansionary fiscal and monetary policies and lower inflation.

Real GDP growth is expected to reach 3.4 per cent in 2011, 4.1 per cent in 2012 and 4.4 per cent in 2013. At these rates, it will take some time before the economy reaches full capacity.

*Wide variations in growth trends between different sectors of the economy place different pressures on individual municipalities*

Wide variations in growth trends between different sectors of the economy place different pressures on individual municipalities, depending on the sectoral make-up of their local economies. The sectors most affected by the economic recession were manufacturing, mining and trade. 2009 and 2010 were also difficult years for the agricultural sector. It follows then that those municipalities whose economies are strongly reliant on these sectors will take longer to recover from the effects of the recession.

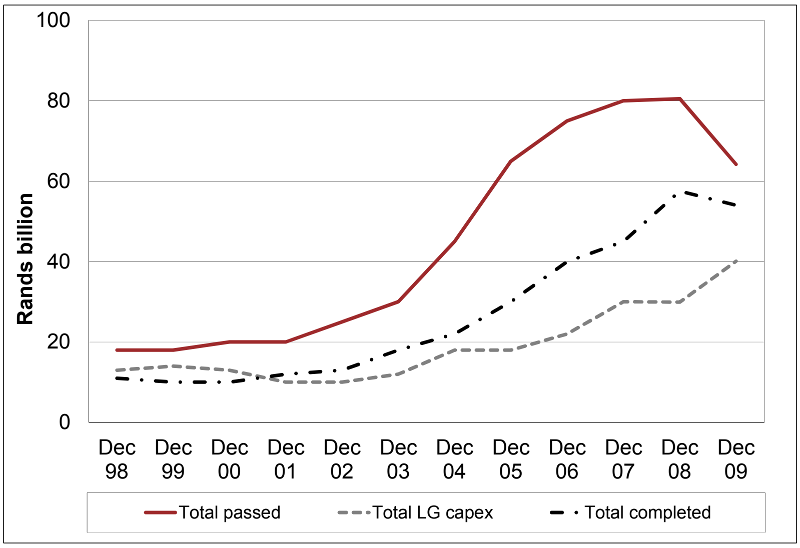
**Figure 2.3 Percentage growth by economic sector, 2006-2009**




*Source: HIS Global Insight, September 2010*

On the upside, the economic recession and slower growth prospects gave municipalities an opportunity to gain some ground on the backlogs in the demand for municipal infrastructure and services. This has also been assisted by the acceleration of projects in preparation for the 2010 FIFA World Cup. Figure 2.4 shows the gap between municipal capital expenditure and the value of buildings completed, which serves as a proxy for demand for municipal infrastructure.

**Figure 2.4 Buildings plans passed versus investment in municipal infrastructure, 1998-2009**




*Source: Statistics South Africa. Selected building statistics of the private sector as reported by local government institutions, 2009*

The trend shown mirrors the declining share of gross fixed capital formation by general government between 2000/01 and 2006/07 (of which municipalities contributed approximately 36 per cent). This was due to the rapid expansion in investment by the private sector and public corporations. The municipal share of public infrastructure expenditure by general government falls from 38.2 per cent in 2007/08 to 33.4 per cent in 2010/11. Capital expenditure continues to fall below budgeted amounts. However, municipal performance has improved from 72 per cent in 2006/07 to 85 per cent in 2008/09, before declining to 80 per cent in 2009/10.

The reasons for municipal underspending on infrastructure are:

- unrealistic budget targets resulting in funding shortfalls, particularly due to low levels of funding from internally generated funds
- inefficient supply-chain management
- lack of capacity to plan and fulfil grant conditions.

Economic developments continue to create pressures on municipalities to expand local infrastructure. Municipalities need to address capacity constraints through increasing the supply of local infrastructure and services, as well as through structuring tariffs to moderate the growth in consumption – particularly of water. Both of these requirements imply that tariffs for municipal services will need to increase. Infrastructure investment requires additional resources, while increasing the price of municipal services is the most effective way of getting consumers to moderate their use of water and electricity.

The major challenge facing municipalities is to reconcile the need for price increases with the imperative of ensuring that services remain affordable to consumers. Ideally, price increases should be balanced with efforts to improve internal cost efficiencies. Stepped tariffs (or inclining block tariffs) are also necessary to protect poor households.

*Most municipalities do not operate their trading services as full cost centres with applied business logic*

As noted in the *2008 Review*, expenditure side productivity improvements remain largely unexplored in municipalities. Most municipalities do not operate their trading services as full cost centres with applied business logic. Few municipalities operate coherent or effective public works programmes.

Measures by municipalities to reduce the costs of doing business in their jurisdictions, through streamlining by-laws and development approvals, may provide some scope for offsetting the negative effects of price increases without expenditure side reforms, but this cannot be the only solution.

## National fiscal policy and local government

The national fiscal stance for 2011/12 to 2013/14 targets a combination of revenue and expenditure that will enable government to pay for existing programmes, while reinforcing the sustainability of the public finances. The main features include higher GDP growth and reduced inflation, increased tax revenue and a reduction of debt stock as a percentage of GDP over the long term.

*The national budget policy framework is informed by the requirements of the new growth path*

The national budget policy framework is informed by the requirements of the new growth path, in which six key sectors and activities have been identified for unlocking employment potential. These are:

- infrastructure, through the expansion of transport, energy, water, communications and housing
- agriculture and the agro-processing sector
- mining and mineral beneficiation
- the green economy and associated manufacturing and services
- manufacturing sectors identified in the industrial policy action plan
- tourism and selected services sectors.

*Municipal expenditure makes a significant contribution towards alleviating poverty and economic development*

National fiscal policy continues to recognise that municipal expenditure makes a significant contribution towards alleviating poverty and economic development: municipalities contribute to providing a social wage through providing free basic services to poor households; and municipal infrastructure investment contributes to total fixed capital formation by the public sector and the provision of associated services is critical for economic activity and household welfare.

National government's fiscal policy has four implications for local government:

First, government has again sought to insulate local government from the ongoing impact of the economic downturn. The increases in government spending favour local government and result in additional resources being made available to municipalities. Due to the tight fiscal circumstances, the pace of increase is slower than in the past.

Nevertheless, local government's share of nationally collected revenues continues to increase relative to the national and provincial spheres. Table 2.1 sets out the division of nationally raised revenue from 2011/12 to 2013/14, which is the most recent information. Table 4.1 in Chapter 4 provides the MTEF information relevant to the period of this *Review*, 2006/07 to 2012/13.

**Table 2.1 Division of nationally raised revenue, 2007/08 – 2013/14**

| | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | % Ave annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Revised | Medium-term estimates | | | 2007/08 - | 2010/11 - |
| R million | | | | Estimate | | | | 2010/11 | 2013/14 |
| **National departments** | **242 580** | **289 236** | **345 366** | **359 120** | **380 154** | **408 439** | **439 049** | **14.0%** | **6.9%** |
| **Provinces** | **207 505** | **246 836** | **293 164** | **323 080** | **357 929** | **380 449** | **404 251** | **15.9%** | **7.8%** |
| Equitable share | 171 054 | 201 796 | 236 891 | 265 139 | 288 493 | 305 725 | 323 604 | 15.7% | 6.9% |
| Conditional grants | 36 451 | 45 040 | 52 073 | 57 941 | 69 436 | 74 724 | 80 647 | 16.7% | 11.7% |
| Gautrain loan | – | – | 4 200 | – | – | – | – | - | - |
| **Local government** | **38 482** | **45 488** | **51 537** | **61 152** | **70 171** | **77 029** | **82 316** | **16.7%** | **10.4%** |
| Equitable share | 20 676 | 25 560 | 23 845 | 30 559 | 34 108 | 37 573 | 39 960 | 13.9% | 9.4% |
| Conditional grants | 17 806 | 19 928 | 20 892 | 23 051 | 27 490 | 30 416 | 32 743 | 9.0% | 12.4% |
| General fuel levy sharing with metropolitan municipalities | – | – | 6 800 | 7 542 | 8 573 | 9 040 | 9 613 | - | 8.4% |
| **Total** | **488 567** | **581 560** | **690 067** | **743 352** | **808 254** | **865 917** | **925 616** | **15.0%** | **7.6%** |
| **Percentage share** | | | | | | | | | |
| *National* | *49.7%* | *49.7%* | *50.0%* | *48.3%* | *47.0%* | *47.2%* | *47.4%* | | |
| *Provincial* | *42.5%* | *42.4%* | *42.5%* | *43.5%* | *44.3%* | *43.9%* | *43.7%* | | |
| *Local* | *7.9%* | *7.8%* | *7.5%* | *8.2%* | *8.7%* | *8.9%* | *8.9%* | | |

*Source: National Treasury Budget Review 2011*

*Fiscal policy recognises the important role of local government and the need to channel more resources to it*

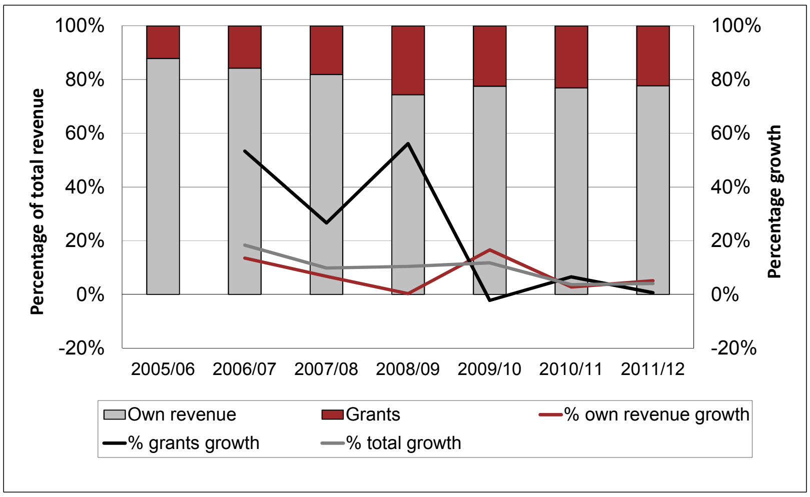
Table 2.1 shows that direct transfers to local government grow by R21 billion over the medium term, of which R5.1 billion is additional to the baseline. National transfers to local government grow by 10.4 per cent between 2010/11 and 2013/14, which is significantly higher than the growth in total government expenditure of 7.6 per cent for the same period. This suggests that fiscal policy recognises the important role of local government and the need to channel more resources to it.

Several amendments have been made to the local government fiscal framework over the last few years to direct more funding towards poor municipalities. A comprehensive review will be undertaken over the medium term that may lead to significant changes in the future configuration of the local government fiscal framework.

*One objective of the Municipal Budget and Reporting Regulations is to ensure that municipal budgets are funded, and that there is better management of municipal cash resources*

Second, transparent and responsible fiscal policy has created a comparatively stable economic and fiscal environment for municipalities to operate in. Figure 2.5 shows that current trends in national transfers to local government are sustainable over the medium term. This is complemented by a provision in the annual Division of Revenue Act that enables municipalities to pledge conditional grant transfers to accelerate capital spending. In addition, this stability enables more accurate planning and better financial management by municipalities. The introduction of the Municipal Budget and Reporting Regulations in July 2009 has placed greater emphasis on ensuring that municipal budgets are funded, and on better management of municipal cash resources.

**Figure 2.5 Revenue trends per major source, 2005/06 – 2011/12**




*Source: National Treasury local government database*

Third, the prudent fiscal stance of national government provides room for expanded borrowing by municipalities. However, as table 2.2 shows, municipalities generally are not fully utilising the borrowing space available to them. Government has also increased the callable capital of the Development Bank of Southern Africa (DBSA) to R20 billion to facilitate greater scope for lending to municipalities.

**Table 2.2 Public sector borrowing requirement[1], 2007/08 – 2013/14**

| R million | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Revised Estimate | | Medium-term estimates | |
| **National budget** | **-19 352** | **27 158** | **167 518** | **143 361** | **159 066** | **161 713** | **148 715** |
| Extraordinary payments | 776 | 4 284 | 671 | 802 | 150 | – | – |
| Extraordinary receipts | -1 850 | -8 203 | -6 435 | -3 148 | -1 350 | – | – |
| **Borrowing requirements** | **-20 426** | **23 238** | **161 754** | **141 015** | **157 866** | **161 713** | **148 715** |
| Social security funds | -8 614 | -12 362 | -10 624 | -10 778 | -10 388 | -11 578 | -11 208 |
| Provinces | -1 062 | 8 927 | 189 | 1 587 | -1 094 | -3 138 | -5 973 |
| Extra-budgetary institutions | -6 155 | 3 802 | 3 993 | 8 183 | 7 215 | 5 870 | 3 052 |
| Local authorities | 4 571 | 13 298 | 16 723 | 7 470 | 9 105 | 8 152 | 8 641 |
| **General government borrowing** | **-31 686** | **36 904** | **172 036** | **147 478** | **162 704** | **161 020** | **143 227** |
| *Percentage of GDP* | *-1.5%* | *1.6%* | *7.0%* | *5.5%* | *5.6%* | *5.0%* | *4.1%* |
| Non-financial public enterprises | 35 503 | 61 804 | 45 325 | 133 731 | 113 718 | 99 063 | 78 733 |
| *Percentage of GDP* | *1.7%* | *2.7%* | *1.9%* | *5.0%* | *3.9%* | *3.1%* | *2.2%* |
| **Public sector borrowing requirement** | **3 817** | **98 708** | **217 361** | **281 209** | **276 422** | **260 083** | **221 959** |
| *Percentage of GDP* | *0.2%* | *4.3%* | *8.9%* | *10.5%* | *9.5%* | *8.1%* | *6.3%* |
| Gross domestic product | 2 078 822 | 2 312 965 | 2 442 593 | 2 666 894 | 2 914 862 | 3 201 299 | 3 536 002 |

1. A negative number reflects a surplus and a positive number a deficit.
2. 2010/11 - 2013/14 are based on National Treasury estimates.
*Source: National Treasury Budget Review 2011*

Finally, for municipalities, expanded public spending by other public entities places pressure on development planning, zoning and environmental approval processes. In addition, it extends demands for municipal infrastructure. For example, a new school or a shopping mall will require infrastructure such as local roads, water, electricity and sanitation. Effective mechanisms to coordinate and sequence public investments are thus required.

## Local government links to the 12 priority outcomes

In January 2010 government adopted 12 outcomes underpinning its long term development strategy. Each outcome has measurable outputs with targets. Furthermore, each of the 12 outcomes has a delivery agreement, which in most cases involves all spheres of government. When municipalities embark on reviewing their integrated development plans (IDPs) and developing their new budgets, they will need to ensure alignment with these outcomes.

*Municipalities need to align their integrated development plans and budgets with government's 12 outcomes*

The text box highlights the areas where municipalities will need to contribute to the realisation of each of the 12 outcomes.

**Government's 12 priority outcomes and the role of local government**

| | Cabinet outcome | Role of local government |
|---|---|---|
| 1 | *High-quality basic education* | • Facilitate the building of new schools through participating in needs assessments done by provinces, identifying appropriate land and facilitating zoning and planning processes<br>• Facilitate the eradication of municipal service backlogs in schools by extending appropriate bulk infrastructure and building connections |
| 2 | *Improved health and life expectancy* | • Many municipalities perform health functions on behalf of provinces<br>• Strengthen effectiveness of health services managed by municipalities by specifically enhancing TB treatments and expanding HIV and AIDS prevention and treatments<br>• Municipalities must continue to improve Community Health Service infrastructure, by providing clean water, sanitation and waste removal services |
| 3 | *All people in South Africa protected and feel safe* | • Facilitate the development of safer communities through better planning and enforcement of municipal by-laws<br>• Direct the traffic control function towards policing high risk violations – rather than revenue collection<br>• Metro police services should contribute by increasing police personnel, improving collaboration with the South African Police Service (SAPS) and ensuring rapid response to reported crimes |
| 4 | *Decent employment through inclusive economic growth* | • Create an enabling investment environment by streamlining planning application processes<br>• Ensure proper maintenance and rehabilitation of essential services infrastructure<br>• Ensure proper implementation of the expanded public works programme (EPWP) at the municipal level<br>• Design service delivery processes to be labour intensive<br>• Improve procurement systems to eliminate corruption and ensure value for money<br>• Utilise community structures to provide services |
| 5 | *A skilled and capable workforce to support inclusive growth* | • Develop and extend intern and work experience programmes in municipalities<br>• Link municipal procurement to skills development initiatives |
| 6 | *An efficient, competitive and responsive economic infrastructure network* | • Ring-fence water, electricity and sanitation functions so as to facilitate cost-reflective pricing of these services<br>• Ensure urban spatial plans provide for commuter rail corridors, as well as other public modes of public transport<br>• Maintain and expand water purification works and waste water treatment works in line with growing demand<br>• Assign the public transport function to cities<br>• Improve maintenance of municipal road networks |
| 7 | *Vibrant, equitable and sustainable rural communities and food security* | • Facilitate the development of local markets for agricultural produce<br>• Improve transport links with urban centres so as to ensure better economic integration<br>• Work with provinces to promote home production to enhance food security<br>• Ensure effective spending of grants for funding extension of access to basic services |
| 8 | *Sustainable human settlements and improved quality of household life* | • Cities to work towards fulfilling the requirements to be accredited for the housing function<br>• Develop spatial plans to ensure new developments are in line with national policy on integrated human settlement<br>• Participate in the identification of suitable land for social housing<br>• Ensure capital budgets prioritise maintaining existing services and extending services |

**Government's 12 priority outcomes and the role of local government *continued***

| | Cabinet outcome | Role of local government |
|---|---|---|
| 9 | *A responsive and, accountable, effective and efficient local government system* | • Adopt IDP processes appropriate to the capacity and sophistication of the municipality<br>• Implement the community work programme<br>• Ensure ward committees are representative and fully involved in community consultation processes around the integrated development plan (IDP), budget and other strategic service delivery issues<br>• Improve municipal financial and administrative capacity by implementing competency norms and standards and acting against incompetence and corruption |
| 10 | *Protection and enhancement of environmental assets and natural resources* | • Develop and implement water management plans to prevent water losses<br>• Ensure effective maintenance and rehabilitation of infrastructure<br>• Run water and electricity saving awareness campaigns<br>• Ensure proper management of municipal commonage and urban open spaces<br>• Ensure development does not take place on wetlands and other sensitive areas |
| 11 | *A better South Africa, a better and safer Africa and world* | Role of local government is fairly limited in this area. It must concentrate on:<br>• Ensuring basic infrastructure is in place and properly maintained<br>• Creating an enabling environment for investment |
| 12 | *A development-orientated public service and inclusive citizenship* | • Continue to develop performance monitoring and management systems<br>• Comply with legal financial reporting requirements<br>• Review municipal expenditures to eliminate wastage<br>• Continue to implement the municipal turn-around strategies<br>• Ensure councils behave in ways to restore community trust in local government |

## Applying the differentiated approach to local government

The Constitution recognises that there will be differences in fiscal capacity among municipalities, and that this should be taken into account in the division of national transfers to local government (see *Chapter 3 Intergovernmental relations and the local government fiscal framework* for further details). There is also a growing sense that current local government funding arrangements may not be addressing the objectives of rural development and redistribution adequately. This has led to calls for a differentiated approach to be implemented for the funding and management of local government.

### Dealing with diversity

*Municipalities differ in terms of size and structure of population, poverty levels, backlogs in basic services, economic activity, employment, land ownership patterns, spatial characteristics, and other factors*

The current legal framework for structuring local government provides for metropolitan, local and district municipalities. These categories (A, B and C) to a large extent determine the powers and functions of the municipality, and so must form the basis of any further differentiation between municipalities. Furthermore, the Municipal Structures Act (1998) provides for functions to be allocated between category B and C municipalities on a differential basis, depending on their capacity – which is assessed by the Municipal Demarcation Board on an annual basis. This allocation of functions must also be taken into account when considering any approach to differentiating between municipalities.

In addition, the preceding sections and other chapters in this *Review* highlight different ways in which municipalities differ from each other. These include: size and structure of population, poverty levels, backlogs in basic services, economic activity, employment, land ownership patterns, spatial characteristics, and a host of other factors. It is also important to take into consideration the institutional capacity of the municipality itself.

What is apparent is that the local government sphere is very diverse and the differences among municipalities are not neatly aligned according to specific groups. This makes categorising municipalities into 'groups' with common characteristics rather difficult – and each classification methodology has its own strengths and weaknesses. National Treasury is of the view that how one classifies municipalities must be specific to the particular purpose of doing so. This means that there cannot be a single approach to classifying municipalities into different groups.

### The differentiated approach in current practice

It should be noted that various approaches to differentiating between municipalities are already being implemented in the design and workings of the local government fiscal framework. These include:

- *Differentiation in the local government equitable share formula.* Each element of the formula is designed to target the allocation of equitable share funding to municipalities on a differentiated basis – primarily according to percentage coverage of basic services, but also on the basis of fiscal and institutional capacity.
- *Differentiation in the allocation of conditional grants.* Each conditional grant is allocated according to specific criteria related to the policy purpose of the grant. For instance the integrated national electrification programme is allocated according to electricity backlogs and the readiness of business plans for electrification projects. The recent introduction of the rural households infrastructure grant further highlights the use of different differentiation criteria depending on the purpose of the grant. The appropriateness of the targeting criteria of each grant is being assessed as part of the conditional grants review that National Treasury is undertaking. Generally, the smaller grants are fairly well targeted. Some inadequacies still exist in the formula and the management processes used to allocate and disburse the municipal infrastructure grant (MIG).
- *Urban settlements development grant.* This grant is a further development of the policy initiative that gave rise to the MIG cities grant. It demonstrates how one differentiation approach can be used to allocate funds, and another approach can be used to manage the disbursement and accountability arrangements for those funds. The metros' shares of MIG funds are determined using the same formula applied to the allocation of the MIG grant, but then through the urban settlements development grant a different management framework has been put in place to allow metros to integrate the use of the funds into their overall capital development plans in exchange for explicit reporting on development outcomes.
- *Differentiation in the allocation of fiscal powers and functions.* Examples of this are:
  - Only metros and local municipalities may levy property taxes.
  - Only metros have been given a share of the general fuel levy.

- Only municipalities that are responsible for delivering a function may charge for that function.

*Greater differentiation in revenue raising powers between metros, local municipalities and district municipalities will be introduced*

It can be expected that when National Treasury issues regulations in terms of the Municipal Fiscal Powers and Functions Act (2007), a greater degree of differentiation in revenue raising powers between metros, local municipalities and district municipalities could be introduced.

### Taking the differentiated approach further

*New municipal level information is required for progress to be made in differentiating between municipalities*

Research on ways of differentiating between municipalities on the basis of fiscal capacity is ongoing. However, it has become evident that new municipal level information is required for progress to be made – hence the critical importance of the national census in October 2011, and ongoing improvements in municipal financial reporting processes.

At this stage, this raises a number of challenges when it comes to (a) developing differentiated policies for local government and (b) refining the local government fiscal framework. Essentially, it means that government needs to proceed with extending the differentiated approach with great care in the absence of credible municipal level information.

*National policy and transfer mechanisms need to better differentiate between rural, more urban and metropolitan municipalities*

Nevertheless, this review seeks to explore key differences between groups of municipalities with a view to informing the debate about how national policy and transfer mechanisms might better differentiate between rural, more urban and metropolitan municipalities, to ensure that they are able to deliver effectively on their functions.

## Governance: the key to effective municipalities

*The greatest challenge facing local government is the decline in public trust in municipalities*

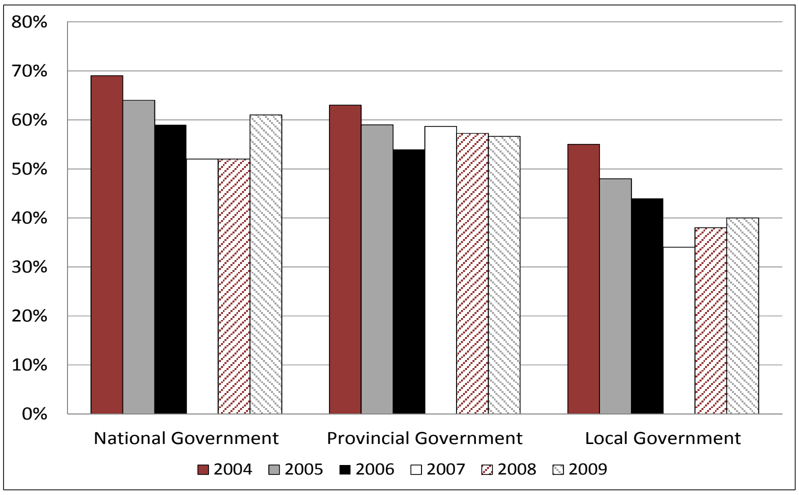
The greatest challenge facing local government is the decline in public trust in municipalities. This is being reflected in public opinion surveys, increased public protests and more militant ratepayer associations. At the heart of the problem appears to be growing public frustration with poor governance, resulting in poor service delivery in many municipalities.

### Crisis in the credibility of local government

*Levels of trust in local government have always been lower than national and provincial government*

Figure 2.6 shows the level of public trust in the three spheres of government as measured by surveys conducted by the Human Sciences Research Council. Since the inception of these surveys in 2004, levels of trust in local government have always been lower than national and provincial government. From a low of 34 per cent in 2007, trust in local government has gradually increased to 40 per cent in 2009. However, the fact that since 2005, less than 50 per cent of people surveyed expressed trust in local government is cause for concern.

**Figure 2.6 Trust in government institutions, 2004 to 2009**



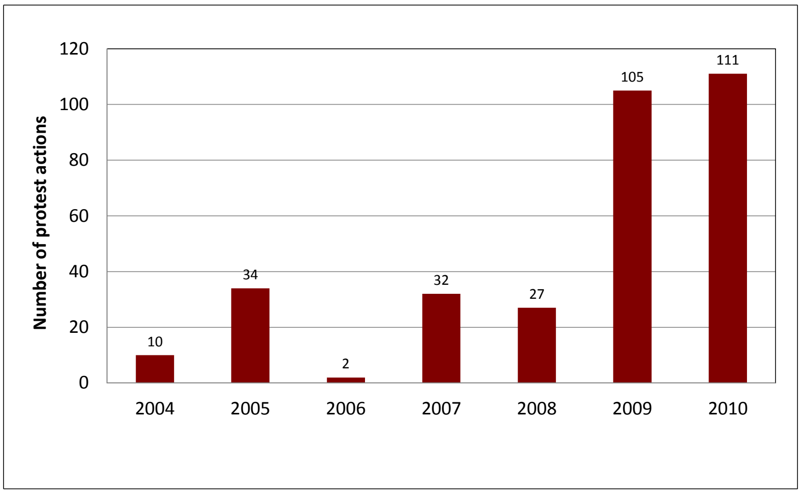

*Source: HSRC South African Social Attitudes Survey (SASAS) 2003–2009*

The high levels of disenchantment with local government finds expression in two main ways: service delivery protests and action taken by the growing number of militant ratepayers associations.

The latest data from Municipal IQ Hotspot Monitor (as at 2 March 2011) indicates that in 2010, there were a record number of 111 protests. The provincial distribution of these protests shows that they were concentrated in Gauteng and Western Cape.

*The 111 service delivery protests that took place in 2010 were concentrated in Gauteng and Western Cape*

**Figure 2.7 Service delivery protests, 2004 to 2010**




*Source: Municipal IQ – 2 March 2011*

While there has been a range of explanations for the growing number of service delivery protests, it would seem that generally poorer communities use these protests to bring their grievances with municipalities to the attention of government.

*Poorer communities use protests to bring their grievances with municipalities to the attention of government*

By contrast, wealthier communities tend to organise themselves into ratepayer associations and seek to engage with municipalities around particular issues, either directly through meetings, or indirectly through letter writing and petition campaigns. According to the National Taxpayers Union of South Africa, ratepayers in 42 towns are currently engaged in legally declared disputes in terms of section 102 of the Municipal Systems Act (2000), and instead of paying rates and

*Wealthier communities tend to organise themselves into ratepayer associations* other service charges over to the municipality, are paying them into trust accounts. In some towns, ratepayer associations have begun to use these funds to do essential maintenance and to pay private companies for the delivery of services.

Both the service delivery protests and actions of ratepayer associations point to the urgent need to improve the service delivery situation in many municipalities.

### Getting governance wrong

To date, there has been a tendency to attribute all failings in municipal performance to a lack of capacity – whether it be individual or organisational capacity. However, when evaluating municipal performance failures, the reality is that many municipal failures can be directly attributed to failures in local political leadership.

Where there are dysfunctional councils and distrust important decisions such as the appointment of senior staff or approvals of plans and budgets get delayed or are not taken. This holds back service delivery.

Provincial governments and national government need to be more proactive in holding municipal councils accountable to the extent provided for in the Constitution. National government has tended to take a lenient approach to applying section 139 of the Constitution. Although this section provides for the dismissal of municipal councils if its financial affairs are in crisis, this has yet to occur. Also, while section 216 enables National Treasury to withhold the transfer of funds to a municipality if it does not comply with prescribed treasury norms and standard (i.e. does not comply with the Municipal Finance Management Act (2003)), this has only ever happened once. Consequently, councils have been allowed to remain in office and have continued to receive transfers from national government despite obvious failures. Generally the interventions that have occurred have been poorly managed and so have not achieved the desired turnarounds.

When governance goes wrong, and concrete steps are not taken to put things right, the municipality’s ability to deliver effective services gets undermined. This impacts on all residents.

### Getting governance right

There are a number of relatively simple things that need to be done to get governance right: First, mayors, councillors and municipal officials need to commit to acting ethically – always seeking the best interests of the municipality and the community as a whole. Second, there needs to be a clear understanding of and respect for the division of roles and responsibilities between the council, mayor and municipal manager as set out in legislation. Third, all appointments need to be on the basis of competence (and nothing else). Fourth, municipal managers need to ensure that the legally required operating policies and procedures are in place and implemented in the day-to-day running of the municipality. Fifth, councils need to fulfill their oversight functions. The establishment of municipal public accounts committees in the larger municipalities is welcomed in this regard.

However, these committees should not be seen as absolving the rest of councils from exercising rigorous oversight.

In addition, government has introduced a range of initiatives to tackle the problems of poor governance:

- The Municipal Budget and Reporting Regulations, which came into effect on 1 July 2009, prescribe the format of municipal budgets and in-year financial management reports. Their aim is to force transparent municipal budgets and so curb malpractices, including corruption.
- The Local Government: Municipal Systems Amendment Act (2011) introduces a range of important reforms. These include barring municipal managers and other managers from holding political office in political parties, regulating the employment of municipal employees who have been dismissed, and prohibiting the employment of a person in a municipality if the post to which he or she is appointed is not provided for in the staff establishment of that municipality.
- National government is currently reorganising the various programmes to provide capacity support to municipalities. The aim is to ensure better overall coordination, improved targeting and closer monitoring of such initiatives.

National Treasury is also working closely with other departments and agencies to improve municipal financial performance and reduce the possibility of fraud and corruption. The approach comprises five broad initiatives, which will include legislative and regulatory reforms:

*National Treasury is working closely with other departments and agencies to combat fraud and corruption*

- Increasing the monitoring capability of government, aimed at early detection of fraud.
- In line with international best practice, transparent public disclosure will be required at each stage of the supply chain process including reasons for award decisions.
- Government will look holistically at identifying procurement requirements that could be better managed centrally, such as the use of transversal contracts for the acquisition of high value and complex goods and services.
- Stiff penalties are proposed for service providers who obtain government contracts fraudulently. Public officials who assist in tender fraud will also be liable for resultant losses incurred by government.
- Tax compliance measures associated with government procurement will be strengthened.

### The importance of the local government elections

The Constitution provides that the first object of local government is to provide democratic and accountable government for local communities. To this end, local government elections are held every five years. The power of the ballot box in addressing failures in local governance should not be underestimated. Elections provide communities with an opportunity to hold their local councillors and

*Elections provide communities with an opportunity to hold their local councillors and the different political parties accountable* the different political parties accountable for their governance performance.

## Conclusion

This chapter highlights the diverse nature of municipalities, and the fact that they operate in a wide range of social and economic contexts. This has meant that while the economic recession in 2009 affected all municipalities, some were more affected than others. The recovery in employment levels is anticipated to take some time, and so municipal own revenues are likely to remain under pressure. Nevertheless, although the national fiscal framework remains tight, government has sought to minimise the impact on national transfers to local government, which have continued to grow more rapidly than general government expenditure.

The 2010 FIFA World Cup provided some relief from the recession, but its greatest contribution has been the way it has changed perceptions about the country. There are also specific lessons from the World Cup that municipalities need to take on board to strengthen their ability to address the key development challenges they face.

While the local government fiscal framework does contain elements that treat municipalities on a differentiated basis, there is a need to re-examine the different revenue streams available to municipalities and ensure that the division of the local government equitable share and conditional grants targets the poorest municipalities. To move forward with policy on a differentiated approach requires accurate information on municipalities. The national census in October 2011 and financial reporting by municipalities is therefore very important.

As noted, the most pressing challenge facing local government is the decline in public trust in municipalities. This is being reflected in various ways: increased public protests, more militant ratepayer associations, as well as in public opinion surveys. There is growing public frustration with poor governance and corruption, resulting in poor service delivery in many municipalities. In this context, local government elections play a very important role in holding mayors, councillors and political parties accountable. However, there is also a need for stronger provincial and national government monitoring, and greater public participation in council processes.

# 3

# Intergovernmental relations and the local government fiscal framework

## Introduction

South Africa has an intergovernmental system that is based on the principle of cooperation between the three spheres of government – local, provincial and national. While responsibility for certain functions is allocated to a specific sphere, many other functions are shared among the three spheres. However, the Constitution specifically envisages that as municipalities develop the necessary capacity, the administration of many functions that are currently the responsibility of national and provincial government will be assigned to municipalities. While this has been taking place, very often the devolution has only been partial – with municipalities not being given the necessary funds, scope of responsibilities or without their being subject to clear forms of accountability for their performance. Over the medium term, government is planning for more functions to be devolved to municipalities. There is therefore a need for clear principles to guide such assignments to ensure that there are appropriate incentives, funding and accountability arrangements.

*The assignment of functions to local government has a direct bearing on the local government fiscal framework*

The assignment of functions to local government has a direct bearing on the local government fiscal framework. Ideally, the framework should provide municipalities with access to revenue sources that are commensurate with the powers and functions that they are responsible for. In this regard, it is important to keep in mind that the *whole* local government fiscal framework is designed to fund local government, and not just the transfers from national government.

It is also important to understand the relationship between the allocation of functions and the fiscal framework, the fiscal effort the municipality makes to collect revenues, the appropriate allocation of those revenues to services, the responsible management of service delivery processes and the effective delivery of services.

*The revenue-service link between municipalities and residents is key to fostering greater accountability*

The revenue-service link between municipalities and residents is key to fostering greater accountability. This suggests that requiring poor households to pay even very small amounts for services may deepen local democracy and municipal accountability.

Municipal councils, mayors and municipal managers are responsible for ensuring that available revenues are collected, resources are allocated appropriately and procurement and service delivery processes are economical, efficient, effective and equitable.

This chapter examines these issues under the following headings:

- intergovernmental relations and the role of local government
- the local government fiscal framework
- services and the local government fiscal framework
- municipal councils' role in the management of resources.

## Intergovernmental relations and the role of local government

Chapter 3 of the Constitution describes the three spheres as being 'distinctive, interdependent and interrelated' and enjoins them to 'cooperate with one another in mutual trust and good faith'. An important element of this cooperative relationship is that there needs to be a clear understanding of each sphere of government's powers and functions to ensure that a sphere of government or organ of state 'does not encroach on the geographical, functional or institutional integrity of government in another sphere'.

In addition to the Constitution, various legislation governs or organises the system of intergovernmental relations (see text box below). Among other things, the legislation formalises the different spheres' roles and responsibilities with regard to various functions and provides for a range of consultative structures.

**Legislation that organises intergovernmental relations**

**Intergovernmental Fiscal Relations Act (1997) –** This Act sets out the process for the division of nationally raised revenues between the three spheres of government. It establishes the Budget Forum, in which local government issues are discussed as part of the national budget process. It also requires that a Division of Revenue Bill is tabled annually, setting out (among other things) the amounts to be transferred to each municipality.

**Municipal Structures Act (1998) –** This Act provides for the establishment of different types of municipalities and the division of powers and functions between local and district municipalities. It also regulates the internal systems, structures and roles of office bearers of municipalities.

**The Municipal Systems Act (2000) –** This Act sets out detailed requirements in relation to community participation, integrated development planning, performance management, administration, service provision and debt collection. It also regulates the publication of by-laws and determines the role of national and provincial government in setting standards and monitoring local government. The Act also governs the assignment of functions to a municipality from another sphere of government.

**Intergovernmental Relations Framework Act (2005) –** This Act provides a framework for the establishment of intergovernmental forums and mechanisms to facilitate the settlement of intergovernmental disputes.

The South African system of intergovernmental relations is complex and continues to evolve as better modes of cooperation and coordination emerge and as functions are shifted between the spheres.

The following key elements and principles underpin the intergovernmental system:

- *Accountability:* Each sphere has specific constitutionally defined powers and responsibilities, is accountable to its legislature or council, and is empowered to set its own priorities. The power of national government to intervene in provincial and local government matters, and provincial governments to intervene in local government matters, depends on whether the relevant sphere fails to carry out an executive obligation.
- *Transparency and good governance:* Accountability of political representatives to the electorate and transparent reporting arrangements within and between spheres is at the heart of the intergovernmental system. While political executives are responsible for policy and outcomes, the accounting officers are responsible for implementation and outputs.
- *Mutual support:* National and provincial governments have a duty to strengthen the capacity of municipalities. Spheres of government must also act cooperatively towards each other, for instance through avoiding legal action until all other mechanisms have been exhausted.
- *Redistribution:* The three spheres all have important roles to play in redistribution, but because inequalities exist across the country, the redistribution of resources is primarily a national function. Where provinces and municipalities undertake redistribution, the challenge is to do this in line with their fiscal capacity and not to undermine economic activity and their financial viability. Redistribution among the three spheres is achieved through the vertical division of revenue. Redistribution among provinces and municipalities is effected through their respective equitable share formulae.
- *Vertical division:* Determining allocations to each sphere of government inevitably involves trade-offs that are made in the course of a comprehensive budget process driven by political priorities, and which covers all aspects of governance and service delivery. Separate and ad hoc requests for funds fragment the coherence of the budget and undermine the political process of prioritisation.
- *Revenue-sharing:* The fiscal system takes into account the fiscal capacity and functions assigned to each sphere. Provinces and municipalities are funded from own revenues, equitable share allocations, and conditional and unconditional grants. The grant system must be simple and comprehensive and not compensate provinces and municipalities that fail to collect own revenues.
- *Broadened access to services:* The Constitution and current government policy prioritises broadening access to services. The responsible spheres are expected to design appropriate levels of

service to meet customer needs in an affordable manner, explore innovative and efficient modes of delivery, and leverage public and private resources to fund infrastructure.

- *Responsibility over budgets:* Each sphere of government has the right to determine its own budget and the responsibility to comply with it. To reduce moral hazard and ensure fairness, national government will not bail out provinces or municipalities that mismanage their funds, nor provide guarantees for loans.

### Intergovernmental forums

*The intergovernmental system depends on well-coordinated policy, planning, budgeting, implementation and reporting*

The intergovernmental system depends on well-coordinated policy, planning, budgeting, implementation and reporting. This is necessary both within spheres and between spheres and is effected through technical, executive and legislative consultative forums.

Municipalities are generally represented on the national intergovernmental structures by 'organised local government' in the form of the South African Local Government Association (SALGA). At the provincial level, municipalities are either represented directly or through the provincial local government associations.

The following intergovernmental forums play an important role in cooperative governance and in shaping policy and resource allocation decisions:

- *Extended Cabinet:* This is made up of the national cabinet, premiers of provinces and the chairperson of SALGA. It is the highest cooperative governance mechanism, advising the national cabinet when it finalises the fiscal framework and the division of revenue on which MTEF budgets are based.
- *The President's Coordinating Council:* This is chaired by the President and comprises the nine provincial premiers, the chairperson of SALGA, the mayors of the metros and the national ministers responsible for cross-cutting functions such as provincial and local government affairs, public service and administration, and finance. Other national ministers may be invited to participate.
- *The Budget Council and Budget Forum:* These are established under the Intergovernmental Fiscal Relations Act (1997). The Budget Council consists of the Minister of Finance and the members of the executive council (MECs) responsible for finance in each of the provinces. The national and provincial spheres consult on any fiscal, budgetary or financial matters affecting provinces as well as any legislation that has financial implications for provinces. The Budget Forum consists of the members of the Budget Council plus representatives of SALGA. It provides a forum for discussing financial matters relating to the local government fiscal framework.
- *MinMECs:* These are sectoral policy forums made up of the national ministers responsible for concurrent functions and their provincial counterparts. SALGA represents local government on a number of these forums.

- *Various technical intergovernmental forums:* These consist of senior officials who provide technical support to the political forums. There are also forums that involve officials from municipalities such as the City Budget Forum.
- *The Financial and Fiscal Commission:* This is an independent constitutional institution that provides recommendations to Parliament and the provincial legislatures on the division of nationally collected revenues between the three spheres of government.

## Allocation of roles and functions between spheres

The Constitution delineates public functions into two categories: those that are concurrent (shared among different spheres) and those that are exclusive (performed by one sphere only).

### *Concurrent functions*

A function is concurrent if more than one sphere of government is responsible for making policy, legislating, administrating or monitoring performance in relation to that function.

*Concurrent functions are shared among different spheres and exclusive functions are performed by one sphere only*

Schedule 4 of the Constitution lists the 'functional areas of concurrent national and provincial legislative competence'. Functions in Part A of Schedule 4 include school education, health services, social welfare services, housing and agriculture. In relation to these functions, national government generally takes the lead in formulating policy, determining regulatory frameworks, setting norms and standards and monitoring overall implementation. Provinces, on the other hand, are mainly responsible for implementation in line with the nationally determined frameworks. This division of responsibilities means that provincial budgets for these functions are far larger than the budget of the relevant national department.

All local government functions listed in Parts B of Schedules 4 and 5 of the Constitution (see detail below) are concurrent functions. This is because, in all instances, either national or provincial government may regulate how municipalities exercise their executive authority in relation to these functions.

### *Exclusive functions*

A function is exclusive if only one sphere of government is responsible for making policy, legislating, administrating or monitoring performance in relation to that function. The Constitution does not define the exclusive functions of national government because it is responsible for all government functions that have not been specifically assigned to either provincial or local government. National government is therefore exclusively responsible for national defence, national fiscal policy, foreign affairs, the criminal justice system (safety and security, courts), higher education and certain administrative functions. These take up a large portion of national government's budget. Provinces have exclusive legislative competence over the functions listed in Part A of Schedule 5 of the Constitution, which include provincial roads, ambulance services and provincial planning. However, national government may legislate in these 'exclusive' provincial functions if it is necessary to maintain essential national standards or for reasons of national security.

*A function is exclusive if only one sphere of government is responsible for making policy, legislating, administrating or monitoring performance in relation to that function.*

*Municipal by-laws may not conflict with either national or provincial legislation*

There are very few, if any, local government functions that can be described as exclusive. In nearly all instances, there is either national or provincial framework legislation. Nevertheless, municipalities do exercise a high degree of autonomy when making by-laws and administrating these functions within the prescribed national or provincial frameworks. It is important to note that municipal by-laws may not conflict with either national or provincial legislation.

### The Constitution and local government's responsibilities

Section 152 of the Constitution sets out the 'Objects of local government' as follows:

**152. Objects of local government**

1. The objects of local government are -
   a. to provide democratic and accountable government for local communities;
   b. to ensure the provision of services to communities in a sustainable manner;
   c. to promote social and economic development;
   d. to promote a safe and healthy environment; and
   e. to encourage the involvement of communities and community organisations in the matters of local government.
2. A municipality must strive, within its financial and administrative capacity, to achieve the objects set out in subsection (1).

The purpose of section 152(2) is to direct municipalities to use their available resources to realise the objects of local government. However, a municipality must do so 'within its financial and administrative capacity'.

Section 153 of the Constitution sets out the 'Developmental duties of municipalities' as follows:

**153. Developmental duties of municipalities**

A municipality must –
   a. structure and manage its administration and budgeting and planning processes to give priority to the basic needs of the community, and to promote the social and economic development of the community, and
   b. Participate in national and provincial development programmes.

*The Constitution requires municipalities to prioritise the delivery of basic services*

There is thus a constitutional requirement that municipalities *prioritise the delivery of basic services* in the way their administrations, planning and budgeting are structured and managed.

Section 156 of the Constitution sets out the 'Powers and functions of municipalities' as follows:

**156. Powers and functions of municipalities**

1. A municipality has executive authority in respect of, and has the right to administer –
   a. the local government matters listed in Part B of Schedule 4 and Part B of Schedule 5, and
   b. any other matter assigned to it by national or provincial legislation.
2. A municipality may make and administer by-laws for the effective administration of the matters which it has the right to administer.
3. …
4. …
5. A municipality has the right to exercise any power concerning a matter reasonably necessary for, or incidental to, the effective performance of its functions.

As noted above, section 153 of the Constitution refers to 'giving priority to the basic needs of the community'. Similarly, section 227 of the Constitution specifies that local government is 'entitled to an equitable share of revenue raised nationally to enable it to provide basic services and perform the functions allocated to it'. It is widely accepted that *basic needs* and *basic services* refer to the same set of functions/services. This set of services is by general agreement regarded as being: water, electricity, sanitation and refuse removal.

*Water, electricity, sanitation and refuse removal make up basic services*

The Municipal Demarcation Board has divided municipal functions into three categories according to its assessment of their relative priority.

**Table 3.1 Priority functions of local government**

| Priority 1 functions | Priority 2 functions | Priority 3 functions |
|---|---|---|
| Water (potable) | Air pollution | Municipal parks and recreation |
| Electricity reticulation | Beaches and amusement facilities | Local sport facilities |
| Sanitation | Cleansing | Public places |
| Refuse removal | Control of public nuisance | Local tourism |
| | Fencing and fences | Local amenities |
| Cemeteries | Sell food to the public | Municipal airport |
| Fire fighting | Noise pollution | Licensing of dogs |
| Municipal health services | Pontoons and ferries | Child care facilities |
| Municipal planning | Pounds | Sell liquor to the public |
| Municipal roads | Street lighting | Markets |
| Storm water | Street trading | Burial of animals |
| Traffic and parking | Trading regulations | Municipal abattoirs |
| Building regulations | | |
| Municipal public transport | | |

*Source: Municipal Demarcation Board, 2005, National Report on Local government Capacity: MDB Capacity Assessment Period 2004/05*

*Note: National Treasury regards 'building regulations' and 'municipal public transport' as priority 1 functions*

The Municipal Demarcation Board's ranking of functions provides a useful framework and municipalities ought to prioritise the priority 1 functions in the way their administrations, planning and budgeting are structured and managed. Nevertheless the specific circumstances within a municipality should also inform the ordering of the priorities and the consequent allocation of resources.

## The municipal planning function

Municipalities are responsible for municipal planning, which encompasses planning related to the spatial, economic and social development of the municipality. Planning is a powerful tool if it informs priorities, budgets and the actual delivery of services.

The main instrument of municipal planning is the five-year integrated development plan (IDP). Each municipal council is required to approve a new IDP in the first year following an election, and then update it on an annual basis. The IDP should be based on long term spatial, infrastructure and finance plans. It should set the priorities for budgets, capital investments and service delivery over the plan's five-year lifespan. The IDP must not simply be a wish list; it should clearly set out what can realistically be achieved given the capacity and resource constraints facing a municipality.

*The main instrument of municipal planning is the five-year integrated development plan*

## Roles of different categories of municipalities

The Constitution provides for three types of municipalities: category A (metros), category B (local municipalities) and category C (district municipalities).

The metros are responsible for all the local government functions within their respective areas of jurisdiction. Each district municipality includes several local municipalities, and the powers and functions assigned to local government in that area are shared between the category B and C municipalities.

The provincial MEC for local government, after receiving advice from the Municipal Demarcation Board, decides which municipalities are authorised for which functions in a particular province. The current division of responsibilities between district and local municipalities needs to be urgently reviewed because it is creating coordination problems and undermining accountability for service delivery.

*National government transfers are made to the municipality that is legally responsible for the function, which is not necessarily the municipality that delivers the service*

There are districts in which some local municipalities are authorised to perform a particular function such as water. In others, the district municipality performs this function and local municipalities are not authorised for the function but provide the service to households under an agency arrangement with the district. The fiscal framework has to be aligned with the legal framework. Hence, national government transfers are made to the municipality that is legally responsible for the function, which is not necessarily the municipality that delivers the service. Most often, it is the district municipalities that have been allocated the function and are receiving the funds. While they are expected to pass the funds on to the local municipalities that perform the functions, very often they fail to do so. Consequently, funds do not follow function. As a result, service delivery is undermined.

## Devolving functions to local government

Functions can be devolved from national and provincial government to local government by delegation or assignment.

When national or provincial government delegates a function to a municipality, it is given responsibility for implementing the function under the authority and direction of the delegating authority. The municipality has to act strictly within the confines of the service level or agency agreement. Provinces often delegate the administration of libraries, clinics, emergency medical services and the implementation of housing projects to municipalities.

Assignment is a more complete way to devolve a function. It can be done either through legislation or by executive decision, and can be to all municipalities or to a specific municipality. The processes set out in sections 9 and 10 of the Municipal Systems Act (2000) are intended to ensure that sufficient funding and capacity building initiatives are made available to municipalities to enable them to successfully carry out assigned functions.

Section 156(4) of the Constitution provides that wherever the decentralisation of the administration of a function to a municipality would facilitate better service delivery, it must be done.

**156 Powers and functions of municipalities**

(4) The national government and provincial governments must assign to a municipality, by agreement and subject to any conditions, the administration of a matter listed in Part A of Schedule 4 and Part A of Schedule 5 which necessarily relates to local government if –

(a) that matter would most effectively be administered locally, and

(b) the municipality has the capacity to administer it.

The legislative authority remains with national and provincial government, while the administration of the function is assigned to the municipality. This means that the municipality is fully responsible for deciding how to carry out the function, the allocation of resources to the function and the actual execution of the function. The municipality is not simply being contracted to do things on behalf of national or provincial government as in the case of a delegation.

To date, few functions have been assigned to municipalities, largely because there has been a perception that assignments have to be done uniformly to all municipalities at once, instead of adopting a differentiated approach as specific municipalities develop the necessary capacity. In addition, national and provincial departments prefer to delegate functions through agency arrangements because this enables them to retain control of the budget, while devolving responsibility for implementation to the municipality. The problem is that this separation of funding and implementation responsibilities often results in unfunded mandates being imposed on municipalities.

*The separation of funding and implementation responsibilities often results in unfunded mandates being imposed on municipalities*

It also means that the advantages of coordinating implementation at the local level are not being fully realised. For example, municipalities are responsible for developing integrated public transport systems while provinces are responsible for licensing public transport operators and subsidising buses, and national government is responsible for passenger rail services. This makes municipalities' task of planning and developing integrated public transport systems exceptionally difficult. Another example is the housing function. Provinces use municipalities as developers for housing projects, but have not assigned the housing function to them. This is despite the fact that well-capacitated municipalities are best placed to plan for the integrated delivery of housing, basic services and transport within the broader spatial development plan of the municipality.

*Well capacitated municipalities are best placed to plan for the integrated delivery of housing, basic services and transport*

Going forward, there is a need to give proper effect to section 156(4) of the Constitution and ensure that functions are assigned to municipalities that have the capacity to administer them effectively. In this regard, government has already indicated that the public transport and housing functions will be assigned to municipalities that have the necessary capacity.

*Government has already indicated that the public transport and housing functions will be assigned to municipalities*

## Capacity support and interventions

An integral part of the intergovernmental system is the responsibility that section 154 of the Constitution places on national and provincial government to support and strengthen the capacity of municipalities to manage their own affairs. There are various national and provincial support initiatives, some of which are described in *Chapter 5 Financial management and MFMA implementation*. In addition,

*Section 139 of the Constitution provides that the provincial executive can intervene in a municipality where it fails to fulfil an executive obligation* section 139 of the Constitution provides that the provincial executive can intervene in a municipality when it fails to fulfil an executive obligation. The same section provides that the provincial executive, or the national executive, *must intervene* in a municipality when it fails to approve a budget or any revenue raising measures necessary to give effect to the budget, or when there is a crisis in its financial affairs. Interventions may include instructing the municipal council to take certain actions, taking over responsibility for particular functions and dissolving the municipal council and appointing an administrator.

## The local government fiscal framework

The constitutional assignment of powers and functions to local government has a direct bearing on the local government fiscal framework. Ideally, the local government fiscal framework should provide municipalities with access to revenue sources that are commensurate with the services they are responsible for providing. Table 3.2 sets out the main sources of local government funding:

**Table 3.2 Sources of local government funding**

| Source of local government funding | Constitutional provisions | Governing legislation |
|---|---|---|
| ***Municipal own revenue sources*** | | |
| Rates on property | Section 229 and 227(2) | Municipal Property Rates Act |
| Surcharges on fees for services provided by or on behalf of the municipality | Section 229 and 227(2) | Municipal Fiscal Powers and Functions Act |
| Service charges/ fees | Section 229 and 227(2) | Municipal Systems Act<br>Municipal Finance Management Act<br>Electricity Act and Electricity Regulation Act<br>National Water Act<br>Provincial land use planning ordinances |
| Other taxes, levies or duties | Section 229 and 227(2) | Municipal Fiscal Powers and Functions Act |
| Administrative fees | | Municipal Systems Act |
| Fines | | National Road Traffic Act |
| Borrowing | Section 230A | Municipal Finance Management Act |
| Credit control and debt collection | | Municipal Systems Act |
| ***Transfers from national and provincial government*** | | |
| Local government equitable share of nationally collected revenues | Section 214 and 227 | Intergovernmental Fiscal Relations Act<br>The annual Division of Revenue Act |
| Fuel levy sharing with metropolitan municipalities | Section 229(1)(b) | The annual Taxation Laws Amendment Act |
| Conditional grants from national government | Section 214(c), 226(3) and 227(1)(c) | Intergovernmental Fiscal Relations Act<br>The annual Division of Revenue Act<br>The annual National Appropriation Act |
| Conditional grants from provincial government | Section 226 | The annual Division of Revenue Act<br>The annual Appropriation Act of the relevant province |

*Source: National Treasury*

### A balance between own revenues and fiscal transfers

There is a widespread perception that municipalities are supposed to be self-sufficient or at least largely ‘self-funded’ and that, therefore, certain poor rural municipalities are ‘non-viable’. However, the fiscal arrangements set out in chapter 13 of the Constitution provide that local government is ‘entitled to an equitable share of revenue raised nationally’ and may also receive additional conditional transfers from national and provincial government. In addition, the Constitution also requires that municipalities raise their own revenues from service fees, property rates, surcharges and other taxes, levies and duties.

The *whole* local government fiscal framework is designed to fund local government, and not just one component of it such as own revenues or the equitable share. How the local government fiscal framework provides for the funding of municipalities must be looked at holistically, taking into account the real differences between municipalities.

Section 227(2) of the Constitution spells out the relationship between a municipality's entitlement to an equitable share, other transfers and its obligation to raise own revenues:

*Section 227(2) of the Constitution spells out the relationship between a municipality's entitlement to an equitable share, other transfers and its obligation to raise own revenues*

> **227. National sources of provincial and local government funding**
>
> 1. Local government and each province –
>    (a) is entitled to an equitable share of revenue raised nationally to enable it to provide basic services and perform the functions allocated to it; and
>    (b) may receive other allocations from national government revenue, either conditionally or unconditionally.
> 2. Additional revenue raised by provinces or municipalities may not be deducted from their share of revenue raised nationally, or from other allocations made to them out of national government revenue. Equally, there is no obligation on the national government to compensate provinces or municipalities that do not raise revenue commensurate with their fiscal capacity and tax base.

The Constitution expects municipalities to show fiscal effort to raise revenue commensurate with their fiscal capacity. On the other hand, section 214(2) of the Constitution provides that when determining the equitable share of a municipality, the government must give consideration to, among other things, 'the fiscal capacity and efficiency of the … municipalities'. Thus when determining a municipality's equitable share of nationally collected revenues, government:

- must have regard for the fiscal capacity of a municipality – i.e. municipalities with low fiscal capacity should get a more generous share than municipalities with high fiscal capacity (all other things being equal)
- may not favour a municipality that does not raise own revenue commensurate with its fiscal capacity and tax base – i.e. municipalities that fail to show fiscal effort cannot look to national government for additional funding
- may not discriminate against a municipality that shows fiscal effort, and collects own revenues in line with or even exceeding normal evaluations of its fiscal capacity.

The Constitution differentiates between actual 'revenue raised' and 'fiscal capacity' (see text box). These concepts are often mistakenly conflated when discussing whether a municipality or group of municipalities have access to sufficient funding.

### The dimensions of municipal fiscal capacity

Section 214(2) of the Constitution provides that when determining the equitable share of a municipality, government must give consideration to, among other things, *'the fiscal capacity and efficiency of the … municipalities'*. It is important to note that fiscal capacity does not include the local government equitable share of nationally collected revenues or other transfers from national and provincial government, but rather the *own revenue potential of the municipality*. This emphasis on 'own revenue potential' is found in section 227 of the Constitution, which differentiates actual own revenue raised from fiscal capacity.

So fiscal capacity does not equal actual own revenue raised. Similarly, the failure to raise own revenue does not equate to a lack of fiscal capacity. In practical terms this means that a municipality's fiscal capacity needs to be determined independently of its *fiscal effort*.

Fiscal capacity also needs to be determined in context. There are four components to municipal fiscal capacity:

1. *The fiscal powers and functions of the municipality.* A municipality is only allowed to raise own revenues from the revenue sources given to the municipality by the Constitution and national legislation. It follows that any nationally imposed restrictions on municipalities' fiscal powers and functions reduce municipal fiscal capacity.
2. *The own revenue potential of the municipality, given a specified set of fiscal powers and functions.* A municipality can only raise revenues commensurate with the incomes of the individuals, households, businesses and other institutions that fall within its area of jurisdiction. The municipality's customer base's *ability to pay* is thus a critical variable in evaluating municipal fiscal capacity.
3. *The powers and functions of the municipality.* A municipality may only raise service charges and surcharges in relation to the functions it is empowered to deliver. Metros, districts and local municipalities have all been allocated different sets of powers and functions – therefore they do not have the same service delivery responsibilities, nor the same fiscal capacities.
4. *The community demand for the services that the municipality is responsible for funding.* The extent of a municipality's service delivery obligations provides the context within which the revenue potential of the municipality derives meaning. The demand for each service is related to the extent of backlogs and the number of indigent households, other households, businesses and other institutions requiring the service. Other variables that impact on the cost of delivering particular services in different geographical locations, such as population density, terrain or rainfall, are also relevant.

Households' *ability to pay* (not households' *willingness to pay)* is relevant to calculating fiscal capacity. This can be a contentious issue. Are there circumstances when the risks and difficulties associated with enforcing payment effectively reduce a municipality's fiscal capacity? For instance, many rural municipalities point to difficulties raising property rates on non-poor households living on traditional land. When does a municipality need to approach the courts to enforce payments?

The fact that municipalities' fiscal capacities differ underpins the rationale for the differentiated approach used to divide the local government equitable share and certain conditional transfers between municipalities. Government, however, recognises the need to provide for greater differentiation in the local government fiscal framework based on municipalities' differing fiscal capacity.

*Municipalities with low fiscal capacity will receive a higher proportion of their funding from national transfers*

Thus, according to the Constitution, a municipality's fiscal capacity needs to be determined independently of its fiscal effort; and only the municipality's fiscal capacity (and the other issues mentioned in section 214(2) of the Constitutions) may be taken into consideration when determining its equitable share or any other transfers from the national budget. Municipalities with low fiscal capacity therefore receive a higher proportion of their funding from national transfers than municipalities with high fiscal capacity. However, all municipalities, irrespective of their fiscal capacity, are expected to show fiscal effort and collect the own revenues that *are* available to them. Together, these different sources of revenue are intended to ensure that all municipalities have access to resources commensurate to their service delivery responsibilities.

The fact that the local government fiscal framework allocates significant own revenue sources to municipalities means that they have greater control over the income side of their budgets than do provinces. However, this also means that municipalities need to pay particular attention to revenue management. If they don't, they will not collect the cash they need to fund their expenditures. This will result in cash-flow problems – as many municipalities have experienced.

*National government will not bail out municipalities that fail to collect own revenues or mismanage their funds*

Section 18 of the MFMA requires a municipal budget to be funded by 'realistically anticipated revenues to be collected', cash-backed accumulated reserves or borrowings (but only for capital). This means that a municipality must limit its expenditures to its available revenues, and if those revenues are not collected, then expenditures have to be cut. As indicated above, national government will not bail out municipalities that fail to collect own revenues or mismanage their funds.

## Municipal own revenues

Section 229 of the Constitution deals with municipal fiscal powers and functions. It provides that municipalities may impose rates on property and surcharges on fees for services provided by the municipality or on behalf of the municipality. It also provides that a municipality may impose other taxes, levies and duties, if authorised by national legislation. In addition, municipalities may charge for the services they provide (service charges and administration fees).

When setting property rates, service charges and other fees, municipalities need to have regard to two key principles of taxation, namely:

- *The benefit principle:* This captures the idea that payments should be related to benefits. Customers need to have the sense that they are getting 'value for money' for the taxes and charges they pay. In this regard one needs to distinguish between individual benefit and general benefit. Individual benefit means that the amount an individual is required to pay for a public service should be more or less equal to the benefit that the individual derives from the consumption of that service. General benefit refers to a situation where beneficiaries of a particular public service do not necessarily derive individual benefits equal to individual costs; rather the benefits of all beneficiaries are equated with the cost to all beneficiaries.

- *The ability-to-pay principle:* This captures the idea that beneficiaries pay taxes according to their income generating capacity, so as to foster greater social equity. It is customary to distinguish between horizontal equity and vertical equity. Horizontal equity is generally accepted to mean that those with the same incomes should pay the same amount of tax. By contrast, it is generally understood that vertical equity means that those earning higher incomes should pay proportionately higher taxes than those earning less income – i.e. the taxes should be progressive.

### *Property rates*

The levying of property rates is governed by the Municipal Property Rates Act (2004). Only metros and local municipalities may raise revenue through property rates. In terms of the Act, they are required to adopt property rates policies. They must also put in place and maintain a property valuation roll. The valuation roll needs to comply with the 'horizontal equity principle' in that similar properties should have similar valuations.

*Property rates are intended to fund municipal services such as municipal roads, storm water systems, street lighting and street cleansing*

Property rates are intended to fund the economic services provided by the municipality, such as municipal roads, storm water systems, street lighting and street cleansing. The consumption of these services is non-exclusive (i.e. they cannot be limited to specific consumers) so they are funded through a general tax on all potential consumers, namely the owners of property within the municipality's jurisdiction. The structure of rates should take account of the 'ability to pay' principle, and so should be progressive. The level of rates should cover the cost of providing a defined basket of economic services efficiently and effectively, and so should be set at a level where the benefits of the collective beneficiaries are commensurate with the cost imposed on those beneficiaries, i.e. the level of rates charged should comply with the 'benefit' principle.

The Act provides that the Minister of Cooperative Governance and Traditional Affairs, after consulting with the Minister of Finance, may regulate various aspects of property rates, including the provision of exemptions, maximum levels of rates and rates ratios between categories of property. The aim is to ensure that property rates are equitable, do not stifle economic growth, and that they support certain national policy objectives.

### *Service charges and administration fees*

A municipality is expected to charge for the services it provides to specific, identifiable customers that derive 'individual benefit' from the consumption of those services. Examples include water, electricity, sanitation, refuse removal, planning and building permissions and the hiring out of municipal facilities.

Section 74(2) of the Municipal Systems Act (2000) prescribes that a municipal council must adopt and implement a tariff policy on the levying of fees for municipal services:

A tariff policy must reflect at least the following principles, namely that

(a) users of municipal services should be treated equitably in the 'application of tariffs;

(b) the amount individual users pay for services should generally be in proportion to their use of that service;

(c) poor households must have access to at least basic services through –

  (i) tariffs that cover only operating and maintenance costs;

  (ii) special tariffs or life line tariffs for low levels of use or consumption of services or for basic levels of service; or

  (iii) any other direct or indirect method of subsidisation of tariffs for poor households;

(d) tariffs must reflect the costs reasonably associated with rendering the service, including capital, operating, maintenance, administration and replacement costs, and interest charges;

(e) tariffs must be set at levels that facilitate the financial sustainability of the service, taking into account subsidisation from sources other than the service concerned;

(f) provision may be made in appropriate circumstances for a surcharge on the tariff for a service;
(g) provision may be made for the promotion of local economic development through special tariffs for categories of commercial and industrial users;
(h) the economical, efficient and effective use of resources, the recycling of waste, and other appropriate environmental objectives must be encouraged:
(i) the extent of subsidisation of tariffs for poor households and other categories of users should be fully disclosed.

These principles create an enabling framework for establishing financially sustainable service charges. While the principles require that 'ability to pay' should inform the structure of tariffs, the Act does not place a legal obligation on municipalities to provide free basic services. It would seem that when Parliament passed the Act, the intention was that all households should always make some payment (no matter how small) for the municipal services they receive, as in each instance there is reference to poor households getting access to services on the basis of a tariff. The requirement that the extent of any subsidisation of tariffs for poor households and other categories of users be fully disclosed is also rarely complied with by municipalities. This lack of transparency means municipal councils and households are not aware of the revenue cost of the free benefits given/received, and consequently there are ongoing demands for greater subsidies and more 'free' services.

*The principles underpinning a municipality's tariff policy create an enabling framework for establishing financially sustainable service charges*

It is also worth noting that tariffs must reflect the costs reasonably associated with rendering the service, including capital, operating, maintenance, administration and replacement costs, and interest charges. This is particularly important in relation to water, electricity, sanitation and refuse removal. These trading services are expected to operate according to good business principles and be largely self-financing. To facilitate this, municipalities are required to ring-fence these functions where appropriate.

*Tariffs must reflect the costs reasonably associated with rendering the service, including capital, operating, maintenance, administration and replacement costs*

The Electricity Regulation Act (2006) empowers the National Energy Regulator of South Africa (NERSA) to issue electricity distribution licences to municipal distributors. Such licences may be made subject to conditions relating to, among other things, the setting and approval of prices, charges, rates and tariffs. Section 15 of the Act sets out tariff principles that must be adhered to when NERSA approves municipal electricity tariffs. These principles are fully aligned with those in the Municipal Systems Act (2000). Of specific importance is section 21(5)(c), which provides that a municipality may terminate the supply of electricity to a customer if that customer has contravened the payment conditions of that licensee (municipality). In other words, if a municipality wants to use electricity cut-offs as a debt management tool, its tariff policy or debt collection policy must specify that this is permitted. This has been tested in court on a number of occasions, and each time the courts have ruled in favour of municipalities provided they have the necessary policies in place.

The Water Services Act (1997) empowers the Minister of Water Affairs (with the concurrence of the Minister of Finance) to issue regulations setting norms and standards in respect of municipal tariffs for water services. Regulations in this regard were issued in 2001, but while setting norms and standards for water tariffs, there is little monitoring of compliance. This means that there is no oversight of municipalities' water tariffs. The concern is that in many instances municipalities are getting their water tariffs wrong, usually by significantly under-pricing the service, thus placing its sustainability at risk. Consequently, the need for a dedicated regulator in the water sector has been raised.

*Some municipalities have already developed the necessary policies to impose development charges*

Extensive work has been done in relation to municipal *development charges*. These charges should be structured to ensure that the cost to the municipality of providing new municipal service infrastructure to new private developments gets properly factored into the cost of those developments. Some municipalities have already developed the necessary policies to impose these charges. In time, these will need to be aligned to the framework National Treasury is currently developing that will set norms and standards to ensure that these charges facilitate (and do not stifle) new property developments.

### *Surcharges, other taxes, levies and duties*

The Municipal Fiscal Powers and Function Act (2007) regulates municipal surcharges and municipal taxes, other than property rates. Only the Minister of Finance may authorise a municipal tax by issuing regulations in terms of the Act. The Act also requires municipalities to get authorisation for all existing municipal taxes – which process still has to be concluded. The Act also empowers the Minister of Finance to prescribe norms and standards for municipal surcharges.

The Minister of Finance, acting on his own initiative, may authorise new municipal taxes, or a municipality may apply for a new tax to be authorised. Such an application must be supported by various studies on the impact of the proposed tax. Since the Act came into effect, no new municipal taxes have been authorised.

The possibility of introducing a local business tax as a new municipal tax, particularly for the metros and large cities, has been raised. Various studies have been undertaken in this regard. However, before any new tax can be considered there needs to clarity regarding the need for such a tax, the equity of any proposed tax and how the tax is going to be administered. In addition, before a new tax can be considered, the municipalities wanting the new revenue source need to demonstrate that they are optimizing revenues from all the existing sources available to them, that their tax expenditures (rebates) are not overly generous, their indigent policies are appropriately structured and efficiently managed and that service tariffs are cost reflective. Furthermore, the municipalities should be able to demonstrate that their billing system is complete, accurate and reliable, and that their collections and debt management policies are being effectively implemented.

### *Other own revenues*

Municipalities also collect revenue from traffic fines, penalties for by-law contraventions, licence fees and permits, agency payments, and interest. These sources, while a lot smaller than other sources, are still significant as in most instances they contribute to the pool of revenues that the municipality can use for redistributive and local economic development purposes.

## Transfers to local government

In general, transfer programmes play three roles:

- addressing the structural imbalance between revenues available to municipalities and the expenditure responsibilities assigned to them
- supporting national priorities as outlined through different sectoral policies, in particular those focused on providing expanded access to basic services
- establishing incentives for good governance and building local government capacity.

The value of national transfers to local government, and the specific allocations to particular municipalities are determined through the division of revenue process and the national budget process. Annexure W1 to the Division of Revenue Act, which is published on the National Treasury website, describes the structure of the different transfers to local government for 2011/12.

*Transfers to local government can be in the form of unconditional transfers, conditional grants and allocations in-kind*

Transfers from national and provincial government may be direct or indirect in nature. Most transfers entail the funds being directly transferred to municipalities, either on a conditional or unconditional basis. Indirect transfers usually take the form of asset transfers or may be services provided by another sphere of government on behalf of the municipality.

### *Unconditional transfers*

The vertical division of nationally collected revenues determines the pool of funds to be transferred to local government as unconditional transfers. Currently, there are three streams of unconditional transfers that flow to local government.

*The local government equitable share is the main unconditional transfer*

- *The local government equitable share:* This transfer is intended to balance the unequal distribution of fiscal capacity between spheres of government and across municipalities. It redistributes funds from the national fiscus to help fund municipalities. The division of the local government equitable share between municipalities takes account of the different needs and responsibilities of municipalities relative to their fiscal capacity, and so is the primary redistributive mechanism between municipalities. While the local government equitable share is an unconditional transfer, there is nevertheless a constitutional expectation that municipalities will prioritise its use to fund the provision of basic services within the broad policy framework defined by national government. The aim is to subsidise the cost of providing these services to poor households, and to contribute to the funding of core administrative functions.
- *RSC levies replacement grant:* Before 2006, district municipalities raised levies on local businesses through either a Regional Services Council (RSC) levy or Joint Services Board (JSB) levy. These taxes were abolished because they were

regarded to be 'bad taxes' when measured against generally accepted principles of sound taxation, namely equity among taxpayers, efficiency, certainty, simplicity and ease of administration. This source of revenue was replaced in 2006/07 with the RSC levies replacement grant, which was allocated to all district municipalities and metros based on the amounts they had previously collected through the levies. This grant is allocated together with the equitable share.

When the RSC levies replacement grant was introduced, there was a firm intention to introduce alternative own revenue sources for municipalities as soon as possible. This has been accomplished in respect of the metros' portion of the grant (see below). However, finding a suitable replacement for the district municipalities' portion of the grant is proving to be difficult. Consequently, the process has been postponed until such time as the future roles and responsibilities of the district municipalities have been clarified.

- *General fuel levy sharing with metros:* The sharing of the general fuel levy with the metros was introduced in the 2009 Budget as the primary replacement for the former RSC levies, in addition to the VAT reforms introduced in 2006. The sharing of the general fuel levy is a direct charge and is formalised annually through the Taxation Laws Amendment Act.

### *Conditional grants*

*The biggest conditional grant is the municipal infrastructure grant*

Direct conditional grants are transfers that municipalities may only spend on particular purposes as set out in the conditional grant frameworks. Collectively, these grants are worth almost as much as equitable share transfers. The biggest conditional grant is the municipal infrastructure grant (MIG), which provides funding for municipal infrastructure, principally for extending access to water and sanitation to poor households. Other grants fund electrification, public transport infrastructure, local economic development projects and capacity building programmes in municipalities.

### *Allocations in-kind*

Allocations in-kind provide a way for departments in other spheres of government to spend funds on providing goods or services in a municipality without having to transfer funds to the municipality. These grants are used in cases where municipalities do not have the capacity to spend the funds themselves, or where there are economies of scale that can be achieved by implementing a project across several municipalities, such as with the regional bulk infrastructure grant that builds dams that supply several municipalities with water.

## Municipal borrowing

*A municipality's capacity to borrow is a function of sound financial management, sound own revenue management and choice of infrastructure projects*

Municipalities may borrow funds from the financial markets to finance part of the economic infrastructure portion of their capital budget. Given that national government does not guarantee municipal borrowing, a municipality's capacity to borrow is a function of sound financial management, sound own revenue management and choice of infrastructure projects. It is envisaged that the metros and the secondary cities should borrow primarily from private capital markets on the strength of their credit ratings, while the Development Bank of Southern Africa (DBSA) will increasingly play its developmental role by lending to the poorer municipalities. See *Chapter 6 Leveraging private finance* for more details.

### Own revenue and accountability

The local government fiscal framework is deliberately designed to raise municipalities' level of accountability to residents. The fact that most municipalities receive the majority of their revenue from service charges and property rates means that they need to ensure that:

*The local government fiscal framework is deliberately designed to raise municipalities' level of accountability to residents*

- residents receive the trading services (so that the municipality can earn income off them)
- the general level of municipal services is adequate to maintain property values (so as to maintain the municipality's rates base)
- residents are generally satisfied with the municipalities' services (so that they are willing to continue paying their rates and service charges).

This revenue-service link means that there is potential for a strong alignment between the municipality's revenue interests and the service delivery interests of residents that pay rates and service charges.

However, providing free services to indigent households does not generate municipal revenues through service fees. Poor households also do not typically pay rates. This means that there is little or no revenue-service link between these residents and the municipality, which means that the revenue interests of municipalities are not aligned with the service interests of poor residents. Consequently, the municipality's incentive to service these customers is reduced.

*The financial interests of municipalities are not aligned with the service interests of poor residents*

The presence or absence of this revenue-service link may partly explain how different groups of residents choose to engage with municipalities. Ratepayer associations are increasingly using their power as taxpayers and paying consumers to leverage greater accountability on the part of municipalities and municipal councils; whereas poorer residents appear to be engaging increasingly in service delivery protests, and so exercising their political power, as well as their power to disrupt.

*Poorer households use service delivery protests to engage with municipalities, while wealthier households organise themselves through ratepayer associations*

The power of this revenue-service relationship in fostering more accountable municipalities highlights the need to bring more residents into the municipal revenue base, even if at very low levels. When residents pay for municipal services it empowers them by establishing a direct, reciprocal link to the municipality. If the municipality does not provide services to these customers, it will not earn any revenue. There is thus a strong incentive for the municipality to ensure services to paying customers are not interrupted.

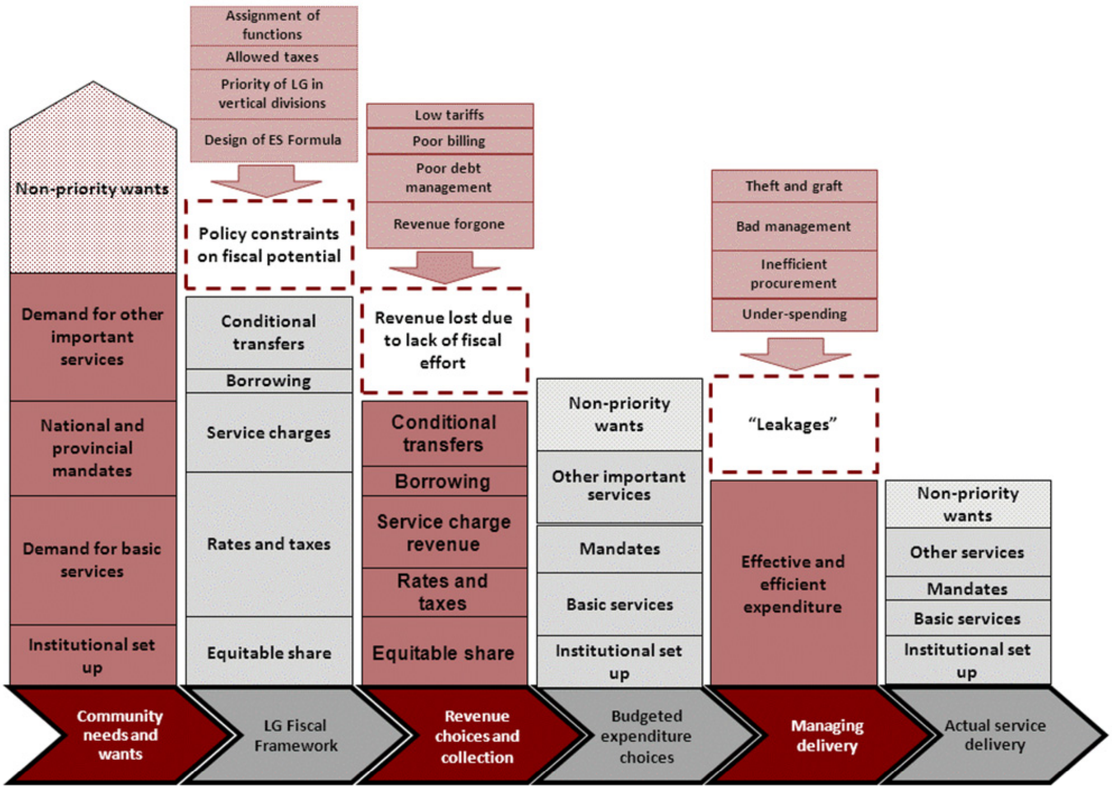
Residents who do not pay for their services can only hold the municipality accountable indirectly, via service delivery protests or once every five years through the ballot box.

Also, municipalities that are highly dependent on transfers will tend to be more accountable to the source of the transfers and less accountable to residents due to the lack of the revenue-service link between them. However, national and provincial oversight of the smaller municipalities is comparatively weak, and not an effective substitute for local oversight by rate-paying residents. This may partly explain why increasing grant dependency seems to be correlated with a lack of accountability for the use of municipal funds in many poorer, more grant dependent district and local municipalities.

## Services and the local government fiscal framework

The following figure provides a conceptual framework that shows how the local government fiscal framework relates to a municipality's service delivery responsibilities.

**Figure 3.1 A model of municipal service delivery and finances**




*Source: National Treasury*

There are five components to this relationship between municipal finances and service delivery:

The first component in the relationship is between the community's demand for services that a municipality is responsible for providing versus the local government fiscal framework. As noted, the Constitution allocates particular functions to local government. In addition, national and provincial legislation may assign further functions to local government. Then there is the actual community demand for each of the services that fall within these functions. Against this there is the local government fiscal framework, which sets out what sources of revenue are potentially available to a municipality to fund these services and functions. Key questions are: Is the local government fiscal framework broadly aligned with the service responsibilities of municipalities? Are there any constraints on the fiscal capacity of local government that arise from certain policy choices?

Ideally, the local government fiscal framework should provide municipalities with access to revenue sources that are commensurate with the powers and functions (or services) that they are responsible for performing.

- The second component in the relationship is between the local government fiscal framework and the actual revenues collected by a municipality. The key issue is whether municipalities are using the 'fiscal space' available to them to raise their own revenues. Or are municipal tariffs too low? Are the billing systems inaccurate? Is there poor debt management? Is the council giving away excessive free services, especially to non-poor households? In sum, is the municipality showing 'fiscal effort'? Or are municipalities simply relying on and dependent on transfers from national and provincial government?
- The third component of the relationship relates to how each municipality chooses to use its available resources. This is generally reflected in the municipal budget. Key questions in this regard are: Is the municipality prioritising the delivery of basic services? What functions and services does the municipality prioritise? What is the balance between the operational budget and the capital budget? Is the municipality budgeting sufficient for repairs and maintenance? How much gets allocated to non-essential, non-priority items?
- The fourth component in the relationship relates to the municipality's governance and management systems to implement the budget and manage service delivery. Are these systems effective and efficient?
- The fifth component relates to what actually gets delivered by the municipality. Are ratepayers getting value for money? Which communities benefit most from the services provided by the municipality? Is there an equitable distribution of services? Is the level of service being provided taking into account the 'benefit principle' and are any cross-subsidies sustainable?

Councillors, mayors and municipal managers are encouraged to use this framework to examine the performance of their municipality in the course of their oversight duties.

## Municipalities' role in the management of resources

Very often the debate around municipal finances only looks at the relationship between the needs in the community and the resources available to meet those needs. This approach fails to recognise that municipal councils, mayors and municipal managers are responsible

*Municipal councils, mayors and municipal managers are responsible for managing the resources of a municipality* for ensuring that available revenues are collected, that resources are allocated appropriately, and that for ensuring that available revenues are collected, that resources are allocated appropriately, and that procurement and service delivery processes are economical, efficient, effective and equitable. In addition, they are responsible for ensuring that the municipality raises own revenues in line with its fiscal capacity.

*The municipal council, mayor and municipal manager are responsible for ensuring that the revenues of the municipality are allocated correctly*

Second, the municipal council, mayor and municipal manager are responsible for ensuring that the revenues of the municipality are allocated in a manner that prioritises basic needs, and the social and economic development of the community. They should evaluate all budget allocations and actual expenditures with a view to identifying all non-essential, fruitless and wasteful expenditure.

Third, the municipal council, mayor and municipal manager are responsible for ensuring that the municipality has sound financial management policies and systems in place. The municipal audit outcomes show that over half of municipalities' financial systems and governance and financial information are deficient. These widespread weaknesses leave municipalities vulnerable to financial mismanagement.

*The municipal council, mayor and municipal manager are responsible for ensuring that service delivery is economical, efficient, effective and equitable*

Last, the municipal council, mayor and municipal manager are responsible for ensuring that the municipality has sound and competent management in place to ensure that service delivery is economical, efficient, effective and equitable.

## Conclusion

The intergovernmental system is continually evolving as contexts change, better approaches to cooperative governance emerge and ways of resolving particular problems are identified. Key areas that need to be addressed are the allocation of functions between district and local municipalities, and the assignment of the housing and public transport functions to municipalities.

All municipalities need to pay particular attention to improving revenue management. While the *whole* local government fiscal framework is designed to fund local government, the existence of national and provincial transfers does not absolve any municipality from showing the necessary fiscal effort – and collecting the own revenues available to it.

The revenue-service link between municipalities and residents is key to fostering greater accountability. This suggests that requiring more households to pay even very small amounts for services may deepen local democracy and municipal accountability.

Clearly, in assessing the relationship between the service delivery responsibilities of municipalities and the local government fiscal framework, issues of good governance are exceptionally important. Mayors, councillors and municipal managers have fiduciary responsibilities to ensure that public funds are safeguarded and only used for the benefit of the community.

4

# Revenue and expenditure trends in local government

## Introduction

In 2010/11 municipalities budgeted to spend R191 billion on their operational budgets. This is about one-fifth of overall government spending. In 2010/11 municipalities were also responsible for managing R41 billion in infrastructure spending, which is 15.9 per cent of total public sector infrastructure spending.

This spending is financed from municipal own revenues, transfers from national and provincial government, and borrowing (for capital). Between 2010/11 and 2012/13, direct national transfers to local government grow by R23 billion or by 13.4 per cent annually. Municipalities own revenues are also growing strongly, particularly services charges which are budgeted to increase by 18.6 per cent per year between 2010/11 and 2012/13. Generally, municipal revenues held up well during the recession. Outstanding consumer debts have increased, but at a slower rate than the growth in own revenues. This reflects some positive action with regards to revenue management.

The revenue and expenditure management capacity of a municipality determine its ability to contribute to poverty reduction and economic development. Any weaknesses in these areas are likely to reflect the existence of other governance challenges in the municipality.

This chapter gives an overview of:

- local government in the system of public finance
- trends in intergovernmental transfers to local government
- revenue trends
- expenditure trends
- key issues in municipal budgets.

## Local government in the system of public finance

*Local government expenditure constitutes one-fifth of total government expenditure*

Local government expenditure constitutes one-fifth of total government expenditure. This ratio has remained almost constant since 2006/07. Table 4.1 shows that local government's contribution is set to increase over the medium term. This is driven by rapid increases in the price of electricity, rising municipal wages and the assignment of the housing and public transport functions to the metros.

**Table 4.1 Local government revenue and expenditure to GDP, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| **R million** | | | | | | | | | |
| **Expenditure** | | | | | | | | | |
| National departments | 210 172 | 242 632 | 289 346 | 346 103 | 359 106 | 370 688 | 393 757 | 18.1% | 4.4% |
| Provinces | 188 913 | 216 976 | 266 591 | 306 255 | 328 224 | 356 567 | 374 471 | 17.5% | 6.9% |
| Local government | 99 707 | 114 450 | 139 337 | 163 177 | 191 441 | 205 084 | 229 132 | 17.8% | 12.0% |
| **Total expenditure** | **498 792** | **574 058** | **695 274** | **815 535** | **878 771** | **932 339** | **997 360** | **17.8%** | **6.9%** |
| *Municipal expenditure as percentage of total government expenditure* | *20.0%* | *19.9%* | *20.0%* | *20.0%* | *21.8%* | *22.0%* | *23.0%* | | |
| *Municipal expenditure as percentage of GDP* | *5.4%* | *5.5%* | *6.0%* | *6.7%* | *7.1%* | *6.9%* | *7.0%* | | |
| **Municipal operating revenue** | **108 781** | **127 508** | **149 480** | **176 342** | **204 535** | **220 529** | **246 537** | | |
| *Municipal revenue as a percentage of GDP* | *5.9%* | *6.1%* | *6.4%* | *7.2%* | *7.6%* | *7.4%* | *7.5%* | | |
| **Property rates** | **18 737** | **21 451** | **22 305** | **26 294** | **31 281** | **33 206** | **35 823** | | |
| *Property rates as % of GDP* | *1.0%* | *1.0%* | *1.0%* | *1.1%* | *1.2%* | *1.1%* | *1.1%* | | |
| **Service charges** | **45 553** | **49 968** | **58 286** | **72 255** | **88 735** | **100 310** | **118 345** | | |
| *Service charges as % of GDP* | *2.5%* | *2.4%* | *2.5%* | *2.9%* | *3.3%* | *3.4%* | *3.6%* | | |
| **Gross domestic product** | **1 833 191** | **2 081 626** | **2 320 117** | **2 449 858** | **2 699 888** | **2 967 560** | **3 295 749** | | |

*Source: National Treasury 2010 Budget Review*

Table 4.1 also shows that municipal operating revenue as a percentage of GDP is growing fairly consistently. It has increased from 5.9 per cent of GDP in 2006/07 to 7.2 per cent in 2009/10. This is primarily due to growth in national transfers, rising electricity revenues (driven by rising electricity prices), as well as above inflation increases in other service tariffs. It is apparent that this increase is not being driven by rising property rates, since rates as a percentage of GDP remain constant at about 1 per cent.

**Table 4.2 Public sector infrastructure expenditure and estimates,[1,2] 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| **R million** | | | | | | | | | |
| **Expenditure** | | | | | | | | | |
| National departments | 4 631 | 5 712 | 6 318 | 6 382 | 6 847 | 7 758 | 10 703 | 11.3% | 18.8% |
| Provincial departments | 27 112 | 29 395 | 36 094 | 41 185 | 45 623 | 49 971 | 50 786 | 15.0% | 7.2% |
| Municipalities | 21 084 | 30 736 | 39 577 | 37 480 | 41 305 | 50 449 | 56 028 | 21.1% | 14.3% |
| Extra-budgetary institutions | 3 699 | 3 726 | 6 194 | 10 859 | 11 175 | 15 083 | 18 821 | 43.2% | 20.1% |
| Public-private partnerships[3] | 1 343 | 3 857 | 4 942 | 13 751 | 9 939 | 11 389 | 6 109 | 117.1% | -23.7% |
| Non-financial public enterprises | 25 736 | 56 765 | 103 322 | 125 504 | 147 025 | 148 665 | 157 970 | 69.6% | 8.0% |
| **Total infrastructure expenditure** | **83 605** | **130 191** | **196 447** | **235 161** | **261 914** | **283 315** | **300 417** | **41.2%** | **8.5%** |
| *Municipalities as percentage of total infrastructure expenditure* | *25.2%* | *23.6%* | *20.1%* | *15.9%* | *15.8%* | *17.8%* | *18.7%* | | |

*Source: National Treasury 2010 Budget Review*

*1. Transfers between spheres have been netted out.*

*2. Includes maintenance of infrastructure assets.*

*3. PPPs reflect private sector contributions and SANRAL toll roads.*

*4. 2010/11 - 2012/13 are based on National Treasury estimates.*

Even though local government infrastructure expenditure shows steady growth, its contribution to total public sector infrastructure spending declines from 25.2 per cent in 2006/07 to 15.8 per cent in 2010/11. This is primarily due to the rapid increase in infrastructure spending by public enterprises, notably Eskom and Transnet.

## Trends in intergovernmental transfers to local government

The following table shows the vertical division of revenue raised nationally between the three spheres of government.

**Table 4.3 Division of nationally raised revenues, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Revised Estimate | Medium-term estimates | | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| R million | | | | | | | | | |
| **Division of available funds** | | | | | | | | | |
| **National departments** | **210 172** | **242 632** | **289 346** | **346 103** | **359 106** | **370 688** | **393 757** | 18.1% | 4.4% |
| **Provinces** | **181 328** | **208 666** | **248 286** | **294 968** | **322 858** | **350 547** | **369 348** | 17.6% | 7.8% |
| **Local government** | **26 501** | **37 321** | **44 037** | **50 146** | **58 821** | **66 640** | **73 187** | 23.7% | 13.4% |
| **Total** | **418 001** | **488 619** | **581 669** | **691 217** | **740 785** | **787 875** | **836 292** | **18.3%** | **6.6%** |
| *Percentage of total* | | | | | | | | | |
| National departments | 50.3% | 49.7% | 49.7% | 50.1% | 48.5% | 47.0% | 47.1% | | |
| Provinces | 43.4% | 42.7% | 42.7% | 42.7% | 43.6% | 44.5% | 44.2% | | |
| Local government | 6.3% | 7.6% | 7.6% | 7.3% | 7.9% | 8.5% | 8.8% | | |
| **Total** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | **100%** | | |

*Source: National Treasury 2010 Budget Review*

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

*Compared to provinces, the Constitution allocates significant own revenue sources to local government*

Compared to provinces, the Constitution allocates significant own revenue sources to local government: property rates, surcharges on service charges, other taxes, levies and duties. In addition, unlike provinces, municipalities are expected to charge for most of the services they provide. This explains why local government’s share of revenues raised nationally is only about 7.9 per cent in 2010/11.

However, ever since 1999, when local government was included in the division of revenue process, national transfers to local government have consistently grown faster than total government expenditure. As a result, local government’s share has been increasing from year to year. This is again true in the period under review: local government’s share of nationally raised revenues increased from 6.3 per cent in 2006/07 to 7.3 per cent in 2009/10, and is projected to reach 8.8 per cent in 2012/13.

With the onset of the economic recession in 2009, government sought to insulate local government from the full impact of the slowdown in national revenues. Between 2010/11 and 2012/13, direct transfers to local government were projected to grow by R14.4 billion, or by 13.4 per cent annually. This is significantly higher than the average annual growth in total government expenditure of 6.9 per cent between 2010/11 and 2012/13.

*The growth in grants is intended to assist municipalities in meeting the operating and capital costs of providing basic services to poor households and fulfilling their other functions*

The growth in grants is intended to assist municipalities meet the operating and capital costs of providing basic services to poor households and fulfilling their other functions. National transfers are not a substitute for a municipality's own revenues. Non-poor households, businesses and other institutions in all municipalities are expected to pay rates and the full cost of the services they receive. As discussed in *Chapter 3 Intergovernmental relations and the local government fiscal framework*, the Constitution provides that national transfers may not compensate municipalities that fail to collect own revenues in line with their fiscal capacity. All municipalities are expected to show fiscal effort.

National transfers to local government are divided into direct transfers and indirect transfers. The indirect transfers are amounts that national departments spend on behalf of municipalities, so the funds are not actually transferred to municipalities. Table 4.4 shows both direct and indirect transfers to local government.

**Table 4.4 Transfers to local government, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth 2006/07 - 2009/10 | 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Revised Estimate | Medium-term estimates | | | | |
| **Direct transfers** | **26 501** | **37 321** | **44 037** | **50 146** | **58 821** | **66 640** | **73 187** | 23.7% | 13.4% |
| **Equitable share** | **11 058** | **12 631** | **16 515** | **21 050** | **26 676** | **30 268** | **33 370** | 23.9% | 16.6% |
| **RSC levy replacement grant** | **7 000** | **8 045** | **9 045** | **3 306** | **3 492** | **3 672** | **3 864** | -22.1% | 5.3% |
| **General fuel levy sharing with metros** | **–** | **–** | **–** | **6 800** | **7 542** | **8 531** | **8 958** | - | 9.6% |
| **Conditional grants** | **8 443** | **16 645** | **18 477** | **18 990** | **21 111** | **24 169** | **26 995** | 31.0% | 12.4% |
| Infrastructure | 7 447 | 15 128 | 17 095 | 16 910 | 19 039 | 22 072 | 24 793 | | *13.6%* |
| Capacity-building and other | 996 | 1 517 | 1 382 | 2 080 | 2 072 | 2 097 | 2 202 | 27.8% | 1.9% |
| **Indirect transfers** | **1 436** | **1 884** | **2 307** | **3 017** | **3 125** | **4 014** | **4 618** | 28.1% | 15.2% |
| Infrastructure | 943 | 1 334 | 1 928 | 2 774 | 2 979 | 4 014 | 4 618 | 43.3% | 18.5% |
| Capacity-building and other | 493 | 550 | 379 | 243 | 146 | – | – | -21.0% | -100.0% |
| **Total** | **27 937** | **39 205** | **46 344** | **53 163** | **61 946** | **70 654** | **77 805** | **23.9%** | **13.5%** |

*Source: National Treasury local government database*

The direct transfers are divided into unconditional transfers (the local government equitable share and the general fuel levy sharing with metros) and conditional grants. Annexure W1 to the Division of Revenue Act, which is published on the National Treasury website, describes the structure and allocations of all national transfers.

## Unconditional transfers

*The local government equitable share is intended to balance the unequal distribution of fiscal capacity between spheres of government and across municipalities*

The local government equitable share is the main unconditional transfer. Since 2006/07 the Regional Services Council (RSC) levy replacement grant for metros and districts was added, and since 2009/10, the metros' share of the RSC levy replacement grant has been going through a process of conversion to the 'general fuel levy sharing with metros' which is to be completed by 2012/13.

The equitable share grows by an annual average of 16.6 per cent over the medium term, from R21.1 billion in 2009/10 to R33.4 billion in 2012/13.

Table 4.5 shows the equitable share and the RSC replacement grant allocations to municipalities. Between 2009/10 and 2012/13, the growth in the equitable share favours metros at 18.9 per cent per year, compared to 14.9 per cent per year for the mostly rural municipalities. In 2009/10 the metros' share of the RSC levy replacement grant was replaced with the general fuel levy sharing with metros. Prior to this change the metros received two thirds of the RSC levy replacement grant.

*Between 2009/10 and 2012/13, the growth in the equitable share favours metros at 18.9 per cent per year, compared to 14.9 per cent per year for the mostly rural municipalities*

**Table 4.5 Equitable share and RSC levy replacement grant transfers, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth 2006/07 - 2009/10 | % Ave annual growth 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Estimate | Medium-term estimates | | | | |
| **Equitable share** | | | | | | | | | |
| Metros | 2 648 | 3 069 | 4 218 | 5 147 | 6 773 | 7 790 | 8 644 | 24.8% | 18.9% |
| Secondary cities | 1 864 | 2 219 | 2 871 | 3 611 | 4 553 | 5 177 | 5 711 | 24.7% | 16.5% |
| Towns | 2 472 | 2 840 | 3 655 | 4 723 | 5 871 | 6 632 | 7 297 | 24.1% | 15.6% |
| Mostly rural | 2 391 | 2 501 | 3 180 | 4 264 | 5 226 | 5 888 | 6 477 | 21.3% | 14.9% |
| Districts | 1 683 | 2 001 | 2 591 | 3 304 | 4 252 | 4 780 | 5 241 | 25.2% | 16.6% |
| **Total equitable share** | **11 058** | **12 631** | **16 515** | **21 050** | **26 676** | **30 268** | **33 370** | **23.9%** | **16.6%** |
| *Percentage of total* | | | | | | | | | |
| Metros | *24.0%* | *24.3%* | *25.5%* | *24.5%* | *25.4%* | *25.7%* | *25.9%* | | |
| Secondary cities | *16.9%* | *17.6%* | *17.4%* | *17.2%* | *17.1%* | *17.1%* | *17.1%* | | |
| Towns | *22.4%* | *22.5%* | *22.1%* | *22.4%* | *22.0%* | *21.9%* | *21.9%* | | |
| Mostly rural | *21.6%* | *19.8%* | *19.3%* | *20.3%* | *19.6%* | *19.5%* | *19.4%* | | |
| Districts | *15.2%* | *15.8%* | *15.7%* | *15.7%* | *15.9%* | *15.8%* | *15.7%* | | |
| **Total** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | | |
| **RSC levy replacement grant** | | | | | | | | | |
| Metros[1] | 4 700 | 5 372 | 6 043 | | | | | - | - |
| Districts | 2 300 | 2 673 | 3 002 | 3 306 | 3 492 | 3 672 | 3 864 | 12.9% | 5.3% |
| **Total RSC levy replace** | **7 000** | **8 045** | **9 045** | **3 306** | **3 492** | **3 672** | **3 864** | **-22.1%** | **5.3%** |
| *Percentage of total* | | | | | | | | | |
| Metros[1] | *67.1%* | *66.8%* | *66.8%* | *0.0%* | *0.0%* | *0.0%* | *0.0%* | | |
| Districts | *32.9%* | *33.2%* | *33.2%* | *100.0%* | *100.0%* | *100.0%* | *100.0%* | | |
| **Total** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | ***100.0%*** | | |

*Source: National Treasury local government database*

*1. From 2009/10 RSC levy removed as it has been replaced by general fuel levy sharing with metros.*

## Conditional grants

National government allocates funds to local government through a variety of conditional grant programmes. All conditional grants are regulated by the annual Division of Revenue Act, which requires that each programme conform to a standard set of financial management and reporting rules. The national departments responsible for managing conditional grants are required to make allocations for each municipality over a three-year horizon to enable better planning.

Conditional grants are generally divided into two groups:

### *Infrastructure grants*

Table 4.6 lists all national government's infrastructure related direct and indirect conditional grants to local government. The municipal infrastructure grant (MIG) is by far the largest of the infrastructure grants. It has grown very strongly since 2006/07, and is budgeted to continue growing at 13.5 per cent per year over the medium term. Note that from 2011/12, the urban settlement development grant is separated from the municipal infrastructure grant.

*The municipal infrastructure grant is by far the largest of the infrastructure grants*

The direct infrastructure grants are intended to supplement municipal capital budgets to accelerate municipalities' capacity to extend access to basic services. In other words, municipalities are still expected to fund infrastructure from their own resources (such as their equitable share, internally generated funds and borrowing).

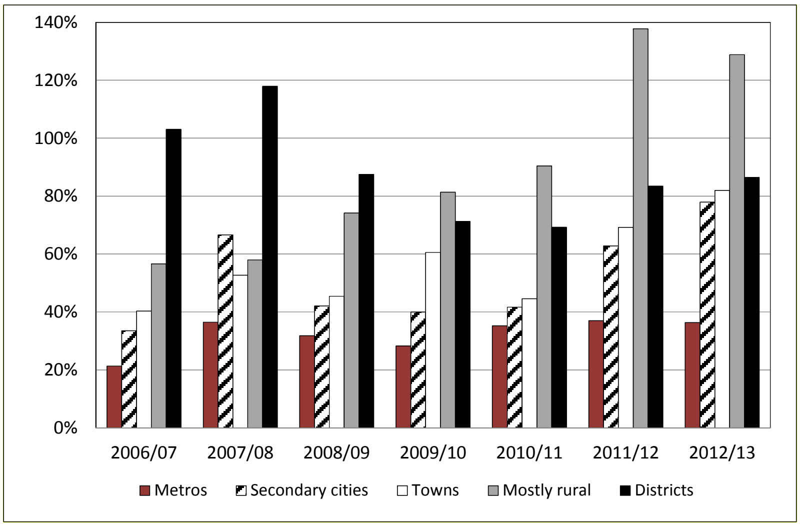
**Table 4.6 Infrastructure transfers to local government, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth 2006/07 - 2009/10 | 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Revised Estimate | Medium-term estimates | | | | |
| **Direct transfers** | **7 447** | **15 127** | **17 095** | **16 909** | **19 038** | **22 072** | **24 792** | **31.4%** | **9.2%** |
| Municipal infrastructure grant | 5 938 | 8 754 | 9 091 | 11 107 | 12 529 | 15 069 | 18 322 | 23.2% | 13.5% |
| National electrification programme | 391 | 462 | 589 | 933 | 1 020 | 1 097 | 1 151 | 33.6% | 4.1% |
| Public transport infrastructure and system grant | 518 | 1 174 | 2 920 | 2 418 | 3 699 | 4 425 | 4 125 | 67.1% | 3.7% |
| Neighbourhood development partnership grant | – | 41 | 182 | 551 | 1 030 | 1 190 | 1 182 | - | 4.7% |
| 2010 FIFA World Cup stadiums development grant | 600 | 4 605 | 4 295 | 1 661 | 302 | – | – | 40.4% | - |
| Rural transport services and infrastructure grant | – | – | 9 | 10 | 10 | 11 | 12 | - | 6.3% |
| Electricity demand side management | – | – | – | 175 | 220 | 280 | – | - | - |
| Municipal drought relief grant | – | 91 | 9 | 54 | 228 | – | – | - | - |
| **Indirect transfers** | **943** | **1 334** | **1 928** | **2 775** | **2 979** | **4 014** | **4 618** | **43.3%** | **15.7%** |
| National electrification programme | 893 | 973 | 1 148 | 1 478 | 1 752 | 1 770 | 1 914 | 18.3% | 3.0% |
| Neighbourhood development partnershop grant | 50 | 61 | 54 | 111 | 125 | 100 | 105 | 30.5% | -5.6% |
| Regional bulk infrastructure grant | – | 300 | 450 | 612 | 893 | 1 675 | 1 849 | - | 27.5% |
| Backlogs in w ater and sanitation at clinics and schools | – | – | 186 | 350 | – | – | – | - | - |
| Backlogs in the electrification of clinics and schools | – | – | 90 | 149 | – | – | – | - | - |
| Electricity demand-side management | – | – | – | 75 | 109 | 119 | – | - | - |
| Rural household infrastructure grant | – | – | – | – | 100 | 350 | 750 | - | - |
| **Total** | **8 390** | **16 461** | **19 023** | **19 684** | **22 017** | **26 086** | **29 410** | **32.9%** | **10.1%** |

*Source: National Treasury 2010 Budget Review*

Figure 4.1 shows the percentage contribution that infrastructure grants make to municipalities' capital budgets.

**Figure 4.1 Infrastructure grants' contribution to municipal capital budgets**




*Source: National Treasury local government database*

In 2006/07 infrastructure grants contributed 21.4 per cent to metros' capital budgets. This increased to 36.5 per cent in 2007/08, largely due to the grants related to the 2010 FIFA World Cup, before declining to around 28.3 per cent in 2009/10. This is probably a healthy balance in the case of the metros. A similar trend would be expected for the secondary cities, but infrastructure grants' contribution to capital budgets increases to 75.6 per cent in 2012/13. The capital budgets for towns, and mostly rural and district municipalities also reflect that infrastructure grants represent an increasing proportion of their capital budgets over the medium term. Indeed, in the case of mostly rural municipalities, infrastructure grants are shown as being more than 100 per cent of their capital budgets. This indicates serious weaknesses in these municipalities' budgeting for capital – as they are not correctly reflecting the national grants due to them on their capital budgets. There was a similar problem with district municipalities in 2006/07 and 2007/08.

Overall, figure 4.1 shows that all municipalities are becoming increasingly dependent on national infrastructure grants to fund their capital budgets. This is not a sustainable trend, because it means the tariffs for the main municipal services are not covering the infrastructure costs of providing those services.

### *Capacity-building grants and other transfers*

National government uses the capacity-building grants to fund various programmes aimed at supporting municipalities to develop in-house systems and skills for planning, project management and financial management. Water service operating subsidy grants are transitional funding arrangements to facilitate the transfer of the water function from the Department of Water Affairs to municipalities.

**Table 4.7 Capacity-building and other current transfers to local government, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Revised Estimate | | Medium-term estimates | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| **Direct transfers** | **996** | **1 517** | **1 382** | **2 081** | **2 072** | **2 098** | **2 202** | 27.8% | 1.9% |
| Municipal systems improvement grant | 200 | 200 | 200 | 200 | 212 | 225 | 236 | 0.0% | 5.7% |
| Restructuring grant | 265 | 530 | – | – | – | – | – | - | - |
| Financial management grant | 145 | 145 | 180 | 300 | 365 | 385 | 404 | 27.4% | 10.4% |
| 2010 FIFA World Cup host city | – | – | – | 508 | 210 | – | – | | - |
| Water services operating subsidy grant | 386 | 642 | 1 002 | 871 | 662 | 380 | 399 | 31.2% | -22.9% |
| Expanded public works programme - Phase 2 incentive grant | – | – | – | 202 | 623 | 1 108 | 1 163 | - | 79.2% |
| **Indirect transfers** | **493** | **550** | **379** | **243** | **146** | **–** | **–** | -21.0% | - |
| Financial management grant: DBSA | 53 | 53 | 50 | – | – | – | – | - | - |
| Water services operating subsidy grant | 440 | 497 | 329 | 243 | 146 | – | – | -18.0% | - |
| **Total** | **1 489** | **2 067** | **1 761** | **2 324** | **2 218** | **2 098** | **2 202** | **16.0%** | **-1.8%** |

*Source: National Treasury 2010 Budget Review*

Table 4.7 shows that the largest of these capacity building initiatives is the financial management grant, which funds the appointment of graduate interns in finance related disciplines. The grant is growing rapidly to fund a growing pool of interns.

*The financial management grant is the largest capacity building grant*

### The balance between unconditional transfers and conditional grants

There is concern that the use of conditional grants by national government reduces municipalities' scope to set their own expenditure priorities, and thus weakens their accountability to local communities. The following table shows the proportion of funds flowing to municipalities as unconditional transfers versus conditional grants and indirect transfers.

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Revised estimates | | Medium-term estimates | |
| ***Percentage of local share of nationally collected revenues*** | | | | | | | |
| *Equitable share* | 64.6% | 52.7% | 55.2% | 45.8% | 48.7% | 48.0% | 47.9% |
| *RSC levy replacement grant* | | | | | | | |
| *General fuel levy sharing with metros* | 0.0% | 0.0% | 0.0% | 12.8% | 12.2% | 12.1% | 11.5% |
| **Total unconditional transfers** | **64.6%** | **52.7%** | **55.2%** | **58.6%** | **60.9%** | **60.1%** | **59.4%** |
| *Conditional grants from national budget* | 30.2% | 42.5% | 39.9% | 35.7% | 34.1% | 34.2% | 34.7% |
| *Indirect transfers from national budget* | 5.1% | 4.8% | 5.0% | 5.7% | 5.0% | 5.7% | 5.9% |
| **Total conditional and indirect transfers** | **35.4%** | **47.3%** | **44.8%** | **41.4%** | **39.1%** | **39.9%** | **40.6%** |

In 2006/07, unconditional transfers were 64.6 per cent of the total transfers to local government. The following year this declined to 52.7 per cent primarily due to the size of the 2010 FIFA World Cup stadiums development grant. Although this grant ended in 2010/11, unconditional transfers only recover to around 60 per cent of total transfers to local government over the medium term. The main reason for this is the ramping up of the regional bulk infrastructure grant and the introduction of a rural household infrastructure grant, both of which are indirect transfers aimed at addressing backlogs in infrastructure for basic services, particularly water.

So although there is a slight increase in conditional and indirect transfers, generally the balance between unconditional and conditional transfers has not changed significantly over the review period.

## Provincial transfers

Table 4.8 shows the transfers that provinces make to municipalities. These transfers are primarily related to the housing function, but also include transfers for clinics, emergency health services and libraries.

**Table 4.8 Provincial transfers to local government, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth 2006/07 - 2009/10 | 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| R thousand | | Outcome | | Estimate | | Medium-term estimates | | | |
| **Provincial transfers** | | | | | | | | | |
| Eastern Cape | 460 645 | 470 736 | 733 245 | 856 121 | 561 362 | 593 509 | 626 355 | 22.9% | -9.9% |
| Free State | 100 662 | 58 322 | 182 436 | 446 751 | 393 813 | 378 172 | 353 893 | 64.3% | -7.5% |
| Gauteng | 405 476 | 454 504 | 476 256 | 622 499 | 607 163 | 630 106 | 663 147 | 15.4% | 2.1% |
| KwaZulu-Natal | 478 394 | 783 710 | 1 115 245 | 1 331 010 | 728 822 | 787 321 | 794 839 | 40.6% | -15.8% |
| Limpopo | 94 906 | 23 034 | 84 272 | 39 431 | 135 311 | 57 334 | 48 154 | -25.4% | 6.9% |
| Mpumalanga | 24 207 | 14 380 | 100 916 | 89 682 | 57 374 | 65 760 | 68 888 | 54.7% | -8.4% |
| Northern Cape | 111 224 | 89 400 | 113 925 | 134 300 | 141 941 | 149 853 | 142 430 | 6.5% | 2.0% |
| North West | – | – | 40 255 | 222 190 | 226 770 | 226 950 | 1 232 319 | - | 77.0% |
| Western Cape | 884 544 | 1 379 595 | 1 416 736 | 1 558 963 | 1 575 760 | 1 779 694 | 1 778 731 | 20.8% | 4.5% |
| **Total** | **2 560 058** | **3 273 681** | **4 263 286** | **5 300 947** | **4 428 316** | **4 668 699** | **5 708 756** | **27.5%** | **2.5%** |
| **Per category** | | | | | | | | | |
| Category A | 1 043 394 | 1 779 290 | 2 233 104 | 2 555 674 | 2 263 079 | 2 483 577 | 2 529 961 | 34.8% | -0.3% |
| Category B | 760 905 | 765 874 | 1 316 596 | 1 529 764 | 1 308 999 | 1 297 911 | 2 285 391 | 26.2% | 14.3% |
| Category C | 755 759 | 728 517 | 713 586 | 1 215 509 | 856 238 | 887 211 | 893 405 | 17.2% | -9.8% |
| **Total** | **2 560 058** | **3 273 681** | **4 263 286** | **5 300 947** | **4 428 316** | **4 668 699** | **5 708 756** | **27.5%** | **2.5%** |

*Source: National Treasury provincial database*

*Certain provinces are in fact reducing the scope of their delegations to municipalities, particularly the housing function, which is contrary to government's policy*

Provincial transfers to local government grew at an average annual rate of 27.5 per cent between 2006/07 and 2009/10. However, the rate of growth declines to just 2.5 per cent per year from 2009/10 to 2012/13. This would suggest that certain provinces are reducing the scope of their delegations to municipalities, particularly the housing function – which is contrary to government's policy to devolve this function to local government. It also suggests that provinces are underfunding certain of the functions they have delegated to municipalities, notably clinics and library services.

## Revenue trends

The new budget formats introduced by the Municipal Budget and Reporting Regulations draw a clear distinction between a municipality's operating budget and its capital budget, and between operating revenues and capital revenues. This is to enable the calculation of an operating surplus that reflects whether the municipality is functioning as a 'going concern' or not. Capital transfers are reflected separately, 'below the line' on the operating budget, while capital funding is shown on the capital budget.

*The new budget formats draw a clear distinction between a municipality's operating budgets and its capital budget*

In addition, only 'realistically anticipated revenues to be collected' may be reflected on a municipality's operating budget (statement of financial performance). This means that revenues that the municipality has 'given away' (so called *revenue foregone*) must not be reflected on the operating budget. It is reported elsewhere in the prescribed budget tables.

### Operating revenue

At an aggregate level, the most important sources of municipal revenue are service charges, transfers and property rates. Table 4.9 shows total operating revenue of municipalities in the new budget format prescribed by the Municipal Budget and Reporting Regulations. This format was introduced with municipalities' 2010/11 budget, which means that the information for prior years is not fully aligned.

*The most important sources of municipal revenue are service charges, transfers and property rates*

**Table 4.9 Municipal operating revenue, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth 2006/07 - 2009/10 | % Average annual growth 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Estimate | Medium-term estimates | | | | |
| **Operating Revenue** | | | | | | | | | |
| Property rates | 18 737 | 21 451 | 22 305 | 26 294 | 30 702 | 32 599 | 35 186 | 12.0% | 10.2% |
| Property rates - penalties & collection charges | – | – | – | – | 579 | 606 | 637 | - | - |
| Service charges | 45 553 | 49 968 | 58 286 | 72 255 | 91 191 | 102 703 | 120 679 | 16.6% | 18.6% |
| *Service charges - electricity revenue* | | | | | *58 978* | *68 916* | *84 172* | - | - |
| *Service charges - water revenue* | | | | | *17 676* | *18 633* | *20 223* | - | - |
| *Service charges - sanitation revenue* | | | | | *7 334* | *7 719* | *8 407* | - | - |
| *Service charges - refuse revenue* | | | | | *4 747* | *5 042* | *5 542* | - | - |
| *Service charges - other revenue* | | | | | *2 456* | *2 393* | *2 334* | - | - |
| Rental of facilities and equipment | | | | | 1 635 | 1 443 | 1 510 | - | - |
| Interest earned - external investments | 3 217 | 3 998 | 4 504 | 2 829 | 1 927 | 1 927 | 2 013 | -4.2% | -10.7% |
| Interest earned - outstanding debtors | | | | | 2 127 | 2 189 | 2 362 | - | - |
| Dividends received | | | | | 3 | 8 | 9 | - | - |
| Fines | | | | | 1 430 | 1 492 | 1 675 | - | - |
| Licences and permits | | | | | 600 | 536 | 554 | - | - |
| Agency services | | | | | 1 327 | 1 375 | 1 477 | - | - |
| Transfers recognised - operational | 28 970 | 39 322 | 49 519 | 57 474 | 39 476 | 39 819 | 42 845 | 25.7% | -9.3% |
| Other revenue | 12 303 | 12 770 | 14 866 | 17 490 | 9 592 | 9 477 | 10 091 | 12.4% | -16.8% |
| Gains on disposal of PPE | | | | | 593 | 278 | 265 | - | - |
| **Total revenue** | **108 781** | **127 508** | **149 480** | **176 342** | **181 181** | **194 453** | **219 301** | **17.5%** | **7.5%** |
| *Percentage of total revenue* | | | | | | | | | |
| Property rates | 17.2% | 16.8% | 14.9% | 14.9% | 16.9% | 16.8% | 16.0% | | |
| Service charges | **41.9%** | **39.2%** | **39.0%** | **41.0%** | **50.3%** | **52.8%** | **55.0%** | | |
| Interest earned - external investments | 3.0% | 3.1% | 3.0% | 1.6% | 1.1% | 1.0% | 0.9% | | |
| Transfers recognised - operational | 26.6% | 30.8% | 33.1% | 32.6% | 21.8% | 20.5% | 19.5% | | |
| Other revenue | 11.3% | 10.0% | 9.9% | 9.9% | 9.9% | 9.0% | 8.5% | | |
| **Total revenue** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | | |

*1. RSC levies abolished from 1 July 2006. Interim replacement grant included in Equitable share.*

*Source: National Treasury local government database*

*Total operating revenue grew by 17.5 per cent between 2006/07 and 2009/10*

The table shows that total operating revenue grew by 17.5 per cent between 2006/07 and 2009/10. This was primarily driven by very rapid growth in ‘transfers recognised – operational’ (i.e. the equitable share, RSC replacement grant and operating conditional grants), and growth in service charge revenues, particularly related to electricity. Property rates revenue showed steady growth between 2006/07 and 2009/10, which suggests that municipalities weathered the impact of the economic recession relatively well. Between 2009/10 and 2010/11, there is a significant decrease in ‘transfers recognised – operational’, which is largely due to the conversion of the metros’ share of the RSC replacement grant into the general fuel levy sharing with metros, which is captured under other revenue. Many district municipalities also appear to be cutting back on operational transfers to the local municipalities within their areas. It is important to note that many of the revenues previously captured under other revenue are now captured separately – hence the decline between 2009/10 and 2010/11. The rate of growth in service charge revenues increases to 18.6 per cent, reflecting the impact of higher electricity prices and the pressure on municipalities to implement cost reflective tariffs for all trading services.

*At 41 per cent in 2009/10, service charges are the largest source of operating revenue for municipalities*

Revenues from service charges are the largest source of municipal revenue. However, a very large percentage of this income simply flows through municipal coffers to Eskom or the water boards (depending on the municipality, between 65 and 85 per cent of municipal electricity revenue goes to paying for bulk electricity from Eskom). Historically, many municipalities have been generating a surplus from their trading services (especially electricity) to cross-subsidise other services. However, the rapid increases in bulk tariffs have squeezed these surpluses. This is due to the fact that municipalities have sought to (and, in some instances, been forced to) absorb some of the increases, and because the higher prices are leading to increasing bad debts and inducing customers to consume less. This highlights the need for norms and standards relating to surcharges on these municipal services, so that this 'surplus share' that municipalities rely on to subsidise other services can be made transparent and can be protected. The process of explicitly ring-fencing municipalities' trading services will also help protect this 'surplus share'.

### Vulnerable cash position of municipalities

At a very minimum, a municipality should maintain a positive cash position. Section 45 of the Municipal Finance Management Act (2003) provides that municipalities are not allowed to close the financial year with a short-term borrowing or overdraft. At the end of 2009/10 (30 June 2010), there were 63 municipalities that reported negative closing cash positions; 8 were secondary cities. The fact that these municipalities were not able to close the financial year with positive cash positions is a strong indicator that they were experiencing financial distress at that date.

The number of months a municipality has ended with a negative cash balance gives an indication of whether the municipality's cash flow problems are transitory or more persistent in nature. In the last six months of 2009/10, 2 metros had negative end of month cash balances for more than three of the previous six months. There were 6 secondary cities, 77 local municipalities and 11 districts in a similar situation at the end of 2009/10.

Ideally, a municipality needs to have enough cash on hand to meet its monthly payments as and when they fall due. The level of cash coverage is especially important if the municipality is faced with circumstances that threaten revenue. It is generally accepted that a prudent level of cash coverage is three months of average operational expenditure. At 30 June 2010, 98 municipalities reported cash on hand in excess of three months of operational expenditure. However, there were 96 municipalities with a cash coverage ratio of less than one month. This is an improvement from the 140 municipalities that were in this position in 2008/09, it is still a cause for concern.

Any one of the following events could push these vulnerable municipalities into a negative cash position:

- a deterioration in revenue collections due to the impact that rising rates and tariffs have on households' ability to pay
- the need to pay suppliers, especially contractors responsible for capital projects (whose billings are often lumpy and come at year-end)
- the need to finance the cash-flow difference between paying for the increased cost of bulk electricity/water and the collection of revenues from customers
- any major breakdown in service delivery resulting in non-supply (especially water and electricity), and therefore no revenue
- a ratepayer/consumer boycott.

The cash coverage position of the metros and secondary cities has remained fairly constant. There has, however, been significant improvement in the cash coverage position among the local municipalities. The number of local municipalities that reported having cash in excess of three months of operational expenditure increased from 44 in 2008/09 to 77 in 2009/10, an improvement of 75 per cent. Furthermore, the number of municipalities with less than one month of cash coverage decreased from 118 in 2008/09 to 68 in 2009/10. The cash coverage for district municipalities has deteriorated significantly between 2008/09 and 2009/10. In 2008/09, while only 4 districts reported having less than one month of cash on hand, this had increased to 15 districts in 2009/10. This constitutes almost one-third of all district municipalities.

*Government transfers are the second largest source of revenue*

National transfers are the second largest source of revenue for local government. The very rapid growth in transfers results in this revenue source's share of total revenue increasing from 26.6 per cent in

2006/07 to 32.6 per cent in 2009/10. As a result, other revenue sources' shares of total revenue decline. This trend changes significantly after 2009/10, with the share of revenues from service charges increasing from 41 per cent in 2009/10 to 55 per cent in 2012/13.

Revenue raised through property rates grew by R7.5 billion or 12 per cent between 2006/07 and 2009/10 and is expected to grow further by 10.2 per cent over the medium term. Revenue from property rates held up well during the economic recession.

Municipalities also generate other revenue in the form of traffic fines, business licences, rental fees, entrance fees for use of municipal facilities and fresh produce markets. It is notable that revenue from interest earned on external investments falls significantly in 2010/11, partly as a result of the decline in interest rates, but also because many municipalities have exhausted their historical cash reserves.

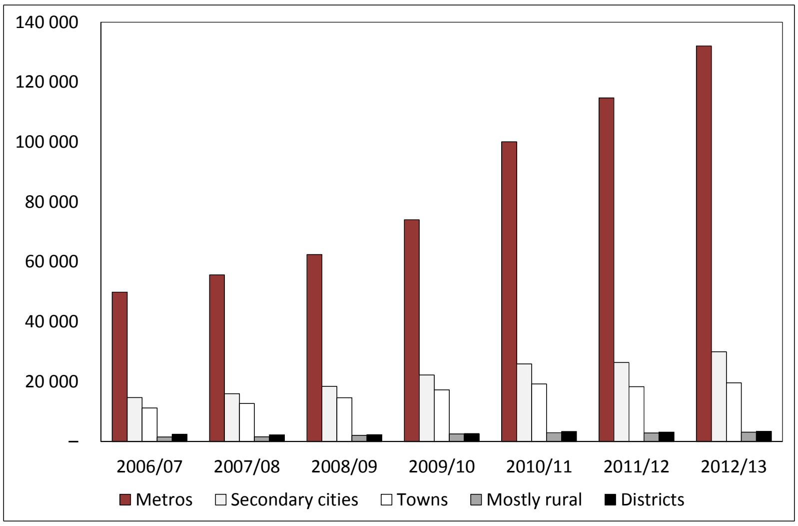
### Own revenues

*A municipality's scope to raise own revenues depends on its fiscal capacity*

All municipalities are expected to raise own revenues in addition to the equitable share transfer they receive from national government. This principle is an important feature of any democratic local government system. It creates a revenue-service link between the municipality and its customers, which empowers customers to hold the municipality directly accountable for the services it provides.

A municipality's scope to raise own revenues depends on its fiscal capacity. The extent to which a municipality does raise own revenues in accordance with its fiscal capacity depends on its fiscal effort; this means the amount of attention it pays to ensuring effective revenue management. Figure 4.2 shows aggregate own revenue for different categories of municipalities and the metros.

**Figure 4.2 Aggregated own revenue of municipalities**




*Source: National Treasury local government database*

### Outstanding consumer debts

*As at 31 December 2010, municipalities were owed a total of R62.3 billion*

As at 31 December 2010, municipalities were owed a total of R62.3 billion. This represents an increase of 10.8 per cent from the same month in 2009. However, consumer debts as a percentage of own revenues have been declining. In June 2008, outstanding debtors stood at R37 billion or 39 per cent of own revenue, and in December 2010 outstanding debtors stood at 30 per cent of own revenue. Part of this can be attributed to the rapid increase in own revenues due to the increase in electricity tariffs, as well as to debt write-offs, but there is also evidence that certain municipalities have been paying greater attention to revenue management.

**Table 4.10 Debtors age analysis, 31 December 2009 and 31 December 2010**

| | 0 - 30 Days | | 31 - 60 Days | | 61 - 90 Days | | Over 90 Days | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|
| R thousand | Amount | % | Amount | % | Amount | % | Amount | % | Amount | % |
| **Debtors analysis as at 31 December 2010** | | | | | | | | | | |
| Category A (Metros) | 6 805 163 | 19.6% | 1 639 690 | 4.7% | 1 156 289 | 3.3% | 25 061 754 | 72.3% | 34 662 896 | 55.6% |
| Category B (Locals) | 2 791 990 | 10.8% | 1 373 927 | 5.3% | 1 369 465 | 5.3% | 20 330 174 | 78.6% | 25 865 554 | 41.5% |
| Category C (Districts) | 112 929 | 6.2% | 90 373 | 5.0% | 68 311 | 3.8% | 1 538 855 | 85.0% | 1 810 468 | 2.9% |
| **Total** | **9 710 081** | **15.6%** | **3 103 990** | **5.0%** | **2 594 065** | **4.2%** | **46 930 782** | **75.3%** | **62 338 919** | **100.0%** |
| **Debtors analysis as at 31 December 2009** | | | | | | | | | | |
| Category A (Metros) | 5 635 881 | 18.0% | 1 603 852 | 5.1% | 1 104 042 | 3.5% | 23 004 527 | 73.4% | 31 348 302 | 55.7% |
| Category B (Locals) | 2 815 289 | 12.1% | 1 151 620 | 4.9% | 929 843 | 4.0% | 18 462 812 | 79.0% | 23 359 564 | 41.5% |
| Category C (Districts) | 153 028 | 9.9% | 71 203 | 4.6% | 55 527 | 3.6% | 1 271 167 | 82.0% | 1 550 924 | 2.8% |
| **Total** | **8 604 197** | **15.3%** | **2 826 674** | **5.0%** | **2 089 412** | **3.7%** | **42 738 507** | **76.0%** | **56 258 791** | **100.0%** |
| **Growth rate between 2009 to 2010** | | | | | | | | | | |
| Category A (Metros) | 20.7% | | 2.2% | | 4.7% | | 8.9% | | 10.6% | |
| Category B (Locals) | -0.8% | | 19.3% | | 47.3% | | 10.1% | | 10.7% | |
| Category C (Districts) | -26.2% | | 26.9% | | 23.0% | | 21.1% | | 16.7% | |
| **Total** | **12.9%** | | **9.8%** | | **24.2%** | | **9.8%** | | **10.8%** | |

*Source: National Treasury local government database*

*Households were responsible for 61.9 per cent of consumer debts at 31 December 2010*

Households were responsible for 61.9 per cent or R38.3 billion of consumer debts at 31 December 2010. National and provincial government owed municipalities R3.1 billion or 5.1 per cent of total consumer debts.

Metros were owed a total of R34.6 billion as at 31 December 2010, a 10.6 per cent increase from December 2009. Secondary cities were owed R11.6 billion at 31 December 2010, which is just a 1 per cent increase from the corresponding period last year.

## Capital budget funding

Table 4.11 shows that municipalities fund their capital expenditure from four sources.

**Table 4.11 Municipal capital funding, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Estimate | Medium-term estimates | | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| R million | | | | | | | | | |
| **Source of finance** | | | | | | | | | |
| *National Government* | | | | | *19 793* | *20 939* | *21 543* | - | - |
| *Provincial Government* | | | | | *1 118* | *1 006* | *1 232* | - | - |
| *District Municipality* | | | | | *42* | *29* | *29* | - | - |
| *Other Transfers and grants* | | | | | *49* | *45* | *35* | - | - |
| Transfers recognised - capital | 9 463 | 13 469 | 19 917 | 19 535 | 21 002 | 22 019 | 22 839 | 27.3% | 5.3% |
| Public contributions and donations | 105 | 175 | 532 | 301 | 1 279 | 1 153 | 1 214 | 19.1% | -48.7% |
| Borrowing | 5 315 | 7 088 | 9 935 | 8 988 | 8 053 | 7 297 | 8 516 | 42.1% | 204.6% |
| Internally generated funds | 6 456 | 9 232 | 11 256 | 12 171 | 8 559 | 7 522 | 6 626 | 23.5% | -18.3% |
| **Total source of finance** | **21 339** | **29 964** | **41 640** | **40 995** | **38 893** | **37 990** | **39 195** | 24.3% | -1.5% |
| *Percentage of source of finance* | | | | | | | | | |
| Transfers recognised - capital | 44.3% | 45.0% | 47.8% | 47.7% | 54.0% | 58.0% | 58.3% | | |
| Public contributions and donations | 0.5% | 0.6% | 1.3% | 0.7% | 3.3% | 3.0% | 3.1% | | |
| Borrowing | 24.9% | 23.7% | 23.9% | 21.9% | 20.7% | 19.2% | 21.7% | | |
| Internally generated funds | 30.3% | 30.8% | 27.0% | 29.7% | 22.0% | 19.8% | 16.9% | | |
| **Total** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | | |

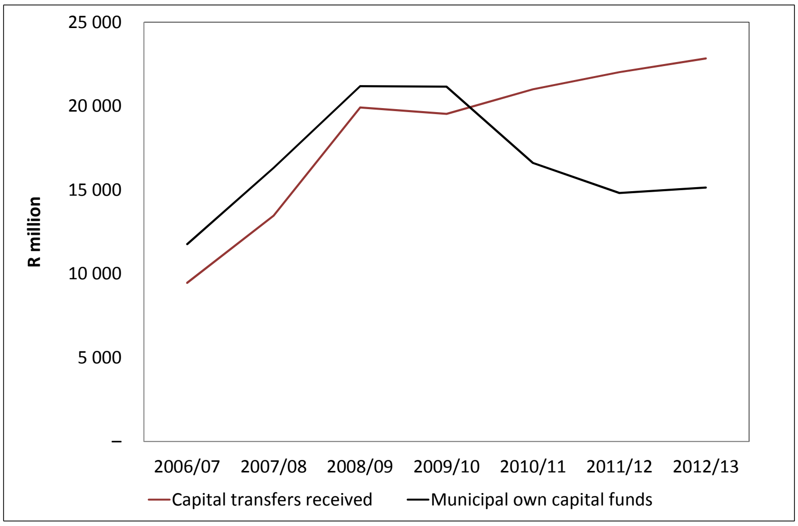
*Source: National Treasury local government database*

The table shows that transfers recognised – capital, i.e. infrastructure grants from national and provincial government, are the most important source of capital funding for municipalities, and its contribution increases from 44.3 per cent in 2006/07 to 58.3 per cent in 2012/13. The increase between 2007/08 and 2008/09 was driven by the infrastructure grants linked to the preparations for the 2010 FIFA World Cup.

*The large decline in municipalities' own contributions to capital expenditure*

The decline in municipalities' own contributions to capital expenditure both by way of internally generated funds and funds from borrowing is cause for concern. In 2009/10, municipalities allocated R12.1 billion to their capital budgets from internally generated funds. This source of funding is set to decline to R6.6 billion by 2012/13. In 2010/11, municipalities were also budgeting to reduce their funding of the capital budget from borrowings. This trend is illustrated in figure 4.3.

**Figure 4.3 Municipal own contribution to capital expenditure, 2006 to 2012**




*Source: National Treasury local government database*

This decline in municipalities' own contributions to capital expenditure can be attributed to the following: (a) municipalities have largely exhausted their historical cash reserves, (b) they are finding it more difficult to generate surpluses on their operating budgets due to various cost pressures, and (c) they are deliberately substituting own contributions with national transfers, and spending the funds elsewhere on their operating budgets.

## Expenditure trends

As noted above, the new budget formats draw a clear distinction between a municipality's operating budget and its capital budget.

### Operating expenditure

Municipalities' actual total operating expenditure increased in real terms by 11.8 per cent annually from 2006/07 to 2009/10 and is estimated to grow by 6.4 per cent over the medium term.

Employee costs account for the largest component of operating expenditure, averaging 30 per cent of total operating expenditure. Between 2006/07 and 2009/10, growth in employee costs was 15.4 per cent, primarily driven by high wage increases. (For a detailed discussion see *Chapter 7 Managing municipal personnel*).

*Personnel costs account for the largest component of operating expenditure*

**Table 4.12 Municipal operating expenditure, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth 2006/07 - 2009/10 | 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Estimate | Medium-term estimates | | | | |
| **Operating expenditure** | | | | | | | | | |
| Employee related costs | 29 057 | 32 672 | 38 307 | 44 678 | 49 843 | 51 622 | 55 750 | 15.4% | 7.7% |
| Remuneration of councillors | 1 557 | 1 671 | 1 876 | 2 013 | 2 146 | 2 149 | 2 291 | 8.9% | 4.4% |
| Debt impairment | | – | – | – | 7 212 | 8 572 | 9 447 | - | - |
| Depreciation and asset impairment | 5 365 | 6 229 | 10 376 | 13 233 | 11 631 | 12 165 | 12 890 | 35.1% | -0.9% |
| Finance charges | 3 503 | 3 475 | 4 265 | 4 882 | 5 612 | 6 008 | 6 364 | 11.7% | 9.2% |
| Bulk purchases | 22 139 | 23 926 | 30 182 | 38 108 | 48 786 | 57 714 | 70 849 | 19.8% | 23.0% |
| Other Materials | | – | – | – | 2 376 | 2 292 | 2 533 | - | - |
| Contracted services | | – | – | – | 8 303 | 8 421 | 9 142 | - | - |
| Transfers and grants | 2 514 | 3 748 | 3 297 | 3 699 | 3 955 | 3 331 | 3 428 | 13.7% | -2.5% |
| Other expenditure | 35 573 | 42 730 | 51 033 | 56 564 | 41 600 | 41 792 | 44 574 | 16.7% | -7.6% |
| Loss on disposal of PPE | – | – | – | – | 29 | 23 | 24 | - | - |
| **Total expenditure** | **99 707** | **114 450** | **139 337** | **163 177** | **181 493** | **194 089** | **217 293** | 17.8% | 10.0% |

*Source: National Treasury local government database*

Bulk purchases constituted 22.2 per cent of municipalities' operating expenditure in 2006/07, and increases to 32.6 per cent in 2012/13. Between 2010/11 and 2012/13, the average annual growth in bulk purchases is anticipated to be 23.0 per cent, driven primarily by the increase in the price of bulk electricity. (See Chapters 8 and 9 for more detailed discussions on water and electricity expenditures).

### Expenditure on repairs and maintenance

The *2008 Local Government Budgets and Expenditure Review* highlighted the serious repairs and maintenance and renewal backlogs that exist in relation to municipal infrastructure, particularly municipalities' electricity, water reticulation, sewerage, storm water and roads systems. These backlogs are impacting negatively on the financial sustainability of municipalities and on the reliability and quality of municipal services, as well as municipalities' contribution to supporting economic growth.

Given government's concerns about the low levels of expenditure on repairs and maintenance and the renewal of existing infrastructure in most municipalities, National Treasury's MFMA Circular 55 provides that when a municipality prepares its 2011/12 budget:

- Where the municipality allocates less than 40 per cent of its 2011/12 capital budget to the renewal of existing assets it must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its asset management plan.
- Where the budgeted amounts for repairs and maintenance are less than 8 per cent of the asset value (write down value) of the municipality's plant property and equipment (PPE) as reflected in the municipality's 2009/10 annual financial statements, the municipality must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its asset management plan.
- In the case of a municipality that received an audit qualification related to its assets register, where the budgeted amounts for repairs and maintenance are less than 10 per cent of the municipality's operating expenditure, the municipality must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its asset management plan.
- More generally, all municipalities should provide narrative information in their budget documents on how they are planning, managing and financing repairs and maintenance and asset renewal, with particular reference to what the municipality has done to assess its repairs and maintenance backlog, its estimate of its repairs and maintenance backlog and the strategy it has put in place to progressively deal with the backlog.

Municipalities' provision for 'depreciation and asset impairment' is growing very rapidly as municipalities implement GRAP 17. This accounting standard requires municipalities to bring all assets that have a material value onto their asset registers. The increase in depreciation reflects the fact that municipalities are now having to account for the 'consumption' of these assets. Although depreciation is a 'non-cash' item on the municipal budget, the cost of this 'consumption' needs to be built into municipalities' rates and tariffs so that the refurbishment and replacement of these assets can be funded once they have reached the end of their useful lives. This implies that all municipalities' capital replacement reserve funds should be cash-backed.

### Per capita operating expenditure by municipalities

*Per capita operating expenditure by each municipality varies greatly*

Per capita operating expenditure by each municipality varies greatly. It is mostly determined by the demographics, the socio-economic context and the powers and functions in a particular municipality, as well as by the nature and extent of business activity. It is also influenced by the history of local government in a particular area and consequently the maturity of the municipality.

Table 4.13 shows that municipalities in Gauteng spend the highest amount per capita, at R6 609 for 2009/10, while Western Cape municipalities spend on average R6 167 per capita. This is despite rapid increases in the populations of both these provinces. According to Statistics South Africa's 2007 Community Survey, Gauteng gained 440 411 more households and 1.2 million more people since the 2001 Census. Western Cape gained 195 000 more households and 754 000 more people over the same period. These are also the provinces where most of the national revenue redistributed through the local government equitable share and conditional grants is generated.

**Table 4.13 Municipal per capita spending by province, 2006/07 – 2012/13**

| Rand | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth 2006/07 - 2009/10 | % Average annual growth 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| | Outcome | | | Estimate | Medium-term estimates | | | | |
| Eastern Cape | 1 944 | 2 057 | 2 544 | 3 029 | 3 302 | 3 485 | 3 769 | 15.9% | 7.6% |
| Free State | 2 226 | 2 871 | 2 885 | 3 336 | 4 167 | 4 499 | 4 709 | 14.4% | 12.2% |
| Gauteng | 4 080 | 4 842 | 6 147 | 6 609 | 7 470 | 8 262 | 9 352 | 17.4% | 12.3% |
| KwaZulu-Natal | 2 208 | 2 592 | 3 335 | 3 929 | 4 281 | 4 491 | 4 958 | 21.2% | 8.1% |
| Limpopo | 859 | 1 372 | 1 757 | 1 993 | 2 125 | 2 156 | 2 405 | 32.4% | 6.5% |
| Mpumalanga | 1 577 | 1 761 | 2 456 | 2 764 | 2 589 | 1 367 | 1 490 | *20.6%* | *-18.6%* |
| Northern Cape | 2 123 | 2 473 | 3 135 | 3 701 | 3 709 | 3 334 | 3 376 | *20.4%* | *-3.0%* |
| North West | 1 720 | 2 006 | 2 351 | 2 668 | 3 141 | 3 264 | 3 478 | *15.8%* | *9.2%* |
| Western Cape | 3 550 | 4 364 | 5 451 | 6 167 | 8 100 | 8 767 | 9 555 | 20.2% | 15.7% |
| **National** | **2 495** | **2 977** | **3 732** | **4 208** | **4 796** | **5 039** | **5 560** | 19.0% | 9.7% |

*Source: Stats SA, 2007 Community Survey; National Treasury local government database*

*Low per capita spending in Limpopo, Mpumalanga and North West points to the historical underdevelopment of local government in these regions*

The lowest municipal per capita spending is in Limpopo, where R1 993 was spent in 2009/10. The fact that per capita spending by municipalities is lowest in Limpopo, Mpumalanga and North West indicates that the low level of spending is probably linked to the historical underdevelopment of local government in these regions. It also indicates the importance of efforts to grow the local economies, as well as the fact that a lot of work still needs to be done to address poverty in these provinces.

Table 4.13 shows that per capita spending by municipalities grew at an average annual rate of 19 per cent between 2006/07 and 2009/10. The highest rate of growth was in Limpopo, where municipal per capita spending grew at an average annual rate of 32.4 per cent per year, while the lowest rate of growth was in Free State, at 14.4 per cent per year. These very rapid increases in per capita spending are primarily due to increases in the cost of providing services (driven by rising wages and the increasing cost of electricity and water), and to a lesser extent due to the extension of municipal services to more customers.

The average annual growth in per capita spending between 2009/10 and 2012/13 is projected to be just 9.7 per cent. This is a significant flattening out. In two provinces, per capita spending is budgeted to decline. If these projections are realised, per capita spending by municipalities in Mpumalanga in 2012/13 will be lower than what it was in 2006/07. While municipal spending is under considerable pressure, it would seem that in this instance the decline is largely attributable to poor quality medium term budgeting by municipalities in the province.

## Capital expenditure

Table 4.14 shows capital expenditure by standard classification by function in line with the new budget formats.

**Table 4.14 Municipal capital expenditure, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| R million | | | | | | | | | |
| **Governance and administration** | **–** | **–** | **–** | **–** | **3 572** | **2 838** | **2 901** | **-** | **-** |
| Executive and council | | | | | 1 160 | 752 | 718 | - | - |
| Budget and treasury office | | | | | 442 | 258 | 350 | - | - |
| Corporate services | | | | | 1 969 | 1 828 | 1 833 | - | - |
| **Community and public safety** | **979** | **1 866** | **1 526** | **1 438** | **6 864** | **5 368** | **5 768** | **13.7%** | **58.9%** |
| Community and social services | | | | | 1 529 | 910 | 900 | - | - |
| Sport and recreation | | | | | 1 240 | 621 | 675 | - | - |
| Public safety | | | | | 656 | 467 | 429 | - | - |
| Housing | 979 | 1 866 | 1 526 | 1 438 | 3 208 | 3 144 | 3 522 | 13.7% | 34.8% |
| Health | | | | | 231 | 226 | 242 | - | - |
| **Economic and environmental services** | **3 178** | **4 017** | **7 335** | **10 548** | **11 857** | **12 141** | **12 340** | **49.2%** | **5.4%** |
| Planning and development | | | | | 3 166 | 2 640 | 2 915 | - | - |
| Road transport | 3 178 | 4 017 | 7 335 | 10 548 | 8 621 | 9 452 | 9 359 | 49.2% | -3.9% |
| Environmental protection | | | | | 70 | 48 | 66 | - | - |
| **Trading services** | **8 907** | **11 230** | **13 863** | **13 750** | **18 768** | **18 881** | **19 453** | **15.6%** | **12.3%** |
| Electricity | 3 093 | 3 833 | 4 748 | 4 784 | 5 848 | 5 177 | 4 912 | 15.6% | 0.9% |
| Water | 5 814 | 7 398 | 9 115 | 8 966 | 7 472 | 8 093 | 8 770 | 15.5% | -0.7% |
| Waste water management | | | | | 4 377 | 4 610 | 4 941 | - | - |
| Waste management | | | | | 1 071 | 1 000 | 830 | - | - |
| **Other** | **8 247** | **12 845** | **18 946** | **15 203** | **131** | **89** | **92** | **22.6%** | **-81.7%** |
| **Total Capital Expenditure** | **21 310** | **29 958** | **41 669** | **40 939** | **41 190** | **39 316** | **40 553** | **24.3%** | **-0.3%** |

*Source: National Treasury local government database*

*Local government infrastructure expenditure almost doubled between 2006/07 and 2008/09, mainly due to projects related to the 2010 FIFA World Cup*

Local government infrastructure expenditure almost doubled between 2006/07 and 2008/09, primarily driven by projects related to the 2010 FIFA World Cup. There was a slight decrease in 2009/10 as a result of the World Cup projects being completed. The fact that capital spending remains at about R40 billion is driven largely by growth in national government transfers to address service delivery backlogs.

Investment in road transport grew at an average rate of 49.2 per cent between 2006/07 and 2009/10, much of which was related to the upgrading of road networks and public transport system in preparation for the World Cup. Following the big drive to build transport infrastructure for the World Cup, spending in this area is budgeted to decline over the medium term.

*Infrastructure budgets for electricity have been growing, but probably not as quickly as required*

Infrastructure budgets for electricity have been growing, but not as quickly as required given the backlogs. It is important to note that this does not include all spending on backlog eradication funded by national government, as part of this is funded by an indirect conditional grant which is managed by Eskom. Investment in electricity networks remains almost flat over the medium term. It is anticipated that this will change significantly going forward, given national government's decision to abandon the idea of creating REDs (regional electricity distributors) and to leave the electricity distribution function with municipalities. This decision brings certainty about municipal ownership of electricity assets, and creates an incentive for them to invest in those assets.

*There are a large number of smaller municipalities whose water and sanitation infrastructure is inadequate or in a very poor state*

There has been constant growth in capital expenditure on water and sanitation. However, the Blue Drop Report and Green Drop Report by the Department of Water Affairs indicate that there are a large number of smaller municipalities whose water and sanitation infrastructure is inadequate or in a very poor state. Therefore, these budgets probably need to grow even more strongly.

Even though the housing function is yet to be devolved, municipalities' housing related expenditures have been growing strongly, at an average annual rate of 13.7 per cent between 2006/07 and 2009/10. Over the medium term, municipalities have budgeted to invest R9.9 billion in housing – mostly as agents of provincial housing departments, but also using their own funds.

*Most municipalities' capacity to budget reliably for infrastructure spending is weak*

Most municipalities' capacity to budget reliably for infrastructure spending is weak. This is reflected by the declining allocations for future years, whereas in practice these will in all probability increase. This is because most municipalities only plan their infrastructure spending within a one-year time horizon. Even then the quality of planning is poor, resulting in significant underspending of capital budgets. In 2009/10 those municipalities' that underspent their capital budgets underspent by R15 billion.

### Conditional grant expenditure

Regular concerns are expressed about the level of municipal spending of conditional grants. Table 4.15 shows that to a large extent these concerns have been addressed by the implementation of the 'use it or lose it' principle set out in the Division of Revenue Act (see the following text box).

**Returning unspent conditional grants to the National Revenue Fund**

In national and provincial government, all departmental budget allocations that remain unspent at the end of the financial year are automatically returned to the relevant revenue fund. The department may then apply for a rollover of such funds, which may or may not be approved. The annual Division of Revenue Act applies the same principles to conditional grants. If a municipality has not spent its grants by the end of the municipal financial year, the municipal manager must apply to National Treasury for the funds to be rolled over. If the municipal manager can prove that the unspent funds are committed to identifiable projects then National Treasury will approve a rollover; if not, then the funds must be returned to the National Revenue Fund.

In 2009/10, National Treasury undertook an extensive exercise to ensure compliance with this aspect of the Division of Revenue Act in respect of the R32.8 billion conditional grants transferred to municipalities between 2005/06 and 2008/09. Working with National Treasury, municipalities had to provide evidence that eligible expenditures against these conditional grants had actually occurred. This verification process was necessary because, first, methods of accounting for grant expenditures in municipalities is different from national government, and, second, there was evidence that many municipalities had chosen to use the grant funding for other purposes, such as paying salaries. National Treasury's initial estimate of the amount of unspent grants was R4.5 billion. Through the verification process this amount came down to R2.5 billion, owed by 213 municipalities. Municipalities were requested to return these unspent funds to the National Revenue Fund in accordance with the Act, to make repayment arrangements with National Treasury. However, very few municipalities did so; the rest simply chose to ignore the instruction. A decision was therefore taken to offset the amount each municipality owed the National Revenue Fund against that municipality's equitable share allocation due to be paid from the National Revenue Fund. This was implemented in November 2009. A total of R1.9 billion was deducted from 178 municipalities' equitable share allocations (35 municipalities were exempted from the first-round off-set process because their cash flows were already negative).

The impact of this action was immediate. No fewer than 151 of the affected municipalities applied to National Treasury for the funds to be rolled over and returned. R1.8 billion was returned to these municipalities between March and June 2010, on the receipt of a written commitment to spend the funds in accordance with the relevant grant conditions before a specified date; for most municipalities this was 30 June 2010. 53 municipalities chose not to meet with National Treasury to request the return of the funds. The R263 million that was off-set against these municipalities' equitable share was therefore retained in the National Revenue Fund.

National Treasury has now developed the systems and capacity to institutionalise the rollover and unspent grants processes at the end of each municipal financial year. The start of the process is determining the quantum of unspent conditional grants as at 30 June. At 30 June 2010, this amount was R3.2 billion. This amount will come down following the verification and rollover processes, but the remainder must be returned to the National Revenue Fund, either as a refund or a deduction against the municipalities' equitable share.

The November 2009 process of offsetting the unspent grants against equitable shares has had a very positive impact on how municipalities manage conditional grants. Previously, many municipalities treated grant funds as another source of own revenue, and made no effort to spend the funds in accordance with the grant conditions or within the required time-period. This has now changed. The application of the 'use-it-or-lose-it' principle creates a clear incentive for municipalities to spend their conditional grants within the financial year and in accordance with grant conditions. This is clearly reflected in the higher levels of spending of the 2009/10 conditional grants.

**Table 4.15 Actual spending of national conditional grants to local government, 2006/07 – 2009/10**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2006/07 | 2007/08 | 2008/09 | 2009/10 |
|---|---|---|---|---|---|---|---|---|
| | Actual expenditure | | | | Percentage of revised allocation | | | |
| **Infrastructure** | **7 286** | **14 981** | **16 823** | **14 292** | **93.9%** | **97.7%** | **97.7%** | **83.0%** |
| *Direct transfers* | | | | | | | | |
| Municipal Infrastructure Grant | 5 801 | 8 238 | 8 912 | 9 371 | 92.8% | 99.7% | 98.0% | 82.0% |
| Urban Transport Fund Grant | – | – | 6 | – | - | - | 67.3% | - |
| National Electrification Programme (Municipal) Grant | 384 | 453 | 534 | 767 | 98.1% | 96.9% | 89.7% | 82.2% |
| Public Transport Infrastructure and Systems Grant | 506 | 1 149 | 2 873 | 1 933 | 97.4% | 97.8% | 98.4% | 80.0% |
| Neighbourhood Development Partnership Grant | – | 41 | 177 | 423 | 92.8% | 99.7% | 98.0% | 82.0% |
| 2010 FIFA World Cup Stadiums Development Grant | 596 | 4 577 | 4 295 | 1 649 | - | 17.8% | 61.3% | 76.7% |
| Municipal Drought Relied funds (DWAF) | – | 69 | 9 | 54 | - | 69.3% | 95.5% | 100.0% |
| Disaster funds (DCOG) | – | 454 | 17 | – | - | 92.2% | 100.0% | - |
| Electricity Demand Side Management (Municipal) Grant | – | – | – | 96 | - | - | - | 54.8% |
| **Capacity building and other grants** | **577** | **863** | **358** | **844** | **73.0%** | **98.6%** | **94.3%** | **83.7%** |
| *Direct transfers* | | | | | | | | |
| Municipal Systems Improvement Programme Grant | 192 | 193 | 188 | 159 | 96.2% | 96.5% | 94.1% | 79.5% |
| Local Government Restructuring Grant | 247 | 530 | – | – | 55.5% | 100.0% | - | - |
| Local Government Financial Management Grant | 138 | 140 | 170 | 219 | 94.8% | 96.5% | 94.5% | 73.1% |
| 2010 FIFA World Cup Host City Operating Grant | – | – | – | 465 | - | - | - | 91.7% |
| **Total** | **7 863** | **15 844** | **17 182** | **15 136** | **91.9%** | **97.8%** | **97.6%** | **83.0%** |

*Source: National Treasury local government database*

Municipalities have spent 91.9 per cent of the conditional grants allocated to them in 2006/07. Similarly high levels of spending are shown for 2007/08 and 2008/09. It must, however, be emphasised that not all this spending would have taken place in the relevant financial year, due to the rolling over of committed funds. Spending for 2009/10 is significantly lower because the process of rolling over committed funds is not reflected. In terms of the annual Division of Revenue Act, conditional grant funds not spent at the end of a financial year and not rolled-over to the following financial year, must be returned to the National Revenue Fund (see textbox above).

## Key issues in revenue and expenditure management

*It is not enough to simply review the size of municipal revenues or expenditures*

Reviewing intergovernmental transfers and the size of municipal budgets does not provide adequate insight into the efficiency or effectiveness of a municipality. Rising expenditures related to the delivery of a particular service may reflect an expansion of services to more citizens or increasingly difficult technical conditions, such as a dispersed population or a municipality reaching a specific stage in the life-cycle of its assets. But it may also reflect higher than average personnel costs or administrative overheads, weak expenditure controls or inappropriate service standards. Inefficiencies in service delivery or corruption might also quickly translate into increased expenditures and reduce the availability of resources to address the core objectives of poverty reduction and economic development.

Key issues in revenue and expenditure management include:

### Revenue management: getting the basics right

Much attention has been given to the need for municipalities to collect outstanding debts. This is important, but municipalities need to pay attention to all aspects of the revenue management value chain in order to ensure completeness of revenues:

- *Integrity of billing information:* Are accounts being sent to everyone who should be receiving an account? If accounts are not being sent, then there is no obligation on the ratepayer or customer of a particular service to pay. This requires the municipality to regularly update its information with reference to the property deeds register. Administratively weak systems are open to fraud. For instance, a seemingly 'innocent' misclassification of a residential property as an agricultural property can 'save' the ratepayer 75 per cent on their rates bill.
- *Accuracy of billing systems:* Are all customers being billed accurately according to the market value of their properties and for the services they consume? Or are customers meters not being read, and estimates being used?
- *Ability to collect:* A municipality can send out as many bills as it likes, but unless these are being delivered to the correct address they mean nothing or very little unless it can enforce payment.

Revenue collection needs to be managed holistically, and it must be everyone's business within the municipality. It involves getting the basics right. Failure to get the basics right cannot be made up for by buying a new IT system or appointing debt collectors. A municipality needs to have sound policies, practices and processes in place for managing revenue – none of these are enormously complicated. What is needed are dedicated managers prepared to build administrative implementation systems that integrate each component of the revenue value chain.

*Revenue management needs to be managed holistically, and it must be everyone's business within the municipality*

### Collecting outstanding debts: getting the basics right

The persistently high debtor levels indicate that most municipalities' efforts to collect billed revenues are deficient. In this regard, it should be noted that the growth in consumer debtors pre-dates the slowdown in the economy in 2009. Far more relevant explanations for the growth in debtors include:

- a failure on the part of mayors and municipal councils to provide political backing to revenue enhancement programmes
- a failure on the part of municipal managers to allocate sufficient staff/capacity to the revenue collection function
- council unwillingness to sanction the use of electricity and other service cut-offs as debt management tools (or Eskom not co-operating with municipalities to enable them to use electricity as a debt management tool in the areas it services)
- poorly designed revenue management, indigent and credit control and customer care policies
- the affordability of municipal bills, especially to households where breadwinners lost their jobs in the recession
- resistance among certain communities to paying for certain types of services (or to being billed in a particular way)

- ratepayer boycotts, sparked by deteriorating service delivery, and perceptions that the municipality is unresponsiveness to community concerns.

The scope for improving own revenues by ensuring payment of current bills and collecting outstanding debtors is very large, given that the majority of municipalities have collection rates below 80 per cent. Indeed, there are a number of municipalities that have demonstrated that collection rates can be improved massively by adopting relatively simple, back to basics type debt management processes.

### Underpricing of services

*Very few municipalities' taxes and tariffs are appropriately structured*

Many municipalities' taxes and tariffs are inappropriately structured. The principal problem is that few municipalities understand how their various activities and services are being funded, and therefore what the balance between taxes and tariffs needs to be to ensure financial sustainability. Other problems include:

- a failure to ensure that on average, service tariffs reflect the costs reasonably associated with rendering the service; i.e. that revenues and expenditures for the trading services breakeven
- limited use of inclining block tariffs, particularly for water and electricity, that show cross-subsidies between tariff groups explicitly
- overly generous rates rebates, exemptions and discounts, and a general movement towards the provision of free basic services (which is engendering a culture of dependency rather than adhering to the principle that everyone should make some payment for the municipal services they receive).

As noted in *Chapter 3 Intergovernmental relations and local government fiscal framework*, the principles for rates and tariff setting in legislation are sound. Application of these principles in practice is where the problem lies.

### Underspending on repairs and maintenance

*The most serious misalignment in municipal budgets probably involves the underfunding of repairs and maintenance*

The most serious misalignment in municipal budgets probably involves the underfunding of repairs and maintenance. When a municipality experiences any kind of financial stress, invariably the first category of expenditure to be cut is repairs and maintenance. This is because the impact of not spending on this area is not visible and not obvious in the short term. It is also less politically sensitive than, say, cutting the capital expenditure programme, or reducing the entertainment budget. However, the medium to long term consequences of underspending on repairs and maintenance include:

- deteriorating reliability and quality of services
- move to more expensive crisis maintenance, rather than planned maintenance
- increasing the future cost of maintenance and refurbishment
- shortening the useful life of assets, necessitating earlier replacement

- increased distribution losses of water and electricity
- reduced revenues due to the failure to sell water and electricity, and other services
- Rising tariffs for consumers over the medium term.

### Spending on non-priorities

Like national and provincial government, local government will have to redirect spending from non-core items and programmes to frontline services that have a direct impact on communities. The textbox below highlights some areas of municipal spending that needs to be curtailed.

### Examples of non-priority spending

The following examples of non-priority expenditure have been observed:

- excessive sponsorships for music festivals, beauty pageants and sporting events, including buying tickets to events for councillors and officials
- public relations projects and activities that are not centred on actual service delivery, for instance celebrations, commemorations, voter education and advertising
- excessive catering for meetings and other events, including the use of public funds to buy liquor
- arranging workshops and events in expensive venues, especially ones outside the municipality
- excessively luxurious office accommodation and office furnishings
- foreign travel by mayors, councillors and officials (especially so-called study tours)
- excessive councillor and staff perks – mayors' cars and houses, cell-phone and telephone allowances, travel and subsistence allowances
- all donations to individuals that are not made in terms of the municipality's indigent policy or a bursary scheme
- costs associated with long-standing staff suspensions and the legal costs associated with not following due process when dismissing staff, as well as the payment of severance packages
- the use of consultants to perform routine management tasks.

The cumulative effect of non-priority expenditures should not be under-estimated. International experience with government cost-saving initiatives indicates that savings of as high as 15 per cent can be realised over time. This suggests that by eliminating non-priority spending, municipalities on aggregate could have saved up to R27 billion on their 2009/10 budgets. This is more than the total equitable share for local government in that year.

## Conclusion

Generally, municipal revenues and expenditures have grown quite rapidly over the review period. Capital spending grew very strongly until 2009/10, but spending over the medium term shows little growth.

However, the disparities in per capita expenditure levels between municipalities are still very large. This highlights the importance of national government transfers to local government, particularly to the poorer municipalities. However, it also highlights the need for municipalities to price their services appropriately, so as to ensure they are able to fund their services on a sustainable basis. The importance of getting the basics right with regard to revenue management, debt management and budgeting for repairs and maintenance cannot be over emphasised. Lastly, preventing spending on non-priorities could save municipalities a vast amount, which would be available for improving and extending basic services.

5

# Financial management and MFMA implementation

## Introduction

*Sound financial management practices are essential to the long-term sustainability of municipalities*

Sound financial management practices are essential to the long-term sustainability of municipalities. They underpin the process of democratic accountability. Weak or opaque financial management results in the misdirection of resources and increases the risk of corruption. The key objective of the Municipal Finance Management Act (2003) (MFMA) is to modernise municipal financial management in South Africa so as to lay a sound financial base for the sustainable delivery of services.

Municipal financial management involves managing a range of interrelated components: planning and budgeting, revenue, cash and expenditure management, procurement, asset management, reporting and oversight. Each component contributes to ensuring that expenditure is developmental, effective and efficient and that municipalities can be held accountable.

The reforms introduced by the MFMA are the cornerstone of the broader reform package for local government outlined in the 1998 White Paper on Local Government. The MFMA, together with the Municipal Structures Act (1998), the Municipal Systems Act (2000), the Municipal Property Rates Act (2004) and the Municipal Fiscal Powers and Functions Act (2007), sets out frameworks and key requirements for municipal operations, planning, budgeting, governance and accountability.

This chapter gives an overview of:

- reforms in municipal financial management
- strengthening planning and budgeting

- strengthening oversight through improved transparency
- institutional strengthening and capacity building.

## Reforms in municipal financial management

The MFMA was introduced in 2003. At that time, the system of local government finance was characterised by practices such as one-year line-item budgeting, which did not support strategic planning and the alignment of budgets with priorities over the medium term. This generally resulted in councils allocating resources based on historical commitments rather than looking at current priorities and the future needs of communities.

Municipal finance practices were also not rooted in a culture of performance and regular reporting. Reports were often irregular or inaccurate, or contained too much data and too little useful information. Often municipalities did not publish annual reports and did not submit their financial statements for audit on time or at all.

Compared to where local government was in 2003, significant strides have been made with implementing the new financial management arrangements spelt out in the MFMA and its regulations. However, progress is uneven and many municipalities are yet to implement both the letter and the spirit of the MFMA, namely 'to enable managers to manage' within a framework of regular and consistent reporting so that they can be held accountable.

### Key mechanisms for strengthening accountability

*The separation of political and management roles is critical for good governance*

The set of legislation governing local government provides for a number of mechanisms for strengthening accountability. The first mechanism involves separating and clarifying roles and responsibilities of mayors, executive councillors, non-executive councillors and officials. This separation of political and management roles is critical for good governance.

The executive mayor and executive committee are expected to provide political leadership, by proposing policies, guiding the development of budgets and performance targets, and overseeing their implementation by monitoring performance through in-year reports. In executing their duties, they may not use their position, privileges or confidential information for private gain or to improperly benefit another person.

The municipal manager holds the primary legal accountability for financial management in terms of the MFMA and, together with other senior managers, is responsible for implementation and outputs. They have a duty to act with fidelity, honesty and integrity, and in the best interests of the municipality at all times.

Non-executive councillors, as elected representatives of the community, debate and approve the proposed policies and budgets and also oversee the performance of the municipality. They hold both the executive mayor or committee and the officials accountable for performance on the basis of quarterly and annual reports.

The second mechanism involves developing a performance orientation. The legal framework introduces requirements and processes for establishing service delivery priorities and plans. The aim is to ensure alignment between the plans, budgets, implementation actions and reporting to ensure proper management accountability for the achievement of service delivery targets.

*A performance orientation is crucial for strengthening accountability*

The third mechanism involves strengthening reporting and disclosure requirements. High quality and timely management information allows management to be proactive in identifying and solving problems as they arise. It also strengthens the separation of roles and supports a performance orientation in local government.

*Reporting and disclosure requirements need to be strengthened*

### Alignment of planning, budgeting and reporting

Section 153 of the Constitution requires that 'a municipality must structure and manage its administration and budgeting and planning processes to give priority to the basic needs of the community, and to promote the social and economic development of the community'.

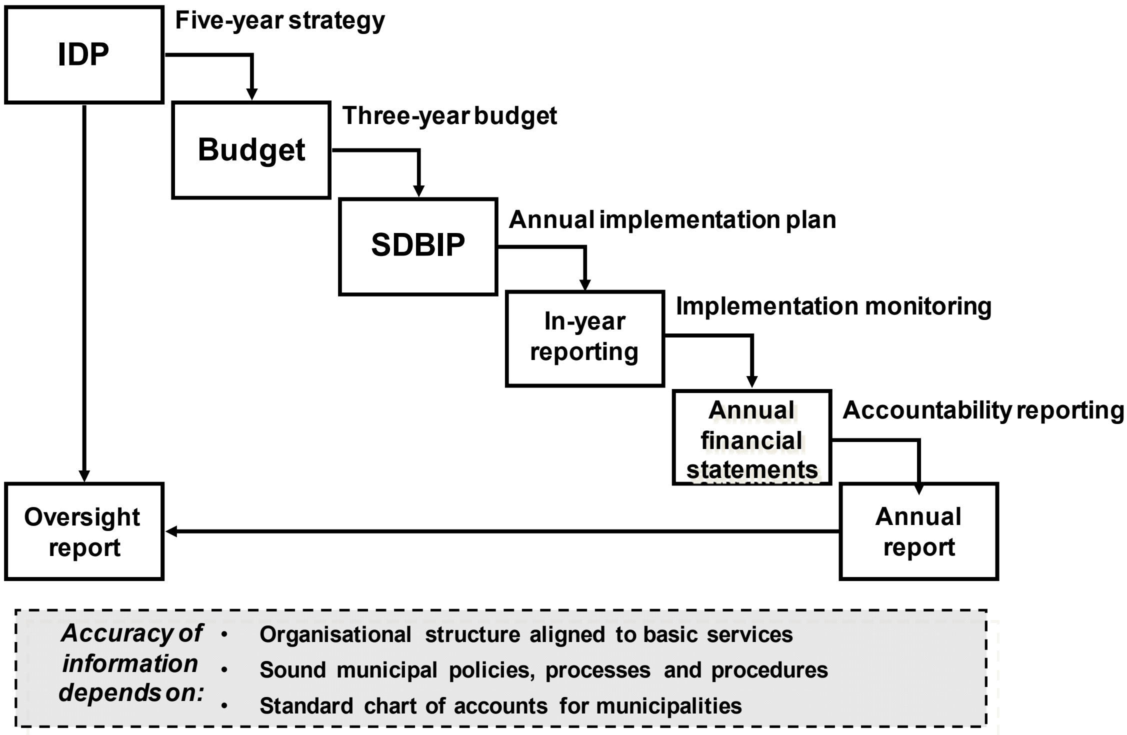
The MFMA, together with the Municipal Systems Act (2000), aims to facilitate compliance with this constitutional duty by ensuring that municipalities' priorities, plans, budgets, implementation actions and reports are properly aligned.

*Municipalities' priorities, plans, budgets, implementation actions and reports need to be properly aligned*

Figure 5.1 shows the main components of the financial management and accountability cycle and how they ought to be aligned:

- *Integrated development plan (IDP):* This sets out the municipality's goals and development plans, which need to be aligned with the municipality's available resources. Council adopts the IDP and undertakes an annual review and assessment of performance based on the annual report.
- *Budget:* The three-year budget sets out the revenue raising and expenditure plan of the municipality for approval by council. The allocation of funds needs to be aligned with the priorities in the IDP.
- *Service delivery and budget implementation plan (SDBIP):* The SDBIP sets out monthly or quarterly service delivery and financial targets aligned with the annual targets set in the IDP and budget. As the municipality's 'implementation plan', it lays the basis for the performance agreements of the municipal manager and senior management.
- *In-year reports:* The administration reports to council on the implementation of the budget and SDBIP through monthly, quarterly and mid-year reports. Council uses these reports to monitor both the financial and service delivery performance of the municipality's implementation actions.
- *Annual financial statements:* These report on the implementation of the budget, and reflect the financial position of the municipality. They are submitted to the Auditor-General, who issues an audit report indicating the reliance council can place on the statements in exercising oversight.

**Figure 5.1 Municipal financial management and accountability cycle**




*Source: National Treasury*

- *Annual report:* It is the primary instrument of accountability, in which the mayor and municipal manager report on implementation performance in relation to the budget and the SDBIP, and the progress being made in realising the IDP priorities.
- *Oversight report:* Council produces an oversight report based on outcomes highlighted in the annual report and actual performance.

The figure also highlights how the level of accuracy of the information set out in each of the accountability documents is dependent on a municipality having a properly aligned organisational structure, and sound policies, processes and procedures (including performance management), and implementing a standard chart of accounts (see below for more detail).

## Recent and future financial management reforms

*Reforming municipal financial management is not an event, but a process*

Reforming municipal financial management is not an event, but a process. The introduction of the MFMA in 2003 laid the foundation for this. Since then, regulations dealing with supply chain management, public private partnerships, the minimum competency requirements of municipal finance officials and asset transfers have been put in place. Each reform aims to build on the foundation laid by previous initiatives, taking into account the time needed for municipal systems and practices to change.

Since 2008, National Treasury has been giving specific attention to strengthening municipal budgeting and reporting practices. Key initiatives have been the introduction of the Municipal Budget and Reporting Regulations in 2009, the enforcement of in-year financial reporting processes and firmer management of conditional grants in accordance with the annual Division of Revenue Act. These reforms have been supported by strengthening National Treasury's local government database and by publishing an increasing range of local government financial information on National Treasury's website.

*Since 2008, National Treasury has been giving specific attention to strengthening municipal budgeting and reporting practices*

Future reform initiatives National Treasury is currently working on include:

- introducing a standard chart of accounts for municipalities to ensure financial transactions are captured consistently by municipalities, and so improve the quality of financial reporting
- strengthening revenue and cash management policies, processes and procedures, with a particular emphasis on tariff setting
- ensuring the better alignment of plans, budgets and reporting by paying attention to the structure and content of SDBIPs and annual reports, and aligning the format of annual financial statements to report against budgets
- strengthening non-financial reporting, to facilitate evaluations of 'value for money'
- finalising of the regulations for financial misconduct to facilitate the enforcement of the provisions dealing with financial conduct in chapter 15 of the MFMA.

## Strengthening planning and budgeting

Improved processes for municipal planning and budgeting empower a council to make more informed decisions and are fundamental to sustainable and efficient service provision.

*Improved processes for municipal planning and budgeting allow for more informed decisions and are fundamental to sustainable and efficient service provision*

The generic municipal budget cycle is set out in the MFMA and described in MFMA circular 19. The cycle involves:

- *a planning phase,* which starts with the mayor tabling in council a budget process schedule by August. This schedule sets key target dates for the budget process. The planning phase involves the strategic review of the IDP, setting service delivery objectives for the next three years, consultation on tariffs, indigent policy, credit control and free basic services, and reviewing the previous year's performance and current economic and demographic trends.
- *a preparation phase,* which involves the analysis of revenue and expenditure projections (based on the mid-year budget and performance assessment), revising budget related policies and considering local, provincial and national priorities.
- *a tabling and public consultation phase,* which requires the mayor to table a proposed budget, IDP revisions and budget policies in council by the end of March. Thereafter, the municipality is required to conduct public budget consultations during April and

May, as well as solicit input from National Treasury (benchmarking exercise), the relevant provincial treasury and other organs of state and municipalities.

- *a revision and debate phase,* which gives the mayor the opportunity to revise the tabled budget in response to inputs received, and then to table the budget in council for consideration before 1 June.
- *approval* of the budget by council before 1 July (the start of the municipal financial year).
- *publishing* the budget, the SDBIP and annual performance agreements of the municipal manager and senior managers on the municipal website.

### The Municipal Budget and Reporting Regulations

*The aim of the Municipal Budget and Reporting Regulations is to promote greater transparency and facilitate the alignment of policy priorities, plans, budgets and reports*

The Municipal Budget and Reporting Regulations came into effect on 1 July 2009. The regulations apply to all municipalities and municipal entities. Their primary purpose is to regulate the format and content of annual budgets, adjustment budgets and in-year reports to promote greater transparency and facilitate the alignment of policy priorities, plans, budgets and reports. The prescribed budget tables (tables A1 to A10) are designed to ensure that municipalities disclose key information regarding the funding of their budget, the management of assets and the delivery of basic services. They also facilitate the comparison and consolidation of municipal budget information in accordance with international financial reporting standards.

The regulations also require the establishment of a budget steering committee, regulate the disclosure of budgets for capital projects and specify the purposes and amounts that mayors may approve as 'unforeseen and unavoidable expenditure'.

**Role of the budget steering committee**

Section 4 of the Municipal Budget and Reporting Regulations requires that the mayor of a municipality establish a budget steering committee. This committee's role is to provide technical assistance to the mayor in discharging his or her responsibilities set out in section 53 of the MFMA. These responsibilities include providing political guidance to the IDP and budget processes and the priorities that must guide the preparation of the budget, ensuring the budget gets approved before 1 July, that a SDBIP is produced and that senior managers' annual performance contracts are signed, submitted to council and made public on time.

The prescribed membership of the committee emphasises the technical nature and role of the committee. It includes all senior managers within the municipality that need to be involved in the IDP and budget processes to ensure that they are aligned and relate directly to the service responsibilities of the municipality. The members of the committee will also ultimately be accountable for the implementation of the IDP and budget, through the SDBIP and their annual performance agreements. The 'councillor responsible for financial matters' is a member of the committee to represent the mayor and provide political guidance. The committee should be chaired by the chief financial officer, or alternatively the municipal manager.

The budget steering committee is not a committee of council, or a subcommittee of the mayor's executive committee. Council may decide to establish a separate council committee to exercise oversight of the IDP and budget, and the mayor may decide to establish a separate subcommittee of the executive committee to provide political guidance to the IDP and budget processes. These committees would need to work closely with the budget steering committee.

National Treasury has issued a range of documents to facilitate the implementation of the regulations. These include Excel schedules of the prescribed budget tables, the Budget Formats Guide, the Funding Compliance Guideline and the annual MFMA budget circulars 48, 51, 54 and 55 (all of which are available on National Treasury's website).

The first time all municipalities were required to produce their annual budgets in accordance with the new regulations was for the 2010/11 financial year. Of the 283 municipalities, 272 municipalities used the prescribed budget schedules (the Excel schedules). This is a major achievement. However, a far lesser number produced annual budget documents in accordance with the format prescribed in schedule A of the regulations. The quality and completeness of the information presented also varied greatly.

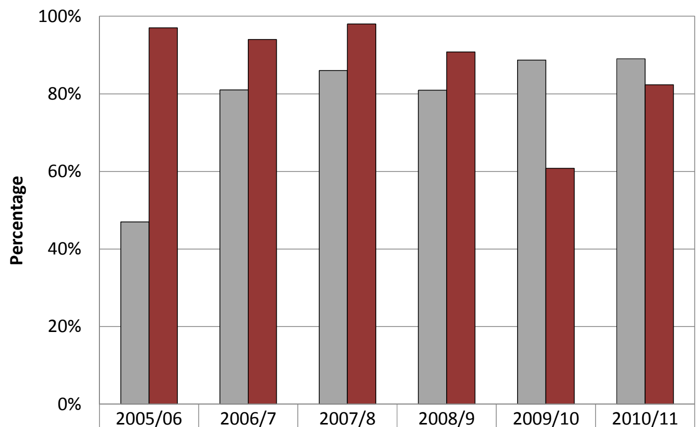
National Treasury's most recent supporting document is the Dummy Budget Guide, which presents the annual budget of a fictitious municipality called Batho Pele City. The aim is to illustrate the kind of information and analysis municipalities are expected to present in their annual budget documents. It is intended that municipal officials will use the guide as a template for producing their own municipality's budget documents in accordance with the requirements of schedule A of the Municipal Budget and Reporting Regulations.

*The aim of the Dummy Budget Guide is to illustrate the kind of information and analysis municipalities are expected to present in their annual budget documents*

### Meeting deadlines for tabling and approving budgets

The deadlines set out in the MFMA for tabling and approving budgets are minimum compliance requirements; municipalities may table and approve their budgets earlier. The budget must be tabled for consultation at least 90 days (31 March) before the start of the financial year (1 July). It must be considered for approval at least 30 days (1 June) before the start of that year, and it must be approved before the start of the financial year (1 July).

**Figure 5.2 Compliance with municipal budget tabling and approval deadlines, 2005 to 2010**




| | 2005/06 | 2006/7 | 2007/8 | 2008/9 | 2009/10 | 2010/11 |
|---|---|---|---|---|---|---|
| Tabled on time | 47% | 81% | 86% | 81% | 89% | 89% |
| Approved on time | 97% | 94% | 98% | 91% | 61% | 82% |

*Source: National Treasury local government database*

*When municipalities fail to meet budget deadlines, it puts the legality of their rates and tariffs at risk*

Figure 5.2 shows that since 2005/06, there has been a steady improvement in municipalities' compliance with the tabling deadline of 31 March. However, in 2010/11 there were still 31 municipalities that failed to meet this deadline, resulting in shortened community consultation processes. The number of councils that approved their annual budgets before 1 July has declined. In 2010/11 there were 50 municipalities that failed to meet this deadline. This poses very significant risks to these municipalities in relation to the legality of their rates and tariffs.

### Funding compliance and benchmarking municipal budgets

Section 18 of the MFMA requires that a municipality's annual budget must be 'funded', and identifies three possible funding sources: (a) realistically anticipated revenues to be collected, (b) cash-backed accumulated funds from previous years' surpluses not committed for other purposes, and (c) borrowed funds (but only for the capital budget). The regulations require the presentation of all the information needed to evaluate whether a municipality's operating and capital budgets are 'funded' or not. The 'funding compliance' process is described in MFMA circular 42 and the Funding Compliance Guideline.

As municipal officials draft a municipal budget, they are supposed to assess whether the budget is funded or not in accordance with the funding compliance procedure. It is a self-assessment process. To strengthen compliance with this process, in 2010, National Treasury introduced the 'budget benchmark hearings' for the 17 non-delegated municipalities[1]. The aim of the benchmarking is to check whether a municipality's revenue assumptions are realistic, whether its budget is 'funded' and whether the budget allocations are aligned with the IDP. As a consequence of the benchmarking process, National Treasury advised a number of municipalities to either redraft their budgets completely or to align their planned capital budgets with their available resources.

### Credibility of municipal budgets

*Evaluating whether a municipal budget is credible is a complex exercise*

Evaluating whether a municipal budget is credible is a complex exercise. It involves, among other things, checking whether the budget meets the constitutional requirement to prioritise basic services, whether it is aligned to the IDP, whether it is funded, whether the rates, tax and tariff increases are fair and sustainable, whether the cash-flow projections are realistic, and whether the budget provides adequately for the maintenance and renewal of existing infrastructure. The information that municipalities are required to present in the new budget formats allows each of these aspects to be evaluated.

[1] These are the municipalities that National Treasury exercises direct oversight of. They include the metros, the ten largest secondary cities and one district municipality. The Minister of Finance has delegated provincial treasuries to exercise oversight of the remaining municipalities within their provinces.

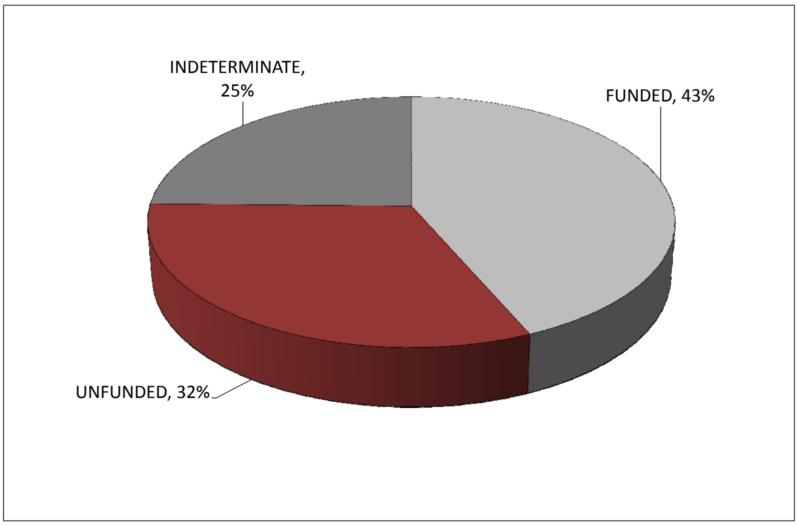
National Treasury analyses each of these aspects in the course of the benchmarking exercise for the 17 non-delegated municipalities. Provincial treasuries are being encouraged to do the same in respect of the delegated municipalities.

### *Are municipal budgets funded?*

National Treasury evaluated all 283 municipalities' 2010/11 budgets against the funding compliance criteria. Figure 5.3 shows that based on the information municipalities presented in their approved budgets, only 123 municipal budgets (or 43 per cent) were appropriately 'funded'. Of the remaining budgets, 90 were unfunded, and for 70, there was insufficient information to carry out the evaluation.

*Too many municipalities' for 2010/11 did not meet the funding compliance criteria*

**Figure 5.3 Funding compliance of municipalities' approved 2010/11 budgets**




*Source: National Treasury local government database*

If a municipal budget is unfunded, it is not a credible budget – either the revenue projections are unrealistic, the operating expenditures are too high, or the capital budget is too ambitious. In most instances, there are problems in all three areas. Correcting these problems involves going back to basics – and ensuring that the municipality only budgets to spend what it will realistically collect in revenue.

*If a municipal budget is unfunded, it is not a credible budget*

### *Are there cash-flow problems?*

In the past, municipalities tended to focus on budgeting first for expenditure and then for revenue. Apart from this being the wrong way round, revenue does not equal cash until it is collected, and if there are significant timing differences between the issuing of municipal bills and the customers paying their accounts, or if there are simply low collection rates, this can lead to severe cash-flow problems. The Municipal Budget and Reporting Regulations therefore require municipalities to budget for both revenue and cash, and also to allow for the timing differences between billing and collection. For many municipalities budgeting for cash, and cash-flow management is new, and many of them already find themselves in vulnerable cash positions (see the textbox in *Chapter 4 Revenue and expenditure trends in local government*). Consequently, having exhausted their historical cash reserves, many municipalities are learning cash

*The Municipal Budget and Reporting Regulations therefore require municipalities to budget for both revenue and cash, and also to allow for the timing differences between billing and collection* management the hard way: first getting into difficulty, facing the reality of not being able to pay staff salaries and creditors, and then putting in place a plan to manage cash carefully and proactively. This means cutting unnecessary expenditures and prioritising revenue management.

### *What is the extent of over and under-spending of budgets?*

*When municipalities do not stick to the approved allocations, they often overspend on the operating budget and under-spend on the capital budget*

If a municipality's budget is not credible, then the municipality will not be able to implement it – i.e. stick to the approved allocations. This most often results in overspending on the operating budget and underspending on the capital budget.

Table 5.1 shows municipalities' percentage over- and underspending of their 2009/10 operating budgets. If the variance on the operating budget is greater than 5 per cent it is very likely that the original budget was not credible.

**Table 5.1 Over and under spending of operating budget for the 4th quarter ended 30 June 2010**

| | Over | | | On target | | Under | | |
|---|---|---|---|---|---|---|---|---|
| Number | More than 15% over | 10% to 15% over | 5% to 10% over | 0% to 5% over | 0% to 5% under | 5% to 10% under | 10% to 15% under | More than 15% under |
| **Province** | | | | | | | | |
| Eastern Cape | 5 | – | 1 | 17 | 1 | 3 | 4 | 14 |
| Free State | 3 | – | – | – | 2 | 4 | 1 | 15 |
| Gauteng | – | 1 | – | – | 3 | 6 | 1 | 4 |
| Kwazulu-Natal | 5 | – | 3 | 3 | 9 | 10 | 8 | 23 |
| Limpopo | 6 | 1 | – | 8 | 3 | 2 | 5 | 5 |
| Mpumalanga | 3 | 1 | – | 5 | 2 | 1 | – | 9 |
| Northern Cape | 2 | – | – | 7 | 3 | 1 | 4 | 15 |
| North West | 2 | – | 3 | 3 | 1 | 2 | 1 | 12 |
| Western Cape | 3 | – | – | 1 | 2 | 7 | 5 | 12 |
| **Total** | **29** | **3** | **7** | **44** | **26** | **36** | **29** | **109** |

*Source: National Treasury Local Government Database*

Given the service delivery pressures at municipal level, the fact that 174 municipalities underspent their operating budget by more than 5 per cent is somewhat surprising. It indicates that: (a) the budgets were over ambitious; (b) there were management problems in implementing the budget; or (c) the municipality did not collect the revenue required to fund the expenditure. All of these explanations point to problems with the credibility of the municipalities' approved budgets.

*Overspending on the operating budget can be due to inadequate expenditure controls in place or non-credible allocations in the approved budget*

On the other side, 39 municipalities overspent their operating budgets by more than 5 per cent. Usually this is due to the municipality having inadequate expenditure controls in place, but may also be due to the allocations in the approved budget not being credible, i.e. too low.

Table 5.2 shows municipalities' percentage over- and underspending of their 2009/10 capital budgets. If the variance on the capital budget is greater than 10 per cent it is very likely that the original budget was not credible. The table shows that 28 municipalities overspent their capital budgets by more than 10 per cent, while 183 underspent by more than 10 per cent. 9 municipalities (or 3 per cent) underspent their capital budgets by between 5 and 10 per cent.

**Table 5.2 Over and under spending of capital budget for the 4th quarter ended 30 June 2010**

| | Over | | On target | | | | Under | |
|---|---|---|---|---|---|---|---|---|
| Number | More than 15% over | 10% to 15% over | 5% to 10% over | 0% to 5% over | 0% to 5% under | 5% to 10% under | 10% to 15% under | More than 15% under |
| **Province** | | | | | | | | |
| Eastern Cape | 5 | – | 1 | 21 | 1 | – | 3 | 14 |
| Free State | 1 | – | 1 | 1 | – | 1 | – | 21 |
| Gauteng | 2 | – | – | 2 | – | – | 1 | 10 |
| Kw azulu-Natal | 7 | 3 | 2 | 5 | 2 | 2 | 3 | 37 |
| Limpopo | 3 | 1 | – | 6 | 1 | 1 | 1 | 17 |
| Mpumalanga | 1 | – | 1 | 5 | – | – | – | 14 |
| Northern Cape | 4 | – | – | 10 | – | 2 | 1 | 15 |
| North West | – | – | – | 3 | – | – | – | 21 |
| Western Cape | 1 | – | – | 1 | – | 3 | 5 | 20 |
| **Total** | **24** | **4** | **5** | **54** | **4** | **9** | **14** | **169** |

*Source: National Treasury Local Government Database*

In total, municipalities underspent their 2009/10 capital budgets by R15 billion. Of this amount, R3.3 billion was under spending of conditional grants for infrastructure. The reasons for capital under spending differ between municipalities, but usually it is either because budgets are unfunded (i.e. the cash for implementation is not available), or because the municipalities do not have the technical management capacity to implement.

*In total, municipalities underspent their 2009/10 capital budgets by R15 billion*

The funding compliance procedure and the emphasis on cash management in the new budget formats seeks to address certain of these problems. However, issues of appropriate prioritisation, costing of services and projects, and technical capacity need to be addressed at an organisational level.

## Strengthening oversight through improved transparency

The system of reporting in the MFMA aims to ensure that municipalities produce financial and performance information that is timely and reliable. This enables managers to act proactively to identify and resolve problems and provide councils with the information they need to fulfil their oversight responsibilities.

The reports on the implementation of the budget and the SDBIP required by the MFMA include monthly and quarterly budget statements, a half-yearly performance assessment, annual financial statements and annual reports.

### Publication of municipal information

Over the past three years, National Treasury has significantly expanded the range of municipal information published on the MFMA section of its website: www.treasury.gov.za

*Over the past three years, National Treasury has significantly expanded the range of municipal information published*

The information now includes annual budget information, quarterly section 71 finance reports and annual financial statements, as well as municipal IDPs, approved budget documents and annual reports. By publishing all this information, National Treasury aims to:

- *increase transparency:* There is a well-known public management maxim that says ‘when performance information gets reported, performance improves; when it gets published, performance improves still further’. This is because the increased transparency places pressure on managers to deliver. It is also well-known that greater transparency forces improvements in the accuracy of information – as no manager wants to explain why the numbers he or she signed off on are wrong.

- *support monitoring:* In the absence of credible information, it is not possible to monitor where there may be problems and to develop appropriate support strategies. By publishing the information, National Treasury aims to support other national departments and provincial treasuries in their monitoring of municipalities.
- *support analysis and research:* By publishing municipal information, National Treasury aims to encourage a broader pool of researchers to engage with the challenges facing local government, and facilitate the development of evidence based policy proposals to overcome the challenges.
- *reduce the reporting burden:* In 2007, National Treasury reviewed the range of information requests that national departments made to municipalities. The findings revealed enormous duplication, particularly in relation to financial information. National Treasury has therefore put in place processes to ensure that municipalities only have to report financial information once. National Treasury checks the quality of the information and publishes it. So there is now, one authoritative, readily accessible national source of municipal financial information, and no need for any other entity to approach municipalities for this information.

*The MFMA requires municipalities to publish key documents and information on their website*

Municipalities are also required by section 75 of the MFMA to publish key documents and information on their website, including the IDP, the annual budget, adjustments budgets and budget related documents and policies. A municipal website should be an integral part of a municipality’s communication strategy. If managed effectively, it allows easy access to relevant information, can serve as a tool for community participation and improve stakeholder involvement in monitoring and evaluation of municipal performance.

### In-year monitoring

*Monitoring the implementation of the budget is a key responsibility of the mayor and should ensure that financial problems are identified early*

Section 71 of the MFMA requires the accounting officer to submit monthly budget statements to the mayor, who must table these in council on a monthly basis. Monitoring the implementation of the budget is a key responsibility of the mayor and should ensure that financial problems are identified early.

Municipalities are also required to submit the section 71 reports to National Treasury on a quarterly basis. This information is captured on National Treasury’s local government database, checked and then published on National Treasury’s website as soon after the end of the quarter as possible. Improving the coverage and timeliness of the section 71 reporting process has been a key priority. In 2007/08 the number of municipalities that reported in the fourth quarter was 271, in both 2008/09 and 2009/10 there were quarters in which all municipalities reported.

While the quality of the information is still uneven, it does improve with each quarter. National Treasury is also working at developing a range of diagnostic and process checks to improve the quality of the information. However, as noted above, if managers have to account for the information, they will take more care when signing off on it.

*If managers have to account for the information, they will take more care when signing off on it*

## Annual financial statements

The annual financial statements are the most important record of the financial status of a municipality and municipal entity. Every municipality and municipal entity must prepare annual financial statements and submit them to the auditor-general for auditing no later than 31 August of each year. In the case of a municipality with municipal entities, the municipality is also required to submit consolidated annual financial statements to the auditor-general no later than 30 September of each year.

*The annual financial statements are the most important record of the financial status of a municipality and municipal entity*

## Annual reports

The MFMA requires that every municipality and municipal entity must prepare an annual report for each financial year.

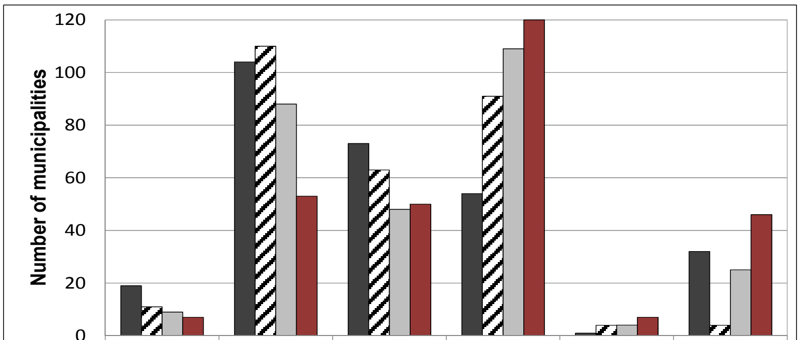
The annual report is the key instrument of transparent governance and accountability and must be used to report on performance for the year. The early completion and submission of annual reports, together with the annual financial statements, will facilitate timely oversight. Oversight of the annual report represents the final stage in the accountability cycle.

Once approved by the council, the annual report must be placed on the municipal website, made available to the wider community and copies must be sent to various stakeholders.

## Audit opinions issued by the Auditor-General

The Auditor-General's opinion is the most important part of the auditor's report provided to the municipality. The audit findings are based on an independent and often extensive verification process of the annual financial statements and the performance information in the annual report.

**Figure 5.4 Municipal audit opinions, 2006/07 – 2009/10**




| | Adverse opinion | Disclaimer of opinion | Qualified | Unqualified - Emphasis of Matter | Unqualified - No findings | Audits Outstanding |
|---|---|---|---|---|---|---|
| 2006/07 | 19 | 104 | 73 | 54 | 1 | 32 |
| 2007/08 | 11 | 110 | 63 | 91 | 4 | 4 |
| 2008/09 | 9 | 88 | 48 | 109 | 4 | 25 |
| 2009/10 | 7 | 53 | 50 | 120 | 7 | 46 |

*Source: Auditor General, Audit opinions 2009/10*

*Since 2006/07, the number of municipalities that received an adverse or disclaimed audit opinion has more than halved*

Figure 5.4 shows that there has been a significant improvement in municipalities' audit outcomes since 2006/07. The number of municipalities that received an adverse or disclaimed audit opinion has more than halved, while the number of unqualified opinions with emphasis of matter has more than doubled. Most of these improvements pre-date the launching of the Department of Cooperative Governance's Operation Clean Audit – so further improvements in audit outcomes are likely as the initiative moves to achieve its objective of clean audits for all municipalities by 2014.

*It is important to note that a compliance audit is not an assessment of financial health*

Where audit outcomes are adverse, disclaimed or qualified it indicates that fundamental principles of good governance, transparency and financial management are not being adhered to. Even an unqualified audit with an emphasis of matter can indicate serious financial management shortcomings – depending on the issues raised by the Auditor-General. It also needs to be noted that an unqualified audit opinion does not mean that the municipality is financially sound. These issues need to be separated from each other – a compliance audit is not an assessment of financial health.

*Common weaknesses identified in the Auditor-General's audit reports are in management and accounting skills, operational financial management, internal controls, and revenue and supply chain management*

The most common weaknesses identified through the Auditor-General's audit reports are in management and accounting skills, shortcomings in operational financial management, lack of internal controls and weaknesses in revenue management, supply chain management and asset management. These weaknesses result in high levels of material losses/impairments, unauthorised expenditure, fruitless and wasteful and irregular expenditure.

**Processes to authorise unauthorised expenditures**

In terms of section 32 of the MFMA, 'unauthorised expenditure' may only be authorised (condoned) by the municipal council in an adjustments budget. In this regard, regulation 23(6) of the Municipal Budget and Reporting Regulations provides that:

> (6) An adjustments budget contemplated in section 28(2)(g) of the Act may only authorise unauthorised expenditure as anticipated in section 32(2)(a)(i) of the Act, and must be –
> (a) dealt with as part of the adjustments budget contemplated in sub-regulation (1); and
> (b) a special adjustments budget tabled in the municipal council when the mayor tables the annual report in terms of section 127(2) of the Act, which may only deal with unauthorised expenditure from the previous financial year which the council is being requested to authorise in terms of section 32(2)(a)(i) of the Act.

In practice this means:

- Unauthorised expenditure that occurs in the first half of a municipal financial year may be authorised by the council in the main adjustments budget that must be tabled in council before 28 February (see regulation 23(1) of the Municipal Budget and Reporting Regulations).
- Unauthorised expenditure that occurs in the second half of the financial year, or that occurred in the first half of the year but was not authorised in the main adjustment budget (above), has to be reported in the annual financial statements, audited and then only when the mayor tables the annual report in council can an adjustment budget be tabled in council to authorise this expenditure.
- If the council decides not to authorise an unauthorised expenditure, then it must be recovered from the person liable for that expenditure unless the council certifies that the amount is irrecoverable and it is written off by the council.

This power to authorise unauthorised expenditure and certify unauthorised, irregular or fruitless and wasteful expenditure as irrecoverable may not be delegated to a council committee or to any administrative committee or official. It is a core competency and function of the council.

In this regard, regulation 74 of the Municipal Budget and Reporting Regulations provides that:

> (1) A council committee contemplated in section 32(2)(a)(ii) of the Act to investigate the recoverability of any unauthorised, irregular or fruitless and wasteful expenditure must consider –
> (a) the measures already taken to recover such expenditure;
> (b) the cost of the measures already taken to recover such expenditure;
> (c) the estimated cost and likely benefit of further measures that can be taken to recover such expenditure; and
> (d) submit a motivation explaining its recommendation to the municipal council for final decision.

Section 32 of the MFMA (nor any other section) does not permit a council to authorise or condone irregular or fruitless and wasteful expenditure under any circumstances. Irregular or fruitless and wasteful expenditure' may only be (1) recovered from the person liable for that expenditure or (2) certified by the council as irrecoverable and written off. Under exceptional circumstances the National Treasury may be approached to condone such expenditure in terms of section 170 of the MFMA.

## Institutional strengthening and capacity building

In most municipalities there is a general lack of the technical skills and knowledge necessary for performing key duties in financial management from an operational perspective. This is a major constraint and one of the biggest challenges facing municipalities. These technical skills include planning, engineering, project management and plant operating. Inadequate capacity at the senior management level and a lack of appropriate financial management skills in municipalities results in poor service delivery. Furthermore, a high turnover of senior management in municipalities, particularly of chief financial officers, is a major issue affecting municipalities' capacity to manage their finances properly and thus lay a sound foundation to expand and improve service delivery.

### The budget and treasury office

*The budget and treasury office is responsible for managing the municipality's finances and overseeing that all branches of the municipality comply with all finance related legislation and council policies*

Section 80 of the MFMA requires that each municipality have a budget and treasury office, headed by the chief financial officer and consisting of the officials that report to him or her. The budget and treasury office is responsible for managing the municipality's finances and overseeing that all units of the municipality comply with all finance related legislation and council policies.

National and provincial programmes to strengthen the financial management capacity of municipalities have invariably focused on strengthening the budget and treasury offices, and building the capacity of staff within the office. While there is progress, and municipal financial management is improving, the effectiveness of these capacity-building initiatives is hampered by low levels of staff experience, staff with inappropriate qualifications, high vacancy rates and high staff turnover. Of concern is that even when a municipality has an opportunity to appoint new staff to the budget and treasury office, very often people with inappropriate experience and qualifications get appointed. This is despite the fact that the Municipal Regulations on Minimum Competency Levels came into effect on 1 July 2007.

### Preparing for the effective date of the competency regulations

According to regulation 18 of the Municipal Regulations on Minimum Competency Levels the continued employment of financial officials and supply chain management officials appointed after 1 July 2007 is subject to them obtaining the required higher education qualification and the required minimum competency level on or before 1 January 2013. If they fail do so their employment will automatically be terminated. There is no problem if the official is working towards obtaining the necessary qualifications and competencies. But it would seem that many are not doing so. This poses an enormous risk both to the officials who stand to lose their jobs, and to the municipalities who may find that few of their officials actually make the grade to work in the budget and treasury office and supply chain management function, and who will then be faced with a forced exodus of staff.

*Municipalities must ensure that their job descriptions, competency requirements, advertisements, selection criteria and appointments are aligned with the requirements set out in the regulations*

National Treasury is working with the South African Local Government Association (SALGA) to raise awareness of the regulations and to ensure that they are institutionalised in municipalities' human resource management processes. This means that municipalities must ensure that their job descriptions, competency requirements, advertisements, selection criteria and appointments are aligned with the requirements set out in the regulations.

## Municipal finance management programme

This is a formal training programme designed to support the implementation of the competency regulations. It is structured to enable officials to attain the required competency levels by participating in accredited training sessions over time. Officials occupying senior financial management positions need to obtain formal qualifications at NQF levels 5 and 6. Entry level positions require competencies at NQF levels 3 and 4.

*The municipal finance management programme is structured to enable officials to attain the required competency levels*

National Treasury, working with the LGSETA, has trained and accredited 41 regionally based training providers, including PALAMA and the DBSA's Vulindlela Academy. These service providers are required to use a uniform set of training and assessment instruments on their courses. Training on the lower level competencies is being done through LGSETA funded learnerships delivered in partnership with the South African Institute of Chartered Accountants. By mid-2010, over 600 learners had graduated from this programme.

Table 5.3 presents a high level summary of the number of municipal officials that have participated in this programme since its inception.

**Table 5.3 Participation in the formal programme - MFMP**

| Learning Programmes | EC | FS | GP | KZN | LP | MP | NW | NC | WC | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Strategic Management; Budgeting Implementation and Performance Management | 584 | 446 | 125 | 282 | 378 | 461 | 400 | 402 | 300 | 3 378 |
| Municipal Accounting and Risk | 330 | 265 | 75 | 154 | 180 | 253 | 211 | 212 | 142 | 1 822 |
| Governance and Legislation | 219 | 186 | 51 | 111 | 141 | 163 | 153 | 166 | 112 | 1 302 |
| Cost and Capital Planning | 2 | – | – | – | 2 | 4 | – | – | 4 | 12 |
| Muncipal IT support and Project | 1 | – | – | – | 3 | 7 | – | – | 2 | 13 |
| SCM and PPP | 205 | 111 | 27 | 85 | 81 | 136 | 103 | 132 | 114 | 994 |
| **Total** | **1 341** | **1 008** | **278** | **632** | **785** | **1 024** | **867** | **912** | **674** | **7 521** |

*Source: National Treasury local government database*

## Municipal finance management internship programme

The programme started in 2004 to help municipalities build up their in-house financial management capacity by providing internships to graduates in accounting, economics, finance and risk management. The internship is for two years, and includes mandatory formal training in the competencies required by the Municipal Regulations on Minimum Competency Levels. Municipalities are encouraged to provide permanent employment to interns once they have completed the programme.

*The municipal finance management internship programme provides internships to graduates in accounting, economics, finance and risk management*

In 2004, the first intake was 114 interns. Table 5.4 shows that there were 1 241 interns on the programme as at 30 September 2010. Past interns are those who are currently in their second year, while current interns are those who are in their first year.

**Table 5.4 MFMIP as at 30 September 2010**

| Province | No. of munici-palities | Captured on Intern Database Past Interns | Current Interns | Cumulative Total |
|---|---|---|---|---|
| Eastern Cape | 45 | 73 | 105 | 178 |
| Free State | 25 | 25 | 117 | 142 |
| Gauteng | 14 | 9 | 46 | 55 |
| Kwazulu Natal | 61 | 78 | 184 | 262 |
| Limpopo | 30 | 51 | 110 | 161 |
| Mpumalanga | 21 | 20 | 67 | 87 |
| North West | 25 | 14 | 61 | 75 |
| Northern Cape | 32 | 38 | 118 | 156 |
| Western Cape | 30 | 43 | 82 | 125 |
| **Total** | **283** | **351** | **890** | **1 241** |

*Source: National Treasury local government database*

### Reform of the Siyenza Manje programme

*The Siyenza Manje programme now includes financial and engineering components*

The Siyenza Manje programme was initiated by National Treasury in partnership with the DBSA in 2006. The programme was designed to run for three years, but was extended for a fourth year to end March 2011. Initially the programme focused on developing municipalities' capacity to manage the implementation of infrastructure projects. So, much of the hands-on support was provided by engineering deployees. Later the programme was expanded to include financial management deployees.

In 2010, government decided to restructure the programme in order to ensure the departments responsible for financial management and infrastructure matters respectively were placed in a position to direct the deployment of support and to monitor the effectiveness of the programme.

## Conclusion

A firm foundation of financial management systems and capacity is key to the successful implementation of infrastructure programmes, service delivery expansion efforts, improvements in the level, reliability and frequency of services. It is therefore absolutely critical that the correct skills, mindset and expertise are located at the right places within the municipality.

Further measures will need to be considered as to how best to enforce compliance with the legal framework for financial management. A combination of measures, such as withholding transfers, firmer implementation of the code of conduct for municipal councillors and officials and withholding performance bonuses when service delivery fails will need to be reinforced. It is now seven years since the Act was introduced. The phasing that was afforded to so-called low, medium and high capacity municipalities lapsed completely in 2007/08, therefore all municipalities are expected to comply fully.

However, the aim is ultimately that municipal officials will do the right thing because they agree with and seek to act in accordance with the principles of good governance, transparency and stewardship of public resources.

# 6

# Leveraging private finance

## Introduction

According to the World Bank's 1994 World Development Report, a 1 per cent increase in the stock of a country's infrastructure is associated with a 1 per cent increase in the country's GDP. This suggests that investment in municipal infrastructure is critical for promoting and sustaining economic growth, as well as for eradicating service delivery backlogs, responding to demographic changes such as urbanisation, and rehabilitating ageing infrastructure.

*The economic recovery is putting more pressure on municipalities to provide infrastructure to support growth*

The economic recovery in South Africa in 2010 has resulted in a resumption of pressure on municipalities to provide infrastructure to support growth. Following a 1.7 per cent contraction in GDP in 2009, South Africa's economy grew by 2.7 per cent in 2010 and is projected to grow at 4.1 per cent by 2012.

Municipalities urgently need to find innovative ways of financing this new infrastructure. Existing sources of capital finance, namely municipalities' internally generated funds, intergovernmental grants and borrowing, are insufficient. Other sources of capital finance, such as development charges, land leases and public private partnerships (PPPs), can play important complementary roles.

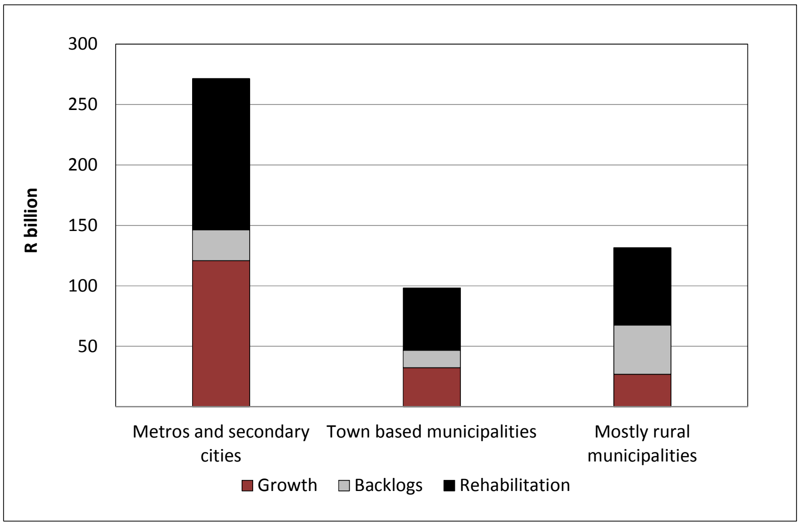
This chapter gives an overview of:

- municipal infrastructure investment requirements
- sources of infrastructure finance
- developing the municipal borrowing market.

## Municipal infrastructure investment requirements

In 2009, the World Bank produced the Municipal Infrastructure Finance Synthesis Report that explored the demand and cost of South Africa's municipal infrastructure needs over the next 10 years. In this report, it is estimated that total municipal infrastructure investment requirements for all municipalities to be approximately R500 billion over the next 10 years. Of this amount, R421 billion is required to finance new infrastructure to support economic and population growth and the rehabilitation of ageing infrastructure, while the remaining R79 billion is required for the eradication of backlogs.

**Figure 6.1 Municipal infrastructure investment requirement, 2009**




*Source: World Bank (2009 Municipal Infrastructure Finance Synthesis Report)*

The burden of this investment requirement, however, differs markedly across municipalities:

*Investment needs of metros and secondary cities are estimated to amount to R271 billion over the next 10 years*

According to figure 6.1, the investment needs of metros and secondary cities are estimated to amount to R271 billion over the next 10 years, of which R26 billion is for the eradication of backlogs, and the remaining R245 billion is needed to fund new infrastructure to support growth and to rehabilitate ageing infrastructure.

*The investment needs in these municipalities is estimated at about R98 billion*

The investment needs of the 140 municipalities that are anchored by smaller cities and large towns (so-called B2 and B3 municipalities) amount to about R98 billion, of which R52 billion is needed for rehabilitation, R14 billion for addressing backlogs and the remaining R32 billion for supporting growth. These municipalities often find it difficult to access capital markets, either because the scale at which they wish to borrow makes lending expensive, or because weaknesses in their financial management make them a poor credit risk to lending institutions.

The investment requirement of the 70 mostly rural municipalities (so-called B4 municipalities) is estimated to be R131 billion over the next 10 years, of which R40 billion is for the eradication of backlogs, and the remaining R91 billion is for infrastructure to support growth and the rehabilitation of existing assets. The borrowing capacity of these municipalities is very limited. As average household incomes in these municipalities are very low, the scope for them to collect revenues from property rates and service charges is limited. Consequently, these municipalities will continue to rely mainly on government transfers to fund their capital budgets. Generally, borrowing to finance their infrastructure needs is not an option, unless provided on special terms by development finance institutions.

## Sources of infrastructure finance

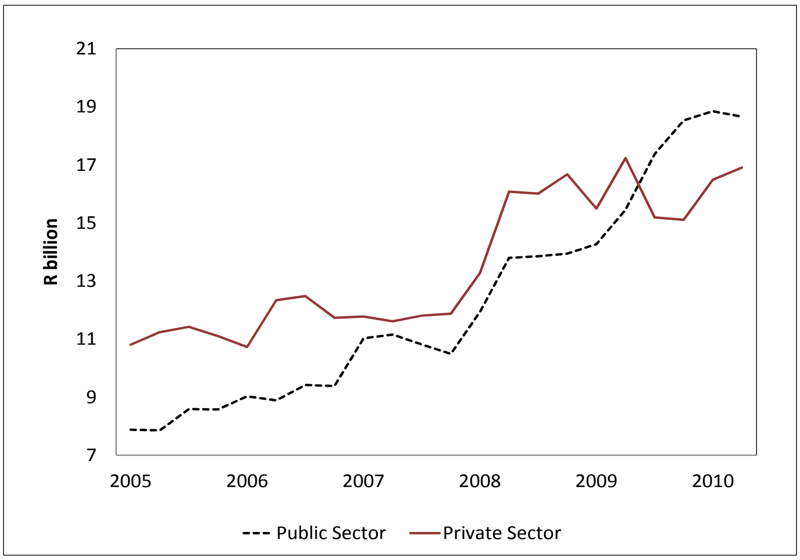
The primary sources of infrastructure finance available to municipalities are internally generated funds and national transfers from government. However, these are insufficient to meet the scale of infrastructure investment required by municipalities. There is thus a need for municipalities to explore ways of leveraging private finance to mobilise additional resources to fund infrastructure investments. Four broad options exist: borrowing, development charges, land leases and PPPs.

*Municipalities need to explore ways of leveraging primary sources of finance to mobilise additional resources for funding infrastructure investments*

### Municipal borrowing

Figure 6.2 shows the trend in public and private sector lending to municipalities from 2005 to 2010. The total closing balances in outstanding municipal borrowings grew from R18.7 billion in 2005 to R38.1 billion in 2010, representing an average annual growth of 15 per cent.

**Figure 6.2 Trends in the municipal borrowing market**




*Source: National Treasury local government database*

The growth in borrowing from the public sector is of particular significance. Private lenders became more risk averse during the recession, with total debt from late 2008 to the end of the third quarter of 2010 remaining flat. In addition, INCA (which is the trading name of the Infrastructure Finance Corporation Limited), a major lender to municipalities, withdrew from the market in 2009 (citing declining margins due to competition from public sector lenders as the main

*During the recession, total public sector lending exceeded private sector lending for the first time* reason). By contrast, public sector lending – almost entirely from the Development Bank of Southern Africa (DBSA) – accelerated sharply during this period, resulting in total public sector lending exceeding private sector lending for the first time.

Most municipal borrowing from both private and public sector financial institutions takes the form of long-term loans. These account for R25.4 billion (64 per cent) of total borrowing. Securities, mainly in the form of municipal bonds, account for R11.8 billion (30 per cent) of total borrowing, while short term debt accounts for 6 per cent, of which R909 million are bank overdrafts and R2.4 billion is commercial paper.

*The municipal bond market accounts for only 2 per cent of total government bonds listed on the Johannesburg Stock Exchange*

Bonds have been issued by three of the six metros (Johannesburg, Cape Town and Ekurhuleni). Due to the limited activity in this area, at R11.8 billion, the municipal bond market remains small and underdeveloped, accounting for only 2 per cent of total government bonds listed on the Johannesburg Stock Exchange.

Municipal bond repayments are typically structured with a large, lump sum (or 'bullet') payment at the end of the repayment period. This creates a spike in municipal debt repayment profiles that requires careful management to minimise the risk of default. This risk is partly offset by the fact that by the time the bond needs to be repaid the municipality's revenues should have grown substantially.

Nevertheless, ideally, the debt service profiles of municipalities should be more or less uniform over time. Deferring higher levels of debt servicing to later years can indicate current fiscal pressure. If adequate reserves (a sinking fund) are not set aside over the period of the bond, the municipality will be forced to refinance the final 'bullet' payments with additional debt.

Although there has been a recent recovery in private lending to municipalities, there is a concern that both the historical and current level of private lending to municipalities is still very limited. This is despite the legislative and policy reforms that have been introduced to stimulate private sector participation. Recent research indicates that the development of the municipal debt market is being limited by the following six factors:

- *The lack of a developed secondary bond market.* A secondary market would enhance the liquidity of bond instruments as it enables municipal bondholders to trade the instrument. However, the limited size of the municipal bond issues to date is itself an obstacle to such a secondary market developing. The South African bond market is dominated by pension funds and insurers which invest funds with the intention to hold until maturity. The lack of a developed secondary municipal bond market means investors with shorter time horizons are reluctant to buy long-term instruments whose term matches the economic life of infrastructure investments.
- *Short maturities on loans.* The short maturities offered by banks means that municipalities cannot obtain loan tenures that are in

line with the life span of assets. Municipalities are compelled to finance long life assets with medium term funds. This means that rates and tariffs have to be higher in the medium term, and funds have to be used to fund higher debt service costs rather than services over the period of the loans.

- *Creditworthiness.* Borrowing should be used to finance infrastructure that will generate income for the municipality, either directly through tariff income or indirectly through higher property rates income. Currently, many municipalities are using borrowing to fund social infrastructure, which costs money to operate, but does not expand their revenue base. This impacts negatively on municipalities' creditworthiness and, together with many municipalities' overall poor financial performance, has reduced their capacity to incur further debt.
- *Lack of treasury management capacity.* Treasury management skills and capacity vary significantly across municipalities. Most municipalities do not have clear borrowing strategies that support their infrastructure investment programmes. Improving treasury management capacity within municipalities will help to optimise their borrowing activities, including their debt profile.
- *The role of the DBSA.* While the DBSA's increased lending to municipalities is a welcome development; going forward, it needs to explore strategies for partnering with the private sector so as to crowd-in lending to local government in line with its mandate. Also, the DBSA's loan book should reflect an appetite for risk that is somewhat different to that of private sector institutions and more commensurate with lending to municipalities at the lower end of the market.

**Sustainability of metros' borrowing**

The sustainability of a municipality's borrowing depends on a wide range of factors, including the strength of its management team, the type of infrastructure funded and the municipalities' revenue management record. Using the traditional gearing ratio within the municipal context does not provide a useful indicator of the sustainability of municipal debt, because in terms of section 48(3) of the MFMA a council may determine that certain assets are necessary to provide the minimum level of basic municipal services and so cannot be used as security for borrowing. Further, many assets now being brought onto municipalities' books in terms of GRAP 17 are not tradable (e.g. roads and pavements). GRAP 17 also allows municipalities to use different methodologies to value their assets; consequently the values reflected in the asset registers may not be comparable.

The following table compares measures of the six metros borrowing. This table should be read together with the information on the following two pages.

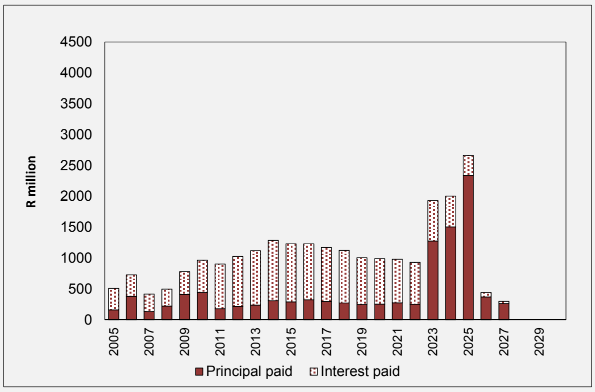
**Measures of metro borrowing, 2011/12 adopted budgets**

| Rand thousands | Johannesburg | Cape Town | eThekwini | Ekurhuleni | Tshwane | Nelson Mandela Bay |
|---|---|---|---|---|---|---|
| Total borrowing liability | 11 456 835 | 6 679 271 | 11 270 509 | 4 333 358 | 6 487 030 | 1 729 021 |
| Proposed borrowing for the financial year | 1 000 000 | 1 357 386 | 2 000 000 | 867 935 | 1 500 000 | – |
| Cost of borrowing for the financial year | 1 844 483 | 966 040 | 1 819 044 | 663 579 | 1 217 198 | 312 128 |
| Total cost of debt as a % of total borrowing liability | 16.1% | 14.5% | 16.1% | 15.3% | 18.8% | 18.1% |
| Total cost of debt as a % of own revenue | 7.5% | 4.8% | 9.4% | 7.8% | 7.7% | 6.2% |
| Total cost of debt as a % of operating expenditure | 6.5% | 4.4% | 8.6% | 6.6% | 6.7% | 4.8% |

*Source: National Treasury local government database*

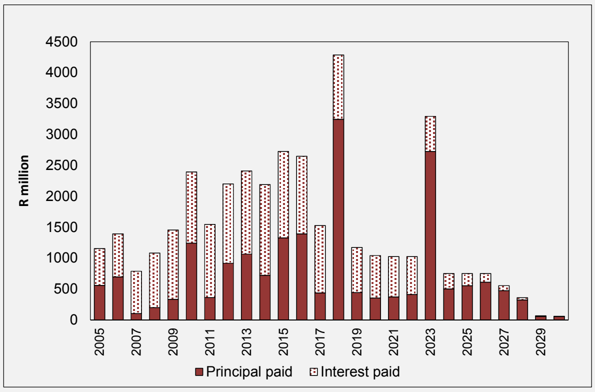
**Debt service profiles of South Africa's metros**

**Cape Town**



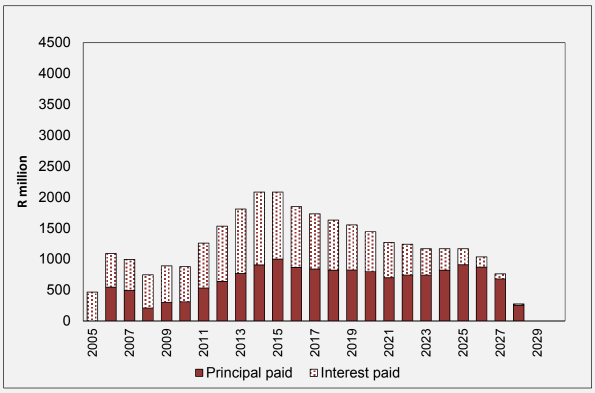

Cape Town's borrowing liability at the end of June 2011 was R6.7 billion. The debt profile shows that debt service costs average R900 million per annum and are expected to increase steeply between 2023 and 2025 as the principals on its three bond issues fall due. At 14.5 per cent, Cape Town's total cost of debt as a percentage of its total borrowing is the lowest of all the metros.

**Johannesburg**




Johannesburg's borrowing liability at the end of June 2011 was R11.5 billion. The peaks in the debt profile in 2018 and 2023 point to the need for the City to smooth the maturity profile of its debt. The use of municipal bonds has enabled the City to keep its total cost of debt as a percentage of its total borrowing to 16.1 per cent. Total cost of debt as a percentage of own revenue is at 7.5 per cent.

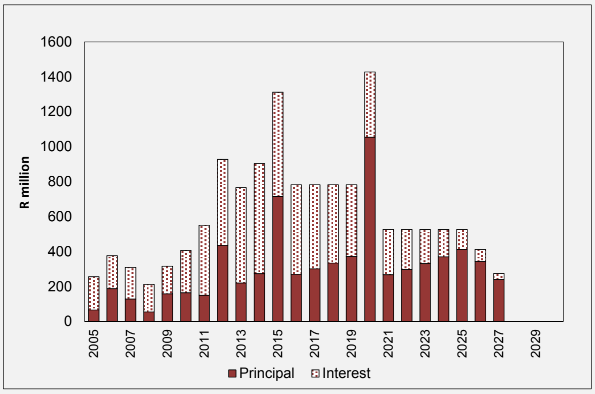
**eThekwini**




eThekwini's borrowing liability at the end of June 2011 was R11.3 billion. Cost of borrowing for 2011/12 is budgeted to be R1.8 billion. Debt costs increase steadily to 2015, where after they decline. The total cost of debt as a percentage of own revenue is at 9.4 per cent, which is the highest among the metros.

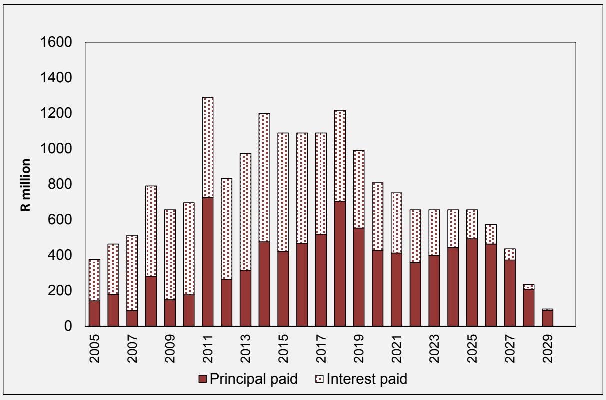
**Debt service profiles of South Africa's metros (continued)**

**Ekurhuleni**



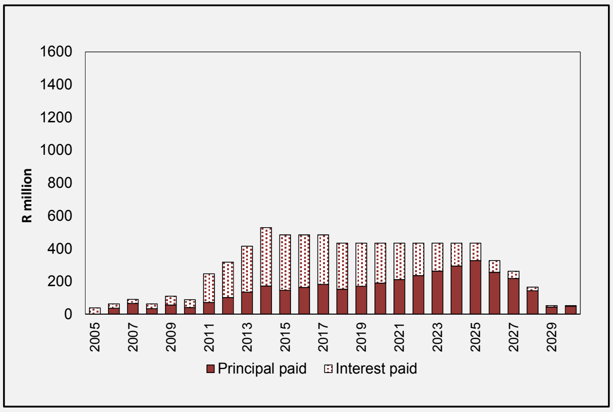

Ekurhuleni's borrowing liability at the end of June 2011 was R4.3 billion. In the medium term, debt service costs peak between 2011 and 2015. There is also a high payment due in 2020. At 15.3 per cent, the City's total cost of debt as a percentage of its total borrowing is the second lowest among the metros. However, its total cost of debt as a percentage of own revenue is at 7.8 per cent, which is the second highest of the metros.

**Tshwane**




Tshwane's borrowing liability at the end of June 2011 was R6.5 billion. The City's debt portfolio is dominated by amortising loans, which have a smooth repayment profile. This partly explains why the City's total cost of debt as a percentage of its total borrowing is the highest among the metros. Total cost of debt as a percentage of own revenue is at 7.7 per cent.

**Nelson Mandela Bay**




Nelson Mandela Bay's borrowing liability at the end of June 2011 was R1.7 billion. Cost of borrowing for 2011/12 is budgeted to be R312 million. Debt service costs increase steeply over the medium term as repayments on two large new loans take effect. At 18.1 per cent, the City's total cost of debt as a percentage of its total borrowing is the second highest among the metros.

## Development charges

The municipal infrastructure required to support new property developments is typically very costly. There are essentially two approaches to financing it:

- The municipality borrows the required funds on the strength of its balance sheet and then repays the debt with income derived from all ratepayers and customers of the municipality, including those that benefit from the new development.
- The property developer is required to pay a development charge equivalent to the up-front cost of the new municipal infrastructure (and the cost of using the capacity of existing infrastructure) and passes these costs on to whoever buys into the development. Essentially, the new landowners finance the cost of the infrastructure, which may be through commercial debt, such as home loans in the case of residential property developments.

*A development charge is designed to pass the up-front costs on to the responsible developers, who will then pass it on to their customers*

Applying the 'benefit' principle of public finance means that those who benefit more from a product or service should pay for it in proportion to the value they derive from it. A development charge is designed to pass the upfront costs of the new municipal infrastructure associated with specific developments on to the responsible developers, who in turn will pass it on to their customers – the users of the new infrastructure. These users derive a direct benefit from the provision of infrastructure, since its value is reflected in their property valuations.

Development charges are thus an important component of a sustainable system of municipal infrastructure finance and, if used judiciously, can play an important role in accelerating the overall development of municipal infrastructure. This is because, without these charges, the infrastructure required for new developments would have to be financed within the confines of the municipality's capital budget. This means that the new infrastructure would need to be prioritised relative to other municipal projects, which may result in it being delayed for many years, particularly where municipalities' scope to borrow is limited due to weak balance sheets and poor credit ratings.

When the municipality decides to invest in the new infrastructure it would mean delaying other capital projects. It would also mean that the costs related to specific developments are unfairly borne by all residents in general, as the municipality would raise the required funds from its entire rates and tariff base.

It is generally accepted that using development charges is economically efficient in that the user pays. Their absence creates distortions in the economy, particularly through underpricing the cost of development in some municipalities and contributing to the under-provision of municipal infrastructure more generally. This, in turn, acts as a significant constraint to growth and job creation.

Development charges are not a general revenue source for municipalities. Rather, they are a once-off fee that must be used to cover the cost of municipal infrastructure associated with a new development. They do not cover the ongoing operating costs of the services that the infrastructure is used to provide, nor the future cost of the rehabilitation or replacement of the infrastructure. These costs ought to be funded through property taxes and user fees. Development charges are also not intended to cover the cost of infrastructure that is internal to a development, such as sewerage or water connections to private stands or infrastructure within the boundaries of a new development. These costs are always borne fully by the land owner.

*Development charges are a once-off fee that must be used to cover the cost of municipal infrastructure associated with a new development*

Development charges are imposed to meet the costs of bulk and connector infrastructure, such as water mains that bring services to the boundary of the development, as well as infrastructure costs associated with the utilisation of existing capacity or the need to expand the capacity of water storage and treatment facilities, substations and sewerage treatment works.

The use of development charges has declined over recent years. Among the metros, development charges were 2 per cent of the value of buildings completed in 2004/05. This has declined to 1.7 per cent in 2009/10. Implementation is also very uneven across municipalities. Both the decline and uneven implementation can be ascribed to weaknesses in the regulatory framework that make them administratively complex.

*The use of development charges has declined over recent years, due to weaknesses in the regulatory framework*

National Treasury has done extensive work in relation to municipal development charges, and is in the process of developing a framework that will set norms and standards to ensure that these charges facilitate (and do not stifle) new property developments. Certain municipalities have already begun revising their policies related to development charges in line with National Treasury's research findings. All municipalities are encouraged to do the same.

### Land based financing strategies

Due to the recent rapid growth in land prices, municipal land sales have become an attractive way of mobilising finance for municipal infrastructure (and sometimes also to finance operating deficits). However, this use of municipal owned land undermines the long-term financial health and wealth of the municipality. Even where a municipality invests the funds in municipal infrastructure it is exchanging an appreciating asset (land) with a depreciating asset (infrastructure). As a principle of good stewardship, municipalities should always use the proceeds of municipal land sales to purchase other land for the municipality – so as to maintain and grow the value of the municipality's land portfolio, and to facilitate the realisation of its spatial development strategy.

Apart from selling land, there are a range of other land based strategies to raise finance for infrastructure investments that municipalities can explore. First, municipalities can use municipal land as security for raising loans to fund infrastructure related to the

*Apart from selling land, there are a range of other land based strategies to raise finance for infrastructure investments that municipalities can explore* development of that land or other infrastructure. This is fairly common practice among municipalities.

Second, municipalities can use leaseholds on municipal land. The experience of other developing countries is that this strategy has the greatest potential where there is rapid urban growth, such as in the metros and cities. The municipality will sell the development rights to the municipal land to a developer subject to the proposed development being in line with the municipalities spatial development framework. The parties may agree that part of the proceeds of the sale should be used to provide infrastructure to the approved development. The developer's rights to the property are spelt out in a leasehold agreement. Typically this agreement should require the lessor to pay a rental at least commensurate to the rates that would be raised on the developed property. The leasehold agreement will have a specific term (20, 40 or 99 years) depending on the type of development. Usually the developer is allowed to sell the leasehold to a third party under certain circumstances. Once the term expires, all rights in the property revert to the municipality. The leasehold system enables a municipality to partner with private developers to accelerate the development of inner city land, while retaining ownership of the land.

Third, municipalities can use land-use exchanges. The basic idea is that certain municipal offices or functions (such as stores, workshops or vehicle depots) are located on land that can and should be used for alternative, higher value purposes. Where this is the case, the municipality should explore relocating these offices or functions to suitable alternative locations (often on the city outskirts), and so release the high-value land for development.

In many instances, inner-city land is owned either by other spheres of government or by state owned enterprises. Municipalities need to engage with these property owners to explore ways in which they too can facilitate development through similar land-use exchanges.

Land-use exchanges may involve land swaps, lease swaps or simply buying land with the funds generated from either selling or leasing the vacated land. The net result should be a more appropriate use of land that fosters development. The best known example of this kind of development is the Victoria and Alfred Waterfront in Cape Town, where a harbour was turned into a shopping mall and tourist destination.

### Public private partnerships

PPPs are important service delivery mechanisms that facilitate rapid infrastructure development. There are different types of PPPs that involve models for risk sharing between the municipality and its partners. In many cases the private party is in a better position to raise debt and equity to finance the project.

*PPPs allow municipalities to take advantage of private sector expertise and experience*

Municipalities can take advantage of private sector expertise and experience in the construction of the infrastructure. Furthermore, the development of PPPs for economically justifiable projects eases the pressure on the municipality's budget and allows for better allocation of funds towards addressing social needs of the community.

## Developing the municipal borrowing market

Through the Regulatory Framework for Municipal Borrowing (1999) and the MFMA, the government has already put in place a range of measures to facilitate municipal borrowing. These are:

*Government has already put in place a range of measures to facilitate municipal borrowing*

- *Sovereign risk.* National government does not stand surety for municipal debt through sovereign guarantees or in any other way, except where such surety or guarantee has been explicitly approved in terms of chapter 8 of the Public Finance Management Act (1999) (PFMA). If a municipality defaults on its debt, lenders may follow the normal legal route to attach certain of the municipality's assets and revenue streams.
- *Credit enhancements.* Section 48 of the MFMA provides that a municipality may provide any appropriate security for its debt obligations, and sets out a range of options in this regard, including pledging specific revenue streams, ceding rights to future revenues and so on. These provisions are supported by a provision in the annual Division of Revenue Act that allows municipalities to pledge future conditional grants as reflected in the medium-term expenditure framework (MTEF). It is important that these credit enhancements are carefully designed and implemented to reduce moral hazard, and that they do not impede the delivery of basic services.
- *Maturities.* The MFMA provides that short-term borrowing for bridging finance purposes must be repaid within the financial year, and may not be refinanced under any circumstances. As regards long term borrowing, the term of the borrowing may not extend beyond the useful life of the property, plant or equipment that is being financed by the borrowed funds.
- *Avoidance of direct government assistance.* There is no legal provision that allows national government or provincial government to lend funds directly to municipalities. The national development finance institutions (such as the DBSA) are responsible for lending to municipalities in line with their mandates, and may provide interest rate subsidies in accordance with their developmental role.
- *Liquidity through the development of secondary markets.* Government is committed to facilitate the development of secondary markets for municipal debt to enhance the liquidity of the municipal credit market.

Generally, municipalities are encouraged to access private finance on the strength of their balance sheets and their credit ratings. The development of secondary markets for municipal debt could lower the risk of lenders and therefore lower the cost of borrowing for these municipalities.

*Generally, municipalities are encouraged to access private finance on the strength of their balance sheets and their credit ratings*

However, government is exploring various ways of enabling municipalities with no or only limited access to financial markets to access private finance.

### Ways in which municipalities can access private finance

*Pool finance for secondary cities*

The basic idea of pool finance is to create an instrument for secondary cities with similar credit qualities that will allow them to pool their financing needs and approach the financial markets as a collective.

Secondary cities have large funding requirements (current borrowing was R4.1 billion at the end of 2010), they have adequate own revenues and good institutional capacity. However, they lack the finance expertise to issue bonds independently, and the scale of their financing needs makes it uneconomical to approach the bond market separately. It is envisaged that this bond pooling instrument would give the necessary scale, would justify contracting in specialised capacity to manage issuing the bonds and would reduce transaction costs in the underwriting process due to increased economies of scale.

*Bond pooling would be cost effective for secondary cities*

Such bond pooling would be cost-effective for secondary cities as they would benefit from the longer maturities and lower debt costs generally associated with bonds. In addition, bond pools can be structured to achieve higher credit ratings in the primary market which will further reduce the cost of the debt.

*DBSA fulfilling its developmental role*

Development finance institutions in other developing countries (such as India) have been instrumental in lending to municipalities with good potential but whose balance sheets are comparatively weak, and so developing the lower end of the capital market.

*The DBSA needs to step up its support for municipalities in line with its developmental mandate*

Government and the DBSA have agreed that the bank should step up its support for municipalities in line with its developmental mandate. This will entail increasing lending to particularly those municipalities that currently do not have access to credit markets. It is also envisaged that the DBSA will increasingly play the role of market facilitator and thereby crowd in private finance, instead of acting as a primary lender and effectively crowding out private finance. Steps the bank is being encouraged to take in this regard include:

- championing a model that involves private sector co-financing of the projects it invests in
- providing technical support to municipalities to build their capacity to participate in credit markets generally, and not simply to facilitate the DBSA's own lending activities
- facilitating municipalities' entry and participation into private capital markets by under-writing municipal borrowing, or offering limited guarantees to municipalities
- managing the development of a bond pooling instrument for secondary cities (using the DBSA's extensive treasury expertise)

- encouraging the development of the secondary market in municipal bonds by selling its current holdings of metro bonds to secondary investors that are more likely to trade them.

To support these initiatives, government has raised the DBSA's callable capital by R15.2 billion to R20 billion, thus increasing its lending capacity to R140 billion. Government is also exploring ways to reduce the DBSA's exposure when lending to municipalities that are a credit risk.

*Government has raised the DBSA's callable capital to R20 billion*

### *Developing the treasury function capacity in municipalities*

Generally, municipalities' treasury function capacity is very poorly developed, even among certain of the metros. The result is that municipalities are not managing their borrowing optimally. This results in municipalities either under-utilising their borrowing capacity or borrowing excessively and getting into financial difficulties. It is also reflected in the unevenness of many municipalities' debt profiles.

National Treasury will be exploring ways of strengthening municipalities' treasury functions, which may include providing specific training, developing appropriate guidelines and providing technical advice to municipalities on how to optimise their borrowing strategies.

*National Treasury will be exploring ways of strengthening municipalities' treasury functions*

## Conclusion

The demand for municipal infrastructure is spread across all municipalities, but is greatest in the metros and secondary cities. The primary sources of infrastructure funding are internally generated funds, transfers and borrowing. Government is exploring ways of deepening and broadening the municipal capital markets through developing a bond pooling instrument for secondary cities and building treasury function capacity. It is encouraging the DBSA to fulfill its developmental role and become a market facilitator and thereby crowd in private finance, instead of acting as a primary lender and effectively crowding out private finance. Government is also exploring ways of facilitating the use of development charges to finance municipal infrastructure required for private sector property developments.

In addition, municipalities need to explore land based financing strategies such as leaseholds and land use exchanges. Selling municipal land to fund operating deficits is discouraged. As a principle of good stewardship, municipalities should always use the proceeds of municipal land sales to purchase other land for the municipality in line with its spatial development plan – so as to maintain and grow the value of the municipality's land portfolio, thereby strengthening the municipality's balance sheet – which can then be leveraged to raise the finance required to fund infrastructure.

# 7

# Managing municipal personnel

## Introduction

The success or failure of a municipality depends on the quality of its political leadership, sound governance of its finances, the strength of its institutions and the calibre of staff working for the municipality.

Although sound financial governance is perceived to be most important, without proper personnel management, municipalities are likely to experience difficulty. This has become increasingly evident in a number of large municipalities that have recently found themselves in precarious financial situations, and is certainly true of many smaller municipalities. An analysis of municipal finances suggests that personnel issues lie at the heart of many of the financial problems experienced by municipalities.

**Impact of personnel on causing and addressing municipal finance problems**

Msunduzi Local Municipality, the capital city of KwaZulu-Natal, provides a good case study. It was placed under administration in March 2010. One of the findings of the team appointed to turn the municipality around was that there had been poor personnel management practices. These included the indiscriminate hiring of employees and a lack of proper performance management and controls. The combined effect of these practices resulted in a bloated and unaffordable organisational structure, which was further aggravated by cases of unethical leadership, greed, corruption and poor accountability. In effect, poor leadership and bad personnel management undermined the municipality's finances, despite its having ample fiscal capacity. By contrast, Tshwane metro experienced severe cash-flow problems in 2009, mainly due to an overambitious capital programme. Once the full extent of the problem was obvious, the municipality tackled it head-on by implementing the required austerity measures and prioritising revenue management. These initiatives were mostly driven by the second-tier management of the municipality, and have resulted in a successful turnaround. The difference between the Msunduzi and Tshwane experiences can largely be attributed to the commitment of staff to doing the right thing or not.

*Personnel management needs to be a core responsibility and priority for all managers in a municipality*

The proper management of personnel is therefore critical to the effective and efficient functioning of municipalities and must be prioritised across all municipal functions. Personnel management should not only be left to corporate services or the human resources department; it needs to be a core responsibility and priority for all managers in a municipality.

At an aggregate level, about 30 per cent of the total municipal operating budget gets spent on the remuneration of personnel. This rate varies among municipalities, depending on the extent to which they may have outsourced some of their service delivery functions, or whether they are responsible for the large revenue generating functions or not. More emphasis needs to be placed on whether this expenditure is yielding value for money for municipalities and the communities they serve. This is why measuring and managing the performance of municipalities, and by implication, the performance of municipal employees, is critical.

The smaller municipalities regularly point to difficulties with recruiting and retaining suitably skilled staff. One proposed solution is to use a shared service centre model built around the district municipalities. However, local municipalities are generally wary of this proposal due to concerns about reporting lines and accountability.

*The Municipal Systems Amendment Act addresses a number of personnel related issues in municipalities*

Personnel management in local government has been marred in many instances by poor recruitment practices, political interference in the appointment and dismissal of employees, the inability to attract and retain suitably qualified staff, high vacancy rates and the lack of performance management systems and other related symptoms.

The Municipal Systems Amendment Act (2011) came into effect on 5 July 2011. This Act seeks to address certain issues, including:

- the appointment and competencies of municipal managers and managers directly accountable to the municipal manager (s57 managers)
- regulating the employment of municipal employees who have been dismissed or are subject to disciplinary processes by other municipalities
- regulating the duties, remuneration, benefits and other terms and conditions of employment for municipal managers and s57 managers.

However, the most topical proposal is the requirement that municipal managers and s57 managers may not simultaneously hold political office in a political party. The aim is to ensure a clear separation between the political leadership roles of the council and mayor and the managerial role of senior managers within the municipal administration, and to ensure lines of authority and accountability between them are aligned with the principles for public administration set out in Chapter 10 of the Constitution, by ensuring that municipal administrations are non-partisan and professionalised.

This chapter provides an overview of:

- trends in local government employment
- building municipal capacity

- sector employment trends
- municipal remuneration
- performance management.

## Trends in local government employment

The contribution made by local government to total employment in South Africa has remained relatively unchanged since 2006. In 2009, local government employed approximately 278 600 people and contributed just over 2 per cent to total employment in the country. Table 7.1 shows the contribution made by each category of municipality towards total employment.

**Table 7.1 Local government's contribution to employment by category of municipality, 2006 and 2009**

| Category<br>Number | Local government employment (2006)* | % of Total Employment | Local government employment (2009) | % of Total Employment |
|---|---|---|---|---|
| Total Employment | 13 601 000 | | 13 369 000 | |
| Category A (Metros) | 137 469 | 1.0% | 134 068 | 1.0% |
| Category B (Locals) | 116 205 | 0.9% | 125 518 | 0.9% |
| *Secondary cities - 21* | *35 568* | 0.3% | *48 784* | 0.4% |
| *Towns - 140* | *61 946* | 0.5% | *59 415* | 0.4% |
| *Mostly rural - 70* | *18 691* | 0.1% | *17 319* | 0.1% |
| Category C (Districts) | 14 184 | 0.1% | 19 005 | 0.1% |
| *Category B + C* | *130 389* | 1.0% | *144 523* | 1.1% |
| *All municipalities* | *267 858* | 2.0% | *278 591* | 2.1% |

**Revised*

*Source: Stats SA, Non-financial census of municipalities (P9115 - 2007 to 2009)*

*Stats SA, Labour Force Survey Historical Revision: September Series, 2000 - 2007*

The table also shows that the six metros employ more than half of the total municipal workforce, thus making a contribution of 1 per cent to total employment. The secondary cities, towns and the 70 most rural municipalities together contribute 0.9 per cent of total employment in South Africa.

*The six metros employ more than half of the total municipal workforce*

Although the trend appears stable, it is important to note that over this period, many municipalities opted to outsource certain activities such as debt collection, repairs and maintenance, refuse removal, and meter reading. Employment related to outsourcing is not reflected as part of municipal employment, but is still paid for by the municipality, usually under ‘contracted services’ and also ‘other expenditure’.

*Employment related to outsourcing is not reflected as part of municipal employment*

Employment levels are also expected to increase slightly from 2010 onwards as certain municipalities that previously employed temporary workers in functions such as refuse removal, have absorbed these workers into permanent positions. This is in response to pressure from labour unions, and general discomfort with the institution of labour brokering. For example, eThekwini metro has reported that approximately 1 300 temporary positions were converted into permanent positions at the start of the 2010/11 financial year.

*Employment levels are also expected to increase slightly from 2010 onwards*

## Growth in local government employment

*Local government employment grew by nearly 4 per cent between 2006 and 2009*

Local government employment grew by nearly 11 000 or 4 per cent between 2006 and 2009. Table 7.2 shows the number of jobs lost or gained per category of municipality since 2006.

**Table 7.2 Total employment in local government by category and by metro, 2006 - 2009**

| Number | 2006* Total employment | 2007* Total employment | Jobs gained (+) and lost (-) | 2008* Total employment | Jobs gained (+) and lost (-) | 2009 Total employment | Jobs gained (+) and lost (-) |
|---|---|---|---|---|---|---|---|
| **By category of municipality** | | | | | | | |
| Category A (Metros) | 137 469 | 142 593 | 5 124 | 136 166 | -6 427 | 134 068 | -2 098 |
| Category B (Locals) | 116 205 | 116 050 | -155 | 120 447 | 4 397 | 125 518 | 5 071 |
| *Secondary cities - 21* | *35 568* | *47 118* | *11 550* | *48 068* | *950* | *48 784* | *716* |
| *Towns - 140* | *61 946* | *52 460* | *-9 486* | *56 703* | *4 243* | *59 415* | *2 712* |
| *Mostly rural - 70* | *18 691* | *16 472* | *-2 219* | *15 676* | *-796* | *17 319* | *1 643* |
| Category C (Districts) | 14 184 | 14 763 | 579 | 17 000 | 2 237 | 19 005 | 2 005 |
| *Category B + C* | *130 389* | *130 813* | *424* | *137 447* | *6 634* | *144 523* | *7 076* |
| **Total** | **267 858** | **273 406** | **5 548** | **273 613** | **207** | **278 591** | **4 978** |
| **By metro** | | | | | | | |
| City of Cape Town | 23 420 | 22 568 | -852 | 26 005 | 3 437 | 26 196 | 191 |
| City of Johannesburg | 30 104 | 31 005 | 901 | 31 506 | 501 | 29 369 | -2 137 |
| City of Tshwane | 21 981 | 22 274 | 293 | 17 673 | -4 601 | 18 954 | 1 281 |
| Ekurhuleni | 18 714 | 17 411 | -1 303 | 17 918 | 507 | 18 027 | 109 |
| eThekwini | 35 255 | 41 569 | 6 314 | 35 902 | -5 667 | 34 860 | -1 042 |
| Nelson Mandela Bay | 7 995 | 7 766 | -229 | 7 162 | -604 | 6 662 | -500 |
| **Total** | **137 469** | **142 593** | **5 124** | **136 166** | **-6 427** | **134 068** | **-2 098** |

**Revised*

*Source: Stats SA, Non-financial census of municipalities (P9115 - 2007 to 2009)*

The table also shows that employment has grown consistently in the secondary cities and district municipalities. Employment in the 21 secondary cities increased by 13 216 or 37 per cent between 2006 and 2009. Most of this growth occurred between 2006 and 2007, the year following the previous local government elections.

*Tshwane metro adopted a deliberate policy of not filling certain positions as a way of dealing with its cash flow crisis*

By contrast, employment by the metros, towns and rural municipalities fell between 2006 and 2009. The most notable decrease is evident in the Tshwane metro, where 4 601 jobs were lost between 2007 and 2008. However, there is a corresponding increase in Tshwane's vacancy rates, which indicates the decline in employment resulted from a deliberate policy of not filling certain positions when they became vacant due to normal staff turnover and retirements. This was one of the measures adopted by the metro to deal with its cash-flow crisis. Cape Town is the only metro to have expanded its workforce over this period.

Table 7.3 examines the growth in employment in key municipal sectors between 2006 and 2009.

**Table 7.3 Growth in municipal positions in key sectors, 2006 and 2009**

| Number | 2006 Total positions | 2009 Total positions | Percentage growth |
|---|---|---|---|
| **By category of municipality** | | | |
| Category A (Metros) | 137 469 | 134 068 | -2.5% |
| *Financial administration* | *13 858* | *15 713* | 13.4% |
| *Electricity* | *10 756* | *13 632* | 26.7% |
| *Water* | *10 987* | *13 872* | 26.3% |
| *Waste water management* | *689* | *2 540* | 268.7% |
| *Waste management* | *8 303* | *11 226* | 35.2% |
| *Other* | *92 876* | *77 085* | -17.0% |
| Category B + C | *130 389* | *144 523* | 10.8% |
| *Financial administration* | *20 094* | *26 501* | 31.9% |
| *Electricity* | *9 335* | *7 643* | -18.1% |
| *Water* | *11 663* | *13 985* | 19.9% |
| *Waste water management* | *7 826* | *9 730* | 24.3% |
| *Waste management* | *15 769* | *13 867* | -12.1% |
| *Other* | *65 702* | *72 797* | 10.8% |
| **Total** | **267 858** | **278 591** | 4.0% |

*Source: Stats SA, Non-financial census of municipalities for the year ended 30 June 2009, (P9115 - 2009)*

Total employment in metros has fallen by 2.5 per cent since 2006. Most of the jobs lost were in the 'other' category, where employment declined by 15 791 or 17 per cent. Indeed, metro employment in the key service delivery sectors has grown since 2006, which suggests that the municipalities are prioritising these functions. The very rapid employment growth in the waste water management sector may be due to incorrect reporting on the 2006 figures.

*Total employment in metros has fallen by 2.5 per cent since 2006*

The employment trends in category B and C municipalities show that most of the growth has been in the financial administration sector, which has increased by 32 per cent since 2006. Employment has also grown considerably in the water and waste water management sectors, although much of this growth can be attributed to the transfer to municipalities of water schemes that were previously owned and run by the national Department of Water Affairs. The decline in employment in the electricity and waste management sectors is a serious concern given the backlogs in repairs and maintenance and service delivery in both these sectors.

*The decline in employment in the electricity and waste management sectors is a serious concern given the high backlogs*

## Why the slow growth in municipal employment?

The growth in the overall economy since 2006 (before the recession in 2009), brought with it an intensified need to address service delivery backlogs and the pressures created by rural-urban migration. It would therefore have been assumed that municipalities generally would have needed to significantly expand their capacity to deliver by employing more staff. However, municipal employment levels have not grown significantly since 2006.

*It is necessary to ask why municipal employment levels have not grown significantly since 2006*

There are a number of possible explanations. First, as noted above, many municipalities are outsourcing activities as a more cost-effective method of delivering services, especially given the rising cost to municipalities of employing staff directly. This means that

*Many municipalities are outsourcing activities as a more cost-effective method of delivering services* employment associated with delivering municipal services may be growing, but is not reflected as municipal employment.

*Financial pressures have constrained the ability of municipalities to increase employment*

Second, many municipalities have faced serious financial pressures during this period, which has constrained their ability to increase employment. Problems with revenue management, over-ambitious capital programmes, non-priority spending, high wage increases and increases in the bulk price of electricity have all contributed to placing pressure on municipal finances. Since 2009, these pressures were further accentuated by the impact the economic recession had on municipal customers' ability to settle their bills. Consequently, many municipalities are delaying filling vacancies as one way of saving.

*A skills shortage and a rigid approach to employment equity make it difficult for towns and rural municipalities to recruit suitably qualified staff*

Third, the towns and rural municipalities may be finding it difficult to recruit suitably qualified staff due to the combined effect of the shortage of certain skills and a rigid approach to employment equity. Also, many people with the necessary skills are reluctant to work for these municipalities due to the politicisation of municipal workplaces, and the lack of amenities such as quality schools and health facilities in those areas.

## Building municipal capacity

*Deploying large numbers of technical advisors to municipalities is having a limited impact on building sustained capacity*

The lack of adequate institutional capacity is often cited as one of the main reasons for poor municipal performance. Despite the substantial investments by national and provincial governments in building municipal capacity, it remains a significant challenge. And yet it seems that capacity building programmes are considered by the departments concerned, to have achieved their objectives.

To date, the preferred methodology of the different programmes has been to provide hands-on-support with a view to facilitating learning-by-doing. This has involved the deployment of a large number of technical advisors to municipalities. In 2009, the Financial and Fiscal Commission commented on this:

> [The narrative assessments] suggest that the impact of the capacity programmes is effective in enhancing service delivery within local government. However the contrary view is that progress has only been made on mobilising various role-players to provide hands-on support, but it remains too early to evaluate the overall effectiveness of these programmes. It should also be noted that these programmes are not independently evaluated and therefore run the risk of being over-rated. The other challenge is that the success of these programmes is mostly dependent on the skills of the deployed experts or service delivery facilitators (SDFs). In many cases, municipalities fail to sustain the success factors introduced by SDFs at the end of the deployment term.

Despite the attractiveness of the logic behind providing hands-on-support, there is growing evidence that the current approach to it is leading to perverse outcomes. These include:

- ‘Experts’ earn more than people working in municipalities, which is resulting in an exodus of skilled employees from municipalities to these programmes.
- In practice most experts are gap filling rather than capacity building, because there is (a) no-one to train, (b) the focus is on quick-wins in service delivery so there is no time to train, (c) the expert does not have an aptitude for training.
- Individuals and organisations have developed vested interests in the current hands-on-approach and therefore want the programmes to continue, because it is their livelihood or they like the power that comes with allocating assistance.
- Programmes that simply provide additional support to failing municipalities most often treat the immediate symptoms of failure rather the underlying causes.

*Dealing with poor performance is a messy and complex process*

The prevailing assumption is that most municipal performance failings are due to a lack of capacity – whether it be individual, organisational or environmental capacity. This is despite there being evidence of laziness, mismanagement, incompetence and political interference. Reducing all municipal performance problems to a lack of capacity enables institutions and government officials to focus on the softer, easier capacity building type interventions, rather than the complex processes of dealing with poor performance, and a longer-term focus on aligning municipal systems and incentives to ensure sound administration.

*Capacity challenges are not the only cause of poor performance*

This is not to say that capacity challenges are not real. They are, but they are not the only cause of poor performance. This therefore suggests that national and provincial support to municipalities needs to address a wider range of root causes than just the lack of capacity.

A discussion on municipal institutional capacity needs to encompass a broad range of issues, such as policies and procedures, knowledge management (institutional memory), competency profiles of staff, background and experience and organisational ethics.

### Municipal spending on training

Section 195(1) of the Constitution sets out some of the basic values and principles governing public administration, and among other things it requires that ‘good human-resource management and career development practices, to maximise human potential must be cultivated’. This requirement is further elaborated on in the Municipal Systems Act (2000).

*Municipalities need to invest in effective training and development initiatives*

It is therefore important that municipalities invest in effective training and development initiatives. While the Local Government SETA has some information, there is no reliable, comprehensive data on what municipalities spend on staff training, or the number of staff that benefit from these programmes. However, going forward it is anticipated that the development and implementation of a standard chart of accounts for local government (which will standardise the classification of items on which municipalities report expenditure) will result in the required data being recorded and reported more accurately.

*There is a tendency for municipalities to select training programmes mainly on the basis of cost*

A further consideration is the tendency to select training programmes on the basis of cost rather than assessing the content and the value of the proposed training to the organisation. There is a perception that the cheaper the course, the more people a municipality can train and hence the value derived should be greater. However, this is very often not the case.

## Vacancies in municipalities

Given the focus of this chapter, institutional capacity can also be viewed from the perspective of vacancy rates in municipalities. The assumption is that the number of vacant positions in an up-to-date organisational structure is often a first indicator of possible capacity problems.

### *Vacancies in metros*

Table 7.4 shows the vacancy rates in the metros between 2006 and 2009.

**Table 7.4 Metro personnel vacancies, 2006 – 2009**

| Percentage | 2006* | 2007* | 2008* | 2009 |
|---|---|---|---|---|
| City of Johannesburg | 4.3% | 4.6% | 17.2% | 14.9% |
| City of Cape Town | 12.7% | 11.5% | 9.1% | 9.3% |
| eThekwini | 40.1% | 40.3% | 27.8% | 29.2% |
| Ekurhuleni | 15.8% | 12.1% | 13.1% | 13.3% |
| City of Tshwane | 48.3% | 47.7% | 48.8% | 51.1% |
| Nelson Mandela | 16.5% | 24.7% | 17.6% | 0.0% |
| **Total for all metros** | **25.4%** | **26.2%** | **24.5%** | **24.2%** |

**Revised*

*Source: Stats SA, Non-financial census of municipalities (P9115 - 2007 to 2009)*

*While the total vacancy rate in metros has been approximately 25 per cent since 2006, there are notable differences between them*

While the total vacancy rate in metros has been approximately 25 per cent since 2006, there are notable differences between them. Tshwane reports a very high vacancy rate: from 48.3 per cent in 2006 it increased to over 51 per cent in 2009. The increase correlates with the number of jobs lost in this municipality since 2006. However, the level indicates that Tshwane is currently operating with less than half of its approved positions filled.

eThekwini also reports high vacancy rates, but these have declined by about 10 per cent since 2006 – despite a marginal decline in actual employment. This indicates a reduction in the number of positions on the metro's organisational structure. Ekurhuleni has shown some improvement in the filling of vacant positions. Nelson Mandela Bay reported a zero per cent vacancy rate in 2009, which is probably due to inaccurate reporting.

### *Vacancies in local and district municipalities*

Table 7.5 shows the vacancy rates in category B and C municipalities.

**Table 7.5 Vacancies in category B and C municipalities, 2008/09**

| Number | 2008/09 Currently employed | Approved positions | Funded vacancies | Unfunded vacancies | Appointments to non-existent positions[1] |
|---|---|---|---|---|---|
| **By category of municipality** | | | | | |
| Category B (Locals) | 98 318 | 128 764 | 18 958 | 27 422 | 15 934 |
| *Secondary cities - 21* | *36 638* | *54 110* | *4 629* | *18 190* | *5 347* |
| *Towns - 140* | *48 383* | *57 452* | *12 267* | *6 043* | *9 241* |
| *Mostly rural - 70* | *13 297* | *17 202* | *2 062* | *3 189* | *1 346* |
| Category C (Districts) | 12 376 | 15 350 | 3 524 | 1 348 | 1 898 |
| **Category B + C** | **110 694** | **144 114** | **22 482** | **28 770** | **17 832** |
| **By province** | | | | | |
| Eastern Cape | 16 370 | 20 408 | 3 298 | 7 181 | 6 441 |
| Free State | 14 393 | 19 025 | 2 037 | 4 047 | 1 452 |
| Gauteng | 8 354 | 12 161 | 477 | 2 871 | -459 |
| KwaZulu-Natal | 18 110 | 21 264 | 3 186 | 3 825 | 3 857 |
| Limpopo | 8 780 | 12 833 | 2 429 | 1 951 | 327 |
| Mpumalanga | 11 030 | 15 157 | 1 970 | 2 818 | 661 |
| Northern Cape | 6 602 | 7 487 | 1 470 | 536 | 1 121 |
| North West | 11 489 | 16 135 | 2 949 | 3 116 | 1 419 |
| Western Cape | 15 566 | 19 644 | 4 666 | 2 425 | 3 013 |
| **Total** | **110 694** | **144 114** | **22 482** | **28 770** | **17 832** |

*1. Calculated as follows: (currently employed + funded vacancies + unfunded vacancies) - approved positions*
*Source: Municipal Demarcation Board, Capacity assessment report, 2008/09*

*Municipalities reported that in 2009, some 17 800 people were appointed to positions that do not exist on their approved organisational structures*

In 2008/09, there were about 144 000 approved positions on district and local municipalities' approved organisational structures. Of these positions, 36 per cent or 51 200 were reported to be vacant, which suggests that municipalities are operating significantly below capacity. However, the table also shows that funding is only available for filling less than 50 per cent of the vacant posts. The remaining 28 700 vacancies are reported as being unfunded. To some extent, the number of unfunded vacancies is offset by the number of appointments to non-existent positions. Municipalities reported that in 2009, some 17 832 people were appointed to non-existent posts. This means that positions that do not exist on the approved organisational structures of municipalities. This number has decreased by almost 46 per cent since the 2008 *Review*, suggesting that municipalities have been revising their organisational structures to legalise these appointments.

### *Vacancy rates among senior managers*

A key consideration in assessing municipal capacity is the level of vacancies among senior management (s57 managers), as they play a key role in providing strategic leadership in municipalities. Table 7.6 provides information on the level of vacancies among s57 managers in each of the different municipal categories.

**Table 7.6 Vacant posts for section 57 managers, 2006 – 2009**

| Number | 2006* | 2007* | 2008* | 2009 |
|---|---|---|---|---|
| Category A (Metros) | 8 | 7 | 3 | 29 |
| Category B (Locals) | 206 | 212 | 163 | 204 |
| *Secondary cities - 21* | 25 | 21 | 26 | 30 |
| *Towns - 140* | 135 | 140 | 99 | 118 |
| *Mostly rural - 70* | 46 | 51 | 38 | 56 |
| Category C (Districts) | 66 | 32 | 49 | 41 |
| *Category B + C* | *272* | *244* | *212* | *245* |
| **Total** | **280** | **251** | **215** | **274** |

**Revised*

*Source: National Treasury local government database*

Between 2008 and 2009, the number of s57 vacancies among the metros increased from 3 to 29. The detailed information indicates that 24 of these 29 vacancies were in Ekurhuleni, where there was significant managerial instability at the time.

*There has not been much improvement in filling senior management vacancies in local municipalities since 2006*

There has not been much improvement in filling senior management vacancies in local municipalities when comparing vacancies in 2006 to those in 2009, though there were fewer vacancies in 2008. The number s57 vacancies have declined by almost 30 per cent between 2006 and 2009 in the district municipalities.

## Sector employment trends

Table 7.7 provides a breakdown of municipal employment by key sectors.

**Table 7.7 Percentage of municipal workers employed in key sectors, 2009**

| Number | Headcount of municipal workers | Financial adminis-tration | Electricity | Water | Waste Water Mana-gement | Waste Mana-gement | Other |
|---|---|---|---|---|---|---|---|
| **By category of municipality** | | | | | | | |
| Category A (Metros) | 134 068 | 8.8% | 6.9% | 6.4% | 1.2% | 6.7% | 70.0% |
| Category B (Locals) | 125 518 | 13.3% | 5.2% | 4.9% | 5.4% | 9.8% | 61.4% |
| *Secondary cities - 21* | 48 784 | 10.9% | 5.7% | 3.9% | 5.8% | 8.7% | 65.0% |
| *Towns - 140* | 59 415 | 14.0% | 5.4% | 5.0% | 5.5% | 10.6% | 59.5% |
| *Mostly rural - 70* | 17 319 | 17.5% | 3.2% | 7.2% | 3.6% | 10.5% | 58.1% |
| Category C (Districts) | *19 005* | 16.0% | 0.1% | 24.0% | 2.3% | 0.1% | 57.5% |
| *Category B + C* | *144 523* | *13.6%* | *4.5%* | *7.4%* | *5.0%* | *8.6%* | *60.9%* |
| **Total** | **278 591** | **11.3%** | **5.7%** | **6.9%** | **3.1%** | **7.7%** | **65.3%** |
| **By metro** | | | | | | | |
| City of Cape Town | 26 196 | 13.5% | 7.8% | 10.2% | 1.0% | 7.0% | 60.4% |
| City of Johannesburg | 29 369 | 7.3% | 6.6% | 8.9% | 0.0% | 9.5% | 67.7% |
| City of Tshwane | 18 954 | 12.1% | 9.7% | 0.0% | 5.7% | 7.2% | 65.3% |
| Ekurhuleni | 18 027 | 9.4% | 5.3% | 5.3% | 0.0% | 7.9% | 72.1% |
| eThekwini | 34 860 | 3.4% | 5.1% | 5.6% | 0.0% | 3.2% | 82.7% |
| Nelson Mandela Bay | 6 662 | 14.5% | 9.5% | 6.3% | 5.8% | 7.2% | 56.6% |

*Source: Stats SA, Non-financial census of municipalities for the year ended 30 June 2009, (P9115 - 2009)*

The majority of municipal personnel are employed in the category ‘other’, which includes municipal support functions, such as corporate services, town planning, economic planning and development, the development of integrated development plans (IDPs) and strategic support. Employment in this category usually accounts for between

58 and 70 per cent of total municipal employment and varies among the different categories of municipalities.

Employment in the financial administration sector accounts for between 9 per cent (in metros) and 17.5 per cent (in rural municipalities) of total municipal employment. Aggregate employment in the technical service sectors (electricity, water, waste water management and refuse removal) accounts for the remaining levels of employment.

*Overall, employment in the financial administration and technical sectors declined between 2006 and 2009*

Comparing the above information to similar information for 2006 reported in the 2008 *Review*, indicates that employment in the financial administration sector has declined from 14.1 per cent in 2006 to 11.3 per cent in 2009. Overall, employment in the technical sectors has fallen from 29 per cent in 2006 to 23.4 per cent in 2009, while employment in the sector 'other' has increased from 56.9 per cent to 65.3 per cent between 2006 and 2009.

*Metros employ a significantly lower percentage of their staff to financial administration functions compared to rural and district municipalities*

There are significant disparities in sectoral balance in employment between the different categories of municipalities. Metros employ a significantly lower percentage of their staff to financial administration functions compared to rural and district municipalities. This is probably because there are economies of scale in financial administration. Disparities in trends for the technical sectors can be attributed to differences in the allocation of municipal powers and functions. For example, district municipalities employ a significantly higher percentage of their staff in the water sector compared to electricity and waste management, because most district municipalities have been granted the authority for this water function.

## Vacancies in key sectors

Table 7.8 shows the vacancy rates in each of the key sectors per municipal category.

**Table 7.8 Filling positions in key sectors, 2008 and 2009**

| | 2008 | | | 2009 | | |
|---|---|---|---|---|---|---|
| Number | Total positions | Positions filled | Percentage positions vacant | Total positions | Positions filled | Percentage positions vacant |
| **By category of municipality** | | | | | | |
| Category A (Metros) | 136 166 | 102 795 | 24.5% | 134 068 | 101 670 | 24.2% |
| *Financial administration* | *13 974* | *11 812* | *15.5%* | *15 713* | *12 207* | *22.3%* |
| *Electricity* | *13 592* | *9 193* | *32.4%* | *13 632* | *9 118* | *33.1%* |
| *Water* | *12 381* | *8 615* | *30.4%* | *13 872* | *10 014* | *27.8%* |
| *Waste water management* | *3 074* | *1 738* | *43.5%* | *2 540* | *1 355* | *46.7%* |
| *Waste management* | *12 603* | *9 033* | *28.3%* | *11 226* | *8 251* | *26.5%* |
| *Other* | *80 542* | *62 404* | *22.5%* | *77 085* | *60 725* | *21.2%* |
| Category B + C | *137 447* | 118 006 | 14.1% | *144 523* | 122 258 | 15.4% |
| *Financial administration* | *23 570* | *19 694* | *16.4%* | *26 501* | *22 099* | *16.6%* |
| *Electricity* | *8 189* | *6 565* | *19.8%* | *7 643* | *6 134* | *19.7%* |
| *Water* | *12 377* | *10 667* | *13.8%* | *13 985* | *12 035* | *13.9%* |
| *Waste water management* | *8 723* | *7 171* | *17.8%* | *9 730* | *7 413* | *23.8%* |
| *Waste management* | *13 932* | *12 382* | *11.1%* | *13 867* | *12 309* | *11.2%* |
| *Other* | *70 656* | *61 527* | *12.9%* | *72 797* | *62 268* | *14.5%* |
| **Total** | **273 613** | **220 801** | **19.3%** | **278 591** | **223 928** | **19.6%** |

*Source: Stats SA, Non-financial census of municipalities for the year ended 30 June 2009, (P9115 - 2009)*

*Vacancy rates in metros are high – more than 20 per cent among all sectors*

Vacancy rates in metros are high – more than 20 per cent among all sectors. The number of vacancies in waste water management is very high, and the number of positions filled in this function has actually declined over the period under review.

Vacancy rates in category B and C municipalities have remained almost unchanged between 2008 and 2009. As previously mentioned, this could be due either to difficulties associated with finding the requisite skills and ensuring that those skills are retained, or it could be due to the fact that the vacant posts are unfunded.

## Municipal remuneration

*The average cost of employment has increased significantly*

Table 7.9 shows that total remuneration has increased by 52.5 per cent between 2006/07 and 2009/10, while growth in municipal employment over the same period was only 4 per cent. The result is a very significant increase in the average cost of employment.

**Table 7.9 Municipal personnel expenditure by category, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % average annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | | | |
| **R millions** | | | | | | | | 2006/07 – 2009/10 | 2010/11 – 2012/13 |
| Category A (Metros) | 16 776 | 18 580 | 21 972 | 25 450 | 28 460 | 30 940 | 33 655 | 14.9% | 9.8% |
| Category B (Locals) | 11 895 | 13 368 | 15 330 | 17 858 | 18 833 | 18 256 | 19 425 | 14.5% | 2.8% |
| *Secondary cities - 21* | 5 053 | 5 584 | 6 374 | 7 369 | 8 095 | 7 827 | 8 454 | 13.4% | 4.7% |
| *Towns - 140* | 5 196 | 5 886 | 6 757 | 7 827 | 7 945 | 7 678 | 8 044 | 14.6% | 0.9% |
| *Mostly rural - 70* | 1 645 | 1 898 | 2 199 | 2 662 | 2 793 | 2 751 | 2 927 | 17.4% | 3.2% |
| Category C (Districts) | 1 943 | 2 395 | 2 881 | 3 383 | 3 891 | 3 847 | 4 209 | 20.3% | 7.6% |
| *Category B + C* | *13 838* | *15 763* | *18 211* | *21 241* | *22 724* | *22 103* | *23 634* | 15.4% | 3.6% |
| **Total** | **30 614** | **34 343** | **40 183** | **46 691** | **51 183** | **53 043** | **57 289** | **15.1%** | **7.1%** |

*Source: National Treasury local government database*

*Between 2006/07 and 2009/10, municipalities' aggregate spending on personnel remuneration grew at an average annual rate of 15.1 per cent*

Between 2006/07 and 2009/10, municipalities' aggregate spending on personnel remuneration grew from R30.6 billion to R46.7 billion, reflecting an average annual growth rate of 15.1 per cent. This is set to grow by an average annual rate of 7.1 per cent over the medium term, to reach R57.3 billion by 2012/13.

Average annual growth in spending on personnel is generally consistent among the metros and most of the category B municipalities. However, in the case of rural municipalities, between 2006/07 and 2009/10, average annual growth in personnel expenditure was 17.4 per cent. This is above the average growth rate and must also be seen in the context of overall employment levels in these municipalities dropping by almost 7 per cent in the same period. This indicates that municipal salaries in rural municipalities have grown very strongly over the period.

While district municipalities have also experienced above average growth rates in personnel remuneration, this can be correlated with the 34 per cent increase in employment since 2006.

In secondary cities, average annual growth in remuneration between 2006/07 and 2009/10 was 13.4 per cent, which is below the average growth rate for all municipalities. So the increase in overall employment in secondary cities by almost 37 per cent in this period is possibly an indicator that a number of lower level positions may have been filled.

### Salaries and allowances of senior managers

*Senior management remuneration accounts for only 3.4 per cent of the total municipal wage bill in 2009/10*

The salaries of senior municipal managers, particularly municipal managers, always attract a considerable amount of public interest, especially given the general perception that municipal officials are overpaid in relation to their performance levels. However, in practice the remuneration of the senior management of municipalities accounts for only 3.4 per cent of the total municipal wage bill of R46.7 billion in 2009/10.

*Metros, and even the secondary cities, are very large, complex organisations*

The metros, and even the secondary cities, are very large, complex organisations (far more complex than the average national or provincial government department). The average salaries for municipal managers and CFOs for these two groups of municipalities do not appear to be out of line with the level of experience, expertise and responsibility required of these positions.

*In district municipalities, municipal managers' average salaries appear to be unreasonably high*

In district municipalities, however, the average salaries paid to the municipal managers and CFOs do appear to be out of line and unreasonably high. District municipalities are relatively straight-forward organisations compared to local municipalities with similar sized budgets. They receive most of their income in the form of transfers and they have limited service related responsibilities. It is therefore not clear what justifies the very high average salaries of district municipal managers and CFOs. Nor is it clear why municipal managers of the mostly rural municipalities earn on average more than those of the towns. A possible explanation is that rural municipalities are having to pay a premium to attract senior staff. However, the poor financial performance of many rural municipalities suggests that this premium is not paying off.

### Personnel costs as a percentage of operating expenditure

Municipalities in aggregate spend between 25 and 30 per cent of their total operating budgets on the remuneration of personnel. This spending trend has remained more or less constant since 2005/06. This is despite the outcome of the municipal wage agreement processes, which saw municipal employees receive increases that were substantially higher than the consumer price index (CPI). Table 7.10 shows municipal personnel expenditure as a percentage of total operating expenditure less the cost of bulk purchases of water and electricity. The reason for excluding bulk purchases is to facilitate greater comparability across the different categories of municipality.

**Table 7.10 Municipal personnel expenditure as % of total operating expenditure (exl bulk purchases), 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | |
| **Percentage** | | | | | | | |
| Category A (Metros) | 39.7% | 38.1% | 38.1% | 38.6% | 34.9% | 34.9% | 34.9% |
| Category B (Locals) | 42.1% | 40.7% | 37.5% | 38.0% | 37.7% | 37.8% | 38.2% |
| *Secondary cities - 21* | 39.7% | 39.7% | 34.0% | 34.4% | 36.7% | 36.8% | 37.4% |
| *Towns - 140* | 45.5% | 41.6% | 41.2% | 41.5% | 38.5% | 38.4% | 38.8% |
| *Mostly rural - 70* | 39.9% | 41.0% | 38.3% | 39.9% | 38.2% | 39.1% | 38.7% |
| Category C (Districts) | 27.3% | 26.6% | 27.1% | 27.9% | 33.4% | 35.1% | 36.4% |
| *Category B + C* | 39.1% | 37.7% | 35.4% | 35.9% | 36.9% | 37.3% | 37.9% |
| **Total** | 39.5% | 37.9% | 36.8% | 37.3% | 35.7% | 35.8% | 36.0% |

*Source: National Treasury local government database*

The trend evident in secondary cities reflects partly the impact of the very strong growth in expenditure on other items thus reducing the share of personnel expenditure, and partly that most of the employment being generated is at lower levels, thus not significantly increasing personnel costs. What this hides is that between 2006 and 2009 secondary cities increased employment by 37 per cent, and their personnel expenditure grew by 13.4 per cent per annum over the period.

*Personnel costs as a percentage of the total operating budget are higher than the average in towns, and rural and district municipalities*

Personnel costs as a percentage of the total operating budget (less bulk purchases) are higher than the average in towns and rural municipalities. It is evident that personnel costs are increasing fast in district municipalities. Two factors are likely to be underpinning this trend.

First, the metros and larger municipalities are better placed to take advantage of the economies of scale associated with mechanisation, and they have been doing this for some time. They are also more able to negotiate the intricacies of outsourcing labour intensive functions. Together, these result in metros and larger municipalities having lower personnel to operating expenditure ratios.

Second, as municipalities become smaller in terms of budget size, the more top heavy their governance and management structures become relative to their overall staffing profile, as well as their budget. The problem is particularly acute among small municipalities, where the revenue bases are so limited that they do not allow for much more than the employment of core staff. This translates into the very high ratios of personnel expenditure to operating expenditure shown among the 70 mostly rural municipalities.

## Average cost per employee

*The average cost of employment has increased at rates well above inflation*

Table 7.11 shows the increase in the average cost per employee between 2006 and 2009. Similar to the findings in the 2008 *Review*, the average cost of employment has increased at rates well above inflation, exceeding 20 per cent in all categories between 2007 and 2008, but then moderating strongly in 2009, except in the metros. The decline in the average cost per employee between 2008 and 2009 among the category B municipalities is linked to these municipalities employing staff at the lower levels.

**Table 7.11 Average cost per employee by category of municipality, 2006 to 2009**

| Rand | 2006 | 2007 | Percentage growth | 2008 | Percentage growth | 2009 | Percentage growth |
|---|---|---|---|---|---|---|---|
| Category A (Metros) | 122 033 | 130 303 | 6.8% | 186 907 | 43.4% | 230 777 | 23.5% |
| Category B (Locals) | 102 361 | 115 188 | 12.5% | 148 263 | 28.7% | 145 445 | -1.9% |
| *Secondary cities - 21* | *142 069* | *118 510* | -16.6% | *153 309* | 29.4% | *160 439* | 4.7% |
| *Towns - 140* | *83 886* | *112 194* | 33.7% | *138 037* | 23.0% | *129 234* | -6.4% |
| *Mostly rural - 70* | *88 029* | *115 222* | 30.9% | *169 785* | 47.4% | *158 826* | -6.5% |
| Category C (Districts) | 137 005 | 162 260 | 18.4% | 198 989 | 22.6% | 202 438 | 1.7% |
| *Category B + C* | 106 130 | 120 501 | 13.5% | 154 537 | 28.2% | 152 940 | -1.0% |
| **By metro** | | | | | | | |
| City of Cape Town | 131 366 | 182 269 | 38.7% | 218 090 | 19.7% | 259 955 | 19.2% |
| City of Johannesburg | 131 134 | 141 218 | 7.7% | 185 141 | 31.1% | 235 499 | 27.2% |
| City of Tshwane | 111 822 | 121 648 | 8.8% | 205 140 | 68.6% | 235 350 | 14.7% |
| Ekurhuleni | 137 261 | 159 771 | 16.4% | 219 150 | 37.2% | 284 775 | 29.9% |
| eThekwini | 90 546 | 79 259 | -12.5% | 131 124 | 65.4% | 165 056 | 25.9% |
| Nelson Mandela Bay | 191 694 | 167 684 | -12.5% | 235 433 | 40.4% | 280 002 | 18.9% |

*Source: National Treasury local government database*
*Stats SA, Non-financial census of municipalities (P9115 - 2007 to 2009)*

Of the metros, the most significant increase in the cost of employment is in Ekurhuleni, where a 29.9 per cent increase was observed between 2008 and 2009. Average growth in the cost of employment in Cape Town, Nelson Mandela Bay and Tshwane is below 20 per cent. The differences are largely dependent on the levels at which the respective metros have been employing staff, as well as the impact of outsourcing arrangements on the composition of municipal personnel.

## Performance management

The measurement of municipal performance is critical to the effective management of municipal performance, and is an essential component to improving the quality of service delivery. Public perceptions of municipal service delivery performance have declined significantly in recent years.

*Public perceptions of municipal service delivery performance have declined significantly in recent years*

Although performance management in local government is governed by a legislative framework and performance management regulations, the actual implementation of performance management systems in municipalities requires significant improvement. While many municipalities have developed sophisticated scorecards to assist in measuring overall organisational performance, the actual translation of these scorecards into individual performance agreements for senior management is often weak.

*The actual implementation of performance management systems in municipalities requires significant improvement*

Two other issues that have impacted negatively on performance management in municipalities are the number of signed s57 contracts in place, and the tenure of contracts for senior managers. The Municipal Systems Act (2000) provided for a choice between contract employment and permanent placement for s57 managers, so it is not clear why municipalities have invariably opted to appoint s57 managers on limited term contracts. The Municipal Systems Amendment Act now provides that all s57 managers, other than the municipal manager, must be appointed on permanent contracts.

## Legislative framework

The legal framework governing performance management in local government includes the Municipal Systems Act (2000) the Municipal Finance Management Act (2003) (MFMA) and the municipal performance regulations for municipal managers and managers directly accountable to municipal managers.

*The Municipal Systems Act (2000) requires all municipalities to promote a culture of performance through the establishment of a performance management system*

The Municipal Systems Act (2000) requires all municipalities to promote a culture of performance through the establishment of a performance management system. The performance management system must set key performance indicators and targets, as well as monitor, review and report on municipal performance based on indicators linked to the IDPs but also including the national indicators prescribed by the minister responsible for local government.

The MFMA requires the mayor to ensure that the performance agreements of s57 managers complies with the requirements of the Municipal Systems Act to promote sound financial management, are linked to measurable performance objectives, approved with the budget and included in the service delivery and budget implementation plan.

In August 2006, the then Department of Provincial and Local Government promulgated regulations for s57 managers, by setting out how the performance of municipal managers and their direct reports has to be planned, reviewed, improved and rewarded. These regulations provide for the conclusion of performance agreements and personal development plans.

## Why is performance still poor?

Despite having a sound legislative framework governing the management of performance in municipalities, municipal performance in most instances remains inadequate. The recent failures witnessed in some of the country's larger municipalities are clearly indicative of failures in governance across all levels.

*In many municipalities, poor performance is compounded by the lack of experienced senior managers in critical positions*

In many municipalities, poor performance is also compounded by the lack of experienced senior managers in critical municipal positions such as planning, infrastructure and financial management.

The performance management system is intended to reflect the relationship between overall performance of the municipality and the performance of individuals employed in the municipality. One of the questions often asked is how a municipality whose performance is visibly poor can award senior managers performance bonuses? If overall organisational performance is suffering, how can individual performance be rewarded? Why is there not a link between the two?

One response to this question is that there is often a link, albeit an extremely weak one, between the scorecard of the municipality, business unit or divisional plans and individual performance agreements. In addition, targets are often incorrectly set, not properly specified and impossible to measure. Another reason is that in many instances managers are allowed to revise or change their performance targets late in the year to ensure they get their bonuses, but these changes do not align to organisational performance. This makes assessing whether they have been achieved or not a subjective activity.

### Signing of performance agreements

*By the end of June 2009, only 78 per cent of municipal managers had signed performance agreements*

The Department of Co-operative Governance and Traditional Affairs' report on the state of local government, issued in 2010, noted that as at the end of June 2009, 250 out of 283 municipal manager positions were filled. Of these filled positions, only 196 (78 per cent) had signed performance agreements in place by the end of June 2009. Although this represented a small improvement of 6 per cent from 2008, it is clear that in order to improve accountability, all municipal managers need to have signed performance agreements in place. The report also noted that the failure to sign a performance agreement is a breach of the employment contract and that there are grounds for the employing municipality to terminate the employment contract unless there are sound reasons for non-compliance. National Treasury's view is that the no performance contract, no bonus principle should apply. There is no information currently available on the actual number of performance agreements signed by s57 managers in general.

## Conclusion

The role of sound and effective personnel management in the creation of a functionally efficient, responsive and accountable local government should not be underestimated. In this chapter, it has been observed that there has been minimal growth in overall municipal employment. The 30 per cent growth in employment in both local and district municipalities is concentrated in the financial and administration, water and waste water sectors, suggesting that these municipalities have been ramping up their capacity to deliver these services.

While a large number of municipal posts are still vacant in all three categories of municipalities, more than half of these vacancies are unfunded among the local and district municipalities. This problem is further compounded by the general inability of smaller and rural municipalities to attract and retain suitably qualified and skilled professional staff.

The Municipal Systems Amendment Act seeks to address a number of the fundamental barriers that exist in relation to effective governance and institutional arrangements in local government.

# 8

# Water and sanitation

## Introduction

In 2002, South Africa hosted the World Summit on Sustainable Development in Johannesburg. At this summit, former President Nelson Mandela said: 'Among the many things that I learned as president was the centrality of water in the social, political and economic affairs of the country, the continent and the world'.

*Water is fundamental to life, the environment, food production, hygiene and power generation*

Water is central to life. In South Africa, water-borne diseases are a major concern, and are listed as a leading cause of death in children under the age of five. Water is also a critical input to almost all forms of economic activity. Statistics South Africa reported that the water industry, made up predominantly by the water boards and other national agencies, contributed about R6.4 billion or 0.4 per cent to the country's annual gross domestic product (GDP) in 2006.

South Africa is facing a number of significant challenges in relation to water, both at the level of the resource as well as in the actual provision of water services by municipalities. Recent studies have estimated that demand for water in South Africa will exceed supply by 2025 if nothing is done to supplement current water resources. The sustainability of the sector as a whole is also at risk due to the poorly maintained and often ill-equipped infrastructure, general under-pricing of water across the value chain and the deteriorating quality of sanitation services in a number of municipalities.

*Demand for water in South Africa will exceed supply by 2025 if nothing is done to supplement current water resources*

Ensuring the future sustainability of water and sanitation services is critical and must be addressed through collective efforts.

This chapter looks at:

- water availability and demand
- water resource management
- the water services sector

- access to water and sanitation
- funding of basic water and sanitation infrastructure
- factors influencing the efficient provision of the water service.

## Water availability and demand

*South Africa is a semi-arid, water scarce country*

South Africa is a semi-arid, water scarce country. Rainfall levels average 450mm per year compared to the world average of 860mm per year. Rainfall patterns also differ between the western and eastern parts of the country, with rainfall levels as low as 100mm per year in the west and as high as 1 500mm per year in the east. This means that water availability varies greatly. While the total annual surface run-off is estimated to be 49 000 million cubic metres, only 14 200 million cubic metres per year or 29 per cent of the total surface run-off is available as a reliable yield.

Ground water resources are also not abundant, as most of South Africa is made up of hard rock formations that do not contain major ground aquifers that can be used on a national scale. It is estimated that only 20 per cent of South Africa's ground water can currently be used. Ground water resources are used extensively in rural and arid areas and it is estimated that about two-thirds of the population are dependent on ground water for domestic needs. Research is currently being undertaken to explore the artificial recharging of ground water resources as one of the mechanisms to meet the country's growing demand for water.

The national water resources strategy (2004) estimates that at current usage and price levels, available water resources will be insufficient to meet demands by 2025. The projected total water requirement in 2025 will be approximately 17 billion cubic metres versus a reliable yield of 15 billion cubic metres (that is at a 98 per cent assurance of supply level). Table 8.1 shows the projected deficit per water management area:

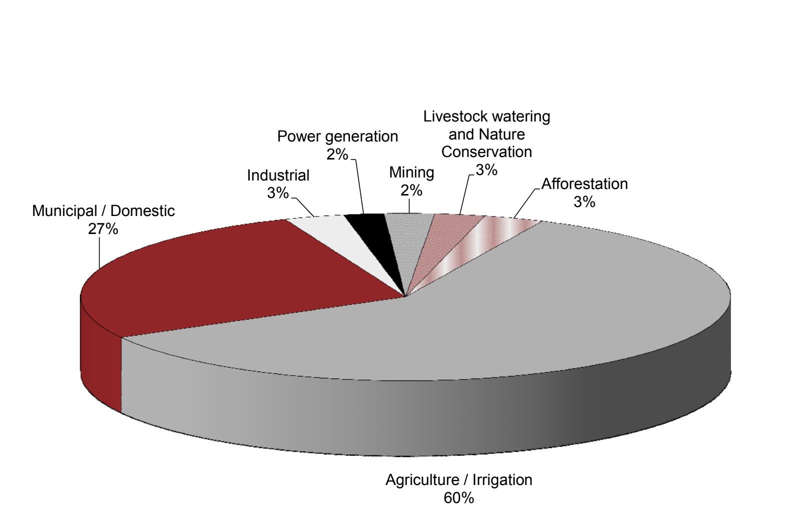
**Table 8.1 Reconciliation of requirements for and availability of water for the year 2025**

| Water management area<br>$m^3$/annum | Reliable local yield | Transfers in | Local requirements | Transfers out | Balance |
|---|---|---|---|---|---|
| Limpopo | 281 | 18 | 347 | – | -48 |
| Luvuvhu/Letaba | 404 | – | 349 | 13 | 42 |
| Crocodile West & Marico | 846 | 727 | 1 438 | 10 | 125 |
| Olifants | 630 | 210 | 1 075 | 7 | -242 |
| Inkomati | 1 028 | – | 914 | 311 | -197 |
| Usutu to Mhlathuze | 1 113 | 40 | 728 | 114 | 311 |
| Thukela | 742 | – | 347 | 506 | -111 |
| Upper Vaal | 1 229 | 1 630 | 1 269 | 1 632 | -42 |
| Middle Vaal | 55 | 838 | 381 | 503 | 9 |
| Lower Vaal | 127 | 571 | 641 | – | 57 |
| Mvoti to Umzimkulu | 555 | 34 | 1 012 | – | -423 |
| Mzimvubu to Keiskamma | 872 | – | 413 | – | 459 |
| Upper Orange | 4 734 | 2 | 1 059 | 3 589 | 88 |
| Lower Orange | -956 | 2 082 | 1 079 | 54 | -7 |
| Fish to Tsitsikamma | 456 | 603 | 988 | – | 71 |
| Gouritz | 278 | – | 353 | 1 | -76 |
| Olifants/Doring | 335 | 3 | 370 | – | -32 |
| Breede | 869 | 1 | 638 | 196 | 36 |
| Berg | 568 | 194 | 829 | – | -67 |

*Source: Department of Water Affairs and Forestry, National Water Resource Strategy, First Edition, September 2004*

South Africa's water resources are comprised of 77 per cent surface water, 9 per cent groundwater, and 14 per cent re-use of return flows. Of the available resources, the demand for water is dominated by agriculture, at 60 per cent of total demand. Domestic demand accounts for 27 per cent in total: 24 per cent for urban areas and 3 per cent for rural supply.

**Figure 8.1 The use of water per main economic sector**




*Source: Department of Water Affairs (Strategic Overview of the Water Sector in South Africa 2010)*

*There needs to be a balance between urban and rural water needs*

It is expected that future growth in water requirements will be mainly in the metros and large cities. However, this needs to be balanced with rural water needs, particularly agriculture, to safeguard food security. Specific attention will therefore need to be given to ensuring adequate future water supplies to urban growth areas, as well as ensuring equitable access to the existing supplies.

The Department of Water Affairs is in the process of updating the National Water Resource Strategy (NWRS). The updated strategy will present the latest picture of water requirements versus availability.

### Composition of the water sector

The water sector in South Africa is divided into two main sub-sectors, namely water resources management, guided by the National Water Act (1998), and water services provision, guided by the Water Services Act (1997). These sub-sectors include stakeholders across the national, regional and local level.

## Water resource management

*The management of water resources is an exclusive national competency*

Water resource management is concerned with the management, protection, utilisation, development, conservation and control of the country's water resources in a manner that will promote sustainability and equity and which will benefit all people. It involves the management of the dams and catchments, as well as the transfer and storage of raw water.

Although water can be treated and discharged back into the environment, it is also a finite resource with no substitute.

Management of South Africa's water resources involves catchment management functions, river systems management, water storage, water abstraction and return-flow management. Water resources must therefore be managed in an integrated way to ensure that water is protected and used to its full potential. As water is a scarce resource, it is critical for water resource management to balance the growing social and economic needs with the sustainability of the resource and environmental health considerations.

Water is a national asset and the Minister of Water Affairs is the custodian and national manager of water resources. The Department of Water Affairs is directly responsible for most of the large water resource infrastructure and undertakes the planning and implementation of large water resource development projects, such as the construction of dams and inter-basin transfer schemes.

*The management of water resources has been decentralised*

In South Africa, the management of water resources has been decentralised. To facilitate this, the country has been divided into 19 water management areas (WMAs). It is envisaged that each of the 19 WMAs will have a catchment management agency (CMA) established in terms of chapter 7 of the National Water Act (1998) and are classified as schedule 3A public entities in terms of the Public Finance Management Act (1999).

The main responsibility of a CMA is to manage water resources at the catchment level. Each CMA must develop a catchment management strategy and advise on the protection, development, use and conservation of water in each catchment. CMAs need to work in collaboration with local stakeholders, including the water user associations and local communities. This is to ensure that decisions made with regard to water use balance meeting basic human needs, promote equitable access to water and facilitate social and economic development.

To date, only two catchment management agencies (Breede River and Inkomati) have been established with active governing boards. The two were delegated full CMA functions in 2010. The process for establishing the remaining CMAs will be finalised once the Department of Water Affairs institutional realignment process has been completed. It is envisaged that this process would guide the total number of CMAs to be established.

### Spending on water resource infrastructure

*It is critical that appropriate investments be made to upgrade current infrastructure, as many of these assets are approaching the end of their useful lives*

The majority of capital investments in water resource infrastructure were made in the 1970s and 1980s. Given that there has generally been a history of underinvestment on maintenance and renewal of assets in the water sector as a whole, it is now critical that appropriate investments be made to upgrade existing infrastructure, as many of these assets are approaching the end of their useful lives. Therefore, funding for major rehabilitation is required to ensure that the useful life of these assets can be extended.

Water resource infrastructure is financed either by the national budget or through the Trans Caledon Tunnel Authority (TCTA). In addition, a Water Trading Entity (WTE) was established within the Department of Water Affairs to promote the efficient management of bulk infrastructure. However, the entity is currently facing significant technical, financial and management challenges, which are severely limiting its capacity to finance and manage the bulk water infrastructure efficiently.

The TCTA operates as a special purpose vehicle responsible for the financing and building of large water infrastructure that is identified by the WTE. The TCTA borrows finance from markets in its own capacity, with government providing explicit guarantees in certain instances. Once the infrastructure is built, the WTE is then responsible for the operation and maintenance of this infrastructure. The TCTA services the debt (usually over 20 years) with payments from the WTE. After the debt is repaid, asset ownership is transferred to the WTE.

The TCTA currently has approximately R22.9 billion worth of infrastructure reflected on its balance sheet and is planning for additional projects to the value of R21 billion over the next few years. The Department of Water Affairs currently owns R120 billion worth of infrastructure.

*The national backlogs in water resource infrastructure are estimated to be approximately R13 billion*

The national backlogs in water resource infrastructure are estimated to be approximately R13 billion, of which R10.1 billion alone relates to dam safety and rehabilitation. Over the next five years, the Department of Water Affairs plans to spend in the region of R15 billion on new capital projects, rehabilitation and maintenance programmes. It is expected that of this amount, approximately R1 billion per year will be spent on capital maintenance programmes, while just over R2.2 billion per year will be spent on dam safety rehabilitation programmes.

In 2010, the department spent approximately R850 million on the construction of the De Hoop Dam and dam and canal rehabilitation. The total estimated cost of this project is R16 billion, which will be financed partly from the fiscus and partly from agreements between industry and the WTE.

## The water services sector

*The Department of Water Affairs, water boards and municipalities are the primary players in water services sector*

Water services refer to water supply and sanitation services and include regional water schemes, local water schemes, on-site sanitation and the collection and treatment of wastewater. The Department of Water Affairs, water boards and municipalities are the primary players in the water services sector.

### National government

The Department of Water Affairs plays the role of sector leader and is responsible for policy development, regulation, monitoring and support functions. The department has phased out its role as an implementing agent by transferring water schemes to the relevant municipalities. 61 transfer agreements were signed to transfer 1 600 individual water schemes from the department to municipalities. The cost of this exercise was approximately R6.6 billion. As a transitional arrangement, a water services operating subsidy grant has been made available to the department and municipalities to ensure that the transferred schemes are fully functional and operated by skilled personnel to ensure optimal service delivery by the municipalities concerned.

### Water boards

Water boards are established in terms of the Water Services Act (1997) as national government business enterprises, in terms of schedule 3B of the Public Finance Management Act (1999).

*Water boards are primarily responsible for bulk water provision, but some water boards also provide retail and reticulation services*

Water boards act as intermediaries to distribute raw and potable water across vast distances to multiple users (the regional water supply schemes). Water boards are primarily responsible for bulk water provision, but some water boards also provide retail and reticulation services. However, in such cases, the water board must be appointed by the relevant municipality as a water services provider.

There are currently 14 water boards in the country. Ikangala Water was recently disestablished and incorporated into Rand Water. Namakwa Water and Albany Water are expected to be disestablished in 2011, leaving the sector with 12 water boards.

Not all municipalities are dependent on regional bulk water supply infrastructure and hence operate independently of the water boards. Where this is the case, norms and standards of the Water Services Act (1997); the National Water Act (1998) and related regulations and strategies govern their operations.

Currently, the 14 operational water boards supply approximately 2.39 billion cubic metres of water per year to approximately 28 million people and several large industries. The average bulk potable water tariff is R3.84 per cubic meter, but varies widely from R2.78 to R7.26 per cubic metre subject to the availability of water, the distance of distribution and raw water quality. According to information published by the Department of Water Affairs, total revenue generated by water boards in 2009/10 was approximately R8.1 billion against total operating expenditure of R4.9 billion. Total aggregated surpluses for that financial year were approximately R910 million. Between 2008 and 2010, aggregated surpluses have declined by almost 35 per cent. The decline is due to several of these institutions incurring operating deficits in 2009/10. The reduction in surpluses can largely be attributed to the stronger role that the Department of Water Affairs and National Treasury are playing in the tariff setting process, which is compelling water boards to absorb increases in operating costs through improving operational efficiency.

The growth in other income of water boards since 2007/08 is significant and indicates that water boards are increasingly being contracted by municipalities to act as water service providers.

*Rand Water accounts for most revenue and operating expenditure*

The water boards vary greatly in terms of budget size and the area they serve. Rand Water and Umgeni Water are the two largest water boards in the country. Rand Water's budget accounted for 62 per cent of the total revenue and 48 per cent of total operating expenditure for all water boards, followed by Umgeni Water, which accounted for 17.6 per cent of the total revenue and 19.2 per cent of total operating expenditure. Although Rand Water services a relatively small area compared to other water boards, it serves the most customers and has the largest number of staff, which reflects the high density of Gauteng's population.

Water boards do face a number of challenges. Many boards find it difficult to conclude long-term bulk water supply agreements with municipalities, which affects their ability to make long-term infrastructure capital projections. Furthermore, a number of municipalities have defaulted on payments to water boards and in some cases these have posed a threat to the financial viability of the water board.

### Local government

*The provision of water services is a municipal competence*

The provision of water services is a municipal competence in terms of Part B of schedule 4 of the Constitution. However, not all municipalities are authorised to provide this function. The two-tiered local government system requires that powers and functions be divided between category B and C municipalities to avoid duplication and coordination problems. An asymmetric approach has been followed in relation to water and sanitation, where all category A (metros) municipalities are authorised, category B (local) municipalities are authorised in certain instances and category C (district) municipalities in others.

A total of 169 municipalities have been authorised to provide water and sanitation services. An authorised municipality may appoint another organisation (including another municipality) to provide the water services function on its behalf. These 'external mechanisms' are referred to as water service providers.

**Municipal membership of fire protection associations**

Fire Protection Associations (FPAs) play a key role in preventing and combating forest and veld fires. This is critical to the protection of water catchment areas, and securing reliable flows of water and preventing the degradation as raw water from burned areas carries increased levels of sediment, organic debris and chemicals into rivers and dams. Section 4(7) of the National Veld and Forest Fire Prevention Act reads as follows:

> (7) Where a fire protection association has been registered in an area –
> (a) all or part of which is controlled by a municipality and that municipality has a service; or
> (b) in which there is a designated service, the municipality or designated service must become a member of the fire protection association.

There is thus a legal obligation on municipalities to join their local fire protection associations, and as members to participate fully in their operations, including paying their membership fees, and ensuring appropriate fire protection measures, such as fire breaks and the eradication of exotic vegetation, are implemented on all municipal land.

The sharing of the water services function between category B and C municipalities has contributed to some of the difficulties currently being experienced in providing the service, including problems in the allocation of resources through the intergovernmental fiscal system. The current practice is that the only recipients of the national grant for water and sanitation are the authorised municipalities. This becomes a problem in cases where authorised district municipalities delegate the responsibility for service provision to local municipalities without passing on the necessary funds.

## Access to water and sanitation

*Government's objective is to ensure that all South Africans have access to basic water supply and sanitation services*

Government's objective is to ensure that all South Africans have access to basic water and sanitation services. Government has prioritised not only the rollout of infrastructure necessary for the rendering of these services but also the provision of free basic services to poor households.

A basic water supply service refers to the infrastructure necessary to supply 25 litres of potable water per person per day from a source within 200m of a household and with a minimum flow of 10 litres per minute (in the case of communal water points) or 6 000 litres of potable water supplied per formal connection per month (in the case of house connections).

A basic sanitation service refers to the provision of a basic sanitation facility which is easily accessible to a household, and the sustainable operation of the facility. This includes the safe removal of human waste and wastewater from the premises where this is appropriate and necessary, and the communication of good sanitation, hygiene and related practices.

*The sustainability of existing infrastructure cannot be neglected and is requiring more and more funding as infrastructure ages*

While there have been substantial improvements in the rollout of water services infrastructure and the rendering of free basic water and sanitation, the sector does face some challenges going forward as implementation capacity remains a constraint. Furthermore, the sustainability of existing infrastructure cannot be neglected and is requiring more and more funding as infrastructure ages. Also, the cost of extending the network infrastructure to outlying communities is not cost-effective or sustainable, which points to the need to explore alternative service delivery options.

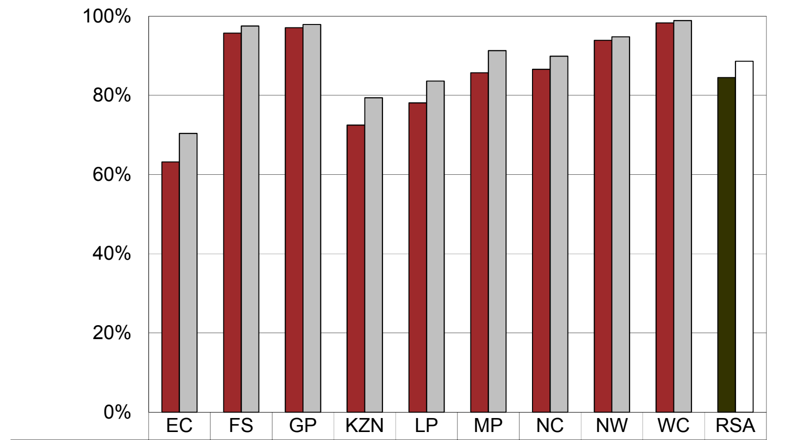
### Progress with basic water infrastructure rollout

*Between 2001 and 2007, access to piped water increased in all provinces*

In 1994, only about 59 per cent of South Africa's population had access to water supply infrastructure. This meant that about 15.9 million people had no access to basic water supply.

Figure 8.2 shows the percentage of households with access to piped water in all nine provinces, based on the Census 2001 and the Community Survey 2007 results. The province with the lowest percentage of access is Eastern Cape (70.4 per cent), followed by KwaZulu-Natal (79.4 per cent) and Limpopo (83.6 per cent). However, these three provinces made the most progress in percentage terms from 2001 to 2007, where access percentage in the Eastern Cape increased by 7.2 per cent, KwaZulu-Natal by 6.9 per cent and Limpopo by 5.5 per cent, compared to Western Cape, which increased by 0.6 per cent and Gauteng, which increased by 0.8 per cent.

**Figure 8.2 Percentage of households with access to piped water by province, 2001 – 2007**




| | EC | FS | GP | KZN | LP | MP | NC | NW | WC | RSA |
|---|---|---|---|---|---|---|---|---|---|---|
| Census 2001 | 63.2% | 95.7% | 97.1% | 72.5% | 78.1% | 85.7% | 86.6% | 93.9% | 98.3% | 84.5% |
| CS 2007 | 70.4% | 97.5% | 97.9% | 79.4% | 83.6% | 91.3% | 89.9% | 94.8% | 98.9% | 88.6% |

*Source: Stats SA, Census 2001 and Community Survey 2007*

*The current backlog is estimated at 3.63 million people*

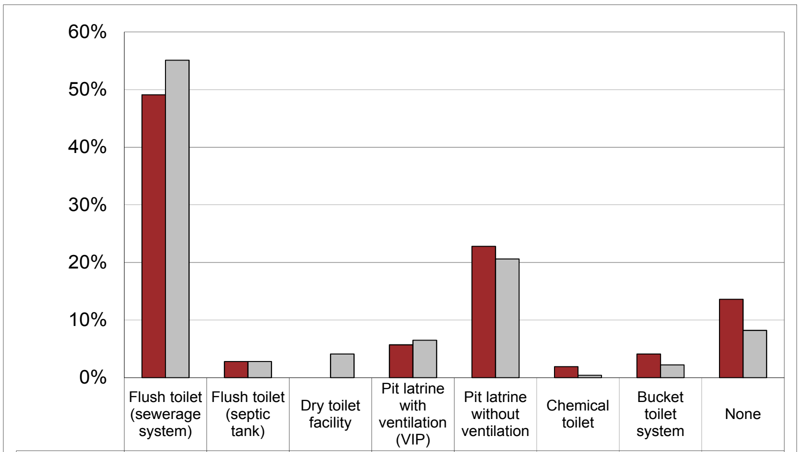
The Department of Water Affairs reports in its 2009/10 annual report that overall access to water supply infrastructure has since increased to 97 per cent. Currently, about 1.65 million people have no access to water infrastructure, while 1.98 million people have access to infrastructure that is below minimum standards. The current backlog is therefore estimated at 3.63 million people as at March 2010. Based on the availability of funding, backlog eradication targets for 2010/11 have been set at 1.5 million people per year or 390 000 households, which suggests that South Africa will come very close to achieving its Millennium Development Goals in relation to access to water.

### Progress with basic sanitation infrastructure rollout

Many different types of sanitation technology are currently used in South Africa, including buckets (priority has been given to eradicating this system), pit latrines (with or without ventilation), chemical toilets (also to be replaced with more appropriate technology types), flush toilets with on-site septic tanks and disposal, and flush toilets with waterborne and central treatment works. In 1994, only 49 per cent of people had access to sanitation facilities.

Figure 8.3 shows the percentage of households by type of toilet facility in 2001 and 2007.

**Figure 8.3 Percentage of households with access to flush toilets, 2001 – 2007**




| | Flush toilet (sewerage system) | Flush toilet (septic tank) | Dry toilet facility | Pit latrine with ventilation (VIP) | Pit latrine without ventilation | Chemical toilet | Bucket toilet system | None |
|---|---|---|---|---|---|---|---|---|
| Census 2001 | 49.1% | 2.8% | 0.0% | 5.7% | 22.8% | 1.9% | 4.1% | 13.6% |
| CS 2007 | 55.1% | 2.8% | 4.1% | 6.5% | 20.6% | 0.4% | 2.2% | 8.2% |

*Source: Stats SA, Census 2001 and Community Survey 2007*

*It is estimated that approximately 10.6 million people or 2.6 million households still do not have access to basic sanitation services*

The figure shows that the percentage of households in the country with access to flush toilets has increased from 49.1 per cent in 2001 to 55.1 per cent in 2007, while households with no toilet at all decreased from 13.6 per cent in 2001 to 8.2 per cent in 2007. Gauteng, Free State, Northern Cape and Western Cape were the only provinces that had more than 50 per cent of households using flush toilets. Although progress had been made with the eradication of the bucket toilet system (from 4.1 per cent in 2001 to 2.2 per cent in 2007), backlogs remain. Government remains committed to fast-tracking the completion of the bucket eradication programme.

The Department of Water Affairs reported that in 2009/10, the overall access to sanitation had increased to 79 per cent. It is estimated that approximately 10.6 million people or 2.6 million households still do not have access to basic sanitation services.

**Bucket eradication programme**

The bucket eradication programme was established in 2005 with the aim of replacing the bucket system in established settlements with more acceptable forms of sanitation. The target date for completing the programme was December 2007. At that stage, an estimated 252 254 households still needed to be reached. 244 258 buckets had been replaced by September 2009. In 2009/10, a further 1 048 buckets were replaced with alternative sanitation arrangements. This left 7 996 buckets in the Free State, Eastern Cape and Northern Cape.

Delays in the programme have been attributed to the slow performance of contractors and the need to complete sewer networks and pump stations, before bucket systems are stopped.

## Funding of basic water and sanitation infrastructure

*As they can cross-subsidise more easily, metros are less reliant on transfers*

Water and sanitation services are financed through the water and sanitation components in the local government equitable share and capital spending on water and sanitation assets are financed through the basic services component of the municipal infrastructure grant (MIG). Metros contribute substantial own revenues towards supplying water and sanitation services to complement the local government equitable share, while other categories of municipalities do not do so (this is indicated by the 'Difference' columns in table 8.2). This could be because metros serve a larger variety of customers, including businesses and industries, compared to smaller municipalities that largely serve a residential customer base. Metros are therefore more able to cross-subsidise between and within different types of customers and services. Infrastructure grant funding is supplemented by internal sources and external borrowing for all types of municipalities, with the exception of district municipalities, where less is spent on water and sanitation infrastructure than what is allocated through the water and sanitation component of the MIG. This may be because the funds are being passed on to local municipalities that are water service providers, or because the funding is being used for other municipal services.

**Table 8.2 Water and sanitation expenditure and grants per capita**

| R thousands | Bulk purchases per capita | LGES per capita | Difference | Capital expenditure per capita | Water and sanitation component of MIG per capita | Difference |
|---|---|---|---|---|---|---|
| Category A (Metros) | 238 | 166 | 72 | 111 | 29 | 82 |
| Category B (Locals) | 54 | 216 | -162 | 56 | 30 | 26 |
| Category C (Districts) | 5 | 57 | -52 | 47 | 53 | -6 |

*Source: National Treasury local government database*

## Free basic water and sanitation

*There has been an increase in the number of households receiving free basic water and sanitation*

Table 8.3 shows the number of households that benefited from free basic water and sanitation services. The total number of households that received basic water increased by 7 per cent or 695 000 between 2008 and 2009, while the number of households that received basic sanitation increased by 7.6 per cent or 657 000.

**Table 8.3 Number of households receiving free basic water and sanitation, 2007 – 2009**

| Province | 2007 | 2008 | 2009 | 2007 | 2008 | 2009 |
|---|---|---|---|---|---|---|
| | Basic water services | | | Free basic water | | |
| Eastern Cape | 1 213 142 | 1 524 805 | 1 500 132 | 574 165 | 775 360 | 786 263 |
| Free State | 626 011 | 656 725 | 681 369 | 569 622 | 402 978 | 470 333 |
| Gauteng | 2 566 240 | 2 419 367 | 2 725 965 | 2 060 021 | 1 461 966 | 1 496 021 |
| KwaZulu-Natal | 1 941 653 | 1 800 759 | 1 881 332 | 1 537 122 | 1 246 349 | 1 329 741 |
| Limpopo | 935 766 | 1 206 009 | 1 296 625 | 535 471 | 567 194 | 609 114 |
| Mpumalanga | 798 967 | 817 719 | 877 148 | 517 861 | 342 915 | 359 510 |
| Northern Cape | 212 499 | 207 321 | 222 800 | 87 432 | 90 530 | 94 267 |
| North West | 678 501 | 658 440 | 697 445 | 497 481 | 353 125 | 342 752 |
| Western Cape | 917 684 | 991 085 | 1 093 934 | 846 112 | 834 372 | 892 850 |
| **Total** | **9 890 463** | **10 282 230** | **10 976 750** | **7 225 287** | **6 074 789** | **6 380 851** |
| | Basic sanitation services | | | Free basic sanitation | | |
| Eastern Cape | 855 035 | 1 001 158 | 1 035 712 | 402 467 | 534 148 | 590 419 |
| Free State | 616 898 | 642 072 | 664 045 | 250 566 | 181 873 | 202 797 |
| Gauteng | 2 120 324 | 2 217 385 | 2 485 321 | 889 946 | 592 101 | 710 015 |
| KwaZulu-Natal | 1 678 489 | 1 669 120 | 1 732 153 | 348 514 | 322 514 | 330 574 |
| Limpopo | 596 899 | 626 576 | 720 631 | 193 444 | 155 780 | 177 207 |
| Mpumalanga | 545 136 | 760 870 | 811 493 | 110 975 | 93 114 | 101 837 |
| Northern Cape | 187 688 | 184 571 | 194 810 | 66 096 | 64 955 | 69 658 |
| North West | 567 800 | 547 126 | 563 394 | 119 167 | 98 887 | 100 037 |
| Western Cape | 934 675 | 989 041 | 1 087 274 | 737 059 | 709 430 | 752 968 |
| **Total** | **8 102 944** | **8 637 919** | **9 294 833** | **3 118 234** | **2 752 802** | **3 035 512** |

*Source: Stats SA, Non-financial census of municipalities for the year ended 30 June 2009*

While there has been good progress in extending access to basic water and sanitation services, there has been a decline in the overall number of households receiving free basic water and free basic sanitation. This is due to many municipalities moving away from providing these services free to all households to targeting the provision of free services to indigent households only. This is a positive development as it strengthens the sustainability of the free basic services programmes of the municipalities.

## Municipal and municipal entity budgets

The water services function is an important municipal function, which comprised 11 per cent of total municipal budgets in 2007/08. Municipalities budgeted to spend R32 billion on water and sanitation in 2010/11, compared to the R8.4 billion spent in 2006/07.

### *Municipal water budgets*

*The significant cost drivers for operating expenditure are bulk water purchases, employee costs and repairs and maintenance*

Table 8.4 indicates that most of the operating expenditure associated with the provision of water occurs in metros and large urban municipalities. In the 2010 MTREF, operational expenditure is expected to increase significantly among all categories of municipalities. Between 2009/10 and 2012/13, operational expenditure is expected to increase at an annual average rate of 35.0 per cent. The significant cost drivers for operating expenditure are bulk water purchases, employee costs and repairs and maintenance.

**Table 8.4 Budgeted water expenditure by category of municipality, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Revised Estimate | Medium-term estimates | | |
| **Operating expenditure** | | | | | | | |
| Category A (Metros) | 6 807 | 6 844 | 9 038 | 6 027 | 14 254 | 14 554 | 15 976 |
| Category B (Locals) | 852 | 1 814 | 3 772 | 3 987 | 6 834 | 6 774 | 7 274 |
| *Secondary cities* | *658* | *1 541* | *2 272* | *2 468* | *3 686* | *3 852* | *4 208* |
| *Remainder* | *194* | *273* | *1 501* | *1 519* | *3 148* | *2 922* | *3 066* |
| Category C (Districts) | 42 | 94 | 1 889 | 1 067 | 3 757 | 3 698 | 3 984 |
| **Subtotal operating** | **7 702** | **8 752** | **14 699** | **11 081** | **24 844** | **25 027** | **27 234** |
| **Capital expenditure** | | | | | | | |
| Category A (Metros) | 470 | 1 050 | 2 945 | 3 087 | 1 889 | 2 335 | 2 320 |
| Category B (Locals) | 189 | 452 | 1 356 | 1 020 | 2 151 | 1 965 | 1 996 |
| *Secondary cities* | *118* | *293* | *602* | *579* | *824* | *788* | *880* |
| *Remainder* | *70* | *158* | *754* | *442* | *1 327* | *1 177* | *1 116* |
| Category C (Districts) | – | 11 | 1 528 | 2 409 | 3 128 | 3 569 | 4 189 |
| **Subtotal capital** | **659** | **1 513** | **5 829** | **6 516** | **7 168** | **7 869** | **8 505** |
| **Total** | | | | | | | |
| Category A (Metros) | 7 277 | 7 894 | 11 983 | 9 114 | 16 142 | 16 889 | 18 296 |
| Category B (Locals) | 1 041 | 2 266 | 5 128 | 5 007 | 8 985 | 8 739 | 9 270 |
| *Secondary cities* | *776* | *1 834* | *2 874* | *3 046* | *4 510* | *4 640* | *5 088* |
| *Remainder* | *265* | *431* | *2 255* | *1 961* | *4 475* | *4 099* | *4 182* |
| Category C (Districts) | 42 | 105 | 3 417 | 3 476 | 6 886 | 7 267 | 8 173 |
| **Total** | **8 361** | **10 265** | **20 528** | **17 597** | **32 012** | **32 895** | **35 739** |

*Source: National Treasury local government database*

Capital spending on water infrastructure by the metros falls significantly in 2010/11, and does not recover to 2008/09 levels over the medium term. However, spending on water infrastructure among the category B and C municipalities is expected to increase significantly in this period.

### *Municipal sanitation budgets*

*Municipalities are prioritising the rollout of sanitation infrastructure*

Table 8.5 shows that overall spending on municipal sanitation is expected to increase at an average annual rate of 31.9 per cent between 2009/10 and 2012/13. Most of this increase is attributed to increases in operational expenditure. Total capital expenditure on sanitation is expected to grow at an annual average rate of

36.3 per cent between 2009/10 and 2012/13, indicating that municipalities are prioritising the rollout of sanitation infrastructure. But good sanitation includes acceptable, affordable and sustainable sanitation services and appropriate health and hygiene awareness and behaviour. It is therefore important that municipalities complement any sanitation infrastructure investment with initiatives focused on behaviour change.

**Table 8.5 Budgeted sanitation expenditure by category of municipality, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 Outcome | 2008/09 | 2009/10 Revised Estimate | 2010/11 | 2011/12 Medium-term estimates | 2012/13 |
|---|---|---|---|---|---|---|---|
| **Operating expenditure** | | | | | | | |
| Category A (Metros) | 1 949 | 2 427 | 2 917 | 2 196 | 5 293 | 5 729 | 6 135 |
| Category B (Locals) | 367 | 805 | 1 865 | 2 186 | 3 291 | 3 114 | 3 204 |
| *Secondary cities* | *273* | *661* | *1 098* | *1 458* | *1 850* | *1 802* | *1 852* |
| *Remainder* | *94* | *145* | *767* | *728* | *1 441* | *1 312* | *1 352* |
| Category C (Districts) | 107 | 80 | 246 | 178 | 443 | 608 | 637 |
| **Subtotal operating** | **2 424** | **3 312** | **5 029** | **4 559** | **9 027** | **9 451** | **9 975** |
| **Capital expenditure** | | | | | | | |
| Category A (Metros) | 735 | 588 | 1 207 | 1 250 | 2 086 | 2 486 | 2 819 |
| Category B (Locals) | 170 | 548 | 1 208 | 645 | 1 894 | 1 993 | 2 029 |
| *Secondary cities* | *95* | *446* | *564* | *331* | *926* | *1 128* | *1 110* |
| *Remainder* | *75* | *102* | *644* | *313* | *968* | *864* | *919* |
| Category C (Districts) | – | – | 757 | 247 | 689 | 522 | 569 |
| **Subtotal capital** | **905** | **1 136** | **3 172** | **2 141** | **4 669** | **5 001** | **5 416** |
| **Total** | | | | | | | |
| Category A (Metros) | 2 684 | 3 015 | 4 124 | 3 445 | 7 379 | 8 215 | 8 954 |
| Category B (Locals) | 537 | 1 353 | 3 073 | 2 830 | 5 184 | 5 107 | 5 232 |
| *Secondary cities* | *369* | *1 107* | *1 662* | *1 789* | *2 776* | *2 930* | *2 962* |
| *Remainder* | *169* | *246* | *1 411* | *1 041* | *2 408* | *2 176* | *2 270* |
| Category C (Districts) | 107 | 80 | 1 003 | 424 | 1 133 | 1 130 | 1 206 |
| **Total** | **3 329** | **4 448** | **8 200** | **6 700** | **13 696** | **14 452** | **15 392** |

*Source: National Treasury local government database*

## Water services pricing and tariffs

The water pricing cycle consists of various stages. These are:

- raw water tariff (water resources development charge)
- bulk water tariff
- retail water tariff
- sanitation charge
- bulk waste-water tariff
- waste water discharge charge.

*The cost of one stage will form an input cost into the next stage of the pricing chain*

All the stages are interrelated and individually costed, except for the waste water discharge charge. The cost of one stage will form an input cost into the next stage of the pricing chain. It is therefore imperative that the costs at each stage are determined as accurately as possible to avoid overall under-pricing of water throughout the value chain.

This charging system is complemented by nationally-funded subsidies for infrastructure and ongoing services to poor households.

### *Water charges and tariffs*

As noted above, the Department of Water Affairs is the custodian of all raw water resources, and owns most major dams. The department sells raw water to either a water board or to the water service authority, i.e. the municipality. Certain municipalities, such as Cape Town, operate their own dams. Municipalities that purchase raw water directly from the department are responsible for purifying the water. In most cases, water boards purchase raw water from the department, purify and refine it and then sell the purified water to municipalities.

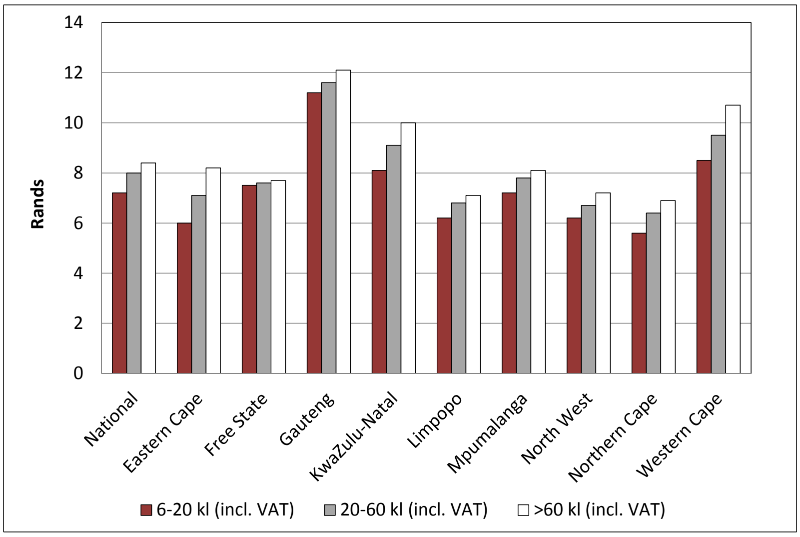
*The Department of Water Affairs regulates the tariff charged by water boards to municipalities*

The tariff charged by water boards to municipalities is regulated by the department. Several factors influence the tariffs that each water board charges. These include the actual purchase price of the raw water, the methods and cost of the purification of water and the cost of the capital investment requirements of the water board. The average bulk price charged by water boards will be approximately R5.12 in 2011/12. The highest bulk water tariff for 2011/12 is R10.07 per kl by Namakwa Water, while the lowest will be approximately R3.55 per kl for the Overberg Water Board. This partly indicates differences in the scarcity of water. These prices for treated bulk water impact directly on municipalities' retail water tariffs, as bulk water forms a large proportion of the overall retail tariff.

The Department of Water Affairs prescribes norms and standards for water services tariffs in terms of section 10 of the Water Services Act (1997). These are aimed at promoting equitable, financially viable and environmentally sustainable tariffs. The regulations apply to all water services institutions and they may not use a tariff that is substantially different from any of the prescribed norms and standards.

The Department of Water Affairs surveys all tariffs along the water provisioning cycle, including water management charges, raw water tariffs, water board tariffs and the municipal tariffs for domestic, commercial and industrial users. The following information relating to tariffs has been extracted from the Strategic Overview of the Water Sector in South Africa (2010).

**Figures 8.4 Average domestic water tariffs in 2009/10**




*Source: DWA Strategic overview of the water sector in South Africa 2010*

Figure 8.4 shows that the highest average domestic water tariffs are in Gauteng, while the lowest average domestic tariffs occur in the Northern Cape.

*Sanitation charges and tariffs*

Municipalities need to take a number of issues into account when setting appropriate tariffs for sanitation. The servicing of on-site sanitation systems is not a monthly activity and is also highly dependent on the type of sanitation system installed, the households' responsibilities for maintaining the system and the accepted final disposal method of the wastes. An investigation of the emptying of pit latrines, for example, has indicated that these should be scheduled for emptying once every five to eight years and will cost between R600 and R1 200 each to empty (2007 prices). The approach to collecting tariffs for providing such a service may either be built into the water bill, to charge a fee for emptying or a number of other alternatives.

## Factors influencing the efficient provision of water services

A range of external and internal factors impact on the ability of municipalities to provide the water services function. These include:

### Non-revenue water

Non-revenue water represents the level of losses or unauthorised use from a water supply scheme. It is defined as the volume of water for which no income is received by the water services provider.

In South Africa, non-revenue water is estimated to be around 35 per cent of the water supplied. This estimate is informed mainly by information supplied by metros and other large municipalities. Non-revenue water may even be higher in rural municipalities, due to the maintenance backlogs that exist in these municipalities.

*The primary concern is with water losses due to poor maintenance, inaccurate or incomplete billing and water theft*

Free basic water is regarded as revenue water charged at a zero rate and is therefore not included in the calculation of non-revenue water. The calculation also excludes non-payment of accounts as these constitute water that is billed for. Although South Africa's non-revenue water is lower than that of other developing countries, much scope still exists for improving operating efficiency. The primary concern is with water losses due to poor maintenance, inaccurate or incomplete billing and water theft.

Municipalities are expected to develop a comprehensive water conservation and water demand management strategy which provides strategic direction to reduce non-revenue water. Included in the strategy, could be programmes for leak detection and repairs, passive leakage control, consumer meter audit and management, water use efficiency education and awareness, water and sewer network information management, water audits and determination of water balance for each of the water network in the supply area. The strategy should also aim at implementing internationally accepted water balance model developed by International Water Association (IWA).

Figure 8.5 shows the 2009 national water balance according to the standards set by the International Water Association.

**Figure 8.5 Standard International Water Association water balance: national, 2009**

<table>
<tr><td rowspan="4">System Input Volume<br><br>(Total supply from own + external sources)<br><br>100%</td><td rowspan="2">Authorised Consumption<br>(Billed metered + Billed unmetered + unbilled metered + Unbilled unmetered)<br><br>70.3%</td><td>Billed Authorised<br><br>(Billed metered + Billed Unmetered (flat rate) + Free basic water)<br><br>65.3%</td><td>Revenue Water<br><br>(Volume of water for which an income is received. Assumes all billed water is paid for)<br><br>65.3%</td></tr>
<tr><td>Unbilled Authorised<br><br>5.0%</td><td rowspan="3">Non-revenue Water<br><br>(Volume of water for which no income is received)<br><br>34.7%</td></tr>
<tr><td rowspan="2">Water Losses (Real + Apparent Loss)<br><br>29.7%</td><td>Apparent or Commercial Loss<br><br>5.9%</td></tr>
<tr><td>Real or Physical Loss<br><br>23.8%</td></tr>
</table>

*Source: Department of Water Affairs: Strategic overview of the water sector in South Africa 2010*

## Maintenance of existing infrastructure

*Most municipalities in South Africa have not paid sufficient attention to the maintenance of their existing infrastructure*

There has been under-investment in the maintenance and refurbishment of infrastructure, which is evident in the number of service delivery failures across the country today. In the water sector, water quality is an important indicator of the performance of a water treatment plant. If the quality of water entering a reticulation system is poor, it usually indicates that there are operational problems with the treatment plants, either in the forms of plant breakdowns, poor maintenance or delayed maintenance, and plants operating at above their build capacities. The Blue Drop system implemented by the Department of Water Affairs in 2008 demonstrates clearly the extent of the maintenance challenges in South Africa.

The high volume of technical water losses, due to pipe bursts, leakages, and so on, also results in substantial revenue losses for municipalities – revenue which could have been used for further maintenance.

*Many municipalities, especially the smaller and more rural municipalities, do not manage their assets strategically*

This infrastructure problem is further compounded by the fact that many municipalities, especially the smaller and more rural municipalities, do not manage their assets strategically. They are often unaware of what assets they have, where those assets are located, how old those assets may be and what investments are required to extend the useful life of these assets. Without this information, it is almost impossible to determine the investment needs required. The development of an asset register is also a costly exercise, as many municipalities outsource this function as they do not having the requisite in house capacity. As a result of funding constraints, this exercise is often deferred or completed through a phased approach.

Municipalities generally allocate approximately 5 to 12 per cent of their annual operating budgets for repairs and maintenance. However, these are budgeted figures. Information on the actual repairs and maintenance spend by municipalities per asset class is currently not available.

### Possible reforms to South Africa's water services sector

The problems that the water services sector faces are similar to the problems experienced in the electricity sector. Many smaller municipalities do not have the necessary economies of scale, skills and specialisation to provide a water services function efficiently and effectively. The Department of Water Affairs is currently supporting a number of institutional reform investigations that are aimed at advising water services authorities (municipalities) on the most appropriate institutional options applicable for that service provision area. Three areas in which reform investigations are currently taking place, are Central Eastern Cape, Western Highveld (Mpumalanga) and Southern Free State.

*The department is also exploring the establishment of an independent regulator for water to improve overall efficiency and effectiveness of water provision*

The department is also exploring the establishment of an independent regulator for water to improve overall efficiency and effectiveness of water provision, and to ensure appropriate price setting at each stage of the water cycle.

### Impacts of climate change

*Possible climate change impacts complicate the planning for future water supplies and investment needs*

While it is difficult to quantify and cost the likely impact of climate change on the country's water system, it is acknowledged that these possible climate change impacts complicate the planning for future water supplies and investment needs. The most likely scenario is that climate change will reduce water availability, though these effects will be unevenly distributed across the country. In general, climate change is likely to lead to weather events that are more intense and variable compared to past patterns, for example, sudden high volumes of rainfall leading to flooding, in addition to severe droughts in other areas.

Increased variability in rainfall patterns will result in less reliable stream flows, which will consequently lead to an increase in the unit cost of water from dams. This cost will need to be passed through the water value chain, which will ultimately result in increases in consumer tariffs.

Climate change also presents challenges to water infrastructure. More extreme wetting and drying cycles causes greater soil movement resulting in water and sewerage pipes being more prone to cracking, resulting in a greater need for rehabilitation and replacement of this infrastructure.

### Acid mine drainage

Acid mine drainage refers to the outflow of acidic water from disused mines. In 2010, several warnings issued by environmentalists stated that South Africa could face a potential water pollution crisis leading to health problems as a result of spillage from acid mine drainage. These warnings focused on the Gauteng gold fields, but acid mine drainage has also been reported in the Mpumulanga and KwaZulu-Natal coal fields, and even the O'Kiep copper district in Northern Cape.

*An inter-ministerial task team was appointed in 2010 to determine the risk that acid mine drainage poses to the environment and water quality*

In response to these concerns, an inter-ministerial task team was appointed in 2010 to determine the risk that acid mine drainage poses to the environment and water quality. The task-team's report found that the flooding of mines and the subsequent spillage of acid mine drainage can result in the contamination of shallow groundwater resources required for agricultural and human consumption, cause geotechnical impacts such as the flooding of underground infrastructure in areas where water rises close to urban areas, and lead to increased seismic activity that could have a localised effect on property and infrastructure. It was also found that acid mine drainage does pose a serious risk to the environment, with localised ecological impacts and regional impacts on major river streams.

The task-team's recommendations have been approved by Cabinet, and the 2011 Budget allocates R3.6 billion for water infrastructure and services, part of which is for projects to deal with acid mine drainage.

### Skills shortage

*Whereas in 1994, there were 20 engineers per 100 000 people, this has now dropped to 3 per 100 000 people*

The water sector is currently experiencing a severe shortage of critical skills - qualified engineers, water scientists, technicians and artisans. This poses a risk to the sector's continued capacity to provide water services effectively. Research[2] indicates that the civil engineering capacity (expressed as civil engineering professionals per 100 000 people) in local government is too low to deliver, operate and maintain local government infrastructure in a sustainable manner. Whereas in 1994, there were 20 engineers per 100 000 people, this has now dropped to 3 per 100 000 people, a ratio that is clearly indicative of a crisis.

### Water availability

Issues relating to water availability and the shortage of water have already been noted above. However, it is important to emphasise water is a public good and therefore it is not just the responsibility of national or local government, but the responsibility of the public to ensure that water is appropriately managed and conserved.

### Water quality

People and firms need access to water, but it is essential that the water being made available for different uses meets the quality standards relevant to that use, either human consumption, industrial purposes or for the maintenance of ecosystems.

*The WSSD recognised the importance of adequate and clean water supplies*

Recognising the importance of adequate and clean water supplies throughout the world, participating countries at the World Summit on Sustainable Development (WSSD) held in Johannesburg in 2002, agreed to:

- intensify water pollution prevention to reduce health hazards and protect ecosystems by introducing technologies for affordable sanitation and industrial and domestic wastewater treatment, by mitigating the effects of groundwater contamination and by establishing, at the national level, monitoring systems and effective legal frameworks

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[2] Alison Lawless, (2010) '*Numbers and Needs in Local Government*'

- adopt prevention and protection measures to promote sustainable water use and to address water shortages.

Historically, South Africa's tap water has been of a very high standard, but due to problems in some areas, quality outside the metros is not always assured. The Department of Water Affairs' Blue Drop Report for 2009/10 shows that only 38 water supply systems in 26 municipalities were awarded the highest blue drop status certificate.

*The blue drop scoring system monitors the management of drinking water quality*

Similarly, a green drop certification programme was launched to evaluate the management of waste water systems. This assessment revealed that about 75 per cent of South Africa's sewerage treatment works are not up to standard. Of the 852 waste water treatment plants, just over 400 could not be assessed. Of the remainder, only 203 plants scored more than 50 per cent.

*The green drop certification programme evaluates the management of waste water systems*

In addition to the above systems, the Department of Water Affairs has also developed a wastewater discharge charge system that works on a 'polluter pays' principle. The aim is to recover the costs associated with different wastewater treatment and water quality management programmes and to provide incentives for large water users to treat their waste in-house rather than discharging it untreated into a water resource. The major sources of direct pollution include industrial effluent, domestic and commercial sewerage, acid mine drainage, agricultural runoff and litter. These wastewater charges will be payable by polluters who exceed certain pollution load standards.

## Conclusion

The quality and availability of the water and sanitation services are of extreme importance to the quality of human life and living standards. The most recent information confirms that progress in extending access to these services continue to be made. However, these efforts are being constrained by skills shortages within the sector.

Several reforms and measures are being implemented to improve the efficiency of the water sector as well as measures to improve sanitation and prevent outbreaks of related diseases. A concerted effort is required from all stakeholders in the water sector to address challenges, such as deterioration in the water services infrastructure, which impact on the quality and reliability of service and ultimately the quality of water itself.

# 9

# Electricity

## Introduction

Electricity services in South Africa are at a crossroads. National economic growth has outstripped available generation capacity, while regulatory uncertainty has undermined the effective management of distribution assets at the municipal level. Consumers are now experiencing significant price rises that are necessary to pay for expanding generation capacity, but there are still financial and operational challenges in securing municipal distribution networks.

*National economic growth has outstripped the available capacity for electricity generation*

Electricity is vital to households, businesses and municipalities. For most households, electricity is the principal source of energy, and extending electricity to households that do not already have access offers a cleaner and safer alternative to other current sources of energy. Businesses need electricity to undertake production, communication and a host of other uses. For municipalities that provide electricity to households and businesses, it is also a major source of revenue and can generate surpluses that can be used to fund other municipal functions.

The supply of electricity involves three phases: generation, transmission and distribution. National government is responsible for ensuring the generation of electricity and its transmission across the country. The state-owned electricity company, Eskom, is responsible for over 95 per cent of electricity generation and all transmission in the country. As a sphere of government, municipalities are responsible for the distribution of electricity to consumers. However, not all households and businesses are supplied with electricity by municipalities as Eskom supplies a large number of customers directly. This can have important implications for municipal revenues, as well as municipalities' ability to manage outstanding debtors.

*Municipalities are responsible for the distribution of electricity to consumers*

This chapter gives an overview of:

- the generation and transmission of electricity

- electricity distribution
- financing electricity distribution
- promoting access to electricity.

## Overview of the generation and transmission of electricity

*The distribution function is shared between municipalities and Eskom*

Electricity provision involves three phases: generation, transmission and distribution. Generation is the process by which electricity is produced; transmission is the transportation of electricity that has been generated in power stations via high voltage, long distance power lines to local networks for distribution; and distribution is the actual delivery of electricity to end consumers. Electricity generation and transmission together constitute electricity supply and in South Africa this is largely the function of Eskom (in some cases, municipalities have their own generation capacity, but on a very limited scale). The distribution function is shared between municipalities and Eskom.

*Shortages of electricity were first experienced in early 2008, when the country's growing economy began to make full use of the electricity generation capacity*

Between 1970 and the early 2000s, South Africa enjoyed a long period of plentiful electricity supply at some of the lowest prices in the world. This situation changed dramatically in June 2006 as the country's growing economy began to make full use of the electricity generation capacity that had been built in the 1970s and 1980s. This led to shortages of electricity and load shedding as the country was not able to generate enough electricity to meet demand, while preventing a collapse of the transmission system.

In response to the shortage of supply, a number of measures were put in place, including immediate efforts to reduce the demand for electricity, and plans to expand generation capacity were fast-tracked. The global recession that began in 2008, and saw South Africa's GDP contract by 1.7 per cent in 2009, resulted in reduced demand for electricity, helping to ensure that demand has remained below the available supply and that there has been no load shedding since April 2008. From the supply side, the other critical factor in keeping the lights on during this period has been improved plant reliability achieved by Eskom technicians.

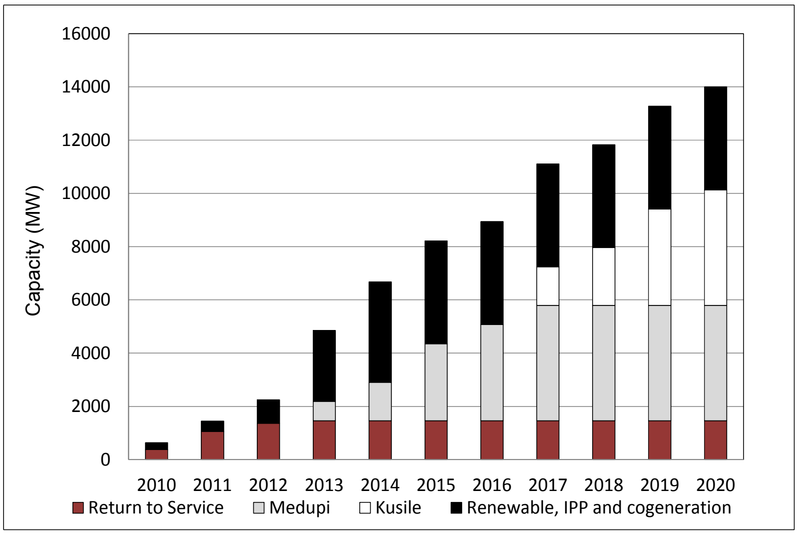
As the South African economy begins to recover (GDP growth is expected to rise to 4.4 per cent by 2013 from the 2.7 per cent estimated for 2010) demand for electricity will also increase, placing strain on the country's ability to generate enough power to meet demand. The ability to avoid load shedding over the coming years will depend on both the success of efforts to limit demand through increased energy efficiency and the timing of the completion of new and refurbished electricity generation capacity, and the pace and nature of economic growth.

### Increasing generation capacity

*Government's integrated resource plan for electricity outlines a strategy for increased generation capacity*

Government's integrated resource plan (IRP) for electricity, approved by Cabinet in March 2011, outlines a strategy for increased generation capacity. This strategy commits government to completing the programme of constructing new generation capacity that is already being implemented and then provides options for further capacity that will allow the country's electricity supply to keep pace with the projected future growth in demand.

**Figure 9.1 Generation capacity to be added in terms of government's current build programme, 2010 to 2020**




*Source: Department of Energy (Integrated Resource Plan for Electricity, 2010)*

The current electricity generation build programme added 640 MW to the electricity supply in 2010 and will add another 1 009 MW in 2011. By 2020, the current build programme will have added a total of 14 000 MW to the country's generation capacity. Although over 70 per cent of this capacity will come from coal-fired power stations, the current build programme will go some way towards diversifying the country's sources of electricity. This is because almost 90 per cent of current generation comes from coal-fired power stations. Of the committed new capacity, 1 020 MW will come from an independent power producer (IPP) (using an open cycle gas turbine) and a total of 1 125 MW will be added by projects using wind, solar, water and landfills as sources of energy. The additional generation capacity already committed to, when combined with the impact of demand side management (DSM) measures, will ensure that, from 2013 to 2018, the country will be able to meet the demand for electricity (as well as provide for 15 per cent reserve margin) under all current demand forecasts.

*Over 70 per cent of committed capacity will come from coal-fired power stations*

Generation capacity may be less than peak demand for electricity again in 2011 and 2012, and depending on the pace of growth in consumption could fall below demand again after 2018. The IRP therefore proposes an ambitious set of options for building additional generation capacity up to 2030 that include: an additional 8 400 MW from wind, 8 400 MW from photo-voltaic solar generation, 1 000 MW from concentrating solar power, 2 609 MW from imported hydro sources, 6 250 MW from coal, 3 910 MW from open cycle gas turbines, 2 370 MW from closed cycle gas turbines and up to 9 600 MW from nuclear energy. After 2018 it is envisaged that renewable energy sources will contribute 47.9 per cent of the new build options, fossil fuels make up 29.5 per cent and nuclear energy accounts for 22.6 per cent. This represents a significant shift away from coal-based technology in the country's electricity generation capacity, an effect that will be reinforced by the decommissioning of several coal-based power stations that will come to the end of their expected lifespans over the next two decades.

*Renewable energy sources make up 47.9 per cent of the new build options*

*Eskom and government agree that the IPPs must play a greater role in electricity generation in South Africa*

Government has decided that the IPPs will play a greater role in electricity generation in South Africa in the period ahead. As noted, an IPP is expected to contribute 1 020 MW of generation capacity by 2013. The Department of Energy is also considering several legislative and policy changes to enable IPPs to sell electricity to the national grid.

Over the next few years (particularly in 2011 and 2012), the lack of an adequate reserve margin between demand for electricity and generation capacity will mean that the country's electricity supply will be at increased risk of interruption. The declining quality of coal delivered to power stations, the reduced time available for scheduled maintenance due to the low reserve margins and the fact that many aging plants are in need of refurbishment will heighten these risks.

### Reducing demand for electricity

*Eskom, national government and municipalities will all contribute to demand side management programmes*

Reducing demand for electricity plays a key part in government's strategy to make sure that there is a sufficient supply of electricity to meet demand. Eskom, national government and municipalities (who are responsible for 42.9 per cent of electricity sales) have all made significant commitments to contribute to demand side management programmes.

**Local government's role in responding to climate change**

Globally, average temperatures are rising as a result of the increased emission of greenhouse gasses such as carbon dioxide. These gasses create a "greenhouse" effect by trapping heat in the earth's atmosphere. South Africa's economy is one of the most carbon-intensive in the world, in large part because of its heavy reliance on coal to generate electricity. South Africa is a signatory to the Kyoto Protocol and accepts the need to find a sustainable path for its future development.

Municipalities are on the frontline of the impact of climate change. Municipalities will have to provide the first response to disasters caused by the extreme weather events that are likely to become more frequent as a result of climate change. Municipalities will also need to invest in infrastructure that can withstand these extreme weather conditions, particularly flooding.

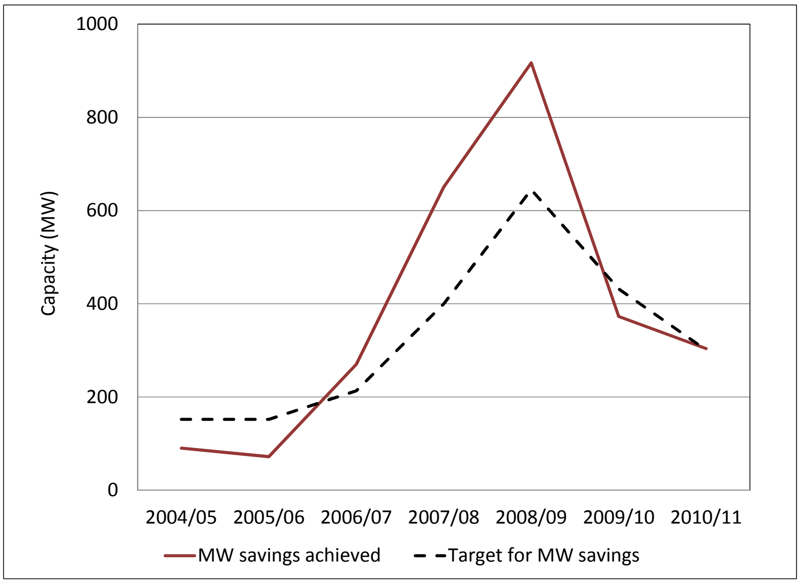
The electricity and transport sectors are two of the largest sources of carbon dioxide emissions in the country and municipalities have substantial influence over the size and shape of both these sectors. South African municipalities have been proactive in responding to these challenges, with the South African Local Government Association (SALGA) and several larger municipalities participating in the African Local Government Climate Roadmap summit in Tshwane in July 2009. The summit's declaration emphasised the key role municipalities can play in mitigating the causes and impacts of climate change, particularly through their role in spatial planning. Several cities are already exploring innovative interventions, including installing solar water heaters to reduce demand for electricity. Cape Town metro intends to buy electricity from renewable sources such as the Darling Wind Farm just north of the city, and eThekwini is producing electricity from landfill gas. These efforts in the electricity sector will be complemented by the rollout of improved public transport that should help to encourage residents to reduce their use of private vehicles – resulting in reduced emissions and improved air quality in urban areas.

*The new South African Energy Development Institute will research and promote energy efficient technologies*

National government committed R978 million to electricity demand side management grants to both Eskom and municipalities over the three years from 2009/10 to 2011/12. This funding has been used to install energy efficient lighting and subsidise solar water heating systems. National government has allocated R66.5 million over the 2010/11 MTEF to establish the South African Energy Development Institute that will research and promote energy efficient technologies. The National Energy Regulator of South Africa's (NERSA) three-year price determination for electricity generation from 2010/11 to 2012/13 also provides Eskom with a margin within its generation tariff to fund demand side management measures, amounting to R5.4 billion over the three years.

The Department of Energy's integrated resource plan for electricity summarises the capacity savings Eskom expects to achieve between 2010 and 2020 through a range of demand side management programmes, including energy efficient lighting, heat pumps, solar water heating, efficient shower heads and process optimisation. These projects were expected to have saved 252 MW in 2010 (actual amount saved was 304 MW), rising to expected savings of 1 310 MW in 2013 and 3 420 MW per year by 2017 – roughly the same capacity as the massive Matla coal-fired power station in Mpumalanga. The plan suggests that in future, costed energy-saving measures should compete with supply-side options when deciding the most desirable way to ensure that the demand and supply of electricity match each other.

**Figure 9.2 Targeted and achieved MW savings per year from Eskom's demand side management programme**




*Source: Eskom, 2010*

Eskom's 2010 annual report estimates that demand side management could reduce the need for electricity generation capacity by between 8 per cent and 15 per cent over the next decade. Since the start of Eskom's demand side management programme in 2003, 2 767 MW have been saved, 304 MW of which were saved in 2010/11. Figure 9.2 shows that after achieving impressive savings through demand side management in 2007/08 and 2008/09, when load shedding was actually taking place, the level of savings has declined. This was not unexpected as initial savings are always more easily implemented.

*Demand side management could reduce the need for electricity generation capacity by between 8 per cent and 15 per cent over the next decade*

## Electricity distribution

In South Africa, the responsibility for distributing electricity to end-users is shared between Eskom and municipalities. This creates a complex situation in some municipalities, where different areas are served by different service providers, with different tariff structures for consumers and revenues going to different institutions.

*The sharing of the responsibility for distributing electricity to end-users between Eskom and some municipalities creates numerous problems*

This creates numerous problems for municipalities, including reducing the value of municipal balance sheets, their ability to raise revenue and manage outstanding debtors. It also creates confusion among consumers about whom they should hold accountable for the delivery of electricity services.

### Attempts to regionalise distribution

Over the last decade, attempts to resolve this situation have centred on efforts to regionalise the distribution of electricity. Government's initial plan was to establish six regional electricity distributors (REDs) that would take over the assets and functions of both Eskom and municipal distributors.

*In December 2010, Cabinet announced that the process of establishing the REDS would be discontinued*

In December 2010, government decided that the process of establishing the REDs would be discontinued and that Electricity Distribution Industry Holdings, the company set up to establish the REDs, would have an administrator appointed to wind down its operations. The Department of Energy will now undertake a review of the whole electricity value chain and develop a holistic approach to revitalising infrastructure in the sector as several of the challenges that the REDs were intended to respond to, including poor infrastructure maintenance and weak capacity in some municipal distributors still need special attention.

*The uncertainty created by the proposed restructuring of the sector has resulted in serious underinvestment in the maintenance and refurbishment of distribution infrastructure*

The uncertainty created by the proposed restructuring of the sector meant that many municipal distributors neglected the maintenance and investment needed on their own infrastructure in the expectation that these assets would be transferred to another entity. This has resulted in serious underinvestment in the maintenance and refurbishment of distribution infrastructure, raising the risk of power outages caused by faults in aging infrastructure. The situation has been compounded by the effects of the electricity supply crisis, where unplanned supply interruptions placed distribution infrastructure under additional pressure and often accelerated the emergence of distribution faults. In 2008, the Department of Energy estimated that R27.4 billion would be needed to upgrade electricity distribution infrastructure.

### Eskom and municipalities as distributors

*In 2009, 56 local municipalities did not provide electricity to any of their residents and relied solely on Eskom to provide the distribution function in their area*

Schedule 4 of the Constitution makes electricity reticulation a municipal responsibility. However, in practice, Eskom and municipalities both distribute electricity to consumers. No district municipality is authorised to distribute electricity. According to Statistics South Africa's Non-financial Census of Municipalities for 2009, 56 local municipalities did not provide any electricity to their residents and relied solely on Eskom to provide the distribution function in their area. Of these municipalities, 43 are large rural municipalities with relatively dense rural populations and only small core towns, like Engcobo in Eastern Cape; another 11 are rural municipalities in low density rural areas and small towns, like Kopanong in Free State; and the remaining two municipalities have large towns like Mafikeng in North West. This confirms that it is typically the most rural municipalities with the least alternative sources of own revenue that do not supply electricity to their residents and therefore cannot use this as a source of revenue. In a number of municipalities, some areas are supplied by Eskom while others are supplied by the municipality.

**Table 9.1 Electricity sales by category for Eskom and municipalities, 2006**

| Category | Average sales price (c/kWh) | Eskom No. of customers | Eskom GWh sales | Municipalities and other No. of customers | Municipalities and other GWh sales | Total No. of customers | Total % of total | Total GWh sales | Total % of total |
|---|---|---|---|---|---|---|---|---|---|
| Domestic | 37.49 | 3 829 986 | 9 736 | 4 043 471 | 29 339 | 7 873 457 | 94.4% | 39 075 | 20.3% |
| Agriculture | 33.52 | 82 583 | 4 732 | 21 162 | 1 110 | 103 745 | 1.2% | 5 842 | 3.0% |
| Mining | 16.90 | 1 127 | 32 421 | 16 | 197 | 1 143 | 0.0% | 32 618 | 16.9% |
| Manufacturing | 20.71 | 2 955 | 52 251 | 30 504 | 23 305 | 33 459 | 0.4% | 75 556 | 39.2% |
| Commercial | 33.90 | 45 233 | 7 842 | 225 847 | 20 924 | 271 080 | 3.2% | 28 766 | 14.9% |
| Transport | 21.13 | 510 | 3 069 | 330 | 207 | 840 | 0.0% | 3 276 | 1.7% |
| General | 28.78 | – | – | 60 432 | 7 638 | 60 432 | 0.7% | 7 638 | 4.0% |
| **Total** | **25.60** | **3 962 394** | **110 051** | **4 381 762** | **82 720** | **8 344 156** | **100.0%** | **192 771** | **100.0%** |

*Source: National Electricity Regulator of South Africa, Electricity supply statistics for South Africa, 2006*

Table 9.1 shows that in 2006, while domestic users made up 94 per cent of customers using electricity, they accounted for only 20 per cent of electricity consumption. However, because of the large number of individual connections dispersed over a wide area required to service households, the average cost of distribution to households is higher than for commercial users. This is reflected in the higher average sales price for domestic users.

*While domestic users make up 94 per cent of customers using electricity, they account for only 20 per cent of electricity consumption*

Table 9.1 shows that although Eskom has almost as many domestic customers as municipalities, Eskom sells only about a third as many GWh to domestic consumers as municipalities. This is consistent with the fact that Eskom tends to supply electricity to poorer consumers (who use less electricity) while municipalities tend to provide electricity to wealthier households (who consume more electricity). Although there are exceptions to this pattern (the wealthy area of Sandton in Johannesburg is supplied by Eskom, for example), it is easy to understand why this pattern holds. Well-capacitated municipalities with established distribution networks in relatively wealthy areas can use the sale of electricity to generate significant revenue that they use to help fund other municipal activities. In poorer areas of the country, where electricity connections may not have been supplied during the apartheid years, municipalities often do not have the requisite technical capacity or funds to expand their reticulation systems to connect non-electrified households. In rural areas it is particularly expensive to extend distribution systems to widely dispersed households. As a result of these difficulties with infrastructure and technical capacity, as well as the limited scope for municipalities to generate revenue from poor areas, municipalities have been slow in extending electricity services to poor households. Eskom has therefore taken on the role of providing connections in these areas (with the help of government funding), resulting in the current pattern of suppliers for domestic users.

*In rural areas, it is particularly expensive to extend distribution systems to widely dispersed households*

This pattern is reversed in the distribution of electricity to the manufacturing sector (the largest consumer of electricity), with Eskom having a much smaller number of customers consuming a much larger amount of electricity. Eskom also supplies the majority of electricity to the agricultural sector and to industries such as mining and transport, while municipalities are the main distributors to commercial customers such as local businesses. This suggests that municipalities

*Eskom supplies the majority of electricity to the agricultural sector and to industries such as mining and transport* have very limited ability to raise revenue from electricity sold to industries in the primary sectors of the economy (mining and agriculture) that are located within their boundaries.

There are a number of important financial implications for municipalities that do not provide electricity to their residents. As electricity sales account for a high proportion of municipal revenues and can generate significant surpluses (see following section), not providing electricity in some or all areas under their jurisdiction means that municipalities lose a significant source of own revenue. (The Municipal Fiscal Powers and Functions Act does allow municipalities to levy a surcharge on electricity tariffs, even if it is provided by Eskom. However, in the absence of guiding norms and standards no municipalities have done so.)

## Financing electricity distribution

*Electricity is a major source of both revenue and expenditure for municipalities*

Electricity is a major source of both revenue and expenditure for municipalities.

### Revenues from electricity services

Electricity sales are a major source of revenue for municipalities. Table 9.2 shows the amounts of revenue the sale of electricity is expected to generate for different categories of municipalities and table 9.3 shows budgeted electricity operating revenue as a percentage of total budgeted operating revenue.

**Table 9.2 Budgeted electricity operating revenue, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| **R million** | | | | | Medium-term estimates | | |
| **Operating revenue** | | | | | | | |
| Category A (Metros) | 16 811 | 18 759 | 21 978 | 30 931 | 39 440 | 48 662 | 60 516 |
| Category B (Locals) | 9 209 | 9 838 | 11 412 | 16 322 | 19 520 | 20 244 | 23 647 |
| *Secondary cities* | 5 321 | 5 511 | 6 447 | 9 449 | 11 893 | 12 819 | 15 446 |
| *Large towns* | 1 679 | 1 857 | 2 140 | 2 940 | 3 715 | 3 652 | 4 000 |
| *Small towns* | 1 864 | 2 058 | 2 387 | 3 294 | 3 384 | 3 266 | 3 626 |
| *Mostly rural* | 345 | 412 | 438 | 639 | 528 | 506 | 574 |
| Category C (Districts) | 8 | 14 | 17 | 14 | 18 | 10 | 10 |
| **Total** | **26 028** | **28 611** | **33 408** | **47 267** | **58 978** | **68 916** | **84 172** |

*Source: National Treasury local government database*

*There is great potential for municipalities to generate revenue from electricity distribution*

Revenue from the sale of electricity accounted for over a quarter of total revenue for municipalities before the rapid tariff increases that began in 2009/10. When only municipalities that sell electricity are considered the proportion of operating revenue coming from electricity rises to around 40 per cent by 2012/13. Given that even in these municipalities there are large areas that are supplied directly by Eskom, the potential for municipalities to generate revenue from electricity is even greater.

**Table 9.3 Budgeted electricity operating revenue as a percentage of total budgeted operating revenue, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | | | | Medium-term estimates | | |
| **Operating revenue** | | | | | | | |
| Category A (Metros) | 26.2% | 26.4% | 27.6% | 33.7% | 32.6% | 35.1% | 38.6% |
| Category B (Locals) | 26.0% | 24.6% | 23.8% | 27.6% | 28.1% | 29.8% | 31.7% |
| *Secondary cities* | 31.5% | 28.6% | 27.7% | 34.1% | 36.9% | 39.3% | 41.9% |
| *Large towns* | 26.2% | 25.1% | 24.5% | 26.4% | 27.4% | 29.5% | 30.6% |
| *Small towns* | 23.5% | 24.7% | 22.9% | 25.2% | 23.7% | 23.8% | 24.6% |
| *Mostly rural* | 8.2% | 8.1% | 8.0% | 8.8% | 5.6% | 5.5% | 5.8% |
| Category C (Districts) | 0.1% | 0.2% | 0.2% | 0.1% | 0.1% | 0.1% | 0.1% |
| **Total Operating revenue** | **24.3%** | **24.2%** | **24.6%** | **29.1%** | **28.8%** | **31.3%** | **34.1%** |

*Source: National Treasury local government database*

A simple comparison of operating revenue in table 9.3 and operating expenditure in table 9.4 shows that there is substantial scope for municipalities to generate surpluses from their electricity operations. These surpluses can then be used to fund other municipal functions. However, it is important not to simply take the full difference between budgeted revenue and expenditure as the surplus, as this does not take account of the need to recover funds for capital investment in the supply of electricity or the impact of non-payment on the cash flow of a municipality. The allowance that needs to be made for these factors will differ from municipality to municipality and so no general figure can be given here.

## Electricity tariffs

*South Africa is currently facing steep annual increases in the tariffs for electricity in order to fund Eskom's massive build programme*

South Africa is currently facing steep annual increases in the tariffs for electricity as a result of the need to fund the massive build programme that Eskom has undertaken in order to increase its generation capacity. Electricity tariffs are regulated by NERSA. It sets the tariffs that Eskom can charge for generating electricity and that municipalities and Eskom can charge for distribution.

### *Bulk supply tariffs*

*Electricity generation tariffs in 2014/15 will be over three times higher than at the start of 2009/10 in real terms*

In mid-2009, in response to an extraordinary application from Eskom as a result of its need to raise funds required for capital investments to increase generation capacity, NERSA allowed Eskom to implement a 31.3 per cent increase in the average standard tariff for the last nine months of the national financial year 2009/10. This was followed in 2010 by NERSA granting Eskom further price increases of 24.8 per cent for 2010/11, 25.8 per cent for 2011/12 and 25.9 per cent for 2012/13 for the generation and sale of bulk electricity. Eskom has indicated it will request further tariff increases in the region of 25 per cent in 2013 and 2014, before returning to inflation-based tariff increases from 2016 onwards. If NERSA approves the proposed increases for 2013 and 2014, then by 2014, electricity generation tariffs will be roughly four times higher in nominal terms than they were at the start of 2009/10. After adjusting for projected inflation, electricity generation tariffs in 2014/15 will be a little over three times higher than at the start of 2009/10 in real terms.

### *Retail tariffs*

The cost of generating electricity is the largest, but not the only, component of the tariff municipalities charge consumers for the distribution of electricity. Consumers must pay a tariff that includes charges for the generation, transmission and distribution of electricity. NERSA-approved tariffs include provision for the costs of staff and repairs and maintenance for the distribution system, assumptions which are made explicit in the case of tariffs approved for municipal electricity distributors. Because these costs increase by much less than the generation tariff, the net effect is that the percentage increase in the retail price to consumers is somewhat lower than the increase in the generation tariff. While Eskom's generation tariff increases by 25.8 per cent for 2011/12, NERSA's guideline for the increase in municipal tariffs is 20.4 per cent.

*For the first time in 2011/12, NERSA's guidelines for increases in municipal tariffs were published with sufficient time for municipalities to use them in planning their budgets*

For the first time in 2011/12, NERSA's guidelines for increases in municipal tariffs were published with sufficient time for municipalities to use them in planning their budgets and apply to NERSA for approval of their final increases in tariffs. Any application for an increase in excess of NERSA's guideline amount must be strongly motivated. Reasons for above-guideline increases usually approved by NERSA include increases to fund repairs and maintenance, capital projects, critical vacancies, municipalities in financial distress and raising funding for demand side management or other electricity related projects. NERSA publishes the approved tariff increases for each municipality.

In Eskom-supplied areas, the increase in tariffs for consumers is also approved by NERSA. The same tariff structure applies to all Eskom supplied areas, though with different rates for urban and rural areas, which reflect the different costs of distribution in these areas.

*The inclining block tariff system divides consumers into four groups based on the amount of electricity they use*

In 2010, NERSA announced a new system of inclining block tariffs (IBT). The inclining block tariffs divide consumers into four groups or blocks based on the amount of electricity they use. Higher-use blocks pay tariffs that include a surplus which is used to cross-subsidise tariffs in the lower-use blocks. This new tariff structure is intended to be both pro-poor and promote energy efficiency. However, it is encountering a number of teething problems in its implementation, particularly in municipalities that do not have sufficient customers in the higher-use blocks to pay for the cross-subsidisation of the lower-use blocks. The low-use customers targeted for cross-subsidies in this policy do not always correlate with the poor households that most need relief from the rising cost of electricity, particularly where several poor households use one connection or wealthy households own a holiday home (which they seldom use). The inclining block tariffs also obscure the actual costs of service provision to any one consumer block. Over time, this can result in service providers capturing the intended subsidy to consumers through raising prices for all groups. However, the strengths of the system are that it is easily understandable and simpler to implement than an indigence-based system and it also promotes the reduced consumption of electricity.

### *Electricity and credit control*

*Electricity is the only basic service that municipalities can cut off to penalise non-paying households*

While providing electricity reticulation services places significant technical and administrative burdens on a municipality, it also gives them a lever they can use to ensure that consumers pay monies owing to the municipality. It is neither legal nor practical for municipalities to penalise households for non-payment by cutting off other basic services: water is essential for life and municipalities cannot legally cut off residents (though they can restrict flow); not removing refuse poses a public health risk and penalises neighbours as much as it does the non-paying household; and it is not technically feasible to disconnect households from sanitation services. This means that electricity is the only basic service that municipalities can cut off to penalise non-paying households and motivate them to pay their arrears owed to the municipality. At present, Eskom may not cut off supplies to customers that fail to pay municipalities for their other services. Consequently municipalities that do not supply electricity to households directly have reduced leverage in ensuring that those households pay for the other basic services the municipality does provide to them. This exposes municipalities to much higher risks of not recovering revenues owed to them.

It should also be noted that even if municipalities move to pre-paid electricity meters, they can still structure their policies to allow some of the customers' payments to settle other municipal accounts, and to allow the electricity to be cut to enforce payment of other municipal accounts

*The amount a municipality is able to borrow to finance the rollout of infrastructure is determined mainly by the size of its balance sheet and expected future revenues*

The amount a municipality is able to borrow in order to finance the rollout of infrastructure is in large part determined by the size of its balance sheet and expected future revenues. Not selling electricity to some or all of its residents reduces the amount of revenue it is able to collect now and in future, and consequently will also reduce the amount it is able to borrow.

## Electricity expenditures

Table 9.4 show that municipal operating expenditure on electricity has grown dramatically as a result of the increase in tariffs to fund the construction of new generation capacity.

**Table 9.4 Electricity operating expenditure by category of municipality, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | | | | Medium-term estimates | | |
| **Operating expenditure** | | | | | | | |
| Category A (Metros) | 9 746 | 10 884 | 13 040 | 19 934 | 25 546 | 32 547 | 41 556 |
| Category B (Locals) | 5 406 | 5 855 | 7 113 | 10 869 | 13 238 | 14 403 | 17 450 |
| *Secondary cities* | 3 154 | 3 426 | 4 109 | 6 376 | 8 087 | 9 035 | 11 362 |
| *Large towns* | 958 | 1 015 | 1 236 | 1 952 | 2 451 | 2 621 | 3 000 |
| *Small towns* | 1 092 | 1 180 | 1 494 | 2 130 | 2 343 | 2 342 | 2 682 |
| *Mostly rural* | 201 | 235 | 275 | 412 | 358 | 405 | 407 |
| Category C (Districts) | 20 | 29 | 46 | 27 | 10 | 10 | 12 |
| **Total** | **15 172** | **16 769** | **20 199** | **30 831** | **38 794** | **46 960** | **59 018** |

*Source: National Treasury local government database*

The table shows that in 2007/08, budgeted expenditure on electricity for all municipalities increased by 11 per cent, followed by a 20 per cent increase in 2008/09. In 2009/10, municipalities' expenditure on electricity shot up by 53 per cent. This followed the normal increase and then the additional tariff increase granted to Eskom by NERSA in response to the need to rapidly commit to building additional generation capacity in the wake of the rolling load shedding at the beginning of 2008. Over the 2010/11 MTEF, expenditure is expected to rise by 26 per cent, 21 per cent and 26 per cent respectively – roughly in line with the tariff adjustments approved by NERSA for the period. Payments to Eskom for the supply of bulk electricity are not the only component of municipal operational spending on electricity, which also includes staff costs and repairs and maintenance. In approving municipal tariffs, NERSA assumes that bulk purchases make up 70 per cent of the cost of municipal electricity services. This explains how it is possible for the average budgeted increase for 2011/12 to be lower than the tariff increase for Eskom approved by NERSA. It also means that the higher increases in 2010/11 and 2012/13 hopefully include increased spending on much needed repairs and maintenance.

## Efficiency and electricity losses

*Very few cities in South Africa achieves the international benchmark for electricity losses in distribution systems*

There is substantial scope for both reducing the amount of electricity demand and increasing revenue by reducing losses in the distribution of electricity. Some losses in the system are inevitable as a certain amount of power is consumed during the transmission and distribution of electricity along long cables. Internationally, the acceptable margin of electricity losses in distribution systems is 3.5 per cent. As table 9.5 shows, very few cities in South Africa achieves this benchmark.

**Table 9.5 Electricity distribution losses, 2005/06 - 2009/10**

| | 2005/06 | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 |
|---|---|---|---|---|---|---|---|
| **Metros** | | | | | | | |
| Nelson Mandela | 6.5% | 6.0% | 6.7% | 7.5% | 7.5% | 7.5% | 7.5% |
| Ekurhuleni | | 1.0% | 3.0% | 7.0% | 7.0% | 7.0% | 7.0% |
| City of Johannesburg | | 12.0% | 12.0% | 12.0% | 12.0% | 12.0% | 11.0% |
| City of Tshwane | 7.7% | 10.0% | 12.1% | 12.0% | 10.0% | 10.0% | 10.0% |
| eThekwini | 5.1% | 5.1% | 5.0% | 5.0% | 5.1% | 5.0% | 5.0% |
| City of Cape Town | 8.9% | 8.3% | 8.4% | 9.3% | 9.3% | 9.3% | 9.3% |
| **Secondary cities** | | | | | | | |
| Buffalo City | 10.7% | 11.9% | 14.0% | 7.5% | 8.0% | 8.0% | 8.0% |
| Mangaung | 8.3% | 9.4% | 9.1% | 15.0% | 16.0% | 16.0% | |
| Matjhabeng | | | | | | | |
| Emfuleni | | | | | | | |
| Mogale City | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | |
| Msunduzi | | 9.5% | 9.1% | 8.9% | 9.5% | 9.5% | 9.5% |
| Newcastle | | | | | | | |
| uMhlathuze | 7.0% | 4.0% | 6.0% | 4.0% | 5.0% | 5.0% | |
| Govan Mbeki | 5.6% | 10.6% | 12.7% | 12.0% | 16.0% | 16.0% | 16.0% |
| Emalahleni | 22.7% | 21.7% | 33.4% | 28.0% | 30.0% | 30.0% | |
| Steve Tshwete | 8.8% | 10.5% | 7.3% | 10.0% | 10.0% | 10.0% | 10.0% |
| Mbombela | | | | | | | |
| Sol Plaatje | 18.0% | 18.0% | 18.0% | 15.0% | 16.0% | 16.0% | |
| Polokwane | 12.6% | 12.2% | 8.1% | | | | |
| Madibeng | | | | | | | |
| Rustenburg | 22.1% | 18.3% | 20.8% | 16.3% | | | |
| Tlokwe | 10.1% | 2.4% | 0.7% | 2.0% | 2.0% | 2.0% | |
| City of Matlosana | | | | | | | |
| Drakenstein | 5.0% | 7.0% | 7.0% | 7.5% | 7.0% | 7.0% | 7.0% |
| Stellenbosch | | | | | | | |
| George | 12.3% | 3.7% | 5.5% | 7.0% | 9.0% | 9.0% | 9.0% |

*Source: National Treasury local government database*

Among the metros, eThekwini has the least losses, at around 5 per cent, while Johannesburg loses 12 per cent of the electricity it purchases, either through technical losses (perhaps indicating the need for urgent refurbishment of aging infrastructure) or through theft. Among secondary cities, losses can be as high as a third of bulk electricity purchased and it is common for municipal distributors to lose in excess of 10 per cent of electricity purchased. These losses represent the loss of a significant amount of revenue, which needs to be recovered from other users, thus unfairly raising the cost of electricity to them.

*Among secondary cities, losses can be as high as a third of bulk electricity purchased*

It is not only municipalities that experience the problem of losses in electricity. It was estimated that in 2008/09 alone, Eskom lost more than R2.5 billion worth of electricity to illegal connections or technical losses in distribution. Reducing technical losses would mitigate the need to add generation capacity to the system, while reducing electricity theft would raise revenues. Both measures could help to lower prices for all consumers. While law enforcement agencies should play a greater role in reducing electricity theft, municipalities and Eskom can achieve far greater efficiency by reducing the technical losses on their distribution systems.

*In 2008/09 alone, Eskom lost more than R2.5 billion worth of electricity to illegal connections or technical losses in distribution*

## Investment and maintenance

In 2008, the Department of Energy estimated a backlog of R27.4 billion in maintenance, refurbishment and short-term strengthening in the electricity distribution industry. This figure is inclusive of both Eskom and municipal backlogs. Both municipalities and Eskom should be increasing the portion of their operating budgets dedicated to the maintenance of electrical distribution infrastructure and their capital budgets for refurbishment.

### *Capital expenditure*

Table 9.6 reflects budgeted capital expenditure on electricity by municipalities. The table shows that capital expenditure grew strongly in 2007/08 and 2008/09, at an average annual rate of 24 per cent.

**Table 9.6 Budgeted capital expenditure on the electricity function, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | | | | Medium-term estimates | | |
| **Operating revenue** | | | | | | | |
| Category A (Metros) | 2 311 | 2 793 | 3 342 | 3 392 | 3 705 | 3 734 | 3 696 |
| Category B (Locals) | 780 | 1 037 | 1 406 | 1 390 | 1 975 | 1 333 | 1 167 |
| *Secondary cities* | 382 | 551 | 874 | 737 | 854 | 474 | 426 |
| *Large towns* | 158 | 243 | 218 | 323 | 405 | 376 | 234 |
| *Small towns* | 149 | 193 | 215 | 288 | 399 | 249 | 225 |
| *Mostly rural* | 91 | 50 | 98 | 43 | 318 | 234 | 282 |
| Category C (Districts) | 1 | 2 | 0 | 2 | 43 | 40 | 35 |
| **Total** | **3 093** | **3 833** | **4 748** | **4 784** | **5 724** | **5 107** | **4 898** |

*Source: National Treasury local government database*

Capital spending, for expanding and upgrading infrastructure, remained flat in 2009/10 but was expected to grow by 20 per cent again in 2010/11. Of great concern, is that on average, municipalities are budgeting to decrease their capital spending by 11 per cent in 2011/12 and a further 4 per cent in 2012/13. Over R1 billion is allocated to municipalities for capital investment in expanding access for poor households through the integrated national electrification programme grant. If this grant, which grows with inflation over the

MTEF period, is subtracted from the budgeted capital expenditure, then capital investment budgeted by municipalities declines by 14 per cent in 2011/12 and 7 per cent in 2012/13.

*If municipalities recognise the importance of investing in electricity, this decrease could still be corrected*

Given the growth in population and the increasing number of households, especially in urban areas, along with the high levels of historical backlogs and the need for upgrading or replacing aging infrastructure, one would expect municipal budgets for capital expenditure on electricity to increase over the medium term, and not decrease. If municipalities recognise the importance of investing in electricity, this decrease could still be corrected in future budgets.

### *Repairs and maintenance*

*It is now clear that municipalities are responsible for electricity infrastructure and so they should now plan to ensure that it is properly maintained*

Aging distribution infrastructure in municipalities requires significant investment in repairs and maintenance if supply disruptions are to be minimised. The uncertainty in the distribution industry during the debate over the REDs led to many municipalities delaying necessary maintenance work. It is now clear that the responsibility for this infrastructure lies with municipalities and they should now plan accordingly and step up efforts to ensure that their infrastructure is properly maintained. Funding this increased investment in the repair, maintenance and upgrading of municipal electricity distribution infrastructure will require municipalities to either increase tariffs to consumers or find the funds from elsewhere in their budgets.

It is difficult to get a clear picture of municipal expenditure on repairs and maintenance for electricity infrastructure due to the previous budgeting reporting formats, which combined repairs and maintenance expenditure for all services (including roads, water and sanitation and solid waste). While there are indications that spending on maintenance increased from 2006/07 to 2009/10, given the uncertainty on the future ownership of electricity infrastructure created by the REDs policy, it is unlikely that electricity was the main beneficiary of this increase.

*If municipalities continue to not invest in the maintenance and upgrading of their electrical infrastructure there will be breaks in supply*

As has been demonstrated earlier in this chapter, electricity distribution can be a very good business for municipalities. It has the potential to generate significant surpluses. The revenues it generates can be used to leverage debt finance. And it provides a powerful lever in managing debtors and collecting revenue owed for other services. However, municipalities cannot take advantage of any of these if they are unable to maintain the supply of electricity to consumers. If municipalities continue to not invest in the maintenance and upgrading of their electrical infrastructure there will be breaks in supply. In addition to being expensive to repair, these interruptions in supply will cause a loss of revenue in the short-term and a breach in the contract between municipalities and their paying consumers that could cause long-term damage to the reputation and trust between the municipality and its residents and customers. It is therefore in the interests of municipalities that distribute electricity to ensure that they budget to reinvest a sufficient portion of the surpluses from the sale of electricity in the maintenance, upgrading and expansion of their electricity supply infrastructure before using the remaining surpluses for other purposes. Failure to do so would be akin to killing the goose that lays the golden egg.

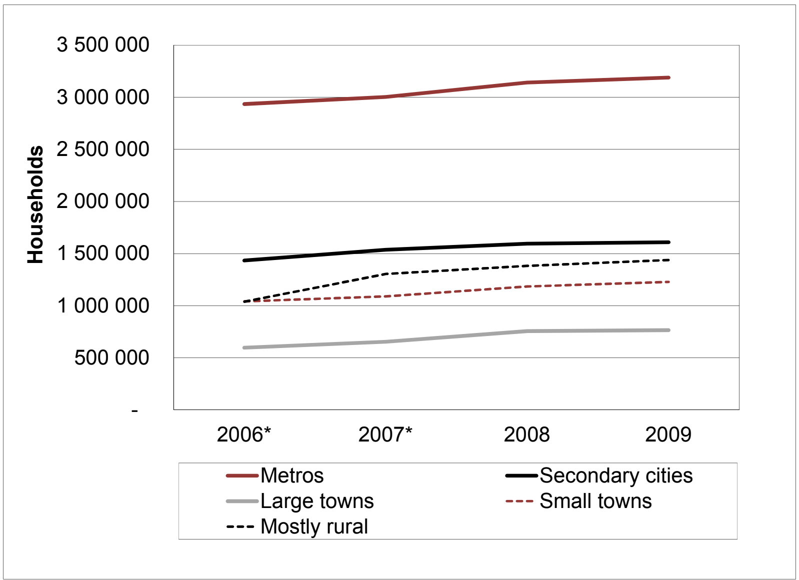
## Promoting household access to electricity

Access to electricity is determined by two factors: the number of households connected to electricity, either through the national grid or alternative sources such as solar panels; and the affordability of that electricity - poor households need to be able to afford electricity in order to benefit from its use.

### Connecting households to electricity

Progress is being made in increasing the number of households with access to electricity.

**Figure 9.3 Number of households with access to electricity, 2006-2009**




*Source: Stats SA, Non-financial census of municipalities*

*Between 2006 and 2009, the total number of connections increased by 1.3 million, from 7.1 million to 8.4 million*

As figure 9.3 shows, between 2006 and 2009, all types of municipalities increased the number of consumers supplied with electricity. Over this period, the total number of connections increased by 1.3 million, from 7.1 million to 8.4 million. While not all of these new connections are households, it is likely that the vast majority are, given that 92 per cent of all consumers are domestic users.

*National government funds the rollout of energy distribution infrastructure through the INEP grants*

National government funds the rollout of energy distribution infrastructure through the integrated national electrification programme (INEP) grants. R9.1 billion has been allocated to these grants over the current MTEF period, with 38.2 per cent of this allocated directly to municipalities and the rest allocated to Eskom. The high level of funding allocated to Eskom recognises the high levels of backlogs in Eskom-serviced areas.

Past performance on this grant shows that 60 726 households were connected to the grid in 2009/10, significantly less than the 123 362 households connected in 2008/09. This decline in the number of new connections was the result of more households being connected in rural areas. Due to their distance from the existing grid, it takes much longer and is more expensive to connect these households.

*INEP allocations are intended to fund the capital costs of providing electrical connections to poor households and providing the bulk infrastructure needed to ensure a stable supply of electricity*

INEP allocations are intended to fund the capital costs of providing electrical connections to poor households and providing the bulk infrastructure needed to ensure a stable supply of electricity. Municipalities should not rely on INEP funds to provide electricity to new commercial developments or wealthy suburbs. Extending electrical infrastructure to these areas should be funded through development charges or debt financed against the future income from rates and levies that these consumers will pay to the municipality.

It is not practical or cost-effective to connect all households to the national grid. In remote areas it can be cheaper to provide households with alternative sources of energy, such as through solar panels. In these areas INEP funds are used to connect households and schools to alternative sources of energy.

### Free basic electricity

*The Department of Energy's free basic electricity policy is that every indigent household should receive 50kWh of free electricity per month*

The free basic electricity policy was announced in 2003 by government and has been funded through the equitable share to municipalities since 2004/05. In terms of this policy every indigent household should receive 50kWh of free electricity per month. In 2011/12, the equitable share includes R9.5 billion in funding towards the provision of free basic electricity

As this is a national policy that applies to a municipal service and is funded through an unconditional allocation, national government does not prescribe how municipalities implement the free 50kWh. Municipalities have therefore had to make their own decisions on how to implement it, with some providing it to all households and some only to households that fall below a poverty line or indigence measure determined by that municipality. Over the last few years, several municipalities have changed their policies from providing free basic electricity to all households to targeting poor households only. This is the most likely explanation for the decline in the number of consumer units receiving free basic electricity reported in Statistics South Africa's annual Non-financial Census of Municipalities (from a peak of 3 351 388 in 2006 to 2 781 043 in 2008). In 2009, the number of consumer units increased to 2 952 682, presumably reflecting an increase in the number of poor households accessing free basic electricity.

*More than 4.3 million households received free basic electricity in 2009*

Statistics South Africa collects data on the level of access to free basic electricity through its annual Non-financial Census of Municipalities. Table 9.7 provides the figures for consumer units receiving basic electricity services from both Eskom and municipalities, and the figures for consumers receiving free basic services from municipalities. An additional 1.3 million consumer units received free basic electricity in Eskom-supplied areas. Note that the figures from both the non-financial census and Eskom are based on consumer units and not households, and are therefore not comparable with household data collected in the census and community survey. Eskom and municipalities have no way of estimating how many households are serviced by a connection, so the number of households receiving free basic electricity could be larger than the 4.3 million consumer units recorded by Eskom and municipalities in 2009. In addition, in areas where it is not possible to provide connections to the grid, residents should be provided with free basic alternative energy. Sources of this kind of energy include paraffin, liquefied petroleum gas, coal and bio-ethanol gel. The non-financial census recorded 107 105 households benefiting from free basic alternative energy.

**Table 9.7 Consumer units receiving free basic electricity services from municipalities, 2008 and 2009**

| Province | 2008 | | | 2009 | | |
|---|---|---|---|---|---|---|
| | Number of consumer units receiving basic electricity services | Free basic electricity services | | Number of consumer units receiving basic electricity | Free basic electricity services | |
| | | Number of consumer units | % | | Number of consumer units | % |
| Eastern Cape | 811 953 | 282 175 | 34.8% | 872 170 | 312 975 | 35.9% |
| Free State | 576 790 | 345 545 | 59.9% | 602 434 | 379 981 | 63.1% |
| Gauteng | 1 802 607 | 706 822 | 39.2% | 1 829 044 | 724 178 | 39.6% |
| KwaZulu-Natal | 1 283 813 | 165 505 | 12.9% | 1 327 485 | 192 265 | 14.5% |
| Limpopo | 1 072 824 | 271 992 | 25.4% | 1 157 388 | 319 559 | 27.6% |
| Mpumalanga | 559 499 | 220 106 | 39.3% | 591 867 | 234 183 | 39.6% |
| Northern Cape | 227 033 | 100 021 | 44.1% | 243 075 | 107 788 | 44.3% |
| North West | 579 004 | 119 919 | 20.7% | 588 298 | 129 443 | 22.0% |
| Western Cape | 1 173 637 | 568 958 | 48.5% | 1 209 566 | 552 314 | 45.7% |
| **Total** | **8 087 160** | **2 781 043** | **34.4%** | **8 421 327** | **2 952 686** | **35.1%** |

*Source: Stats SA, Non-financial census of municipalities for the year ended 30 June 2009*

At the guideline municipal tariff set by NERSA for the lowest-usage block in the tariff structure (63 cents per kWh for 2011/12) it will cost a municipality R31.50 to provide 50 kWh to a poor household for a month. The tariff in the lowest usage block is cross subsidised and so may not offer a fair reflection of the cost of providing electricity, but even at the highest guideline tariff for domestic users in the NERSA guidelines (114 cents per kWh for 2011/12) it will cost only R57.00 per month to provide 50 kWh to a household. These amounts are well within the average R188.04 per poor household per month provided through the equitable share to enable municipalities to provide free basic electricity to poor households connected to the grid. The equitable share also includes funding for water, sanitation, refuse removal and institutional costs.

*In Eskom-supplied areas, municipalities are expected to pay Eskom for any free services provided to their residents*

In Eskom-supplied areas, municipalities are expected to pay Eskom for any free services provided to their residents. In its annual report for 2009/10, Eskom records invoicing an amount of R308 million to the 243 municipalities it has contracts with to provide free basic electricity to 1.3 million consumer units. This amounts to an average cost of R235 per consumer unit per year. This is a great deal less than the average subsidy to municipalities through the equitable share of R2 256 per year for poor households connected to electricity services. Eskom's charge to municipalities for providing free basic electricity to households in its areas is based on a standard tariff for free basic services. There is an under-recovery between this tariff and the consumer tariff that would otherwise have been charged for the electricity. Between 2006 and 2010, the cumulative value of this under-recovery was R165 million. Even taking this under-recovery into account, the low cost of Eskom supplying free basic electricity in its areas of supply relative to the funding made available for free basic electricity to municipalities through the equitable share, demonstrates that the free basic electricity policy is amply funded.

*Many poor households still cannot afford to use electricity as their primary source of energy*

Many poor households still cannot afford to use electricity as their primary source of energy and opt to use their free basic electricity allocation for lighting while continuing to use more dangerous and environmentally damaging materials such as wood, coal or paraffin as their primary energy source for more energy-intensive activities such as cooking and heating. This situation will be worsened by increases in the cost of electricity, though the system of inclining block tariffs will help to mitigate this impact for low-usage households.

## Conclusion

Significant annual tariff increases are set to be a feature of the electricity industry for a few more years. Increases already approved by NERSA are needed to fund the building of the increased generation capacity required to meet the demand for electricity from a growing economy. The poor condition of distribution infrastructure (in part as a result of past uncertainty over the future ownership of this infrastructure) means that there is a great need for increased investment in maintenance and refurbishment. Funding this investment may require additional increases in tariffs. While higher tariffs will place an unwelcome burden on households and increase the costs of business, one positive effect is that they will incentivise consumers to use less electricity, thereby reducing the need for additional generation capacity and the environmental damage associated with high levels of electricity use.

For poor households these increases are cushioned by the free basic electricity policy, as well as the implementation of inclining block tariffs that will see the tariffs for low-use households increase at a lower rate, roughly in line with inflation.

After the disbanding of the REDs policy, municipalities are assured that electricity distribution will remain their responsibility. Electricity distribution is a service that can provide many benefits to municipalities, including increased revenue, greater ability to borrow funds and leverage to improve the collection of other monies owed to the municipality. However, these benefits can only be realised if municipalities provide an efficient and reliable service - that will require much greater investment in infrastructure.

The sale of electricity is a major source of revenue for municipalities, but also a technically difficult operation, requiring skills and investment that not all municipalities have the capacity to manage. Municipalities will have to carefully manage their relationship with Eskom in areas where Eskom distributes electricity. Municipalities must ensure that they have supply contracts with Eskom for these areas and, together with NERSA, develop the capacity to oversee Eskom's operations.

# 10

# Roads

## Introduction

South Africa's road infrastructure is relatively well developed compared to most sub-Saharan African countries and even by international standards, particularly in the urbanised areas. Road infrastructure supports both domestic and regional needs and is an effective catalyst for spatial development, and the development of business and residential areas. Road infrastructure also facilitates the mobility of goods and people. Road infrastructure provides connections to the external world, and specifically, access to markets and public services, such as ambulances and police services. The building of roads creates jobs, especially if labour intensive methods are used, which helps alleviate poverty and unemployment.

*Road infrastructure supports domestic and regional needs and is an effective catalyst for spatial development, and the development of businesses, transport systems and human settlements*

The 2010 FIFA World Cup was a catalyst for developing road infrastructure, particularly in the host cities. However, much more development still needs to take place. Social and economic development is constrained where there is a lack of reliable access to services, materials and markets for people and firms. Roads infrastructure is key to this access. This requires not only the installation of a road, but also its regular maintenance to ensure that access is sustained.

Roads are expensive to develop and maintain. According to the Centre for Scientific and Industrial Research (CSIR), the total asset value of South African roads in 2010 has been estimated at R1 trillion, with the value of the paved road network probably making up about 80 per cent of this (about R800 billion). New roads and major repairs of existing roads typically cost about R3.5 million per kilometre for a lightly trafficked paved rural road, while constructing and maintaining heavy freeway structures can cost tens of millions of rands per kilometre.

*Roads are expensive to develop and maintain*

Government in all spheres is responsible for funding the maintenance of the current road infrastructure, as well as providing new roads where necessary. Yet there is ample evidence pointing to road and storm water infrastructure not being maintained adequately, and this is worsened by the continual increase in traffic volumes and heavy rains. It is essential that the enormous value of the country's roads assets are not allowed to deteriorate further, as the costs of restoration would be extremely high.

Road construction at the provincial and local level needs to be informed by projected mobility and settlement patterns, which take into account plans for key economic nodes and spatial development. This should become an intrinsic part of integrated planning and development by all spheres of government. Municipalities need to enhance their capacity to effectively perform their role in relation to roads. Municipalities' integrated transport plans should provide a long term vision of local mobility, as a guide to the investment in and maintenance of road infrastructure. Municipalities also need to increase their investments in storm water management systems, especially in urban areas to mitigate incidences of flooding that are likely to be associated with the extreme weather conditions associated with climate change.

This chapter gives an overview of:

- the institutional arrangements for roads
- the state of the country's roads
- funding and expenditure on road infrastructure and maintenance
- policy and funding developments in the roads sector.

## Institutional arrangements for roads

Schedules 4 and 5 of the Constitution outline the various transport and road infrastructure functions of the different spheres of government. In terms of Part A of Schedule 5 of the Constitution, provincial roads and traffic are an exclusive provincial function, while municipal roads, traffic and parking are municipal functions in terms of Part B of Schedule 5. Municipalities are responsible for investments in local infrastructure, including the construction and maintenance of roads and streets that are within their jurisdiction and proclaimed as municipal roads.

The national Department of Transport plays a largely facilitative and regulatory role. It is responsible for the development of policy and the legislative framework that is implemented through provincial departments, local government and public entities. The main transport policies are spelt out in two key policy documents – the 1996 White Paper on National Transport Policy, and the Moving South Africa document, which emanated from the white paper and sets out an integrated strategy for improving and maintaining transport infrastructure in South Africa.

Effective institutional arrangements and proper coordination remain a challenge in road infrastructure delivery due to the broad constitutional assignment of functions for roads. The challenge emanates from the fact that national roads pass through provincial and municipal areas and provincial roads are located within municipal areas. The expansion of a road network needs to be communicated across all spheres to achieve alignment within the context of integrated road and transport planning. National, provincial and local government, as well as their associated agencies, each have responsibilities for sections of the road network. Excellent capacity and capability exist in the national road authorities (the South African National Roads Agency Limited (SANRAL)) and limited capacity at some provincial and local roads authorities, with the exception of metros and secondary cities. While SANRAL has managed to build and retain expert technical staff over the years, this has not been the case in other public sector agencies. Coordination between the provincial and municipal spheres, from both technical and political perspectives, is far from perfect.

*Effective institutional arrangements and proper coordination remain a challenge in road infrastructure delivery*

Generally, municipal infrastructure departments have a roads and storm water unit, which has capacity to carry out routine maintenance. Some municipalities have the capacity to also handle light construction activities. However, large rehabilitation and new infrastructure projects generally get outsourced to private sector civil engineering firms. Some metros have dedicated entities to focus on roads such as the Johannesburg Roads Agency, which is responsible for the management of over 10 000 km of paved roads, 1 040 km of gravel roads (excluding informal settlements) and 60 000 storm water channels and waterways. The entities themselves generally also outsource new infrastructure design and large rehabilitation projects, as their internal capacity is constrained.

*Large rehabilitation and new infrastructure projects generally get outsourced to private sector civil and mechanical engineering firms*

The municipal entities sign a service delivery agreement with the municipalities in relation to roads and storm water management. Some of the key required outcomes are construction, maintenance, and management of infrastructure networks associated with roads, storm water, footways, and traffic mobility management. For example, the Johannesburg Roads Agency's core business is to plan, design, construct and maintain municipal roads and road infrastructure within the City of Johannesburg in terms of the service delivery agreement. Politically, the road entities' boards are accountable to the member of the mayoral committee responsible for transportation/infrastructure, who, in turn, reports to the municipal council. The relationship between the council and the agency is based on a performance contract, which is governed by the city's contracting unit. This relationship sometimes poses challenges if the targets set out in the service delivery agreement cannot be supported by the available funding. The contracting city may fail to provide sufficient funding to carry out the agreed mandate and this makes monitoring and accountability difficult. Another issue with agencies is that their organisational structure may duplicate those of the contracting city as most of the entities have finance, human resources, planning directorates over and above their core engineering and technical departments. This results in a large proportion of funding being

*The entities are required to carry out construction, maintenance, and management of infrastructure networks associated with roads, storm water, footways, and traffic mobility management* diverted to an entity's non-core functions. Ideally, entities should have large, highly functional technical departments that receive the bulk of the funding.

## The state of the country's roads

*South Africa's total road network is estimated to be 746 978 km*

According to SANRAL estimates (2010), the South African road network comprised some 606 978 km of proclaimed national, provincial and municipal roads and approximately 140 000 km of unproclaimed roads[3] that are predominantly in the rural areas. This gives a total road network of 746 978 km.

*When a road is unproclaimed, there are no maintenance and rehabilitation programmes in place*

Unproclaimed roads were never formally adopted by a particular sphere of government as part of its official network. Legally, no authority can spend money on roads that are not proclaimed. This means that many people living in rural areas, which is where the unproclaimed roads are, do not have access to roads that are maintained by one or other sphere of government. When a road is unproclaimed, there are no maintenance and rehabilitation programmes in place. The lack of reliable roads infrastructure undermines prospects for development in these areas.

*Most municipalities lack road management information and decision support systems*

Data on the state of the country's roads and the extent of refurbishment and maintenance backlogs in the road network vary due to an out-of-date national public road inventory, which is supposed to be compiled by the national Department of Transport. The department attributes this information lag to the fact that it is reliant on provinces and municipalities to supply information based on their monitoring of roads. The absence of accurate data makes effective analysis difficult. Most municipalities lack road management information and decision support systems, which should assist in decision-making on the construction, maintenance and rehabilitation of roads. Very importantly, this lack of information also hinders accurate budgeting at the local level. This is certainly an area where national government needs to provide support to municipalities.

*The condition of the country's roads dropped from a VCI of 65 in 1998 to 46 in 2008*

Provincial road authorities and municipalities used to carry out annual studies using the visual condition index (VCI), which expresses the condition of a road from 0 (very poor, requires reconstruction) to 100 (very good). However, most have stopped these surveys, mainly because of a lack of technical capacity and budgets. According to a study by the Automobile Association (2008), the condition of the country's roads dropped from a VCI of 65 in 1998 to 46 in 2008[4]. A VCI score of between 35 and 50 falls within the poor road category, indicating that the 'road has failed and extensive work is immediately necessary to salvage the road'.

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[3] Public roads not formally managed by any authority.

[4] A VCI of between 0-35 indicates very poor, requires reconstruction, while 85-100 is very good.

**Table 10.1 South Africa Road Network (2010)**

| Road Authority | Paved (km) | Gravel | Total | Network Split |
|---|---|---|---|---|
| National Roads | 16 170 | – | 16 170 | 2% |
| Provincial Roads | 48 176 | 136 640 | 184 816 | 25% |
| Metros & Municipalities | 89 373 | 316 619 | 405 992 | 54% |
| Unproclaimed Rural Roads | | 140 000 | 140 000 | 19% |
| **Total** | **153 719** | **593 259** | **746 978** | **100%** |

*Source: SANRAL (2010)*

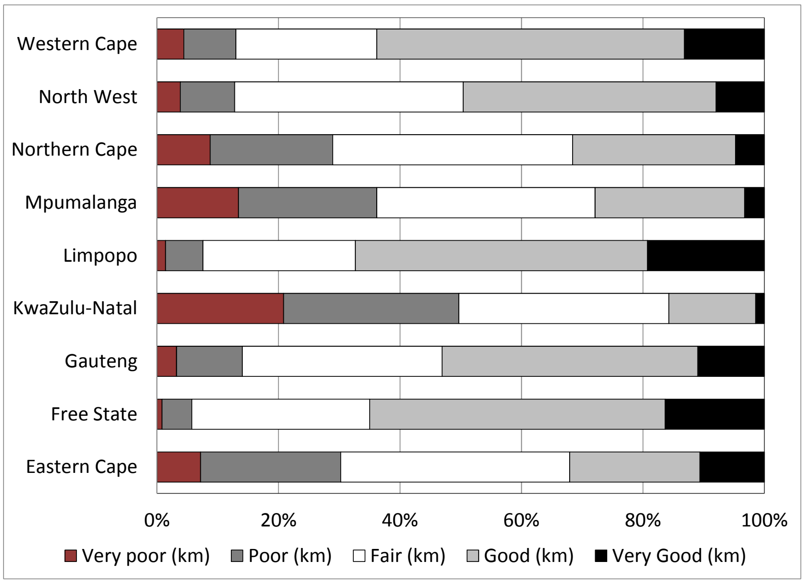
*Municipal budgets for maintenance have been less than adequate*

Table 10.1 shows that 79 per cent of the roads in South Africa are gravel roads and only 21 per cent are paved. This needs to be taken into consideration when budgeting for maintenance as gravel roads require maintenance more frequently than paved roads. Generally, municipal budgets for maintenance have been less than adequate, averaging at around 5 per cent of property, plant and equipment (PPE) for metros and 3 per cent for the top 21 municipalities. For other municipalities, maintenance averages at around 2 per cent of PPE. (National roads, which are all paved, account for only 2 per cent of the road network and their condition is generally good.)

*With an estimated 63 per cent of the proclaimed road network condition not known, it is difficult to quantify maintenance backlogs*

It is also estimated that only 37 per cent (222 507 km out of 606 978 km) of the proclaimed roads' condition is known. This means that if 63 per cent of the proclaimed road network condition is not known, so it is difficult to quantify maintenance backlogs. It also implies that road authorities are probably not channelling investments in an optimal and cost-effective way. Asset management systems are important for recording the stock of infrastructure owned, as well as its worth and condition. This provides guidance on whether the asset should be maintained, rehabilitated or replaced, and also helps to estimate the budget requirements and ensure long-term affordability. However, the national Department of Transport estimates that 66 000 km (as at 2009/10) of secondary roads are in either poor or very poor condition. Figure 10.1 summarises the state of paved roads per province.

**Figure 10.1 State of the paved roads per province**




*Source: SANRAL 2010*

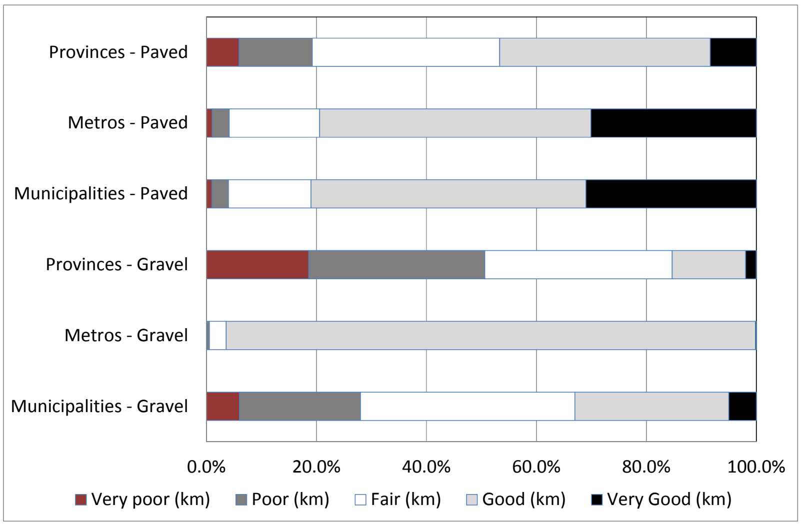
The provinces that have a significant portion of their road network in a very poor state include KwaZulu-Natal (22 per cent), Mpumalanga (15 per cent), Northern Cape (9 per cent) and Eastern Cape (7 per cent).

*Financial and planning constraints have contributed to considerable parts of municipal access roads (including unproclaimed roads) being among the poorest in the world*

Severe financial constraints, coupled with structural damage caused by road freight activities in major haulage corridors and consequent inefficiencies in road infrastructure delivery, have contributed to the inability of many provincial authorities to maintain the quality of the provincial transport system. This problem is further exacerbated at the municipal level, where financial and planning constraints have contributed to considerable parts of municipal access roads (including unproclaimed roads) being in very poor condition, a factor that denies many rural communities access to opportunities.

According to a 2008 Automobile Association report that provides a review of South Africa's national and provincial roads over 20 years, only 7 per cent of the country's rural road surfaced network was deemed to be in a poor or worse state in 1998 (in terms of VCI). However, recently published data by SANRAL (2010) indicates that the proportion of paved provincial and national roads in a poor or worse condition now constitutes nearly 20 per cent of the paved road network. Figure 10.2 shows the condition of roads under the different jurisdictions.

**Figure 10.2 Summary of paved and gravel road conditions under the different jurisdictions**



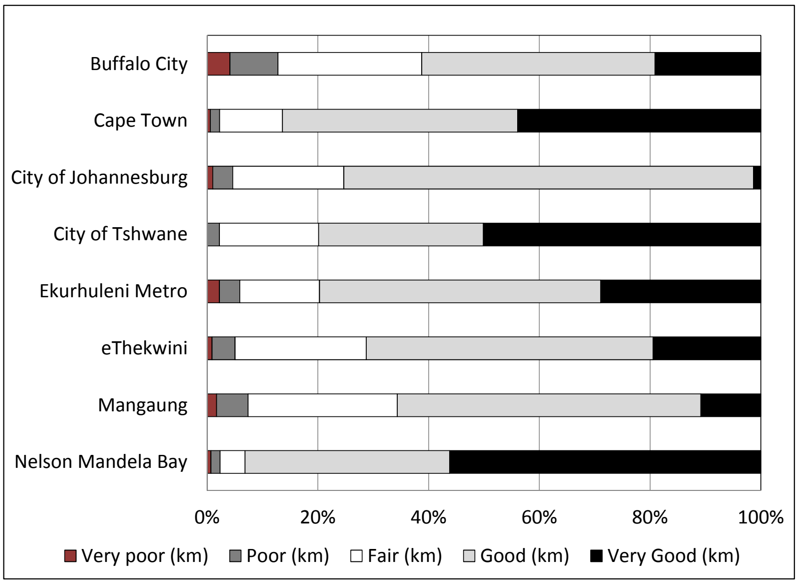

*Source: SANRAL 2010*

Local government is now responsible for 54 per cent of South Africa's road network. Figure 10.2 shows that almost 80 per cent of the paved roads in metros[5] and over 82 per cent in other municipalities are in good and very good condition. The state of gravel roads in metros is generally good, while 30 per cent of gravel roads in municipalities are in bad condition. 50 per cent of gravel roads under provinces are in very bad condition, while 35 per cent are in a fair state.

[5] SANRAL's classification comprises nine metros (Johannesburg, Tshwane, Ekurhuleni, eThekwini, Msunduzi, Buffalo City, Nelson Mandela, Cape Town, Mangaung and Mogale City).

Figure 10.3 shows that Nelson Mandela Bay metro has nearly 85.7 per cent of its paved road network in very good and good condition, followed by Cape Town (85.2 per cent) and Tshwane (79.7 per cent). Johannesburg has only 1.1 per cent of its paved road network in very good condition and 62.9 per cent in a good condition.

**Figure 10.3 State of the paved roads in metros**




*Source: SANRAL 2010*

### Potholes

Over the past few years, the emergence of potholes in South African roads has accelerated considerably, leading to serious concern among road users and widespread media coverage. The increase in pothole damage can be attributed primarily to reduced preventative maintenance and the rapidly increasing numbers of heavy vehicles. The actual costs of potholes in South Africa in terms of damage to vehicles and accidents caused directly by the presence of potholes and other road-user effects have not been quantified. However, the study by the South African Road Federation estimates that potholes are costing motorists R50 billion in vehicle repairs and injury every year.

*The increase in pothole damage is due to reduced preventative maintenance and an increase in the number of heavy vehicles*

### Vehicle population and the impact on roads

One effect of the strong economic growth experienced in South Africa between 2000 and 2008 has been an increasing number of vehicles on the roads. However, growth started to slow with the onset of the economic downturn in late 2008. Between 2008 and 2009, nearly 284 000 new vehicles were registered, 244 000 being motorised and 40 000 towed vehicles[6].

*Even with slower growth in recent years, the number of new vehicles puts pressure on the already straining road infrastructure*

[6] These include caravans, and light and heavy trailers.

**Table 10.2 Vehicle population per province, 2008 and 2009**

| | 2008 | | | 2009 | | |
|---|---|---|---|---|---|---|
| Province | Motorised | Towed | Total | Motorised | Towed | Total |
| Eastern Cape | 576 015 | 61 278 | 637 293 | 595 622 | 64 207 | 659 829 |
| Free State | 447 083 | 77 620 | 524 703 | 459 991 | 79 714 | 539 705 |
| Gauteng | 3 220 050 | 355 522 | 3 575 572 | 3 309 076 | 371 083 | 3 680 159 |
| KwaZulu-Natal | 1 177 105 | 103 217 | 1 280 322 | 1 201 536 | 106 554 | 1 308 090 |
| Limpopo | 395 122 | 41 171 | 436 293 | 423 428 | 44 262 | 467 690 |
| Mpumalanga | 496 568 | 71 426 | 567 994 | 531 682 | 76 995 | 608 677 |
| Northern Cape | 176 572 | 29 329 | 205 901 | 183 376 | 30 850 | 214 226 |
| North West | 459 311 | 66 641 | 525 952 | 471 298 | 69 489 | 540 787 |
| Western Cape | 1 409 741 | 140 743 | 1 550 484 | 1 424 024 | 144 598 | 1 568 622 |
| **Total** | **8 357 567** | **946 947** | **9 304 514** | **8 600 033** | **987 752** | **9 587 785** |

*Source: Road Traffic Management Corporation*

As table 10.2 shows, as at December 2009, South Africa's motor vehicle population stood at 8.6 million and towed vehicles at 988 000, bringing the total to close to 9.6 million vehicles. This amounts to a 3 per cent increase, which is much lower than the 7 per cent increase experienced between 2005 and 2007. This decline is due to the effects of the recession. By 30 June 2010, the total number of registered vehicles had increased to only 9.7 million, with only 100 000 new vehicles registered in the first half of the year. As the economic climate improves, the rate of new vehicle purchases is increasing.

Between December 2008 and December 2009, the number of heavy vehicles grew by 1.3 per cent or some 4 000 units and that of heavy trailers grew by 1.4 per cent of some 2 000 units. The increases were much smaller than in the previous years due to the effects of the global recession. In 2010, the motor vehicle industry started showing significant signs of recovery. In spite of the slower growth rate, as heavy vehicles' wear and tear impact on roads is far greater than that of light vehicles, future maintenance needs are nevertheless significant, particularly for municipal roads.

*At least 80 per cent of new registrations are in the light vehicle category, which are generally privately owned*

At least 80 per cent of new registrations are in the light vehicle category, which are generally privately owned. This rapid growth in the number of this category of vehicle has resulted in increasing congestion problems.

In terms of provinces, Gauteng contributes over 37 per cent of the total vehicle population in South Africa, even though it has the smallest share of the road network. This means that the municipalities in Gauteng that are responsible for the greatest proportion of the roads in the province are under a lot of pressure in relation to roads infrastructure. For example, traffic between Johannesburg and Pretoria is much heavier than the roads were originally designed to carry. It is reported that the N1 between Johannesburg and Pretoria now carries 250 000 vehicles a day, which is almost double the amount of vehicles it was designed to carry, prior to the recent upgrading. Traffic congestion is also a growing problem in Cape Town and Durban.

*Municipalities need to try to mitigate the costs associated with rising private vehicle usage*

If improvements to existing roads infrastructure challenges are not tackled in a resolute way, municipalities will find that the growth in private motor vehicle usage will increasingly become a problem. There are essentially three ways in which municipalities (and government) can begin to mitigate the costs associated with rising private vehicle usage. First, in the short term it can extend, enhance and maintain the existing road network. Second, it can encourage a shift away from private vehicle usage to public transport. This can only be done by addressing safety concerns associated with public transportation and ensure that existing public transport modes are convenient in terms of location. Third, over the medium to long term it can encourage more integrated and sustainable human settlement patterns that encourage people to live closer to their places of employment and where land uses are mixed. Developing an integrated, safe, customer-oriented public transport system supported by a good roads infrastructure is essential.

### Road safety

Vehicle overloading and breaches of road safety regulations continue to be major problems despite enforcement efforts. Overloading causes premature road deterioration and, together with speeding and bad driver behaviour, inadequate vehicle maintenance and driver fatigue, all contribute to South Africa's poor road safety record.

*Vehicle overloading and breaches of road safety regulations continue to be major problems*

In 2009, the country recorded approximately 498 000 traffic accidents, 46 500 serious injuries and 13 768 traffic fatalities, of which 4 678 were pedestrians.

### Challenges faced by municipalities

Some of the problems that municipalities need to address in managing the roads and storm water infrastructure include:

- *Inappropriate prioritisation in allocating budgets*: Prioritisation of new infrastructure happens at the expense of maintaining existing assets.
- *Maintenance budgets:* These are often treated as discretionary budget line items and are the first to be cut to realise savings. Municipalities need to be constantly investing in the refurbishment of their infrastructure and ensuring that aging assets are upgraded timeously.
- *Non-integrated housing developments:* These occur because provinces are not working closely with municipalities to plan the location of new housing developments, as a result houses get built where the support road infrastructure does not exist.
- *Excavations by other service providers and illegal practices:* These excavations damage the road infrastructure, as does overloading of heavy transport vehicles.
- *Loss of key technical staff:* Often key staff are not replaced or they are replaced by less qualified staff. A recent survey by the South African Institute of Civil Engineering revealed that 79 of the 231 local municipalities had no civil engineers, technologists or technicians on their permanent staff.
- *Lack of asset lifecycle planning capability:* Maintenance of roads and storm water infrastructure is mainly done on an ad-hoc basis as there is no proper base for planning and budgeting for planned maintenance of infrastructure.

## Funding and expenditure on road infrastructure and maintenance

### Funding the municipal roads network

*Municipalities might therefore decide to use a portion of the local equity share to finance road infrastructure projects*

Municipalities receive intergovernmental transfers in line with the Division of Revenue Act and this includes the local government equitable share, which is an unconditional grant. Municipalities might therefore decide to use a portion of the local government equity share to finance road infrastructure projects, guided by their own needs and priorities. Municipal internally generated funding should also be used to finance roads infrastructure.

*For many municipalities, the most significant source of road infrastructure funding is the municipal infrastructure grant*

For many municipalities, the most significant source of road infrastructure funding is the municipal infrastructure grant (MIG). The grant is aimed at assisting municipalities to deliver basic infrastructure to poor communities. Another major source of funding road infrastructure at the municipal level is the public transport infrastructure and systems grant (PTIS), which is a conditional grant administered by the Department of Transport. The grant provides for the planning, establishment, construction and improvement of new and existing public transport infrastructure and non-motorised transport infrastructure systems.

For many of the poor and rural municipalities, the public works programmes implemented by both national and provincial departments of public works serve as an important means of developing roads within their jurisdictions, as illustrated in the Zibambele case study.

**Zibambele – KwaZulu-Natal Department of Transport Initiative**

The Zibambele programme in KwaZulu-Natal aims to involve local people in road maintenance. It has been very successful in this regard The fact that the programme is being replicated in Mpumalanga and Eastern Cape, with a number of municipalities now formally participating, is an indication of its success.

Zibambele is a routine road maintenance programme using labour-intensive methods. Instead of appointing a firm to do the maintenance, Zibambele appoints households, who are responsible to:

- Maintain the road drainage system
- Ensure good roadside visibility
- Maintain the road surface in good condition
- Clear the road verges of litter and noxious weeds

Zibambele emerged as a plan to create jobs and other income-generating opportunities, while simultaneously addressing the apartheid legacy of inadequate mobility for rural communities. The initiative was adopted as one that could place rural economies on a labour-absorptive growth path. The main objectives of the programme are to:

- Maintain the province’s rural road network
- Provide destitute households with regular income
- Put the long-term unemployed to work
- Promote gender affirmative opportunities
- Improve the life chances of Zibambele households through: providing work; training; better nutrition; obtaining identity documents and access to banking facilities; experiencing the dignity of employment; and becoming involved in further economic activities.

In its first year in 1999/2000, 2 700 households were employed as contractors. The number is expected to rise to 40 000 in 2010/11. In its first year 11 000 km of rural road was maintained compared to 25 000 km that is expected in 2010/11. Expenditure on the programme was R5.6 million in 2006/07 and this is expected to increase to R31.3 million in 2010/11.

*Source: KwaZulu-Natal Department of Transport 2010/11 annual performance plan*

### Road maintenance initiatives through the expanded public works programme

The expanded public works programme is a government wide programme that focuses on the creation of work opportunities through infrastructure delivery. The programme provides dedicated resources to provincial and local governments for, among others, labour-intensive programmes such as road construction and maintenance, and the development of permanent capacity for the maintenance of infrastructure on a sustainable basis.

*Municipalities have not taken enough advantage of the expanded public works programme for road infrastructure and maintenance projects*

To date, municipalities have not taken significant advantage of the expanded public works programme, implementing around 13 per cent of the projects (2 266 out of 16 869 projects) as table 10.3 shows. The bulk of municipal activities has been in the infrastructure sector, of which road construction is a significant component and is estimated to account for 65 per cent of the infrastructure sector projects. These projects are often aligned with MIG funding, with 1 866 infrastructure projects reported in 2008/09 out of 2 266 municipal projects (or 82 per cent of the sector total).

**Table 10.3 Projects per sector and sphere of government**

| Sector | Municipal | National | Provincial | Total |
|---|---|---|---|---|
| Economic | 116 | 4 | 234 | 354 |
| Environment and Culture | 230 | 897 | 250 | 1 377 |
| Infrastructure | 1 866 | 5 404 | 2 333 | 9 603 |
| Social | 54 | – | 5 481 | 5 535 |
| **Total** | **2 266** | **6 305** | **8 298** | **16 869** |

*Source: Expanded Public WorksProgramme, Five Year Report 2004/05-2008-09*

The total infrastructural output across the country was the development and maintenance of over 37 000 km of roads, 31 000 km of pipelines, 1 500 km of storm water drains and 150 km of sidewalks through the expanded public works programme infrastructure projects.

### Municipal expenditure on roads infrastructure and maintenance

Maintaining the municipal roads infrastructure includes routine maintenance, upgrading and rehabilitation activities, all of which require planning and adequate budgets.

*Metros account for 71 per cent of all municipal roads expenditure*

It is difficult to get a clear picture of consolidated municipal expenditure on roads infrastructure (including storm water infrastructure) and maintenance, due to the previous budgeting reporting formats. The current reporting requirements have been refined to allow for more detailed breakdowns. In 2008/09, total provincial and municipal roads infrastructure expenditure was R20.1 billion. Of this, municipalities spent R7.3 billion or 36 per cent and provinces spent R12.8 billion or 64 per cent. Of the R7.3 billion spent by all municipalities, metros account for R5.2 billion, or 71 per cent of all municipal roads expenditure. For the smaller municipalities, the fact that expenditure on roads and storm water infrastructure is as low as R200 000, is an indication that this is not being prioritised.

### Metros' and secondary cities' expenditure on roads infrastructure and maintenance

Table 10.4 shows that road infrastructure budgets increased from R1.8 billion in 2006/07 to R6.4 billion in 2009/10, and are set to decrease to R3.6 billion in 2010/11 before increasing to R5.8 billion in 2011/12. Generally the low level of spending in the outer year of MTREF by most metros suggests that these budgets are not based on sound forward planning of projects. The rapid increase between 2006/07 and 2009/10 was largely driven by developments for the 2010 FIFA World Cup, as five of the six metros were host cities.

**Table 10.4 Metro roads infrastructure expenditure, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Ave annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | | 2006/07 - | 2009/10 - |
| R thousands | | | | | | | | 2009/10 | 2012/13 |
| City of Cape Town | 255 533 | 385 761 | 747 859 | 1 588 087 | 870 504 | 1 335 457 | 779 116 | 83.9% | -21.1% |
| City of Johannesburg | 298 033 | 180 100 | 1 352 672 | 1 381 806 | 245 193 | 1 358 371 | 994 022 | 66.7% | -10.4% |
| City of Tshwane | 234 192 | 438 469 | 561 732 | 525 780 | 485 065 | 561 621 | 521 401 | 30.9% | -0.3% |
| Ekurhuleni | 397 391 | 389 691 | 1 003 577 | 575 628 | 437 580 | 399 906 | 370 766 | 13.1% | -13.6% |
| eThekwini | 415 389 | 635 141 | 822 635 | 1 405 087 | 675 502 | 740 580 | 692 510 | 50.1% | -21.0% |
| Nelson Mandela Bay | 207 732 | 348 280 | 695 415 | 875 287 | 898 856 | 1 402 190 | 1 516 143 | 61.5% | 20.1% |
| **Total** | **1 808 270** | **2 377 442** | **5 183 890** | **6 351 675** | **3 612 699** | **5 798 125** | **4 873 958** | **52.0%** | **-8.4%** |

*Source: National Treasury local government database*

Johannesburg's roads infrastructure expenditure and budgets vary widely from year to year. This points to poor planning of projects. Over the MTREF, Johannesburg has budgeted to spend R2.6 billion on roads infrastructure. This is less than Nelson Mandela Bay (R3.8 billion) and Cape Town (R3.0 billion), both of whose road networks are less extensive and in far better condition than those of Johannesburg.

Table 10.5 shows that the road infrastructure budgets for the 21 secondary cities

**Table 10.5 Secondary cities roads infrastructure expenditure, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| R thousands | | Outcome | | Estimate | | Medium-term estimates | |
| Buffalo City | 42 405 | 64 409 | 83 519 | 152 396 | 95 600 | 122 867 | 141 019 |
| City of Matlosana | 29 769 | – | 58 382 | 47 269 | 46 066 | 63 257 | 56 757 |
| Drakenstein | 7 010 | 12 187 | 15 235 | 17 202 | 29 096 | 30 922 | 28 532 |
| Emalahleni | 12 059 | 36 986 | 36 829 | 27 503 | – | – | – |
| Emfuleni | 55 542 | 17 515 | 12 200 | 102 638 | 57 257 | – | – |
| George | 79 042 | 452 | 189 | – | 23 885 | 42 330 | 44 250 |
| Govan Mbeki | 7 331 | – | 15 045 | 9 537 | 44 570 | 28 500 | 29 000 |
| Madibeng | 24 410 | 26 378 | – | – | 44 400 | 47 064 | 49 888 |
| Mangaung | 80 702 | 70 822 | 82 651 | 125 064 | 100 552 | 129 413 | 139 616 |
| Matjhabeng | 3 892 | – | – | – | 33 442 | 63 409 | 93 381 |
| Mbombela | 25 994 | 40 542 | 51 926 | 38 424 | 41 593 | – | – |
| Mogale City | 479 | – | 23 970 | 23 970 | 27 625 | 37 660 | 69 342 |
| Msunduzi | 26 565 | 69 891 | 119 262 | 21 811 | 36 315 | 63 837 | 56 996 |
| Newcastle | 25 486 | 18 165 | 27 619 | 107 152 | 53 790 | 20 000 | 20 000 |
| Polokwane | – | 32 258 | 49 772 | 181 853 | 202 067 | 96 000 | 92 000 |
| Rustenburg | 49 676 | 40 480 | – | 22 692 | 140 068 | 7 000 | 7 000 |
| Sol Plaatje | 17 331 | 39 673 | 27 146 | 40 012 | 20 900 | 4 200 | 7 225 |
| Stellenbosch | 12 687 | 15 198 | 20 365 | 25 400 | 24 599 | 7 600 | 9 070 |
| Steve Tshwete | 21 703 | 47 191 | 58 521 | 65 490 | 69 133 | 65 728 | 72 892 |
| Tlokwe | 19 210 | 6 377 | 13 940 | – | 44 526 | 32 631 | 20 144 |
| uMhlathuze | 59 435 | 48 552 | 64 968 | 41 208 | 15 846 | 14 079 | 47 613 |
| **Total** | **600 728** | **587 076** | **761 539** | **1 049 621** | **1 151 331** | **876 497** | **984 725** |
| *Percentage growth (average annual)* | | **2006/07 – 2009/10** *20.4%* | | | | **2010/11 – 2012/13** *-7.5%* | |

*Source: National Treasury local government database*

The above table shows that secondary cities' spending increased by 20.4 per cent annually between 2006/07 and 2009/10, but is set to decrease by 7.5 per cent per year over the medium term. While most of the secondary cities' integrated development plans (IDPs) list roads and storm water upgrading as an important priority, roads infrastructure budgets over the MTREF period are actually decreasing. This reflects a serious misalignment between planning and budgeting.

## Policy and funding developments in the roads sector

In the execution of its mandate, the Department of Transport has identified the following strategic priority outcomes and key policy developments for the medium term in relation to roads:

- *Development of an effective and integrated infrastructure network that serves as a catalyst for social and economic development:* This will be achieved by ensuring maintenance and the strategic expansion of the road network.
- *Development of road asset management and preservation policy:* This will begin in 2011/12 to effectively support the implementation of the road infrastructure strategic framework of South Africa. Furthermore, it will ensure that road authorities conduct road condition surveys regularly and use road asset management systems in planning for investments. This will allow optimum decisions to be taken on increasing the asset lifespan of roads, reducing transport costs, and improving accountability and expenditure outcomes.

The government plans to spend a total of R22.3 billion rand on the S'hamba Sonke project (its road construction and maintenance plan) over the next three years. This amount, however, is inadequate. The Department of Transport is moving towards striking a balance between road construction and maintenance in line with the international benchmark of 40 per cent construction and 60 per cent maintenance.

To support the initiatives of the Department of Transport, the Minister of Public Works launched a R150 million project in March 2011 to address potholes across the country by cooperating with provinces. This initiative will be delivered through the expanded public works programme.

## Conclusion

Current funding available for roads and storm water infrastructure is insufficient for meeting existing maintenance and rehabilitation requirements in the sector. There is therefore a need for reprioritisation on municipal budgets to effectively deal with its core services and manage competing needs. To strike a balance remains a critical challenge for most municipalities as there is always a gap between conditions on the ground and the councils' priorities. If improvements to the existing roads infrastructure are not tackled in a robust way, either by increasing budget allocations or making effective use of expanded public works programmes, municipalities will be faced with increasing backlogs which will further compromise general service delivery and undermine economic growth. Furthermore, municipalities should increase their investments in storm water channels, especially in urban areas, to mitigate flooding and the associated damage. Ideally, municipalities' integrated transport plans should provide a long term vision of road infrastructure that facilitates mobility. This will inform sound decision-making relating to investment in and maintenance of road infrastructure.

# 11

# Solid waste services

## Introduction

Solid waste management and service delivery systems can make critical contributions to public health, environmental sustainability, economic development and poverty reduction.

Effective solid waste management systems can contribute to improving public health outcomes through reducing opportunities for disease spreading vermin to thrive, such as occurs at unregulated local dumpsites. They contribute to enhancing environmental quality by protecting watercourses, ground water and preventing illegal dumping and littering. Well-designed solid waste management systems support both higher levels of economic activity and can contribute directly to poverty alleviation through job creation. Conversely, a failure to provide effective solid waste systems is felt most severely by poor households.

*Effective solid waste management systems can contribute to improving public health outcomes*

The National Environmental Management: Waste Act (2008) uses the waste hierarchy as its overarching principle for waste management. This hierarchy focusses on waste minimisation, reuse, recycling and recovery in preference to waste disposal. The Act also provides tools to implement the waste hierarchy through integrated waste management planning, providing for the development of integrated industry waste management plans, the identification of priority waste, waste licencing and the development of regulations to manage specific waste streams. Managing waste in line with the waste hierarchy has the potential to provide jobs as recycling requires infrastructure and opens new markets. The Department of Environmental Affairs and Tourism's Waste Management Strategy seeks to address the backlog in the provision of waste services particularly to urban informal settlements and rural/tribal areas.

This chapter gives an overview of:

- institutional arrangements for solid waste services
- access to solid waste services
- financing solid waste services
- waste minimisation, recycling and energy recovery.

## Institutional arrangements for solid waste services

*Solid waste management in South Africa is primarily a local government function*

Solid waste management in South Africa is primarily a local government function. Section 156(1)(a) of the Constitution, read with Schedule 5, assigns responsibility for refuse removal, refuse dumps, solid waste disposal and cleansing to local government. The Waste Act outlines the roles of both national and provincial government in waste management. National government's competence to legislate is established in line with section 44 of the Constitution on the grounds of the need to maintain essential national standards, establish uniform norms and standards, and to promote and give effect to the right to an environment that is not harmful to health and well-being. Provincial governments are tasked with the implementation of the national waste management strategy and national norms and standards, and may set additional, complementary provincial norms and standards. Local governments are required to ensure the sustainable delivery of services, subject to national and provincial regulations and standards.

*The National Environmental Management: Waste Act promotes the regionalisation of solid waste management services*

The most innovative feature of the National Environmental Management: Waste Act is the preference for the regionalisation of solid waste management services. The Act also places considerable emphasis on the development of an integrated waste planning system, through the development of interlocking integrated waste management plans by all spheres of government and industry waste management plans for specified waste generators. This planning system is the primary tool for cooperative governance within the sector. While the requirement for these plans is new for national and provincial governments, and for waste generators, this is not the case for local governments, which previously included waste management plans within their integrated development plans.

Other focal areas of the Act include provisions for the development of norms and standards, financial management systems, standard by-laws and tariffs. These aspects of the Act largely repeat existing national or provincial powers that are provided for in other legislation. The key change is that the Minister of Environmental Affairs and Tourism now assumes these powers in terms of the Act, albeit concurrently with other ministers, notably in the local government and finance portfolios.

### The assignment of solid waste functions

Table 11.1 shows the assignment of solid waste functions, following the generic schema of waste management responsibilities outlined by the Department of Environmental Affairs and Tourism in 2007[7] and in terms of current practice.

**Table 11.1 Current allocation of solid waste functions between roleplayers**

| Area | Broad Function | Activity | Current assignment | | | | Issue |
|---|---|---|---|---|---|---|---|
| | | | Nat | Prov | Local | Pvt | |
| Policy-making | Standard Setting | Norms and standards | X | X | | | What is to be provided |
| | | Access targets | X | | X | | |
| | Planning | Plans for service expansion | | X | X | | Adequate facilities and services |
| | | Plans for service improvement | | X | X | X | |
| Service Provision | Asset creation | Social capital | | | X | | Adequate facilities and services |
| | | Physical capital | | | X | X | |
| | Financing | Tariffs | | | X | | Financial sustainability |
| | | Subsidies to Consumers | | | X | | |
| | | Grants to Service Providers | X | | | | |
| | Operation | Consumer selection | | | X | | Effective and sustainable services |
| | | Recurrent expenditures | | | | | |
| | | - General area cleansing | | | X | X | |
| | | - Waste minimization | | | X | X | |
| | | - Waste collection | | | X | X | |
| | | - Waste transport | | | X | X | |
| | | - Waste disposal | | | X | X | |
| | | Maintenance | | | X | X | |
| | | Staffing | | | X | | |
| Regulation | M&E | Economic | X | X | X | | Quality of service delivery |
| | | Financial | X | X | X | | |
| | | Operational | X | X | X | | |
| | | Monitoring & Evaluation | X | X | X | | |

*Source: Department of Environmental Affairs and Tourism (2007)*

### *Policy making functions*

To date, the focus of government has been on creating an overarching legislative framework to regulate waste management. Since the promulgation of the Waste Act in 2009, attention is now being given to implementation and the provision of basic refuse removal services. To this end, the Minister of Environmental Affairs and Tourism has issued the following regulations and standards:

- The national domestic waste collection standards, which came into effect on 1 February 2011. These standards seek to ensure uniformity in relation to the frequency of collections, transportation, receptacles and storage. The standards promote the separation of waste at source; meaning domestic waste should be sorted into recyclable and non-recyclable materials.
- The municipal waste sector plan that requires municipalities to indicate how they are going to address the backlogs in waste services and the associated infrastructure.
- Regulations prohibiting the use, manufacture, import and export of asbestos and asbestos containing materials which is aimed at phasing out the use of asbestos in products in the country.
- Regulations providing for the management and financing of the disposal of waste tyres

The Minister of Environmental Affairs and Tourism has also determined that the lighting, tyre, paper and packaging and

[7] Department of Environmental Affairs and Tourism. Assessment of the status of waste service delivery and capacity at the local government level. Directorate: General Waste Management, August 2007, Draft 3

veterinary industries must develop industry waste management plans that indicate how their products will be managed once they become waste, as well as how the waste management system for their products will be financed.

Government has attached comparatively greater importance to the development of integrated waste management plans by all spheres of government. These plans are seen as the primary tool for strengthening cooperative governance in the sector.

### Establishing service standards in solid waste management

The Department of Environmental Affairs has sought to provide substantive guidance on the establishment of standards in the waste sector. The emerging approach recognises that differing service standards are appropriate in different settlement types and densities. Moreover, issues of affordability, municipal capacity, the quality and nature of waste generated, climate, availability of storage, topographic conditions, road conditions (width and quality) all impact on the nature of the service that can be provided in an area.

Importantly, standards are not limited to collection services alone, but must also deal with waste regulation, minimisation, storage, transport and treatment. Perhaps the most important finding of the research is that municipalities themselves must accept and take ownership of the appropriate set of standards for their areas. Although a single set of national standards is desirable, they will need to differentiate between the levels and kinds of service expected in different areas of the country. Household waste generation characteristics vary considerably by settlement type and income. A comparison of the waste generated by urban residents in different settlement types demonstrates the point that wealthier consumers are predominantly located in low density suburbs.

**Production of waste by urban settlement type**

| Settlement | Waste |
|---|---|
| Suburban | 0.8 - 3kg per capita per day |
| Township | 0.2 - 0.8kg per capita per day |
| Informal settlement | < 0.2kg per capita per day |

*Sources: Mbande, 1996; Lombard in Palmer Development Group, 1996; Benting, 2000.*

The department also suggests that municipalities should adopt a mixture of geographic targeting and self-targeting approaches in the implementation of their free basic refuse services, and that subsidies should cover both regular service provision and the provision of waste receptacles.

*Planning systems are intended to guide an integrated waste management approach and ensure that waste management systems contribute to socio-economic development*

The Department of Environmental Affairs and Tourism reports that, in 2009, 177 municipalities submitted integrated waste management plans. This accounts for 75 per cent of municipalities authorised to perform solid waste functions. The quality of the plans is highly variable across municipalities and reflects lack of clarity about what constitutes an integrated waste management plan. This will change going forward given that the Waste Act now clearly outlines the minimum information to be included in such plans.

Cooperative governance is also pursued through the appointment of waste management officers in all spheres of government. Section 10 of the Act requires that the national minister, provincial members of the executive councils (MECs) and each local government must designate in writing a waste management officer from its administration to be responsible for coordinating matters pertaining to waste management. This role encompasses both policymaking roles (specifically in terms of planning and standard setting activities) and regulatory roles. Waste management control officers, with enforcement responsibilities, are also recognised in section 58 of the Act. This system is still in its infancy and thus, while it explicitly intends to improve coordination between spheres of government, its performance cannot be assessed.

### *Regulatory functions*

The Waste Act empowers the Minister of Environmental Affairs and Tourism to set norms and standards for the planning and provision of waste management services, as well as standards for the storage, treatment and disposal of waste, including the planning and operation of waste treatment and disposal facilities. The provisions in the Act dealing with the economic and financial management of the sector are largely aligned to existing municipal finance legislation. It is envisaged that the Department of Environmental Affairs and Tourism will play an important role in providing technical waste management support.

*The National Environmental Management: Waste Act empowers the minister to set norms and standards for the planning and provision of waste management services*

### *Service provision functions*

It is important to note that the Act provides municipalities with an effective legal monopoly over the provision of solid waste services. The Act specifically requires that private waste service providers have the approval of municipalities before they begin any waste collection activities, and may also be required to register with national or provincial governments.

Statistics South Africa reports that 239 municipalities performed solid waste management functions in 2009, up from 226 in 2005. The data since 2005 suggests that solid waste functions are increasingly being assigned to local municipalities even in predominantly rural areas. This is in marked contrast to the stated policy preference for the regionalisation of solid waste service provision that is contained in the Act.

**Table 11.2 Municipalities performing solid waste functions, 2005 and 2009**

| | With function | With infra-structure | Provide service | Outsource service |
|---|---|---|---|---|
| **2005** | | | | |
| Metros | 6 | 6 | 6 | 1 |
| Secondary Cities | 20 | 21 | 21 | 5 |
| Large towns | 28 | 29 | 29 | 8 |
| Small towns | 107 | 108 | 109 | 6 |
| Mostly rural | 55 | 49 | 51 | 9 |
| Districts | 10 | 12 | 10 | 1 |
| **Total** | **226** | **225** | **226** | **30** |
| **2009** | | | | |
| Metros | 6 | 6 | 6 | 3 |
| Secondary Cities | 21 | 21 | 21 | 1 |
| Large towns | 29 | 29 | 29 | 3 |
| Small towns | 111 | 111 | 111 | 1 |
| Mostly rural | 63 | 58 | 56 | 8 |
| Districts | 9 | 9 | 9 | – |
| **Total** | **239** | **234** | **232** | **16** |

*Source: StatsSA, P9115 (2007, 2008, 2009, 2010)*

Almost all municipalities that have been assigned solid waste functions report having infrastructure available to perform the function. This figure is lowest in mostly rural municipalities, with 92 per cent reporting that this was the case in 2009.

In most municipalities, a municipal solid waste department is responsible for implementation (and therefore the associated expenditure), while revenue and financial management functions related to the function are undertaken by the budget and treasury office. Exceptions to this arrangement do exist, such as Pikitup, which is a municipal entity owned by the City of Johannesburg.

*Outsourcing and commercialisation are mostly used by metropolitan and district municipalities, with 50 per cent reporting such arrangements*

Outsourcing and commercialisation are mostly used by metropolitan and district municipalities, with 50 per cent reporting such arrangements. There are also indications that municipalities are moving away from outsourcing the solid waste function. Most municipalities thus deliver these services in-house. Similarly, the use of community-based delivery mechanisms is limited, despite the potential for creating jobs in this way. National government has begun piloting labour intensive approaches to the expansion of solid waste services, but these have yet to be rolled out at scale. Initial estimates suggest that this approach has the potential to create over 3 000 permanent, non-public sector jobs in waste collection.

### Challenges with current institutional arrangements

A number of weaknesses exist in the current institutional arrangements of the solid waste function:

*Vagueness or overlap in the assignment of responsibilities can undermine accountability for service delivery*

- *Division of roles between district and local municipalities:* Vagueness or overlap in the assignment of responsibilities tend to undermine accountability for service delivery. In instances where district and local municipalities share responsibilities, a clear contracting framework is required to ensure that a single authority remains politically and administratively accountable for the service. However, such contracts are not the norm.
- *Regionalisation of service delivery:* The trend has been towards greater decentralisation rather than regionalisation, because policy on the regionalisation of the function remains vague.
- *Ring-fencing of solid waste finances:* This is an important but insufficient step to improving efficiencies in the sector. Additional organisational reforms to combine revenue and expenditure authority and accountability in municipal solid waste functions may also be required. It is also not practical to ring-fence the function in all contexts, especially in smaller municipalities.
- *Effective systems of cooperative governance:* This is complicated by an inadequate distinction between the policy-making, regulatory and service provider roles across spheres of government. This can lead to private service providers playing regulators off against each other which weakens enforcement.

## Access to solid waste services

Statistics South Africa reports that 64.5 per cent of households had access to some form of solid waste management service in 2007. The number of served consumer units has risen by 6 per cent per year since 2005. Access to services is greatest in metro areas (92.5 per cent) and small towns (73.5 per cent), while it is lowest in rural municipalities (16 per cent). Access levels are lowest in Limpopo (25.5 per cent), followed by Eastern Cape (46.6 per cent) and Mpumalanga (46.7 per cent).

*The number of served consumer units has risen by 6 per cent per year since 2005, with 8.4 million units served in 2009*

**Table 11.3 Access to refuse removal services, 2005 - 2009**

| Category | Total number of households 2007 | Consumers receiving services 2005 | 2006 | 2007 | 2008 | 2009 | % of all households 2007 |
|---|---|---|---|---|---|---|---|
| Metros | 4 714 022 | 3 421 122 | 4 029 732 | 4 358 630 | 4 355 942 | 4 548 979 | 92.5% |
| Secondary cities | 2 207 003 | 1 232 347 | 1 253 940 | 1 389 260 | 1 393 949 | 1 596 674 | 62.9% |
| Large tow ns | 1 095 456 | 564 322 | 587 670 | 628 276 | 643 503 | 696 636 | 57.4% |
| Small tow ns | 1 637 412 | 983 981 | 1 066 597 | 1 204 108 | 1 071 349 | 1 118 202 | 73.5% |
| Mostly rural | 2 824 259 | 493 226 | 413 560 | 453 061 | 388 900 | 408 704 | 16.0% |
| Districts* | 22 482 | 6 357 | 28 906 | 29 531 | 27 224 | 27 379 | |
| **Total** | **12 500 634** | **6 701 355** | **7 380 405** | **8 062 866** | **7 880 867** | **8 396 574** | **64.5%** |

*Sources; Stats SA 2007, 2008, 2009, 2010*

*Note: District figures reflect only additional households served and DMA areas*

Levels of service differ markedly by type of municipality. The bulk of those consumers with basic services are receiving at least a weekly collection service. Yet 19 per cent (or 1.3 million) of households in metros and secondary cities do not receive weekly refuse services, with 23 per cent of households in secondary cities making use of their own refuse dumps. Outside of these areas, 13 per cent (or 726 000) of households do not receive any refuse service or make use of on-site disposal.

*Levels of service differ markedly by type of municipality*

**Table 11.4 Households with inadequate access to services by municipal context[1]**

| | Less than weekly | Communal refuse dump | Own refuse dump | No rubbish disposal | Other | Underserved HH Total | Underserved HH % | Total households |
|---|---|---|---|---|---|---|---|---|
| Metros | 81 558 | 113 496 | 255 026 | 133 474 | 17 861 | 601 415 | 12.8% | 4 714 022 |
| Secondary cities | 30 313 | 54 398 | 512 993 | 113 776 | 3 448 | 714 928 | 32.4% | 2 207 003 |
| Large tow ns | 22 316 | 23 665 | – | 70 639 | 4 662 | 121 282 | 11.1% | 1 095 456 |
| Small tow ns | 41 947 | 39 372 | – | 124 337 | 4 418 | 210 074 | 12.8% | 1 637 412 |
| Mostly rural | – | – | – | 449 004 | 9 130 | 458 134 | 16.2% | 2 824 259 |
| Districts* | – | – | – | 1 379 | 141 | 1 520 | 6.8% | 22 482 |
| **Total** | **176 134** | **230 931** | **768 019** | **892 609** | **39 660** | **2 107 353** | **16.9%** | **12 500 634** |

*Source: Community Survey, 2007, adjusted (see footnote)*

1. This assumes basic service levels to be (i) a w eekly collection service in metropolitan municipalities and secondary cities; (ii) that ow n refuse dumps in large and small tow ns and rural municipalities are predominantly used outside of urban settlements and thus constitute an appropriate basic level of service delivery; (iii) that less than w eekly services and communal refuse dumps are found in urban areas of large and small tow ns, and do not meet basic service standards.

Comparing the data in tables 11.3 and 11.4 highlights some of the difficulties in obtaining reliable information on backlogs and access to services. The data from the Community Survey 2007 (table 11.4) indicates the backlog in the provision of solid waste services is 2.1 million households, with some 892 000 households not receiving any service. Whereas the information gathered by Statistics South Africa in its annual service delivery survey (table 11.3) indicates that some 4.1 million households do not have access to solid waste or refuse removal services.

### Extending access to basic refuse removal services

In 2001, government set itself the target of providing all households access to refuse removal services by 2012. Significant progress has been made in expanding access, but significant challenges remain.

*Lack of access to services remains highest in rural municipalities*

Lack of access to services remains highest in rural municipalities, where consumers either dispose of waste themselves or dump it in an unregulated manner. But domestic waste collection services are often neither necessary nor viable in many rural areas, with households producing mostly organic waste that can be disposed safely on-site.

*The failure to provide services in informal settlements and other underserviced areas leads to the unregulated dumping of solid waste*

Extending access to basic solid waste collection services remains a critical policy priority, even in large cities. Table 11.4 shows that over 1.3 million households in metros and secondary cities currently receive below basic levels of service. This amounts to 62 per cent of the total number of underserviced households.

Smaller municipalities can also make significant strides in improving access through encouraging and regulating appropriate on-site disposal. 645 000 households have no access to waste disposal in these areas, constituting over 30 per cent of the total number of underserviced households.

The failure to provide services in informal settlements and other underserviced areas leads to the unregulated dumping of solid waste, the volume of which is increased by home-based enterprises. The burning of waste on such dumps is also relatively common, contributing to both air and soil pollution.

### Sustaining access to basic services

Municipalities have shown a commitment to addressing backlogs in domestic solid waste collection services. However, as services have been expanded, average revenues per consumer have fallen as more poor households are serviced. This disjuncture between access levels and revenues has been most severe in the metros, which have seen the most rapid expansion of services.

Most municipalities have introduced free basic refuse services. This means the service is being subsidised by the municipality. Most municipalities report using a self-selection system for targeting solid waste subsidies. This typically involves either a tariff-based subsidy or a beneficiary applying for access to the subsidy on a means-tested basis. The aim of the latter approach is typically to reduce leakage of the subsidy outside of the target group. Metros report the use of varying subsidy systems. Geographic targeting effectively occurs in informal settlements in both Ekurhuleni and Cape Town. Tariff-based systems, based on staggered tariffs relative to property values, are applied in Cape Town, eThekwini and Johannesburg. Nelson Mandela Bay operates an application based system, while Tshwane does not offer any subsidies for refuse services.

Municipalities reported a declining number of consumers receiving subsidies for basic refuse services between 2005 and 2009. 1.9 million consumers benefited from subsidies for the costs of receiving solid waste services in 2009. This represents a decline of over 37 per cent since 2005, when over 3.1 million consumers were reported to have benefited. This decline is probably due to a shift from geographic targeting of subsidised services to application based targeting approaches.

*Municipalities reported a declining number of consumers receiving subsidies for basic refuse services between 2005 and 2009*

In 2010, cabinet approved the national policy for the provision of basic refuse removal services to indigent households, which aims to facilitate the delivery of these services.

## Financing solid waste services

Information on operating revenues and expenditures for the solid waste function is generally weak, with many municipalities only beginning to report on these areas separately, in accordance with the formats required in terms of the Municipal Budget and Reporting Regulations.

### Solid waste revenues

The following table shows operating revenue for the solid waste function.

**Table 11.5 Operating revenue for the solid waste function by category of municipality, 2006/07 – 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth | |
|---|---|---|---|---|---|---|---|---|---|
| R million | | Outcome | | Preliminary Estimate | | Medium-term estimates | | 2006/07 - 2009/10 | 2009/10 - 2012/13 |
| **Operating revenue** | | | | | | | | | |
| Metros | 1 280 | 2 465 | 2 965 | 2 841 | 4 909 | 5 343 | 5 794 | 30.4% | 26.8% |
| Local municipalities | 673 | 731 | 1 268 | 2 256 | 3 050 | 2 895 | 3 064 | 49.6% | 10.7% |
| *Secondary cities* | 467 | 506 | 737 | 1 115 | 1 540 | 1 396 | 1 522 | 33.6% | 10.9% |
| *Large towns* | 142 | 142 | 311 | 444 | 640 | 655 | 644 | **46.0%** | **13.3%** |
| *Small towns* | 50 | 57 | 130 | 581 | 653 | 628 | 662 | **126.7%** | **4.4%** |
| *Mostly rural* | 14 | 25 | 90 | 116 | 217 | 217 | 235 | **104.0%** | **26.6%** |
| Districts | 8 | 11 | 9 | 34 | 37 | 37 | 35 | **65.3%** | **0.9%** |
| **Total** | **1 960** | **3 206** | **4 243** | **5 131** | **7 996** | **8 275** | **8 893** | **37.8%** | **20.1%** |

*Source: National Treasury local government database*

The above table indicates that municipal income from solid waste services has been growing very rapidly. Most of this growth can be attributed to more complete reporting of this category of revenue as municipalities move to identify the streams of revenue associated with the respective trading services. Metros' revenue related to solid waste services is budgeted to grow by 26.8 per cent over the medium term.

Table 11.6 shows increases in user charges for a typical large and small household. Smaller households pay a larger share of their total municipal bill in refuse charges, though the tariff itself is lower.

**Table 11.6 Monthly account for an average household, 2009/10**

| Rand | Property rates | Electricity Basic levy | Electricity Consumption (per Kw) | Water Basic levy | Water Consumption (per Kl) | Sanitation | Refuse removal | Other | VAT on services | Total | Refuse as % of total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Large household**[1] | | | | | | | | | | | |
| Metros | 660 | 75 | 669 | 46 | 191 | 104 | 73 | – | 133 | **1 952** | 3.7% |
| Local municipalities | 324 | 106 | 645 | 41 | 151 | 81 | 75 | – | 163 | **1 587** | 4.7% |
| **Small household**[2] | | | | | | | | | | | |
| Metros | 304 | 59 | 318 | 146 | 148 | 98 | 50 | – | 83 | **1 206** | 4.1% |
| Local municipalities | 86 | 77 | 291 | 36 | 96 | 63 | 55 | – | 98 | **802** | 6.8% |

*1. Use as basis 1000m$^2$ erf, 150m$^2$ improvements, 1000 units electricity and 30kl water.*
*2. Use as basis 300m$^2$ erf, 48m$^2$ improvements, 498 units electricity and 25kl water.*
*Source: National Treasury local government database*

*This under-recovery of costs requires subsidies from the municipal rates account*

A striking feature of most municipalities' budgets for solid waste is that budgeted revenues (see table 11.5) do not cover budgeted expenditures (see table 11.7). This is even evident at the aggregate level, where total operating revenue in 2009/10 was 43 per cent less than total operating expenditure on solid waste services. Although the aggregate figures show a surplus over the medium term, this is largely due to the metros, while most of the remaining municipalities continue to show deficits. This under-recovery of costs means municipalities have to subsidise the service from other revenue sources, most notably rates revenues. Deficits are particularly prevalent among the smaller municipalities

*On aggregate, municipalities are under-pricing their solid waste services*

This means that, in aggregate, municipalities are under-pricing their solid waste services. This under-pricing is likely to be significant as the full costs of service delivery are not necessarily properly recorded for the sector due to current accounting practices, nor are current or historical capital costs necessarily fully apportioned to the sector. This under-pricing sends inappropriate signals to households and other waste generators about the cost of their activities, resulting in limited incentives for waste minimisation.

**Tariff setting approaches for solid waste**

Most municipalities charge for refuse removal through a fixed monthly rate. This is based either on the nature of the service, property values or property sizes. At the household level this direct charge to consumers does not vary by the amount of waste generated. This system is administratively easy to manage. These tariff structures provide no incentives for waste minimisation by consumers, as they seek to reflect the average cost of service for all customers, irrespective of the amount of waste each customer producers.

Property-based tariff structures are based on the assumption that the size and / or value of a property influences the amount of waste produced. Service based tariff structures vary by the size of bin, but typically without encouraging households to reduce bin sizes.

Tshwane has recently introduced a volumetric charge for refuse services. This is intended to provide strong incentives for consumers to reduce the amount of waste set out for collection. Volumetric charging is administratively more complex, requiring recording and billing of individual household waste disposal. This scheme is new, and its impacts on household waste management behaviour (in particular their sensitivity to price) still needs to be evaluated.

However, in addition to refuse removal charges, there are a range of other potential revenue streams in the management of solid waste that municipalities need to explore: landfill dumping fees, hazardous waste disposal fees, fines for littering and illegal dumping, recycling concessions, sale of compost produced from organic waste, revenues from using waste for electricity generation and the earning of carbon credits. Generally, municipalities need to pay more attention to optimising their revenues from these other sources.

## Solid waste expenditures

The following table shows budgeted operating expenditure for the solid waste function.

**Table 11.7 Budgeted operating expenditure for the solid waste function by category of municipality, 2006/07 – 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth 2006/07 - 2009/10 | % Average annual growth 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| **Operating expenditure** | | | | | | | | | |
| Metros | 2 837 | 3 412 | 3 908 | 4 639 | 3 219 | 3 619 | 4 029 | 17.8% | -4.6% |
| Local municipalities | 715 | 806 | 1 510 | 2 584 | 3 128 | 3 126 | 3 357 | 53.4% | 9.1% |
| *Secondary cities* | 523 | 588 | 965 | 1 404 | 1 548 | 1 544 | 1 709 | 39.0% | 6.8% |
| *Large towns* | 133 | 133 | 341 | 434 | 709 | 718 | 743 | 48.4% | 19.7% |
| *Small towns* | 43 | 51 | 117 | 565 | 704 | 698 | 729 | 136.1% | 8.9% |
| *Mostly rural* | 16 | 35 | 87 | 181 | 166 | 166 | 175 | 122.8% | -1.1% |
| Districts | 9 | 10 | 56 | 82 | 20 | 23 | 25 | 111.4% | -32.5% |
| **Total expenditure** | **3 561** | **4 228** | **5 474** | **7 305** | **6 367** | **6 768** | **7 411** | **27.1%** | **0.5%** |

*Source: National Treasury local government database*

As with revenue, the above table indicates that municipal expenditure on solid waste services has been growing very rapidly. Again, most of this growth can be attributed to more complete reporting by municipalities. Metros' budgeted expenditure for solid waste services grew by 17.8 per cent between 2006/07 and 2009/10, but is set to decline by 4.6 per cent over the medium term, driven by a sharp decline in budgets in 2010/11. The erratic budgets for the districts are largely due to incomplete reporting, and poor quality budgeting.

Very few municipalities are setting aside funds (in dedicated cash-backed reserve funds) for the rehabilitation and management of their landfill sites once they reach the end of their useful lives.

The main cost drivers in solid waste management are labour, transport and repairs and maintenance.

### *Labour costs*

*10 per cent of the municipal workforce, or 25 450 people, were employed in solid waste management activities in 2007*

10 per cent of the municipal workforce, or 25 450 people, were employed in solid waste management activities in 2007, of which 34 per cent were employed in the metros. Over 75 per cent of personnel were in full-time positions. Municipalities reported 20.9 per cent vacancies against established posts in the sector in 2007. Over a quarter of vacant posts (2 259 positions) were reported in metros. These figures exclude the staff employed in instances where the function has been outsourced. Consequently the total number of people employed in this function is higher than the above figures indicate.

According to information from the Department of Environmental Affairs and Tourism in 2007 municipalities employed on average 4.8 staff per 1 000 customers. This figure varies significantly between municipalities, with metros employing on average 1.5 staff per 1 000 customers, and rural municipalities employing 6.5 staff. A strong negative correlation exists between the size and density of settlement and the number of staff employed. This can be attributed to economies of scale and efficiencies associated with servicing denser settlements.

*The absence of adequate managerial capabilities in smaller municipalities is a significant concern*

The Department of Environmental Affairs and Tourism[8] also noted that local municipalities tend to have much smaller 'intermediate' staff complements than metros, and that the proportion of labourers in the total staff complement rises as settlements become more dispersed. While differing operational requirements may partially explain this trend, the absence of adequate managerial capabilities in smaller municipalities is cause for concern.

### *Waste transportation and disposal*

*Significant costs are associated with the transport of waste*

Significant costs are associated with transporting waste from collection points to disposal sites. Information collected by Statistics South Africa indicates that annual capital expenditure on specialised vehicles in the refuse sector averages R127 million between 2005/06 and 2010/11, accounting for nearly 20 per cent of total capital spending in waste sector.

Industry experts estimate that transport costs amount to 45 per cent of total operating costs of the function. This estimate includes transport costs associated with collection and excludes disposal costs, and is composed of truck costs of 26 per cent and fuel costs of 19 per cent. However, current data from municipalities indicate that expenditures that can be associated with transportation activities account for less than 10 per cent of the function's operating expenditures. This suggests significant under-reporting of these expenditures.

The Department of Environmental Affairs and Tourism reports that the total municipal waste fleet amounts to 44 225 vehicles. Over 50 per cent of these vehicles are owned by secondary cities, with another 29 per cent stationed in large towns. Unsurprisingly, these municipalities also record the lowest productivity per vehicle in terms of consumers served, with secondary cities serving 62 consumers per vehicle and large towns 49.

**Table 11.8 Municipal waste fleets, 2007**

| | Total Waste Fleet function | Consumers per vehicle |
|---|---|---|
| Metros | 5 546 | 786 |
| Secondary cities | 22 522 | 62 |
| Large towns | 12 935 | 49 |
| Small towns | 3 208 | 375 |
| Mostly rural | 14 | 32 362 |
| **Total** | **44 225** | **182** |

*Source: Calculated from DEAT (2007)*

Transport costs are ultimately a function of the distance travelled between the point of waste collection and disposal. As distance rises, fuel and maintenance costs also rise, while additional staff and fleet are needed to accommodate expanded travel times. A conservative

[8] Department of Environmental Affairs and Tourism. Assessment of the status of waste service delivery and capacity at the local government level. Directorate: General Waste Management, August 2007, Draft 3

estimate of the cost implications of expanding transport distances to disposal sites from 20km to 100km indicates that costs may rise by 50 per cent, while costs to households may rise by over 25 per cent. This suggests that the regionalisation of waste services, and particularly the location of dump sites, requires careful cost-benefit evaluation.

**Table 11.9 Cost implications of increased distance to disposal sites**

| | 20 km | 100 km | % change |
|---|---|---|---|
| Number of trips | 3 | 2 | -33.3% |
| Monthly km travelled | 3 140 | 13 700 | 336.3% |
| Monthly bulk transport cost (Rand) | 143 939 | 215 909 | 50.0% |
| Monthly total cost per household (Rand) | 24.67 | 30.96 | 25.5% |

*Source: Scenarios based on cost evaluation of Mafikeng domestic solid waste services pilot, which provided services to 35 000 households*

### *Capital expenditure*

*Overall, municipalities place little priority on solid waste investments in their capital budgets*

Solid waste services do not require network infrastructure such as electricity, water and sanitation services. Therefore the level of capital investment required to provide the service is far lower than for the other basic services, consisting largely of specialised vehicles (dump trucks) and equipment to compact and cover the waste at landfill sites (mainly bulldozers). Where a municipality invests in, say, a methane driven generation plant, that investment would be classified under electricity infrastructure. It is therefore to be anticipated that capital spending on solid waste services will only represent a relatively small percentage of overall municipal capital budgets. Nevertheless, among small municipalities the purchase of a single dump truck can represent a very significant capital outlay, given the limited size of their capital budgets generally.

The following table shows capital budgets for the solid waste function grew very rapidly between 2006/07 and 2009/10 – at average annual rates of over 100 per cent. This growth can largely be attributed to more complete reporting, but there is no doubt that it has also been driven by municipalities expanding access to solid waste services.

**Table 11.10 Capital budgets for the solid waste function by category of municipality, 2006/07 – 2012/13**

| R thousand | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | % Average annual growth 2006/07 - 2009/10 | % Average annual growth 2009/10 - 2012/13 |
|---|---|---|---|---|---|---|---|---|---|
| **Budgeted capital expenditure** | | | | | | | | | |
| Metros | 102 430 | 174 093 | 513 795 | 523 963 | 650 985 | 720 647 | 651 183 | 72.3% | 7.5% |
| Local municipalities | 16 137 | 52 284 | 270 624 | 407 943 | 366 241 | 301 692 | 256 884 | 193.5% | -14.3% |
| *Secondary cities* | 13 976 | 43 856 | 128 771 | 222 442 | 170 369 | 145 229 | 100 234 | 151.5% | -23.3% |
| *Large towns* | 351 | 7 690 | 36 340 | 48 055 | 61 740 | 65 609 | 82 335 | **415.3%** | **19.7%** |
| *Small towns* | 1 810 | 738 | 76 210 | 77 530 | 86 288 | 71 568 | 55 232 | **249.9%** | **-10.7%** |
| *Mostly rural* | – | – | 29 303 | 59 916 | 47 844 | 19 286 | 19 083 | - | **-31.7%** |
| Districts | – | – | 23 | 18 909 | 62 596 | 62 895 | 60 028 | - | **47.0%** |
| **Total expenditure** | **118 568** | **226 377** | **784 443** | **950 815** | **1 079 822** | **1 085 234** | **968 095** | **100.2%** | **0.6%** |
| *Percentage of total municipal capital expenditure* | 0.6% | 0.8% | 1.9% | 2.3% | 2.6% | 2.8% | 2.4% | | |

*Source: National Treasury local government database*

Over the medium term capital spending on solid waste services grows at a far more moderate pace, and even declines in certain categories of municipality. Among the metros, growth stabilises at 7.5 per cent per year.

### Financing requirements for municipal solid waste services

The Department of Environmental Affairs and Tourism has estimated financing requirements for the provision of solid waste services at the municipal level using a municipal services financial model. The model projects capital and operating costs associated with the provision of municipal services. This helps to assess the appropriateness and affordability of addressing municipal infrastructure investment needs, such as extending services or rehabilitating assets.

The model projects an average annual capital expenditure requirement of between R1.4 billion to R1.6 billion, or a total of R14.2 billion to R16.4 billion over the 10-year period. In 2010/11, budgeted capital expenditure levels were about 75 per cent of the lower of these target levels. However, capital spending may not be taking place in the municipalities where it is most required. In these municipalities the capital investment requirements of the function need to be re-evaluated and raised in priority relative to other areas of capital spending, especially projects that do not relate to the provision of basic services.

*The funding model developed by the Department of Environmental Affairs highlights the critical state of financing in the solid waste sector*

The model also highlights the critical state of financing in the solid waste sector, relative to policy intentions. Capital and operating expenditures are both lower than the levels estimated to ensure high levels of access. The model suggests there is substantial subsidy leakage to non-poor consumers, and user charges are too low. As with other municipal functions, there is an urgent need to assess the sustainability of the solid waste services, and ensure tariffs and revenue management strategies cover the cost of the service.

## Waste minimisation, recycling and energy recovery

*South Africa has experienced rapid growth in waste volumes, associated with a prolonged period of economic growth*

South Africa has experienced rapid growth in waste volumes, associated with a long period of economic growth. About 42 million cubic metres of general waste required collection and disposal in 1997. Gauteng, which generates 42 per cent of South Africa's waste, reported a growth in waste volumes of over 365 per cent between 2004 and 2008, averaging 79 per cent per year. In 1997, it was predicted that total general waste generation would be 68 million cubic metres in 2010,[9] however it would seem this is a serious under-estimate. It is envisaged that the waste information regulations will improve the future availability of data on waste management.

[9] Department of Water Affairs and Forestry. Waste generation in South Africa (Baseline study in preparation for the national waste management strategy for South Africa). 2001.

**Table 11.11 General waste generation by province in 1997 (estimated) and 2010 (projected)**

| Province | 1997 m³ | 1997 % of total | 2010 m³ | 2010 % of total | Total growth % | Annual average growth % |
|---|---|---|---|---|---|---|
| Eastern Cape | 2 281 000 | 5.4% | 3 105 989 | 4.5% | 36.2% | 2.6% |
| Free State | 1 674 000 | 4.0% | 3 877 380 | 5.6% | 131.6% | 7.3% |
| Gauteng | 17 899 000 | 42.4% | 26 085 304 | 38.0% | 45.7% | 3.2% |
| KwaZulu-Natal | 4 174 000 | 9.9% | 5 749 959 | 8.4% | 37.8% | 2.7% |
| Limpopo | 3 831 000 | 9.1% | 11 200 387 | 16.3% | 192.4% | 9.4% |
| Mpumalanga | 733 000 | 1.7% | 956 369 | 1.4% | 30.5% | 2.2% |
| Northern Cape | 1 470 000 | 3.5% | 2 374 864 | 3.5% | 61.6% | 4.1% |
| North West | 1 625 000 | 3.8% | 2 296 489 | 3.3% | 41.3% | 2.9% |
| Western Cape | 8 543 000 | 20.2% | 12 979 785 | 18.9% | 51.9% | 3.5% |
| **Total** | **42 230 000** | **100.0%** | **68 626 526** | **100.0%** | **62.5%** | **4.1%** |

*Source: DWAF, 2001 and own calculations*

Economic growth and demographic change have quickened the pace at which waste is being generated. Urban residents typically generate more waste than their rural counterparts. Urban household waste also is less conducive to on-site disposal, due to settlement density, and thus these households contribute greater volumes to the waste stream.

*There have been few efforts to encourage households to minimise the generation of waste*

There have been few efforts to encourage households to minimise the generation of waste. The Department of Environmental Affairs and Tourism (2007) reports that 87 per cent of municipalities lack capacity and infrastructure to pursue waste minimisation strategies. Some municipalities do provide incentives for waste minimisation, though this is neither widespread nor effective. Johannesburg theoretically limits each household to two bags of waste per week, though for reasons of public health, this is not enforced. As noted, Tshwane has recently introduced volumetric user charges that discriminate between households on the basis of the volume of waste produced. Cape Town metro reports that, in 2006/07, 14 per cent of waste was diverted from landfill sites, and was recycled or reused.

Waste management services rely heavily on landfills for the disposal of waste, which account for 80 percent of currently licensed waste facilities. In Gauteng, waste going to landfills comprises the vast majority of all waste disposed or recycled, and has grown at an average annual rate of 66 per cent since 2004, while waste generated has grown at an average of 37 per cent a year. This is despite the existence of a range of alternative disposal technologies, including waste incineration and recycling.

The Department of Environmental Affairs and Tourism reported in 2007 that there are over 2 000 waste handling facilities nationally, of which only 530 are licensed. Licensing of dump sites in mostly rural municipalities and secondary cities is limited, at 13 per cent and 68 per cent respectively. Landfills differ markedly in size, with larger landfills typically being operated by the large cities.

About 95 per cent of all South Africa's waste is disposed of in landfill sites. This reliance on landfills has limited the incentive to devise alternative methods of dealing with waste. In Gauteng, it is estimated that only 2.2 per cent of waste collected is sent for recycling. It is estimated that only approximately 20 per cent of household waste is recycled in South Africa (presumably mainly prior to collection from households). It is envisaged that the move towards making industries responsible for their products once they become waste will improve recycling rates in future.

*An estimated 18 recycling facilities have been permitted nationwide*

Only 18 recycling facilities have been licensed nationwide, ranging from the 5 Buyisa-e-Bag plastic bag recycling facilities in Gauteng to multi-purpose privately owned facilities. Many additional facilities appear to exist, although these are not recorded on the permit database. One large South African firm reports collecting in excess of 1.5 million tons of recyclables each year.

*Some municipalities have begun waste-to-energy schemes*

Some municipalities have begun waste-to-energy schemes. eThekwini is extracting landfill gas and generating electricity from the Marian Hill and La Mercy landfills. More recently, Johannesburg has piloted energy generation from incinerating waste. Energy recovery schemes are strongly incentivised by the potential to generate carbon credits and their associated revenues. Eskom estimates that landfill energy plants can have a capacity of between 20 and 50 megawatts, with a life-of-plant of 30 years.

## Conclusion

Municipalities are facing the challenge of rising unit costs and falling per capita revenues associated with expanded access to services. This may slowdown the pace at which services are expanded to unserviced households and a growth in uncontrolled dumping, and littering that will inflate operating costs for municipalities or exacerbate environmental damage. It is also possible that efforts to bring down the unit cost of the service will result in greater mechanisation that may reduce jobs in the sector. Already there is evidence that larger municipalities have significantly mechanised their operations. Municipalities are also seeking ways to reduce subsidy leakage through improved targeting.

Municipalities and industries currently do not give sufficient attention to waste minimisation. This impacts negatively on their operating and capital cost structures associated with collection, transport and disposal. It also militates against the achievement of the waste minimisation targets of the Polokwane Declaration on Waste Management (2001). The introduction of volumetric user charges by Tshwane, however, offers some prospect of reversing this situation and may provide a precedent for other municipalities to follow. In addition the move towards producer responsibility seeks to place greater responsibility for promoting recycling on industries in line with the producer responsibility approach.

There is a need to establish differentiated targets on basic access to services that take account of varying municipal contexts and capacities. Greater differentiation and improved specification of the targets for municipal service provision will provide an important focus to their strategies to expand access and improve the quality of service delivery.

12

# Delivering municipal services in rural areas

## Introduction

According to Global Insight's 2009 estimates, 15.9 million South Africans live in poverty; and of these, 11 million people, representing 69 per cent of all South Africans that live in poverty, live in rural areas. Poor households in rural areas depend on a combination of subsistence agriculture, social grants and remittances from family members working in the cities or mines. Household assets are often tied to traditional forms of land tenure, making it difficult for households to leverage their assets to generate wealth. The challenges of poverty and unemployment are compounded by limited access to basic municipal services such as water, sanitation and electricity, as well as a lack of good quality social services (education, health and ambulances) and transport services (roads and buses).

By providing basic services effectively, leveraging municipal spending to create local jobs, and facilitating local economic development (LED), rural municipalities can play a very important role in alleviating the worst forms of poverty and facilitating development in rural areas. However it needs to be emphasised that municipalities are not solely responsible for addressing the enormous challenges of rural poverty and rural development. Indeed, the sustainability of rural municipalities themselves is dependent on overall government policy on rural areas, and the development of rural economies.

*The sustainability of rural municipalities themselves is dependent on overall government policy on rural areas, and the development of rural economies*

Government policy, initially through the rural development strategy (1995) and the rural development framework (1997), began the process of prioritising the transformation of rural areas from 'surplus labour reserves' into dynamic local economies that are able to provide sustainable self-employment opportunities and remunerative jobs. A number of rural development programmes are currently pursuing this objective, including land reform and restitution programmes and various LED initiatives. The critical challenge in the short term is to ensure that municipal spending is aligned with local developmental needs and priorities. In the medium term, rural municipalities need to ensure that they raise own revenues in accordance with their fiscal capacity so as to reduce their dependence on national transfers, and optimise their ability to deliver services and facilitate development.

This chapter reviews:

- the definition of a rural municipality in South Africa
- the demographic, social and economic profile of rural municipalities, and the state of service delivery
- debates on rural development and the role of rural municipalities in LED
- emerging lessons from municipal LED programmes.

## Defining rural areas and municipalities

*The re-demarcation of municipal boundaries has complicated the administrative determination of what constitutes a rural area and, by extension, a rural municipality*

The transformation of local government after apartheid led to a large scale re-demarcation of municipal boundaries. This process removed the administrative distinction between urban and rural areas, recognising the strong inter-linkages between towns and the countryside. While this has been a largely positive development, it has complicated the administrative determination of what constitutes a rural area and, by extension, a rural municipality.

The rural development framework (1997) defined rural areas as having the following two characteristics:

- sparsely populated areas in which people farm or depend on natural resources, including villages and small towns that are dispersed through these areas
- areas that include large settlements in the former homelands, which depend on migratory labour and remittances as well as government social grants for their survival, and typically have traditional land tenure systems.

*The constitutional classification of municipalities does not distinguish between municipalities in urban and rural areas*

The constitutional classification of municipalities does not distinguish between municipalities in urban and rural areas. Outside of metropolitan municipalities, the only distinction made is between local (category B) and district (category C) municipalities. It is also important to note that many large urban municipalities, such as eThekwini and Tshwane metros, contain areas that are functionally rural.

The primary mechanism used in this *Review* and elsewhere to define rural municipalities is the methodology adopted by the Department of Cooperative Governance. This method is based on the context within which municipalities operate and uses variables such as the number of poor households, the proportion of households with access to services (water, sanitation and electricity), and information on capital and operating budgets to group municipalities in seven different categories.

**Table 12.1 Classification of municipalities into categories for analysis**

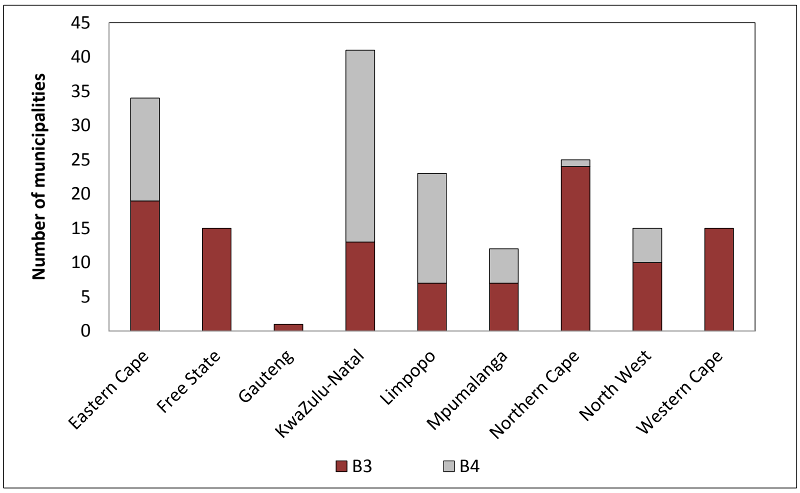
| Class | Characteristics | Number |
|---|---|---|
| **Metros** | Category A municipalities | **6** |
| **Secondary cities (B1)** | All local municipalities referred to as secondary cities | **21** |
| **Large towns (B2)** | All local municipalities with an urban core. There is huge variation in population sizes amongst these municipalities and they do have large urban dwelling population. | **29** |
| **Small towns (B3)** | They are characterised by no large town as a core urban settlement. Typically, these municipalities have a relatively small population, a significant proportion of which is urban and based in one or more small towns. Rural areas in this category are characterised by the presence of commercial farms, as these local economies are largely agriculturally based. The existence of such important rural areas and agriculture sector explains its inclusion in the analysis of rural municipalities. | **111** |
| **Mostly rural (B4)** | These are characterised by the presence of at most one or two small towns in their areas, communal land tenure and villages or scattered groups of dwellings and typically located in former homelands | **70** |
| **Districts (C1)** | District municipalities that are not water services providers. | **25** |
| **Districts (C2)** | District municipalities that are water service providers | **21** |

*Source: Palmer Development Group (PDG)*

*Rural municipalities are concentrated in KwaZulu-Natal, Eastern Cape, Northern Cape and Limpopo*

Rural municipalities are those classified as B3 (small towns) and B4 (mostly rural) municipalities in the typology outlined in Table 12.1. The geographic location of B3 and B4 municipalities largely corresponds with the definition of rural areas provided in the rural development framework. They are concentrated in KwaZulu-Natal, Eastern Cape, Northern Cape and Limpopo, as illustrated in figure 12.1. Free State, North West, Mpumalanga, and Western Cape also host some rural (mostly B3) municipalities.

**Figure 12.1 Number of rural local municipalities per province**




*Source: PDG's classification of municipalities*

## The demographic, social and economic context of rural municipalities

### Human settlement characteristics in rural municipalities

*There are significant differences in settlement types between B3 and B4 municipalities*

There are significant differences in settlement types between B3 and B4 municipalities. Statistics South Africa reported in Census 2001 that 52 per cent of households in B3 municipalities live in small urban settlements, 29 per cent on farms and 10 per cent in settlements located on tribal land. In B4 municipalities, 83 per cent of households live in tribal settlements, while only 7 per cent live on farms and in small towns respectively.

### Demographic and education profile

*The economically active population (measured as the population aged 20 to 64 years) in rural municipalities is considerably smaller than in urban areas*

Rural municipalities are home to larger numbers of women than men, and to generally younger populations than urban municipalities. Women account for 54 per cent of the population in B4 municipalities and 52 per cent in B3 municipalities. The economically active population (measured as the population aged 20 to 64 years) in rural municipalities is considerably smaller than in urban areas. This population accounts for 41 per cent of people in B4 municipalities and 51 per cent in B3 municipalities, while it accounts for 60 per cent of the population in urban areas. Young people under the age of 20 account for 52 per cent of the population in B4 municipalities and 43 per cent in B3 municipalities, against only 36 per cent in urban municipalities, as indicated in table 12.2 below.

**Table 12.2 Demographic profile of urban and rural municipalities**

| | B4 | B3 | Urban (Top 27) | South Africa |
|---|---|---|---|---|
| Population / population SA | 27.0% | 13.0% | 52.0% | |
| Male Population / population SA | 46.0% | 48.0% | 49.0% | 48.0% |
| Female population / population SA | 54.0% | 52.0% | 51.0% | 52.0% |
| Population 0 - 19 yrs / population SA | 52.0% | 43.0% | 36.0% | 42.0% |
| Population 20 - 64 yrs / population SA | 41.0% | 51.0% | 60.0% | 53.0% |
| Population 65 yrs and older / population SA | 6.0% | 6.0% | 5.0% | 5.0% |
| Population aged 20 yrs and older w ith no school qualification | 10.0% | 8.0% | 3.0% | 6.0% |
| Population aged 20 yrs and older w ith at least matric | 7.0% | 23.0% | 22.0% | 16.0% |

*Source: Stats SA, Community Survey 2007*

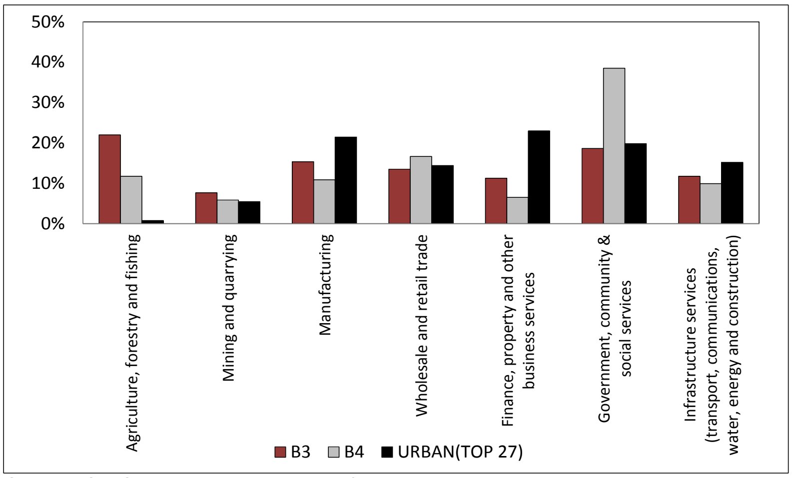
*People in rural municipalities are also less likely than their urban counterparts to have school qualifications*

Table 12.2 shows that people in rural municipalities are also less likely than their urban counterparts to have school qualifications. 10 per cent of the population over 20 years old in B4 municipalities, and 8 per cent in B3 municipalities, have no school qualifications, compared to only 3 per cent in urban areas.

### The economic profile of rural municipalities

Figure 12.2 shows that the economies of rural areas are less diversified than their urban counterparts.

**Figure 12.2 Share of GVA by sector in rural and urban areas**




*Source: SA Geospatial Analysis Platform, 2004*

In B4 municipalities, government, community and social services contribute more than 35 per cent to total gross value added (GVA). Agriculture contributes 20 per cent to GVA in B3 municipalities, reflecting the presence of commercial farming in these areas, while it only contributes 10 per cent to GVA in B4 municipalities. Wholesale and trade, infrastructure and manufacturing are also significant contributors to GVA in all rural (B3 and B4) municipalities.

*The economies of rural areas are less diversified than their urban counterparts*

Total GVA in rural municipalities grew in real terms from 2005 until 2008, after which a slight decline was recorded as the economic downturn impacted on rural areas. The increase was driven by growth in the manufacturing sector, while core rural sectors such as agriculture remained constant. Projections of GVA to 2012 suggest that rural growth will resume, though at lower rates than in urban areas. While the growth in GVA will be accompanied by a similar growth in rural household incomes, it is likely to be concentrated in B3 municipalities.

Formal employment opportunities in rural areas are limited, often to seasonal employment. It is therefore not surprising that the average levels of unemployment in the B3 municipal areas is 23 per cent and 36 per cent in the B4 municipal areas using the official (or narrow) definition of unemployment.

*Formal employment opportunities in rural areas are limited, often to seasonal employment*

Development strategies need to account for wide variations in demographic, social and economic contexts and needs as well as available institutional capacities.

*Development strategies need to account for wide variations in demographic, social and economic contexts and needs as well as available institutional capacities*

Rural municipalities are not homogenous, and development strategies need to account for wide variations in demographic, social and economic contexts and needs as well as available institutional capacities. For example, many B3 municipalities have active agricultural sectors that carry significant development potential but would require concomitant improvement in extensions of farmer support services for emerging farmers. Other areas may need to focus on human capital development, specifically in areas of women's health and education.

## Rural development and local government

Successful rural development is critical for the long term sustainability of rural municipalities. Vibrant local economies generate both demand for basic municipal services and the resources to pay for them. Government has identified rural development as a key priority area and the Department of Rural Development and Land Affairs has been created to focus specifically on this issue.

*Municipalities are responsible for the effective provision of basic services, and associated support to local economic development*

Rural development is a broad concept (see text box) that engages agencies across the public and private sectors. Municipalities have two core responsibilities with respect to rural development: the effective provision of basic services, and associated support to local economic development (LED). Other agencies in national and provincial government, state-owned enterprises and the private sector also need to contribute in their areas of responsibility.

**Defining rural development**

Rural development is typically defined according to the mechanisms and goals of development. In the 1970s it was defined as a structural transformation of the rural economy as it diversified from agriculture. Another important school of thought defined rural development by focusing on the provision of social services to the rural poor. This definition was based on the fact that even under rapid growth of income in rural areas, the equitable access to social services was not necessarily guaranteed. The definition of rural development has expanded to include the development of human capital, through social services such as education and health, improvement of standards of living.

The South Africa Rural Development Quarterly[10] defines rural development as 'positive advancement of communities in rural areas through improvement of rural institutions and systems, expansion of rural infrastructure, and growth in rural economic activities'. This definition recognises that rural development is not just about agricultural activities but includes poverty alleviation, infrastructure provision and other actions to uplift the economic status of people in rural areas.

Current government policy on rural development is informed by the comprehensive rural development strategy. This strategy establishes agrarian transformation and land reform as pillars of rural development, alongside infrastructure provision (such as. schools, clinics, boreholes and water reticulation systems) that can support both agricultural development and basic service delivery to rural households. This implies an important role for local government, working in conjunction with other actors.

### Access to basic services in rural areas

*The provision of basic services can be an important agent in the reduction of poverty and unemployment and strengthening of social capital*

The provision of basic services can be an important agent in the reduction of poverty and unemployment and strengthening of social capital. It can also be a factor in reviving agriculture, tourism and other rural non-farm enterprises. For instance:

Road infrastructure connects rural areas to urban centres and facilitates the mobility of goods and people within the area. Roads provide the connections necessary for local markets to develop and facilitate the provision of public services, such as ambulances and policing. Good feeder roads (access roads) can allow the supply of perishable foods to high-value urban markets. Opportunities for job creation through labour based maintenance approaches can also

[10] South Africa Rural Development Quarterly, volume 2, first quarter, 2004.

support household income and retain resources in local areas. The lack of road infrastructure hinders development.

The supply of water infrastructure, depending on the nature and scale of technology, has great potential for stimulating small and large scale agricultural activities.

The importance of electricity infrastructure in rural areas cannot be over emphasised. Besides improving the lives of people, it can facilitate small business development.

Government has emphasised the critical role that rural municipalities must play in reducing backlogs in access to basic services. Careful choices need to be made to match service levels to what households can afford. The use of appropriate technologies is important in ensuring available resources are used optimally to meet households' needs.

Table 12.3 summarises the acceptable minimum levels of access to basic services as defined in various policy frameworks:

**Table 12.3 Basic service levels**

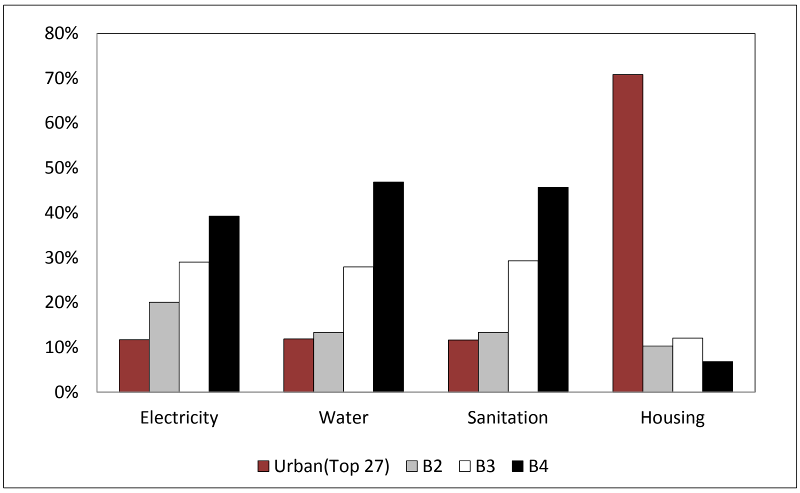
| Service Type | Level 1 Basic | Level 2 Intermediate | Level 3 Full |
|---|---|---|---|
| **Water** | Standpipes within 200 metres | Yard taps or tanks | In house water |
| **Sanitation** | Sewage collection/disposal | VIP Latrine Septic tanks | Full water borne |
| **Electricity** | 5-8 Amp or non-grid | 20 Amps | 60 Amps |
| **Roads** | Graded | Gravel | Paved/tarred & kerbs |
| **Stormwater** | Earth lined open channel | Open channel lined | Pipe and canal systems |
| **Solid Waste disposal** | Communal (Residents) | Communal (Contractors) | Kerbside collection |

### *Backlogs in service and infrastructure delivery*

Rural municipalities (both B3 and B4) have the highest number of backlogs in sanitation, electricity and water. This contrasts with large urban municipalities, where the lack of access to housing is a significant challenge, as figure 12.3 shows.

*Rural municipalities (both B3 and B4) have the highest number of backlogs in sanitation, electricity and water*

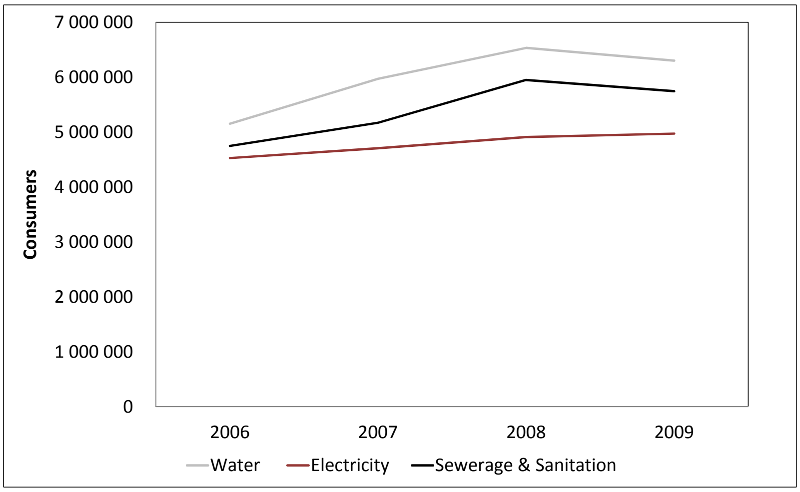
**Figure 12.3 Distribution of national service backlogs between urban and rural municipalities in 2007**




*Source: Stats SA, Community Survey 2007*

Recent trends in access to basic services in rural municipalities demonstrate a slowdown in delivery occurring in 2009 across all services. In small town (B3) municipalities, little growth in access was reported in 2009, other than in electricity provision. In mostly rural (B4) municipalities, a decline in access to water services was reported, as figure 12.4 shows. From 2008, service delivery in sanitation has not been growing. It is important to note that these municipalities (B4) depend mostly on government transfers to fund their capital programmes. Among these transfers, the most important is the municipal infrastructure grant (MIG).

**Figure 12.4 Number of consumers receiving services in B4 municipalities**




*Source: Stats SA, Non-Financial Census of municipalities*

*Concerns have been raised that the manner in which the MIG is designed and managed does not allow a sustainable eradication of backlogs in rural villages*

Significant progress has been made in delivering basic infrastructure in rural municipalities. However, there is still much to be done. The supply of these services has often been attempted using urban based technologies, which have proved expensive due to the dispersed nature of rural settlements. Concerns have been raised that the manner in which the MIG is designed and managed does not allow a sustainable eradication of backlogs in rural villages. Municipalities tend to use it for upgrading and rehabilitating network infrastructure in towns, because town-based households are more likely to be able to pay for services. There is also a general lack of familiarity with alternative, appropriate technology options that can be used to provide services to villages, given water shortages, low population density, and typology that render conventional technologies costly to install and operate.

### *Extending and sustaining access to basic services*

Extending and sustaining access to basic services in rural areas requires clear direction on:

First, a new consensus needs to be forged with rural communities on the necessity to use appropriate and affordable technologies. In many rural areas, networked services such as water-borne sewerage and piped water are simply too expensive to install, and unaffordable to operate. This needs to be recognised, and alternative technologies need to be used to optimise access given existing affordability levels, and the availability of resources.

Second, greater innovation is required in the development and deployment of technologies that are appropriate to rural areas. These include water harvesting, ground water supply through boreholes for water; on-site sanitation options, and non-grid energy options. If properly managed, these are not only environmentally friendly service options, but could provide a more efficient and affordable way of supplying rural services.

Finally, technical skills supporting infrastructure delivery are a scarce resource in the country, and even more so in rural areas where attracting these skills remains a challenge. New institutional models of service delivery are required that allow municipalities to leverage local knowledge and capacities.

*The rural households' infrastructure grant*

In 2010/11, government introduced the rural households infrastructure grant (RHIG) to fund rural infrastructure, in addition to the MIG. Government allocated R1.2 billion to cater for 56 selected municipalities over the 2010/11 MTEF. This grant focuses on the eradication of sanitation and water backlogs in rural municipalities using the on-site approach, such as the ventilated improved pit (VIP) latrines and rainwater tanks. The technologies envisaged will rely on rural communities to support the implementation of the programme, and they should be trained to manage the operation and maintenance of the installations. This could help municipalities find innovative ways of providing services while reducing the burden on their operating budgets.

*The rural households' infrastructure grant focuses on the eradication of sanitation and water backlogs in rural municipalities using the on-site approach*

## Local economic development activities by municipalities

Sections 152(1)(c) and 153 of the Constitution state that one of the objectives of local government is to promote social and economic development. These objectives are further articulated in the Municipal Systems Act (2000).

Since 1995, considerable energy and resources have gone into enabling municipalities to play a meaningful role in LED. The purpose of LED is to build up the economic capacity of a local area to improve residents' quality of life. It is a process by which public, business and social sector partners work collectively to create better conditions for economic growth and employment generation. While municipalities have a key role to play in LED, they generally do not have the resources necessary to implement large scale projects outside of strong partnerships with other public and private agencies. LED projects must complement a strategic regional economic strategy, and be individually evaluated in terms of their costs and benefits.

*The purpose of LED is to build up the economic capacity of a local area to improve residents' quality of life*

Government's new growth strategy highlights the potential of rural development as a driver of job creation. It emphasises the importance of developing a clear spatial development perspective to enhance rural development opportunities in relation to the real comparative advantages of local areas. In addition, the spatial perspective will set out opportunities available and the basis for government spending

*Government's new growth strategy highlights the potential of rural development as a driver of job creation* choices with respect to infrastructure, housing and local economic development initiatives. The strategy also emphasises the importance of investment in infrastructure for creating jobs.

## Municipal spending on LED

*Expenditure directed to LED initiatives is very limited compared to other service delivery priorities of local government*

Although LED has been identified as a key role for local government, expenditure directed towards LED initiatives is very limited compared to other service delivery priorities of local government. On average, approximately less that 1 per cent of the operating budgets of municipalities is directed towards LED initiatives, either directly or through municipal entities (development agencies). Initiatives vary from tourism to agriculture, depending on the geographical location and comparative advantages of the municipality. For instance, most coastal municipalities' LED initiatives are focused on tourism development and urban regeneration initiatives that will further attract investment and tourism.

A portion of the MIG may be used to support LED-related investments in economic infrastructure in line with the municipality's integrated development plan (IDP).

### *Neighbourhood development partnership grant*

*The neighbourhood development partnership grant seeks to improve the quality of life of households through the creation of economically viable and sustainable community and business infrastructure*

The neighbourhood development partnership grant (NDPG) is another conditional grant to municipalities, established in 2006. The grant seeks to improve the quality of life of households through the creation of economically viable and sustainable community and business infrastructure. It has an LED bias as it supports investments intended to promote participation in LED initiatives. The grant is targeted at mostly those municipalities with the largest concentrations of people living in poverty, so as to capitalise on economies of scale, or a critical mass of people needed for sustaining particular kinds of developments.

**NDPG case study: Ngangelizwe township regeneration, King Sabata Dalindyebo local municipality (KSD) in Mthatha**

KSD local municipality was awarded a neighbourhood development partnership grant to the value of R59 million (R10.8 million of technical assistance and R48.2 million of capital grant) to leverage further public and private sector investment in Ngangelizwe. Leveraging to the value of R1.3 billion is currently secured in letters of intent as part of the municipal drive to attract investment into the township. KSD developed a township regeneration strategy that focuses on developing a number of prioritised neighbourhood nodes. Some of the projects include the construction of a business site for light industry, developing sporting facilities and upgrading health facilities. This is part of an initiative facilitated by the Sustainable Communities initiative of the Development Bank of Southern Africa, and it hinges on a social compact signed with the local participating communities. It is therefore a people-driven approach focusing on participation, adding value and training support to existing SMMEs in the township. It also adds to existing services, for example, by upgrading and extending the local clinic in partnership with the Eastern Cape Department of Health, and renovating and upgrading the sports facilities through a partnership with the private sector.

Key to the KSD approach is to view the re-development as 'not business as usual' but to allow space for new and innovative approaches to support improved service delivery. In this instance, the Department of Human Settlements supports the use of alternative technologies to deliver a more sustainable neighbourhood by incorporating solar energy and labour intensive construction approaches that support local SMME development.

The neighbourhood development partnership grant targets about 54 per cent of South Africa's poorest people, with R5.2 billion allocated to metros and secondary cities and a further R3.6 billion allocated to other areas, including rural municipalities, as indicated on table 12.4. The grant is currently not open for new applications.

**Table 12.4 Neighbourhood development partnership grant awards per type of municipality**

| Category | Type of municipality | Number of type | Number of NDPG municipa-lities | No of program-mes | NDPG allocation (R bn) | As % of NDPG committed | No of people in poverty (millions) |
|---|---|---|---|---|---|---|---|
| A | Metros | 6 | 6 | 35 | 3.44 | 39 | 3 |
| B1 | Secondary Cities | 21 | 11 | 14 | 1.74 | 20 | 2 |
| B2 | Large towns | 29 | 11 | 12 | 0.82 | 9 | 1 |
| B3 | Small towns | 111 | 11 | 11 | 0.66 | 7 | 0 |
| B4 | Mostly rural | 70 | 12 | 12 | 1.47 | 17 | 2 |
| C | Districts | 46 | 6 | 6 | 0.69 | 8 | 2 |
| **Total** | | **283** | **57** | **90** | **8.82** | **100** | **11** |

*Source: National Treasury local government database*

## *Expanded public works programme*

*To date, municipalities have not taken significant advantage of the expanded public works programme*

The expanded public works programme is a government wide programme that focuses on the creation of work opportunities through infrastructure delivery. The programme provides dedicated resources to provincial and local governments for labour-intensive programmes for the building of roads, environmental projects, water, sanitation and other social and economic services. It also supports the development of permanent capacity for the maintenance of infrastructure on a sustainable basis, the provision of community services in health, welfare and other areas and investments in early childhood development programmes. Municipalities have, to date, not taken significant advantage of the expanded public works programme, implementing less than 13 per cent of the total number of projects (in number). The bulk of municipal activities have been in the infrastructure sector, often aligned with MIG projects. In 2008/09, a total of 1 866 infrastructure projects were reported to be linked to the programme, out of a total of 2 266 municipal infrastructure projects in that year.

*Rural municipalities, particularly in Eastern Cape and KwaZulu-Natal, have been the main beneficiaries of the expanded public works programme*

Rural municipalities, particularly in Eastern Cape and KwaZulu-Natal, have been the main beneficiaries of the expanded public works programme, although accurate data by municipality is not available. The programme's infrastructure sector created a cumulative total of over 1 million work opportunities between 2004/05 and 2008/09, surpassing a target of 750 000, as indicated on table 12.5.

**Table 12.5 EPWP work opportunities created, 2003/04 – 2009/10**

| | Target | 2004/05 | 2005/06 | 2006/07 Q2 | 2007/08 | 2008/09 |
|---|---|---|---|---|---|---|
| Infrastructure | 750 000 | 158 277 | 103 343 | 136 035 | 236 951 | 377 356 |
| Environment and culture | 200 000 | 58 796 | 78 855 | 117 502 | 115 686 | 96 882 |
| Social | 150 000 | 1 650 | 17 858 | 34 332 | 61 018 | 59 508 |
| Economic | 12 000 | 4 687 | 1 833 | 3 231 | 3 697 | 6 930 |
| **Annual total** | | **223 410** | **201 889** | **291 099** | **417 351** | **540 676** |
| **Cumulative total** | | | **425 299** | **716 399** | **1 133 749** | **1 674 425** |

*Source: Expanded Public Works Programme, Five Year Report 2004/05-2008/09*

### Other rural local economic development programmes

Rural municipalities are by no means the sole agency seeking to support rural LED. National and provincial governments, state-owned enterprises and the private sector are all involved in rural development initiatives. National and provincial government programmes include:

- *Land reform programmes:* The land reform programme is primarily focused on redressing the racially skewed patterns of rural land ownership that resulted from the forced removal of black communities from areas and black people being denied opportunities to own land. Land reform has three components:

    1. *Land restitution* aims at restoring land rights to people who were victims of land dispossession or giving them monetary compensation for the loss

    2. *Land redistribution* involves the state purchasing land and making it available to emerging farmers from previously disadvantaged groups, with a view to changing the composition of land ownership, and ensuring equitable access to land

    3. *Tenure reform* seeks to protect the land tenure rights of farm workers and communities, especially those living in commercial farming areas. However, the greatest challenges with land tenure are to be found in traditional areas.

- *Agricultural support programmes:* A successful agricultural sector provides employment opportunities, enhances national food security and creates markets for non-agricultural products. These programmes focus on improving the productivity of the agricultural sector. This requires effective farmer support programmes targeted at emerging commercial farmers and beneficiaries of land reform who are predominately in the B3 municipalities, and improving land utilisation for subsistence, especially in the B4 municipalities.

- *Tourism support programmes:* There is great potential for tourism in rural areas that are home to specific cultural, historical, ethnic and geographical (wildlife) features. These features can stimulate a wide range of tourist products, including community-based tourism, ecotourism, cultural tourism, adventure tourism, guest farms, backpacking, riding and agri-tourism. Three factors are critical for the development and success of rural tourism: first, clear forms of community participation and ownership of tourist products; second, adequate skills to provide necessary products and services; and third, local infrastructure development, including water, electricity, sanitation and road infrastructure.

- *Human capital development:* Sustainable rural development depends on the development of human capital. Municipalities can play an important support role, by ensuring that schools and health facilities are connected to roads, and have access to water, sanitation and electricity. Municipalities can also become directly involved, for instance by acting as agents for provincial health departments in managing clinics.

In addition to the initiatives of national and provincial government, a range of public entities and state-owned enterprises are also responsible for various LED initiatives. In certain instances these initiatives are part of the entities' corporate responsibility programme; in others, specific programmes have been established to offer technical support to municipalities and to provide financial support for the implementation of projects. The two main initiatives in this regard are:

*A range of public entities and state-owned enterprises are also responsible for various LED initiatives*

- *Agency development and support programme:* This is an initiative of the Industrial Development Corporation (IDC) that supports the establishment of local economic development agencies by municipalities. Currently, 32 such agencies are in the process of being established or are operational. There are, however, concerns that using the agency route creates another level of governance and bureaucracy which is costly to manage and dilutes the development impact.
- *Local economic development initiative:* This is a project of the DBSA that is currently being piloted in three municipalities. The aim of the project is to explore ways of implementing the following seven common development principles for effective LED: plotting the path; shifting stakeholder focus from the consumption economy to the productive economy; acknowledging the importance of a large, diversified economic development portfolio; identifying bold project; promoting and facilitating partnerships; facilitating improved municipal performance; and developing strategic policies to promote sound economic development.

Private sector initiatives in support of LED take a wide range of forms, ranging from initiatives by individual firms, farmers and churches, to research institutions and non-profit organisations focussing on particular aspects of development such as micro-finance, subsistence gardening, skills development etc. Examples of initiatives offering micro-finance assistance include the Women's Development Bank (WDB) and Project Imbizo of the Old Mutual Group.

*Private sector initiatives in support of LED take a wide range of forms*

**The natural fibre cluster in the Cacadu district municipality**

This LED project seeks to catalyse the growth of new industries based on innovative uses of natural fibres produced in the Eastern Cape region. It is a partnership between the CSIR, local government, other research organisations and the agricultural sector. It has explored how plant and animal fibres – including fibre from agave Americana plants, pineapples, wool and mohair – can be processed in innovative ways to develop new products. The aim is to create more profitable value chains by linking agricultural production with scientific research into new products. Thus far, the project has succeeded in revitalising the struggling pineapple industry in Eastern Cape, with the promise of major new revenue streams from extracting a range of new products fibre related products from the pineapple fruit and plant in addition to juice pulp. These products include dietary fibre used in food processing, enzymes and other cellulose material useful in pharmaceuticals, as well as fibre material that can be used to produce insulation panelling. It is anticipated that the commercialisation of these innovations will result in significant new investments in the region, which will also support job creation.

International donors also play a valuable role in funding and facilitating LED. For example, the EU LED support programmes operate in Eastern Cape, KwaZulu-Natal and Limpopo, providing both financial and technical support to municipalities, as well as private sector initiatives.

### Emerging lessons from municipal LED programmes

*Municipal LED activities have often met with only limited success*

Municipal LED activities have often met with only limited success. Very often this has been due to poor project selection, such as someone's pet project being chosen, which is later found to be unsustainable. In other instances, the programmes have been corrupted to serve the interests of particular individuals, rather than the community as a whole. And very often projects have failed due to poor implementation management.

The International Labour Organisation suggests that successful LED strategies have four dimensions:

- participation and social dialogue
- a clear location territory
- mobilisation of local resources and competitive advantages
- local ownership and management.

Careful analytical work is required to orient municipal activities towards real economic opportunities that are consistent with the development potential of the local economy. There is consensus that municipal LED strategies should aim to support rural people to participate more fully in the market economy, particularly by creating an enabling environment for both formal and informal business to operate. This suggests a threefold agenda for municipal LED strategies.

- The provision of municipal *infrastructure,* particularly access roads. The absence of essential infrastructure will tend to stifle economic development. This must also include the maintenance of infrastructure, which is often overlooked in LED initiatives.
- Putting in place a user-friendly *regulatory environment* that supports new investment. Key elements include having a clear spatial plan to guide development, and providing timely development approvals, trading permits, health certificates, and so on. Municipalities play a leading role in regulating land use and enabling the development and release of land for productive purposes. They also play an important supportive role in land reform and restitution programmes. Yet many rural municipalities do not have functional land use management systems in place.
- *Catalytic partnerships:* Municipal LED strategies cannot exist in isolation, but rather must be coordinated with complementary interventions by other public and private agencies. Poor coordination of efforts can lead to duplication and gaps in service delivery. Partnerships are necessary with: (i) other government agencies that hold complementary responsibilities; (ii) the private sector; (iii) intermediary institutions that provide funding,

research and development, advocacy and facilitation services; and (iv) communities in order to encourage participation in the local economy, strengthen entrepreneurship and build local business networks.

Failure to clearly demarcate the scope of municipal LED activities often results in the misallocation or capture of resources by vested interests at the local level without benefiting all residents.

Promising examples of effective LED approaches have begun to emerge. Initiatives that focus on community-based service provision seem to hold significant potential as they move financial resources into communities that create a basis for increased economic activity. The Zibambele programmes in KwaZulu-Natal, which involve local people in road maintenance, is a leading example of a programme that has used government procurement to stimulate the local economy (see text box in *Chapter 10 Roads*).

*Initiatives that focus on community-based service provision seem to hold significant potential*

## Financing rural municipalities

As outlined in *Chapter 3 Intergovernmental relations and the local government fiscal framework*, the Constitution provides the key parameters for the local government fiscal framework. Section 229 assigns significant revenue powers to all municipalities that, in addition to user charges, include rates on property and surcharges on fees for services provided by or on behalf of the municipality. Section 224 and 227 guarantee that municipalities should receive an equitable share of nationally raised revenues, based on their assigned functions, fiscal capacity and developmental needs, among other matters. However, Section 227(2) relieves national government of any obligation to compensate municipalities that do not raise revenue commensurate with their fiscal capacity and tax base, and prevents it from penalising those municipalities who demonstrate fiscal effort.

### The fiscal framework for rural municipalities

Given most rural municipalities' weak economic base and high levels of poverty, the fiscal framework is primarily focussed on addressing backlogs in basic infrastructure and subsidising basic service delivery. The local government equitable share subsidises the institutional capacity of rural municipalities, and the provision of basic services. Various conditional grants support the expansion of infrastructure and support capacity development. However, it is important that rural municipalities also show fiscal effort in raising own revenues according to their fiscal capacity.

*Given most rural municipalities' weak economic base and high levels of poverty, the fiscal framework is primarily focussed on addressing backlogs in basic infrastructure and subsidising basic service delivery*

It is important to distinguish between the roles of district and local municipalities in rural areas. District municipalities encompass a number of local municipalities and are responsible for district wide-integrated planning, including land-use planning, economic planning and development, and transport planning. Many of them have played an historical role as infrastructure development agents and bulk service providers. District municipalities are supposed to support the capacity of local municipalities through providing assistance and capacity building. However, this often does not happen. They also play a role where local municipalities have inadequate administrative capacity to manage particular services. In such instances, districts have been made responsible for the direct provision of services, such as water and sanitation provision in some provinces.

*Local municipalities are intended to be the actual locus of service delivery*

Local municipalities are intended to be the actual locus of service delivery. In instances where district municipalities provide such services it is supposed to be a transitional arrangement while the necessary capacity is established in the local municipalities. However, there are many instances where the district has been designated as the service delivery authority for a particular service, but actual service delivery is done by the local municipality.

*District municipalities are expected to pass on funding to enable local municipalities to subsidise services appropriately*

The current design of the local government fiscal framework provides that funding related to a particular function gets paid to the municipality that is legally responsible for the delivery of a function. So funds will be paid to the district municipality that is the service delivery authority, even though the function is provided by the local municipality. In such instances the district municipality is expected to pass on the funding to enable the local municipality to subsidise the service appropriately. In many instances, this does not happen.

**Grant programmes for rural municipalities**

Government has prioritised assistance to municipalities to extend access to basic services and subsidise their provision to poor households. Doing so requires support to the creation of infrastructure assets by rural municipalities as well as the development of critical financial and technical capabilities.

***Capacity support***

Significant grant allocations have been made to support capacity development but concerns remain over the depth and sustainability of the impact of these programmes. The total allocation of capacity building grants amongst small town municipalities amounted to R241 million in 2008/09 financial year, and R350 million in mostly rural municipalities. The key programmes supported by these funds are:

- The *municipal systems and improvement grant* aims to assist municipalities in building in-house capacity to perform their functions and stabilise institutional and governance systems. Key aims of this programme are to develop planning capacity and build governance systems.
- The *financial management grant* aims to support sustainable management of the fiscal and financial affairs of municipalities. The grant promotes multi-year budgeting, linking integrated development plans to budgets and producing quality reports.
- *The expanded public works programme incentive for municipalities grant* encourages municipalities to adopt labour intensive investment and service delivery methods.

***Infrastructure support***

Infrastructure grants (direct and indirect) to rural municipalities are an important source of capital finance. Small town municipalities received infrastructure grants amounting to R1.4 billion in 2008/09, while mostly rural municipalities received R2.2 billion.

In 2004, government consolidated all the previous capital grants into the Municipal Infrastructure Grant (MIG) to correct for deficiencies and lack of coordination observed with the fragmentation of grants. MIG is intended to supplement municipal capital budgets so as to assist municipalities address infrastructure backlogs related to basic services.

In addition to MIG, there are other national grants to fund infrastructure such as Integrated National Electrification Programme (INEP) that aims to ensure all clinics and schools have access to electricity, and to extend access to poor households. Part of this grant is implemented directly by Eskom, who is the service provider in many rural areas.

## Grant dependence and fiscal effort in rural municipalities

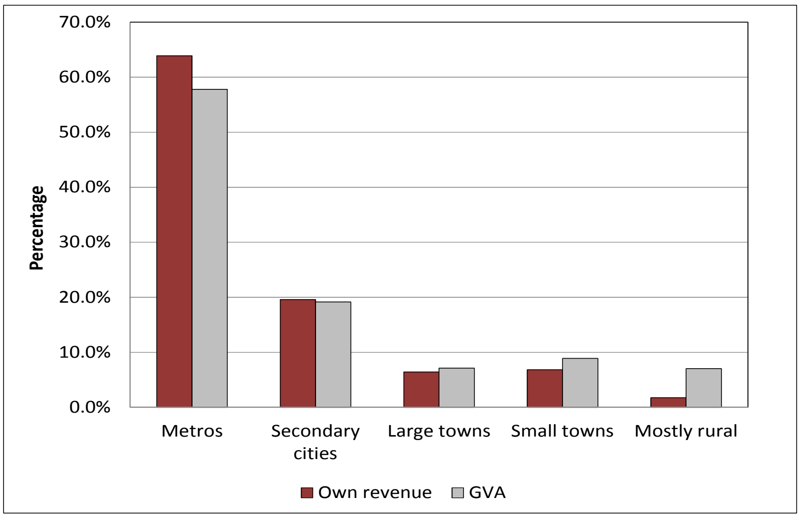
*Government transfers alone cannot address all the service delivery pressures that local government face.*

Government transfers alone cannot address all the service delivery pressures that local government face. They are intended to supplement the municipalities' own revenues, with a particular focus on facilitating the provision of services to poor households and addressing rural infrastructure backlogs.

*The fact that grants are 'easy money' effectively reduces the incentive for municipalities to collect own revenues*

The very high level of grant dependence among rural municipalities reflects the unequal distribution of development across the country and these municipalities' relatively limited fiscal capacity. Consequently, rural municipalities' dependence on transfers will be an on-going feature of the local government fiscal framework. However, it remains a cause for concern, given that grants are seen as 'easy money' which effectively reduces the incentive for municipalities to collect own revenues. This undermines the accountability and responsiveness of municipalities to their own communities, and given the extent of investment needs in these areas also reduces the ability of the municipality to address these needs.

**Figure 12.5 GVA vs own revenue per municipal category, 2008/09**




*Source: National Treasury local government database*

Figure 12.5 compares own revenues to GVA by municipal group. This provides a proxy measure of fiscal effort. The figure shows that 58.6 per cent of GVA is generated within the metros, and from this economic base they collected 64.4 per cent of municipal own revenues. The secondary cities and large town municipalities share of own revenues is almost equal to their share of GVA. However, the figures shows that 5.6 per cent of GVA is generated in mostly rural municipalities, but their share of own revenue is just 1.9 per cent. This means that the mostly rural municipalities are collecting less revenue than this proxy measure of their fiscal capacity suggests they should be, and are consequently overly dependent on government transfers and grants.

## Own revenues

*In many instances, rural municipalities do not levy property rates and service charges to non-poor households and businesses in their areas*

Most rural local municipalities face a challenge in raising own revenue. Although the majority of the households are indigent, there are those households and local businesses that can afford to pay for services. In many instances, rural municipalities do not levy property rates and service charges to non-poor households and businesses in their areas. This both undermines the finances of the municipality, and also breaks the revenue-service link between the municipality and the ratepayer/customer that entitles them to demand better quality services because they are paying for them.

In rural areas property taxes present a challenge in many developing countries, given the levels of poverty, and the difficulties of valuing properties and administering the tax. The text box below shows different approaches which have been adopted by different countries.

**Approaches to property rates in rural municipalities**

What is the best approach to property taxes in rural areas? This depends on the state of property markets, the system of tenure and what the country most wants to accomplish with its property tax. If the test for 'best' is the most common practice in developing countries, then the preference would seem to be for a capital value system where both land and improvements are taxed, as is currently implemented in urban areas in South Africa. The following additional policy options exist

- *Flat rates taxes* These taxes can lay the foundation for future tax reforms by fostering a culture of payment in rural areas. This approach should only be used in areas of traditional land tenure. It may be necessary to set the levels for the tax to prevent abuse. The main disadvantage of a flat-rate tax is that it is not vertically equitable: rich and poor people will pay the same rate, which is regressive. This may be tolerable if implemented within communities where disparities in income are not pronounced, or as a transitional instrument to a more progressive tax.
- *An area based property tax* Residents of a particular area identify primary determinants of value and apply them to the land in their village. This type of approach can be understood by people in rural areas where they are not accustomed to thinking of monetary value of real estate and the conversion of buying and selling it. This approach could promote acceptance of property rates.
- *Self-property-valuation approach* In this system residents are encouraged to determine the value of their property if they were to sell it. Property rates can then be determined on the basis of the information given by residents. This approach is working in developing countries like India. The challenge in South Africa is that most rural properties have very low values and residents generally do not have any intention to sell or cannot sell (due to it being traditional land), so they might not see the benefit of discussing a hypothetical price for the purpose of paying the tax.

In making the choice of tax base, developing countries have tended to focus on ease of administration. This has often meant opting for an area-based approach to raising property taxes. This approach involves converting the property tax into a specific excise tax on land space (size of plot). This approach is easy to administer, and is easily understood. However, area does not necessarily equate to value, and it does not take into consideration improvements. These considerations give rise to concerns about the fairness of an area-based tax. There are also concerns that the tax will not generate sufficient revenue – if the rate is to be set at a level that is affordable to the majority of households. One might be prepared to live with these disadvantages if the area-based approach to property taxes is a transition measure to developing a complete value-based tax roll and developing capacity to administer a more complicated system of property rates. This approach has been followed in the Indian city of Bangalore.

Good practice suggests looking for the strongest correlation between the availability of transaction data and the property tax base. So if most property is held in leasehold, then the focus might be on annual rental value. If tenure is dominated by owner-occupancy, there is a stronger argument for an (improved) capital value base. If the country has some large cities but is still heavily agrarian, then a combination of an ad valorem system for urban places, and an area-based system for the more rural areas, may work best. In urban areas where land is subject to speculation, or is not being developed intensively, a social cost might be imposed. In this case, a land value tax might be considered preferable for its ability to encourage efficient land use. Where no real property market exists, the area-based system has much to offer.

In South Africa, the imposition of a property tax has faced two additional difficulties:

- Unclear powers between government and traditional leaders in the management of rural land. At present, government issues letters of occupation to rural households, but ownership is not transferred. It would appear that municipalities seldom use this record system as a basis for determining liability for property rates. In addition, it is not clear whether such households are legally liable for rates on the land they occupy, as they do not own the land.
- A weak social contract at the local level, which finds expression in widespread unwillingness to pay for services. Levels of trust in local government are very low, particularly with respect to procedural fairness and equity in taxation, and the use of tax revenues. This is compounded by a limited understanding of the role of value-based property taxes. In rural areas, households have been more accustomed to the payment of flat levies.

Experience has shown that the key to improving own revenues is to re-establish the link between user charges for services and the value of the service delivered. In many rural municipalities access to services is restricted by lack of funding, which is compounded by the municipality insisting on providing free basic services to all customers – through so-called geographic targeting. Internationally, there is strong evidence that poor households are willing to pay for a service that they regard as valuable, and that collectively the revenues from such payments can exceed government subsidies in amount.

## Conclusion

Rural municipalities have an important role to play in supporting rural development through providing basic infrastructure, particularly access roads. In doing so, municipalities need to explore the use of appropriate technologies that can be sustainably implemented and managed within rural contexts. The rural household support grant is a significant initiative in this regard, aimed at supporting the rollout of enclosed, VIP toilets and rainwater tanks to rural households. Innovative service delivery approaches can also enhance the development impact of the municipalities' normal activities, such as contracting households to provide road maintenance services.

Municipalities should be playing a key role in LED, by progressively extending basic infrastructure and ensuring that existing infrastructure is maintained, by providing a user-friendly regulatory environment and by facilitating catalytic partnerships with other role players.

The ability of rural municipalities to collect own revenues are largely influenced by their socio-economic circumstances. However, rural municipalities themselves also show little fiscal effort in raising own revenues from non-poor households, businesses and from charging for services. The consequence is that these municipalities are becoming increasingly dependent on government grants and transfers.

Whether a particular municipality is an obstacle or a catalyst to local development depends largely on: the quality of leadership the mayor and council provide, improving the skills of the officials employed in the municipality, whether there are problems with corruption and maladministration, and whether the municipality mobilises and utilises the resources available to it effectively. In many rural areas, municipalities need to find ways of working co-operatively with traditional authorities to facilitate appropriate land use management, the rollout of basic services and the collection of rates from non-poor households and businesses located on traditional land.

13

# Cities and the management of the built environment

## Introduction

South Africa is among the most urbanised countries in Africa. It has the third largest number of people living in urban centres (after Nigeria and Egypt), and a higher proportion of people living in urban areas than any comparable African country (excluding very small, desert or island states). The urban population is growing rapidly; it is expected to increase by 13.8 million people by 2050. The location of economic activity mirrors this situation, with cities hosting the vast majority of economic activity and increasingly becoming the engines of growth. However, the pace of urban population growth is outstripping economic growth. Effectively, this means cities are increasingly becoming home to expanding poor populations.

*As the pace of urban population growth is outstripping economic growth; cities are increasingly becoming home to expanding poor populations*

The inequalities in South African society are most evident in its cities. Apartheid patterns of spatial segregation persist, with poor people located in townships and peripheral areas, far from social and economic opportunities. These settlement patterns undermine economic growth prospects as they absorb considerable household spending and require large public transport subsidies to sustain them. It is clear that 17 years into democracy, South Africa has yet to find an appropriate model for effectively harnessing the potential of its cities to drive economic growth and redress the spatial patterns that continue to marginalise poor people.

Government recognises that large urban municipalities need to play a leading role in the management of the built environment. Cities already have the responsibility for the provision of basic services and associated infrastructure. However, to effectively manage the built environment, large municipalities need to be established as the centre of planning and service delivery coordination. In particular, this

*Government recognises that large urban municipalities need to play a leading role in the management of the built environment* requires greater responsibilities for cities in land use management, the development of human settlements and the provision of public transport services.

In accordance with Section 156(4) of the Constitution, national and provincial government must assign functions that would be more effectively administered locally, including housing and municipal public transport, to municipalities that have the capacity to administer these functions. Four recent developments have underscored this leading role for city governments in the built environment:

- The formation of a new urban settlements development grant and the accreditation of large urban municipalities to manage public housing programmes in terms of the Housing Act (2007) have reinforced the centrality of these municipalities in developing integrated human settlements.
- The National Land Transport Act (2009) accords municipalities the leading role in the planning and regulation of public transport services in cities, across all modes of urban transport.
- The withdrawal of proposals to form regional electricity distributors has emphasised the role of municipalities in the provision of basic services.
- The recent Constitutional Court judgement on the Development Facilitation Act (1994) has clarified the responsibility of municipalities to lead land use planning and administration. This will be further confirmed in revisions to the land use management legislation.

*Empowering cities to perform these functions will support integrated planning and spatial development*

Empowering cities to perform these functions will support integrated planning and spatial development, as well as ensure greater accountability to communities. However, the successful devolution of these functions requires clarity on roles and functions, reforms to intergovernmental fiscal arrangements, enhanced capacity at the local level and sufficient resources and incentives to effectively address the spatial legacy of the past. Importantly, it requires cities themselves to make clear trade-offs between the development of social and economic amenities in close proximity to residential areas, and a transit-based development approach that seeks to increase the mobility of residents and thus their access to existing amenities and opportunities.

This chapter reviews:

- the demographic, economic and spatial context of cities
- public expenditure on the built environment
- institutional and fiscal arrangements for managing cities
- reconsidering the fiscal framework for large cities.

## The demographic, economic and spatial context of cities

In 2007, at least 52 per cent of the population resided in the 27 largest municipalities in South Africa. The population growth in these cities has been driven by both rural-urban migration and organic growth in urban populations, as well as by migration from Southern Africa and further afield. This trend is set to continue, though at a slower pace than in the past, as shown in figure 13.1. The United Nations Development Programme estimates that 71 per cent of South Africans will live in urban areas by 2030, growing to nearly 80 per cent by 2050. This implies that a further 7.8 million people will live in the country's cities by 2030, followed by an additional 6 million people by 2050.

A further 7.8 million people will live in South Africa's cities by 2030, followed by an additional 6 million people by 2050

**Figure 13.1 Urban population projections to 2050**

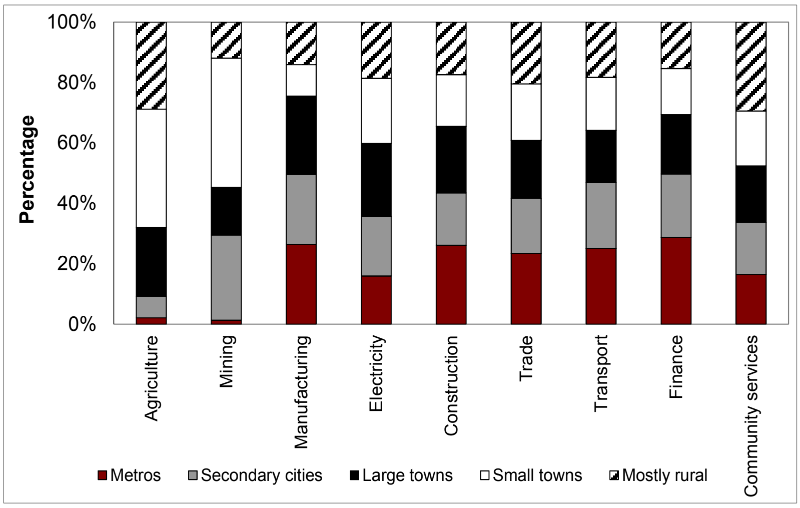

*Source: World Urbanization Prospects, the 2009 Revision*

The character of the urban population has changed along with its growth. A notable change is the average size of households, which declined from 3.9 to 3.6 people between 2001 and 2007 in the metros. Similar trends are evident in secondary cities.

*The average size of households in the metros declined from 3.9 to 3.6 people between 2001 and 2007*

South Africa's cities are the drivers of economic development, being host to around 80 per cent of economic activity. Figure 13.2 highlights the significant contribution of the finance, property and infrastructure sectors to urban economic activities. Economic growth in cities has exceeded the national average.

**Figure 13.2 GVA per capita by type of municipality**

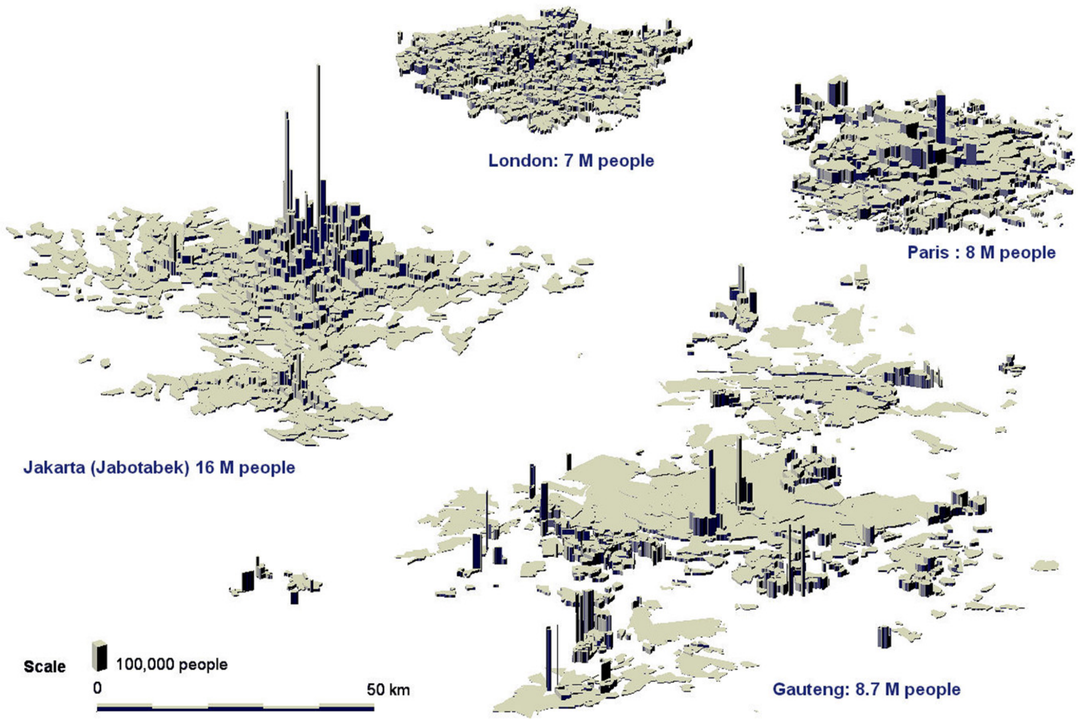



*Source: HIS Global Insight, September 2010*

*Glaring apartheid spatial patterns persist and are being perpetuated by the location of new, low cost housing projects on the periphery of cities*

Despite great progress over the past 17 years in the delivery of housing and related infrastructure, glaring apartheid spatial patterns persist and are being perpetuated by the location of new, low cost housing projects on the periphery of cities where land is cheapest. The consequence is that people, particularly poor people, continue to be forced to live in dysfunctional and disjointed settlements with limited social and economic infrastructure. These spatial inefficiencies mean that poorer people travel longer distances to places of employment and to access social services.

**Spatial distribution of population in Gauteng (2001 census) compared to Jakarta, London and Paris**




*Source: World Bank, Municipal Infrastructure Finance Synthesis Report, 2009*

International trends suggest that to better manage the urban space, cities need to densify along economic corridors and in areas of economic growth, so as to reduce travel times for commuters and ensure more efficient use of urban land. The above figure reflects the disparities in land use densities between three international cities, comparing them to the Gauteng city region (which includes Ekurhuleni, Johannesburg and Tshwane). The fragmented and low density nature of the Gauteng city region even within each metro boundary is particularly noticeable, alongside the very high densities on the urban peripheries.

*Cities need to densify along economic corridors and in areas of economic growth, to reduce travel times for commuters and ensure more efficient use of urban land*

These demographic, economic and spatial trends have placed increasing pressure on urban municipalities and raise four critical challenges for municipalities to address:

- *A growth in the number of poor people living in cities:* The largest number of unemployed people reside in metros and big cities. Urban areas were hardest hit by the economic downturn, with job losses impacting on the ability of households to pay municipal rates and user charges, and increasing demand for free basic services. As the proportion of poor people in cities grows, additional pressure is placed on municipalities to provide infrastructure to support subsidised housing developments and provide free basic services.
- *Supply side constraints to economic growth:* Municipalities provide much of the infrastructure and services that support economic activities. A failure to provide this infrastructure to scale and on time creates a bottleneck that constrains private investment. Higher than average economic growth rates in cities have placed added pressure on these municipalities to expand and refurbish infrastructure.
- *An inefficient urban form:* The sprawling, low density nature of South Africa's cities imposes significant costs on households, firms and the public sector. Poor households must bear the costs of long transport journeys and low levels of community cohesion, while the public sector must subsidise access to both housing and public transport. Municipalities have to provide infrastructure networks across vast distances, particularly to give poor households access.
- *Rising demand for urban services:* Population growth and declining average household sizes place increasing pressure on urban municipalities, which deliver many services (such as water or electricity) at the level of the household rather than the individual. In large cities, backlogs in the provision of land and housing are reflected in the growth of informal settlements. Table 13.1 below illustrates the distribution of backlogs across municipal type.

**Table 13.1 Distribution of backlogs across municipal type**

| Households | Housing | Basic water | Basic sanitation | Basic electricity |
|---|---|---|---|---|
| Metros | 1 461 815 | 193 033 | 620 485 | 955 090 |
| Secondary cities - 21 | 616 006 | 123 194 | 497 116 | 548 188 |
| Other municipalities | 475 027 | 1 021 034 | 2 193 911 | 1 998 420 |
| **Total** | **2 552 848** | **1 337 261** | **3 311 512** | **3 501 698** |
| *Percentage of backlogs* | | | | |
| Metros | 57.3% | 14.4% | 18.7% | 27.3% |
| Secondary cities - 21 | 24.1% | 9.2% | 15.0% | 15.7% |
| Other municipalities | 18.6% | 76.4% | 66.3% | 57.1% |
| **Total** | **100.0%** | **100.0%** | **100.0%** | **100.0%** |

*Source: Stats SA, Community survey 2007*

## Public expenditure on the built environment

*Most public expenditure on the urban built environment is focused on housing, transport and related infrastructure, and social services*

Most public expenditure on the urban built environment is focused on housing, transport and related infrastructure, and social services. These investments complement far larger private investments, particularly in the property sector.

While public expenditure on housing increased from 2005/06, the scale of delivery of houses completed and under construction has decreased after peaking in 2007/08. The decrease is partly due to higher tendered prices per unit driven by high demand and high input prices in the construction industry, and partly due to weak planning, project and programme management. Most housing related expenditure is financed by a national conditional grant that flows through the provinces, with limited funding provided by municipalities. Private investment in housing still exceeds public investment despite the demand for subsidised housing.

With the introduction of the public transport infrastructure and systems grant to local government in 2005/06, public transport expenditure increased, largely driven by investments in infrastructure. In addition, bus subsidies have been shifted from the national sphere to the provincial sphere of government through the creation of the public transport operations grant, with further devolution to local government expected.

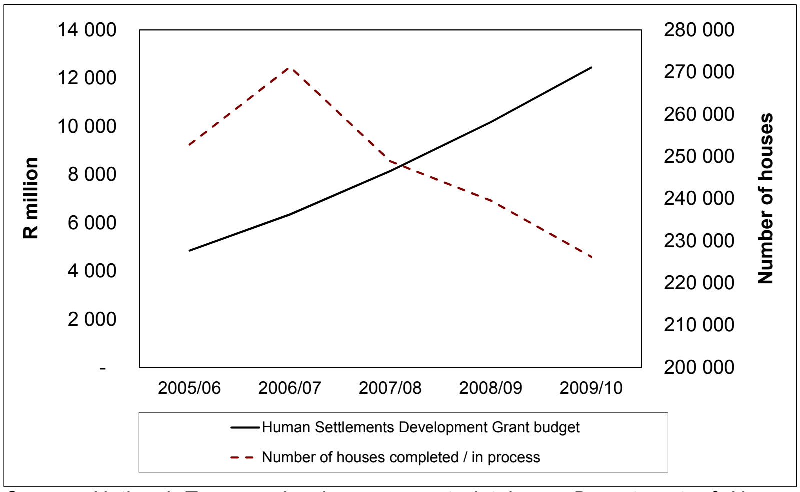
Investments in community assets also increased, largely due to investments in sports facilities linked to the 2010 FIFA World Cup.

### Human settlements

*Public housing programmes are funded through the human settlements development grant to provinces*

Public housing programmes are funded through the human settlements development grant to provinces. In terms of the Housing Act (1997), provinces may use municipalities as developers in the housing construction process.

**Figure 13.3 Expenditure on housing and housing delivery, 2005-2009**




*Source: National Treasury local government database, Department of Human Settlements, Housing delivery 2005/06 – 2009/10*

Spending on the human settlements development grant increased from R4.9 billion in 2005/06 to R12.4 billion in 2009/10, at an average annual rate of 26.6 per cent. Despite the robust growth in housing expenditure, housing delivery has fallen to 228 218 houses completed and under construction in 2009/10, after peaking in 2007/08, with 271 219 houses built. The largest decline in delivery occurred in Mpumalanga, where the province delivered 7 800 houses in 2009/10, down from 14 986 houses in 2005/06. Delivery did not decline in Eastern Cape and Western Cape.

*Compared to provincial expenditure, municipal expenditure on housing reflects the functional misalignment within the sector*

Compared to provincial expenditure, municipal expenditure on housing reflects the functional misalignment within the sector. Metros' expenditure in 2008/09 constituted 22.2 per cent of the total allocation to provinces. The housing transfers from provinces to municipalities are classified on municipalities operating expenditure budgets as transfers to households, because households are the ultimate beneficiaries of the expenditure. In 2011, government will put in place budgeting and reporting procedures to ensure transparency in the total transfer of housing funds to metropolitan municipalities.

*Provinces' inability to provide funding certainty to municipalities over the MTREF limits their ability to plan and coordinate development*

Expenditure by metros is expected to increase from R1.2 billion in 2009/10 to R2.3 billion in 2012/13. Expenditure by secondary cities shows a declining trend, but this is in all likelihood due to the nature of the agency agreements with provinces. These agreements provide for funds to flow after delivery of project milestones have been achieved and hence are not budgeted for over the medium term, unlike most government expenditure. Provinces' inability to provide funding certainty to municipalities over the MTREF period limits their ability to plan and coordinate development.

**Table 13.2 Municipal expenditure on housing, 2006/07 - 2012/13**

| R million | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | |
| **Category A (Metros)** | **663.6** | **1 509.5** | **1 226.8** | **1 180.2** | **2 072.5** | **1 949.4** | **2 321.8** |
| Johannesburg | 116.1 | 212.1 | 144.7 | 373.8 | 272.9 | 300.0 | 489.9 |
| Cape Town | 171.8 | 116.5 | 226.9 | 228.6 | 310.9 | 225.3 | 311.7 |
| eThekwini | 46.9 | 822.3 | 302.7 | 136.2 | 1 182.7 | 1 133.3 | 1 202.5 |
| Ekurhuleni | 133.4 | 171.6 | 268.5 | 284.5 | 303.5 | 287.8 | 314.6 |
| Tshwane | 195.5 | 187.0 | 283.9 | 157.1 | – | – | – |
| Nelson Mandela | – | – | – | – | 2.5 | 3.0 | 3.0 |
| **Category B (Locals)** | **314.9** | **354.9** | **298.8** | **250.1** | **747.2** | **890.9** | **688.3** |
| *Secondary cities - 21* | *200.0* | *61.7* | *65.4* | *117.6* | *170.1* | *187.2* | *63.4* |
| Buffalo City | – | – | – | – | 112.3 | 36.2 | – |
| Mangaung | 17.0 | 7.1 | – | 5.1 | 2.6 | 22.5 | 32.0 |
| Matjhabeng | – | – | – | – | – | – | – |
| Emfuleni | – | – | – | – | – | – | 0.3 |
| Mogale City | 3.3 | – | – | 0.0 | – | 1.5 | 0.0 |
| Msunduzi | 21.0 | 6.4 | 0.0 | – | – | 4.5 | 2.2 |
| Newcastle | – | – | 0.3 | – | 0.6 | – | – |
| uMhlathuze | 1.5 | 0.3 | 0.2 | 4.9 | 6.6 | 8.6 | 11.0 |
| Govan Mbeki | – | – | 0.0 | – | – | – | 0.2 |
| Emalahleni (Mp) | – | 0.1 | – | – | – | – | – |
| Steve Tshwete | 0.1 | 0.0 | – | 0.3 | – | – | – |
| Mbombela | – | – | – | – | – | – | 0.1 |
| Sol Plaatje | – | – | – | 23.2 | – | 31.4 | – |
| Polokwane | – | – | – | – | – | – | – |
| Madibeng | – | – | – | – | – | – | – |
| Rustenburg | 103.0 | – | 0.2 | – | – | – | – |
| Tlokwe | – | – | – | 0.2 | – | – | 0.0 |
| Matlosana | – | – | – | – | – | 26.0 | – |
| Drakenstein | 11.9 | 17.6 | 39.3 | 54.7 | 48.0 | 48.0 | 7.9 |
| Stellenbosch | 34.6 | 17.1 | 22.7 | 23.6 | – | 6.6 | 9.7 |
| George | 7.7 | 13.1 | 2.7 | 5.7 | – | 1.8 | – |
| *Towns - 140* | *82.7* | *222.9* | *223.0* | *88.8* | *534.3* | *668.7* | *589.9* |
| *Mostly rural - 70* | *32.3* | *70.2* | *10.4* | *43.7* | *42.9* | *35.0* | *35.0* |
| **Category C (Districts)** | **–** | **1.4** | **–** | **7.5** | **33.5** | **36.1** | **38.9** |
| *Category B + C* | *314.9* | *356.3* | *298.8* | *257.6* | *780.7* | *927.0* | *727.2* |
| **Total** | **978.5** | **1 865.8** | **1 525.5** | **1 437.8** | **2 853.2** | **2 876.3** | **3 049.0** |

*Source: National Treasury local government database*

*The formal subsidised housing market currently serves 36 per cent of the total housing market*

Local government expenditure on housing represents 4.7 per cent of the total gross fixed capital formation for residential buildings in 2008, which totals R48.1 billion[11], while provincial expenditure represents 21.2 per cent of this total. When these expenditure trends are compared to the housing need, 17 per cent of the population is able to finance housing privately, while 45 per cent of the population rely on one or other form of housing finance to finance their homes. However, there is a severe shortage of houses and housing finance in the affordable category of the housing market (i.e. housing properties valued less than R500 000)[12]. The formal subsidised housing market currently serves 36 per cent of the total housing market. In essence, 25.9 per cent of expenditure needs to service 36 per cent of the population, with a large gap market between the subsidised and the formal housing market, due to affordability and supply constraints.

[11] South African Reserve Bank, Quarterly Bulletin, December 2010.

[12] Finmark Trust, 2010

## Public transport

Total spending on public transport (excluding roads), at national, provincial and local level, amounted to R16.6 billion in 2008/09. Expenditure largely related to capital expenditure for local public transport and the national rail function, totalled R9.85 billion, while subsidies, which include national taxi, bus and rail subsidies, contributed R6.8 billion. Provincial spending on public transport totalled R1.5 billion. Growth in public spending has, until recently, been constrained. However, significant investments are now under way in rail infrastructure as well as through the introduction of bus rapid transit systems in major cities.

*Significant investments are now under way in rail infrastructure as well as through the introduction of bus rapid transit systems in major cities*

### *Bus subsidies*

The subsidisation of bus services is currently funded through a provincial conditional grant. The services provided in all provinces total 80 812 vehicles providing subsidised services with an annual ridership of 653 129 019 passengers and non-subsidised services to 95 298 136 passengers in 2009/10. In 2009/10, North West provided the highest subsidy per passenger at R16.30, while Limpopo contributes an average of R2.22 per passenger. Details are provided in table 13.3.

*The subsidisation of bus services is currently funded through a provincial conditional grant*

**Table 13.3 Delivery of bus subsidised services, 2009/10**

| Province | Number of vehicles subsidised | Number of routes operated | Number of staff | Number of trips operated | Number of kms operated | Number of cash passengers | Number of MIT passengers | Total no of subsidised passengers |
|---|---|---|---|---|---|---|---|---|
| *Interim* | | | | | | | | |
| Limpopo | 5 334 | 3 021 | 11 021 | 434 054 | 23 058 029 | 12 005 534 | 20 479 661 | 55 996 654 |
| Gauteng | 20 774 | 13 262 | 53 811 | 1 437 412 | 82 871 945 | 10 945 637 | 94 758 296 | 190 101 137 |
| Mpumalanga | 6 950 | 1 794 | 14 927 | 843 539 | 36 148 262 | 5 670 465 | 47 581 435 | 90 267 372 |
| KwaZulu-Natal | 696 | 214 | 1 424 | 42 898 | 424 481 | 180 691 | 2 043 448 | 2 693 852 |
| Free State | – | – | – | – | – | – | – | – |
| Eastern Cape | 4 378 | 15 994 | 8 567 | 409 432 | 10 987 780 | 11 470 787 | 4 186 859 | 27 083 797 |
| Western Cape | 12 626 | 17 880 | 32 719 | 1 802 117 | 44 818 258 | 9 706 936 | 38 108 982 | 94 499 518 |
| Northern Cape | 108 | 12 | 34 | 953 | 44 737 | 15 553 | 47 293 | 108 690 |
| North West | – | – | – | – | – | – | – | – |
| **Subtotal** | **50 866** | **52 177** | **122 503** | **4 970 405** | **198 353 492** | **49 995 603** | **207 205 974** | **460 751 020** |
| *Tendered* | | | | | | | | |
| Limpopo | 472 | 75 | 1 072 | 22 276 | 1 250 871 | 642 621 | 868 975 | 2 786 362 |
| Gauteng | 6 163 | 5 060 | 10 823 | 320 410 | 13 222 359 | 5 904 678 | 12 150 246 | 31 619 739 |
| Mpumalanga | – | – | – | – | – | – | – | – |
| KwaZulu-Natal | 11 244 | 14 544 | 26 303 | 758 065 | 27 729 760 | 20 857 223 | 28 516 909 | 77 914 049 |
| Free State | 2 028 | 2 028 | 4 704 | 207 294 | 8 782 894 | 2 786 401 | 11 561 380 | 23 346 728 |
| Eastern Cape | – | – | – | – | – | – | – | – |
| Western Cape | – | – | – | – | – | – | – | – |
| Northern Cape | 434 | 530 | 784 | 21 318 | 1 188 658 | 513 761 | 766 435 | 2 491 920 |
| North West | – | – | – | – | – | – | – | – |
| **Subtotal** | **20 341** | **22 237** | **43 686** | **1 329 363** | **52 174 542** | **30 704 684** | **53 863 945** | **138 158 798** |
| *Negotiated* | | | | | | | | |
| Limpopo | 2 584 | 3 129 | 5 848 | 159 231 | 7 879 831 | 5 495 188 | 6 317 849 | 19 863 660 |
| Gauteng | – | – | – | – | – | – | – | – |
| Mpumalanga | – | – | – | – | – | – | – | – |
| KwaZulu-Natal | 6 061 | 5 628 | 8 982 | 302 588 | 9 609 747 | 6 567 754 | 6 964 689 | 23 465 449 |
| Free State | 444 | 1 296 | 432 | 36 097 | 1 845 353 | 1 145 946 | 1 738 476 | 4 768 044 |
| Eastern Cape | – | – | – | – | – | – | – | – |
| Western Cape | – | – | – | – | – | – | – | – |
| Northern Cape | – | – | – | – | – | – | – | – |
| North West | 516 | 974 | 650 | 60 842 | 3 070 031 | 1 388 961 | 1 600 075 | 6 122 048 |
| **Subtotal** | **9 605** | **11 027** | **15 912** | **558 758** | **22 404 962** | **14 597 849** | **16 621 089** | **54 219 201** |
| **Total** | **80 812** | **85 441** | **182 101** | **6 858 526** | **272 932 996** | **95 298 136** | **277 691 008** | **653 129 019** |

*Source: Department of Transport*

In terms of the National Land Transport Act (2009), subsidised bus services that are currently managed by provincial government will be integrated into the metropolitan based networks, where these services have their destination in the metropolitan municipality. To date, no metropolitan municipality has been assigned the function. However, some progress has been made to achieve this in Cape Town.

### *Integrated rapid public transport networks*

Public transport allocations have increased significantly since the introduction of the public transport infrastructure and systems grant in 2005/06.

**Table 13.4 Public transport infrastructure and sytems grant allocations, 2006/07 - 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | |
| **R million** | | | | | | | |
| **Category A (Metros)** | **423.5** | **934.0** | **2 284.1** | **2 102.3** | **3 177.2** | **3 940.0** | **3 340.0** |
| Johannesburg | 184.0 | 329.0 | 661.2 | 652.8 | 1 300.5 | 1 200.0 | 800.0 |
| Cape Town | 120.0 | 230.0 | 424.8 | 332.5 | 1 018.4 | 1 600.0 | 900.0 |
| eThekwini | 11.8 | 125.0 | 624.9 | 376.9 | 330.0 | 20.0 | 20.0 |
| Ekurhuleni | 27.7 | 13.0 | 7.6 | 27.7 | 20.0 | 20.0 | 20.0 |
| Tshwane | 11.0 | 105.0 | 260.0 | 565.2 | 100.0 | 500.0 | 800.0 |
| Nelson Mandela | 69.0 | 132.0 | 305.5 | 147.1 | 408.3 | 600.0 | 800.0 |
| **Category B (Locals)** | **94.0** | **210.0** | **635.7** | **315.9** | **522.3** | **485.0** | **785.0** |
| *Secondary cities - 21* | *94.0* | *196.0* | *635.7* | *315.9* | *522.3* | *485.0* | *785.0* |
| Buffalo City | – | – | 8.6 | 31.2 | 71.5 | 400.0 | 700.0 |
| Mangaung | 29.5 | 25.0 | 242.6 | 82.2 | 166.0 | 15.0 | 15.0 |
| Matjhabeng | – | – | – | – | – | – | – |
| Emfuleni | – | – | – | – | – | – | – |
| Mogale City | – | – | – | – | – | – | – |
| Msunduzi | – | – | 2.1 | 7.7 | 15.0 | 15.0 | 15.0 |
| Mbombela | 1.0 | 55.0 | 170.5 | 60.8 | 120.0 | 15.0 | 15.0 |
| Sol Plaatje | 1.5 | 11.0 | – | – | – | – | – |
| Polokwane | 10.5 | 50.0 | 143.2 | 66.1 | 60.3 | 20.0 | 20.0 |
| Madibeng | – | – | – | – | – | – | – |
| Rustenburg | – | 33.0 | 68.7 | 67.8 | 89.6 | 20.0 | 20.0 |
| Tlokwe | 1.0 | – | – | – | – | – | – |
| Matlosana | 30.5 | 22.0 | – | – | – | – | – |
| Drakenstein | – | – | – | – | – | – | – |
| Stellenbosch | 20.0 | – | – | – | – | – | – |
| George | – | – | – | – | – | – | – |
| *Towns - 140* | – | – | – | – | – | – | – |
| *Mostly rural - 70* | – | *14.0* | – | – | – | – | – |
| **Category C (Districts)** | **1.5** | **30.0** | **–** | **–** | **–** | **–** | **–** |
| *Category B + C* | *95.5* | *240.0* | *635.7* | *315.9* | *522.3* | *485.0* | *785.0* |
| **Total** | **519.0** | **1 174.0** | **2 919.8** | **2 418.2** | **3 699.5** | **4 425.0** | **4 125.0** |

*Source: National Treasury local government database*

Between 2006/07 and 2009/10, the average annual increase was 67 per cent. Over the MTREF period, the allocations are expected to continue to increase above inflation, with an estimated average annual increase of 19.5 per cent.

Initially, metros were unable to meet expenditure targets. This was largely due to the function being relatively new, the publication of the public transport strategy only being approved in 2007, and a lack of focus due to 2010 FIFA World Cup operational preparations.

**Table 13.5 Expenditure of the public transport infrastructure and systems grant, 2006/07 - 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | |
| **R million** | | | | | | | |
| **Category A (Metros)** | **415.4** | **923.2** | **2 284.1** | **1 810.2** | **3 177.2** | **3 940.0** | **3 340.0** |
| Johannesburg | 184.0 | 329.0 | 661.2 | 652.5 | 1 300.5 | 1 200.0 | 800.0 |
| Cape Town | 120.0 | 230.0 | 424.8 | 332.5 | 1 018.4 | 1 600.0 | 900.0 |
| eThekwini | 11.8 | 125.0 | 624.9 | 376.6 | 330.0 | 20.0 | 20.0 |
| Ekurhuleni | 20.1 | 2.2 | 7.6 | 0.6 | 20.0 | 20.0 | 20.0 |
| Tshwane | 11.0 | 105.0 | 260.0 | 300.9 | 100.0 | 500.0 | 800.0 |
| Nelson Mandela | 68.6 | 132.0 | 305.5 | 147.1 | 408.3 | 600.0 | 800.0 |
| **Category B (Locals)** | **88.9** | **210.0** | **589.3** | **123.3** | **522.3** | **485.0** | **785.0** |
| *Secondary cities - 21* | *88.9* | *196.0* | *589.3* | *123.3* | *522.3* | *485.0* | *785.0* |
| Buffalo City | – | – | 3.2 | 0.8 | 71.5 | 400.0 | 700.0 |
| Mangaung | 29.2 | 25.0 | 203.7 | – | 166.0 | 15.0 | 15.0 |
| Matjhabeng | – | – | – | – | – | – | – |
| Emfuleni | – | – | – | – | – | – | – |
| Mogale City | – | – | – | – | – | – | – |
| Msunduzi | – | – | – | 0.0 | 15.0 | 15.0 | 15.0 |
| Mbombela | 0.8 | 55.0 | 170.5 | – | 120.0 | 15.0 | 15.0 |
| Sol Plaatje | 1.5 | 11.0 | – | – | – | – | – |
| Polokwane | 10.4 | 50.0 | 143.2 | 54.6 | 60.3 | 20.0 | 20.0 |
| Madibeng | – | – | – | – | – | – | – |
| Rustenburg | – | 33.0 | 68.7 | 67.8 | 89.6 | 20.0 | 20.0 |
| Tlokwe | 0.6 | – | – | – | – | – | – |
| Matlosana | 30.5 | 22.0 | – | – | – | – | – |
| Drakenstein | – | – | – | – | – | – | – |
| Stellenbosch | 15.9 | – | – | – | – | – | – |
| George | – | – | – | – | – | – | – |
| *Towns - 140* | – | – | – | – | – | – | – |
| *Mostly rural - 70* | – | *14.0* | – | – | – | – | – |
| **Category C (Districts)** | **1.3** | **15.4** | **–** | **–** | **–** | **–** | **–** |
| *Category B + C* | *90.3* | *225.4* | *589.3* | *123.3* | *522.3* | *485.0* | *785.0* |
| **Total** | **505.7** | **1 148.6** | **2 873.4** | **1 933.5** | **3 699.5** | **4 425.0** | **4 125.0** |

*Source: National Treasury local government database*

Expenditure by Johannesburg metro has increased from R184 million in 2006/07 to R652.5 million in 2009/10 and will continue to increase over the MTREF, which will cover the completion of phase one of the Rea Vaya services. Similarly, Cape Town metro has increased expenditure from R120 million in 2006/07 to R332.5 million in 2009/10 and will also increase over the MTREF to introduce its local variant of bus rapid transit, known as the My CiTi services. Nelson Mandela Bay metro has also increased expenditure significantly from R68.6 million in 2006/07 to R305.5 million in 2008/09, with road construction being initiated and planning finalised. Full operational plans and financial modelling for public transport investments are still under way in Tshwane, eThekwini and Ekurhuleni metros.

### *Passenger rail transport*

*Investment in passenger rail has increased significantly in line with the national rail plan*

Investment in passenger rail has increased significantly in line with the national rail plan, which aims to stabilise passenger numbers, increase levels of service and expand services. The key areas of expenditure are in the metropolitan areas, and passenger trips in the five key regions are reflected in table 13.6.

**Table 13.6 Passenger rail transport outputs, 2009/10**

| Region | Annual passenger trips |
|---|---|
| Western Cape | 201 538 211 |
| Eastern Cape | 13 909 404 |
| KwaZulu-Natal | 87 960 091 |
| Witwatersrand | 242 099 325 |
| City of Tshwane | 88 485 561 |
| **Total** | **633 992 592** |

*Source: Passenger Rail Agency SA*

The increased investment in passenger rail has increased the number of coaches in the system, which should lead to increased levels of service. The table below provides an overview of key performance indicators, showing little actual change experienced, but with more positive projections over the MTREF.

**Table 13.7 Selected performance and operations indicators**

| | Past | | | Current | Projections | | |
|---|---|---|---|---|---|---|---|
| **Indicator** | **2005/06** | **2006/07** | **2007/08** | **2008/09** | **2009/10** | **2010/11** | **2011/12** |
| Total number of coaches overhauled | 375 | 310 | 489 | 680 | 700 | 700 | 500 |
| Percentage of Metrorail trains on time (A corridors) | 89.0% | 87.0% | 86.0% | 88.0% | 90.0% | 92.0% | 93.0% |
| Metrorail: Passenger trips (number of commuters in the system) | 512m | 530m | 592m | 385m | 677m | 745m | 815m |
| Metrorail: Fare revenue (R million) | 1 020 | 1 060 | 1 191 | 787 | 1 347 | 1 465 | 1 610 |
| Metrorail: Accidents per million train km | – | 1.2 | 1.2 | 1.7 | 1.6 | 1.5 | 1.5 |
| Service efficiency index (R): Subsidy per passenger km | – | 0.17 | 0.14 | 0.15 | 0.15 | 0.15 | 0.15 |

*Source: National Treasury, 2009 Estimates of National Expenditure*

The challenges in addressing mobility needs in South African cities were captured by the Cities Network[13] as follows:

- Trip distances can be three times those of the average trip in countries with denser cities.
- Car ownership is high and on the increase.
- Modal efficiencies are decreasing as bus services are losing market share to minibus taxis.
- The industry needs to be more responsive to off-peak travel needs.
- The safety and security concerns of public transport users need to be addressed.

*There has been progress with integrated rapid networks in certain cities, such as Johannesburg and Cape Town*

Despite these challenges, there has been progress with integrated rapid networks in certain cities, such as Johannesburg and Cape Town. Key constraints remain high operational costs, the lack of a policy guiding subsidisation, high private vehicle usage, the complexities in integrating ticketing across modes of transport and the need to conclude negotiations with existing operators – mostly in the taxi industry.

[13] Cities Network, *Sustainable Cities,* 2009.

## Community assets

Community assets include parks and gardens, recreational facilities, sports fields, stadiums, community halls, libraries, clinics, theatres, museums and art galleries. Most cities also have programmes that seek to upgrade urban spaces such as business hubs, pedestrian paths and bridges, parks, taxi ranks, customer care centres, pension payout facilities and wetlands. Table 13.8 provides an overview of expenditure on community assets.

**Table 13.8 Municipal capital expenditure on community assets, 2006/07 - 2012/13**

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|---|---|---|---|
| | | Outcome | | Estimate | | Medium-term estimates | |
| R million | | | | | | | |
| **Category A (Metros)** | **1 665.0** | **2 121.3** | **3 098.6** | **2 695.3** | **1 526.3** | **1 097.2** | **1 109.6** |
| Johannesburg | 605.9 | 99.1 | 626.6 | 100.8 | 175.5 | 125.2 | 159.8 |
| Cape Town | 301.0 | 1 197.4 | 1 323.5 | 1 514.0 | 365.5 | 178.7 | 181.6 |
| eThekwini | 99.8 | 53.7 | 57.9 | 59.7 | 176.3 | 71.8 | 68.4 |
| Ekurhuleni | 110.3 | 131.5 | 280.1 | 383.2 | 268.5 | 274.7 | 265.0 |
| Tshwane | 84.1 | 242.9 | 293.9 | 308.4 | 207.0 | 276.1 | 308.5 |
| Nelson Mandela | 463.9 | 396.8 | 516.6 | 329.4 | 333.4 | 170.7 | 126.2 |
| **Category B (Locals)** | **241.9** | **2 731.4** | **2 181.1** | **2 357.5** | **1 531.5** | **722.0** | **799.7** |
| *Secondary cities - 21* | *665.8* | *1 830.9* | *1 207.5* | *1 347.6* | *600.8* | *182.7* | *182.7* |
| Buffalo City | 38.6 | 49.1 | 52.8 | 127.2 | 23.1 | 23.3 | 23.3 |
| Mangaung | 62.3 | 190.3 | 191.9 | 59.5 | 5.0 | 65.3 | 65.3 |
| Matjhabeng | 4.0 | 1.0 | 4.1 | 15.7 | 21.9 | 18.1 | 18.1 |
| Emfuleni | 15.9 | – | 98.6 | 41.7 | 60.5 | -87.2 | -87.2 |
| Mogale City | 6.3 | 8.9 | 16.5 | 16.1 | 31.8 | 18.5 | 18.5 |
| Msunduzi | 28.2 | 17.5 | 2.6 | 32.3 | 33.3 | 7.3 | 7.3 |
| Newcastle | 9.4 | – | 1.7 | 1.8 | 21.9 | 1.0 | 1.0 |
| uMhlathuze | 16.8 | 15.9 | 22.8 | 7.2 | 30.0 | 31.1 | 31.1 |
| Govan Mbeki | – | 0.1 | 14.8 | 12.0 | 19.1 | 14.6 | 14.6 |
| Emalahleni (Mp) | 8.2 | 3.1 | 65.6 | 21.2 | – | – | – |
| Steve Tshwete | 26.3 | 15.9 | 30.5 | 67.0 | 58.2 | 11.9 | 11.9 |
| Mbombela | 309.0 | 861.6 | 138.9 | 272.4 | 6.2 | – | – |
| Sol Plaatje | 1.5 | 76.3 | 19.5 | 21.7 | 50.0 | – | – |
| Polokwane | 64.9 | 481.9 | 454.3 | 497.8 | 119.5 | 6.3 | 6.3 |
| Madibeng | 7.8 | 16.0 | 13.7 | 26.2 | 24.4 | 25.9 | 25.9 |
| Rustenburg | 27.1 | 47.5 | 12.8 | 5.6 | 7.3 | 2.3 | 2.3 |
| Tlokwe | 2.3 | – | 5.6 | 4.4 | 2.9 | 3.4 | 3.4 |
| Matlosana | 2.9 | 18.5 | 12.8 | 20.9 | 39.2 | 17.0 | 17.0 |
| Drakenstein | 16.7 | 7.6 | 24.0 | 10.0 | 28.8 | 10.1 | 10.1 |
| Stellenbosch | 7.9 | 4.9 | 13.6 | 68.1 | 5.2 | 9.8 | 9.8 |
| George | 10.0 | 14.8 | 10.6 | 18.7 | 12.5 | 4.1 | 4.1 |
| *Other Local municipalities* | *608.5* | *900.5* | *973.6* | *1 009.9* | *930.7* | *539.2* | *616.9* |
| **Category C (Districts)** | **204.6** | **114.3** | **380.5** | **446.2** | **115.3** | **90.4** | **207.1** |
| *Category B + C* | *446.5* | *2 845.7* | *2 561.7* | *2 803.7* | *1 646.8* | *812.3* | *1 006.8* |
| **Total** | **2 111.5** | **4 967.0** | **5 660.3** | **5 499.0** | **3 173.0** | **1 909.5** | **2 116.3** |

*Source: National Treasury local government database*

Investments in community assets appear to be extremely volatile. They have increased significantly between 2006/07 and 2009/10, growing at 37.6 per cent per year. This increase was largely due to investments in sports facilities linked to the 2010 FIFA World Cup. Over the MTREF, expenditure is projected to decrease in metros, and secondary cities.

*Over the MTREF, expenditure on community assets is projected to decrease in metros, and secondary cities*

In addition to the above expenditure, the neighbourhood development partnership grant (NDPG) to local government supports the development of community infrastructure and services, in partnership with the private sector. All metros are represented in the portfolio of this grant. They take up 40 per cent of the share of the grant that has been allocated to a total of 57 municipalities in South Africa since the grant was introduced in 2006. Metros have already been responsible for R666 million expenditure on the grant to March 2010. Progress, however, is not uniform across municipalities, as table 13.9 shows.

**Table 13.9 Municipal expenditure relative to NDPG award as at 31 March 2010**

| R thousand | NDPG Cumulative spending | Total NDPG Award | % spending |
|---|---|---|---|
| eThekwini | 206 733 | 693 463 | 29.8% |
| Johannesburg | 185 911 | 517 446 | 35.9% |
| Tshwane | 36 725 | 701 581 | 5.2% |
| Ekurhuleni | 67 165 | 164 758 | 40.8% |
| Cape Town | 122 829 | 950 851 | 12.9% |
| Nelson Mandela | 47 100 | 299 079 | 15.7% |
| All Other NDPG-Recipients | 653 495 | 5 062 661 | 12.9% |
| **Total** | **1 319 958** | **8 389 839** | **15.7%** |

*Source: National Treasury local government database*

Much effort is being directed at internal institutional coordination necessary to develop township regeneration plans that align interests for effective programme design and project packaging. Embedding the neighbourhood development partnership grant programme in the planning and budgeting process of municipalities requires that the appropriate skills and capacity are put in place to align, sequence and coordinate sectoral investment interests in targeted urban spaces.

## Institutional and fiscal arrangements for managing cities

*The demographic, economic and spatial challenges that cities face are exacerbated by institutional and fiscal misalignments*

The demographic, economic and spatial challenges that cities face are exacerbated by institutional and fiscal misalignments that have prevented cities from responding adequately to these pressures. Key problems include:

- *Sectoral discontinuities in the performance of functions:* Despite constitutional imperatives, sectoral policy frameworks continue to promote duplication and fragmentation in the delivery of built environment services. In particular:
  - Provinces continue to manage the national housing programme and various public entities hold significant, strategically located urban land. Housing development has remained on the periphery of cities to take advantage of low land costs. The cost of these locational choices are felt by poor people, and municipalities.
  - Public transport services continue to be subsidised by national government via a grant to provinces, with little role for city administrations in public transport. This means that investment choices are separated from the institutions that have to eventually carry the costs associated with the location of those investments.

### International lessons with large city management

A study was undertaken in June 2010 that reviewed city management models and challenges in Brazil, China, India and Canada and assessed the policy responses by local, provincial and central governments. The study aimed to stimulate thinking on South African cities specifically in relation to: (i) the appropriate scope of powers and functions required for effective city management; (ii) the role of other spheres (tiers) of government in supporting urban development; (iii) the appropriate structuring of city governance; and (iv) the fiscal framework for financing urban development. Three key themes emerged from the review:

*Empowering cities to integrate urban development:* All countries have accepted the need to give greater powers to city governments to manage built environment infrastructure and services**.** Countries have sought to strengthen the integration of urban service delivery to obtain a greater return on public investments (India, Brazil), to accelerate investment spending (China) and to improve asset maintenance (Canada). If cities are 'choking on their own growth', then the policy response has been to 'loosen the knot' through providing them with adequate powers and functions to manage their built environments. The key functions assigned to cities have been those of public transport, housing, basic services infrastructure and land use management. In India, extensive administrative approval is required for cities to proceed with investments, even in relation to functions assigned to them. In states such as Gujarat, where these approvals have been relaxed, investment is more rapid. Similarly, in China, where approvals are technically required, in reality this is only necessary for large scale ('mega-project') investments. In Brazil, the administrative discretion of cities has been expanded by strengthening their access to national decision-making processes. Empowering cities to manage their built environments appears to have been instrumental in forcing clear policy trade-offs to be made at the city level.

A noticeable trend is for countries to pursue integrated spatial development through adopting a sector-led investment approach encouraged by national government. In China and India, strong support for public transport infrastructure investments is in effect exercising a coordinating function at the city level. In Brazil, a city led approach to slum upgrading plays a similar role. This highlights the power of specific, limited national priorities to guide city investments and provide incentives for integration across sectors**.** It has allowed a break with historical patterns of investment, particularly with the tendency to prioritise investment in roads at the expense of public transport. This has begun to encourage greater integration in the overall spatial management of cities that is particularly noticeable in China and Brazil, as well as the more progressive cities in India, such as Ahmadabad.

*Creating a sustainable, pro-investment fiscal framework:* Cities in all four countries are actively seeking mechanisms to achieve a step-change in levels of urban infrastructure investment. In India, a national fiscal incentive programme (JnNURM) aims to guide and assist cities in making new investments, contingent on the introduction of a pre-specified list of 'urban reforms'. Central government in China co-finances urban mega-projects that fit with national priorities, while Infrastructure Canada provides fiscal incentives for infrastructure maintenance. In Brazil, government has introduced grant programmes to finance additional urban investments rather than providing additional taxes to cities, largely as it wants to incentivise improved performance by city governments. National grant programmes have been largely successful, but require ongoing management and fine-tuning. The JnNURM in India has been criticised for crowding out private sector capital from municipal financing. The Chinese approach, where cities are left to finance all infrastructure outside of national priority schemes has led to significant borrowings by cities (although within a poorly constructed borrowing framework).

*Developing innovative approaches to funding housing needs:* All countries have realised that government alone is unable to raise the resources necessary to finance urban housing needs. This has led to a search for financing mechanisms that move beyond subsidies. In particular:

- The demand for housing is increasingly being disaggregated by market segment at a city and sub-city level, with policy focused on ensuring that each segment is adequately serviced. Greater emphasis is being placed on gaps in the housing market, with public resources used to complement private credit markets in enabling low income households to enter the market.
- The mobilisation of the private sector to address housing supply shortage across the entire housing market, often through direct investment incentives such as tax deferrals or exemptions to the property development sector (as in Brazil).
- The mobilisation of households themselves to make financial contributions towards their own housing needs. In all other countries all households are expected to make a partial co-payment in return for the receipt of a public subsidy.

An opportunity remains for South Africa to learn from other countries, and to then adapt the ideas to the South African context.

- *Duplication of land regulation responsibilities:* This duplication between cities and provinces has significantly expanded the time required to obtain development approvals, imposing deadweight costs on the economy. Efforts to overcome delays in land release, even at the national government level, often fail to account for the role of cities in spatial management. This undermines city efforts to guide spatial planning, and contributes to diluting the impact of public spending.
- *Failure to adequately exploit existing revenue sources:* Most funding for infrastructure investment must ultimately come from within city administrations. Grant funding to municipalities has expanded, but own sources of capital finance have not been as buoyant. Beyond the impacts of the recession on local revenues, this reflects a substitution of own funding with increasing grant funding. An opportunity exists for cities to enhance existing own source so finance, such as development charges levied on new property developments, and additional borrowing. Grants have the potential to be used as a form of security that can reduce the cost and expand the tenure of municipal borrowings.
- *Weak asset management practices at city level:* In most cases asset registers are not fully up to date, and asset maintenance and replacement is under-funded. New accounting treatment for assets reveals significant historical underfunding of asset management. The growing outcomes focus of grant programmes will enable national government to monitor municipal prioritisation of new asset creation as well as asset maintenance, refurbishment and replacement.

City administrations have access to significant institutional and human resource capacity. Most large urban municipalities have been able to almost double their levels of capital expenditure in the last two years (and increase its proportion to operating expenditures). Although skills gaps remain, city administrations are increasingly able to respond to this challenge.

## Reconsidering the fiscal framework for large cities

*Government is reviewing the existing institutional arrangement and fiscal framework to strengthen the management of South African cities*

Municipalities are closer to communities and businesses, and thus able to determine and respond to their specific local needs more accurately and rapidly than other spheres of government. Recognising this, government is reviewing the existing institutional arrangement and fiscal framework to strengthen the management of South African cities. The programme explicitly seeks to differentiate cities from other municipalities in order to recognise their specific contexts and needs. In particular, cities need to play a far larger role in economic growth, dealing with urban poverty and facilitating improved built environment outcomes, across land management, transport and human settlement sectors.

### Spatial planning and land-use management

Land use management planning in South Africa is governed by various provincial ordinances, including the Development Facilitation Act (1995) and the Less Formal Township Establishment Act (1991).

The Constitutional Court judgment on the case between the City of Johannesburg Metropolitan Municipality and the Gauteng Development Tribunal highlighted the need to ensure legislative clarity regarding the roles of provincial and local government. The City of Johannesburg, which was joined by eThekwini, successfully argued that the Development Facilitation Act was unconstitutional in that it intruded on municipal powers with respect to land use management. The judgment confirmed that the re-zoning of land and the establishment of townships are exclusively the function of local government in support of municipal planning.

The judgment highlights the flaws in existing legislation and the need to finalise comprehensive land use legislation. There is currently a process under way to review land use management legislation, in order to clarify roles and functions and to empower municipalities to fulfil their constitutional mandate in this regard. As housing and public transport play such a vital role in land use patterns, the consolidation of these functions at the local level will provide both the leverage to change spatial patterns as well as improve accountability at the level of delivery.

*There is currently a process under way to review land use management legislation to clarify roles and functions and to empower municipalities to fulfil their constitutional mandate*

### Devolution of the housing function

To support coordinated development, municipalities are the logical place to plan and provide for human settlement development. Housing delivery has declined since 2006/07, despite the strong growth in the human settlements development grant. The underperformance of the housing programme signals an inefficient subsidy system that does not meet the needs of subsidy beneficiaries. The Housing Act (1997) provides for the accreditation of local government to administer housing programmes to enable them to plan the implementation of their developmental objectives in a coordinated manner through a three step process:

| | |
|---|---|
| Level 1 - delegation | Beneficiary management, subsidy budget planning and allocation, and priority programme management and administration |
| Level 2 - delegation | Full programme management and administration of all housing programmes and subsidy instruments |
| Level 3 – assignment | Financial administration, which involves the formal assignment of all functions including subsidy payment disbursements |

Progress on accreditation has been slow. Five metros have recently been accredited to level two, while the two new metros, Mangaung and Buffalo City, will be accredited to level one. No municipality has been accredited to level three. This limits the ability of municipalities to structure housing subsidies to facilitate planning, development and improve service delivery. The process has been hampered by concerns relating to capacity at the local level, among other things. Cities face

*The slow accreditation process limits the ability of municipalities to structure housing subsidies to facilitate planning, development and improve service delivery* infrastructure and service costs, which escalate when settlements are not well located; it is therefore critical to overcome the delay in full accreditation to ensure that the right levers are in place to improve the spatial development of cities.

*Serviced urban land and housing top structures are key to the delivery of sufficient, affordable housing*

The weak linkage between demand for housing and supply can be addressed on a planning level through increasing densities and stimulating supply as a more sustainable solution to manage increase housing prices. There are two factors that are key to the delivery of sufficient, affordable housing: serviced urban land and housing top structures.

The more rapid development and release of serviced urban land is being supported through the urban settlements development grant. This provides funding directly to cities to buy, service and release land for urban development specifically for low income households. Already, upgrading informal settlements represent a current municipal function, in the form of providing serviced sites. To facilitate the upgrading of more informal settlements, investments in these areas need to be the responsibility of municipalities.

The development of houses on serviced land units is primarily the responsibility of households. Affordability constraints mean that poor households struggle to make the necessary investments. Housing finance policies can assist these households, including through the provision of subsidies. At present, most housing subsidies are provided in the form of completed housing units. In future, alternative and more incremental models of supporting housing investments are increasingly becoming important.

Municipal accreditation for the housing function is necessary to assist cities in guiding housing production in relation to their spatial plans and the availability of land and infrastructure. This would allow cities to address the housing need of households that are unable to access the subsidised market, but for whom affordable housing stock is not available through private finance.

### Public transport regulation

*The devolution of public transport regulatory functions to local government will allow for the integration of the planning, regulation and management of public transport services at the local level*

The devolution of public transport regulatory functions to local government will allow for the integration of the planning, regulation and management of public transport services at the local level. The National Land Transport Act (2009) provides clarity on roles and responsibilities for public transport services, and delineates the public transport function as services that happen within the boundaries of the municipality or between municipalities if there is an agreement. The regulation of bus and taxi routes and operator licensing is currently provided by provincial licence boards. The National Land Transport Act has divided responsibility for these services as follows:

- local government is responsible for services in a municipality or between municipalities where the municipalities have an agreement;
- provincial government is responsible for services between municipalities; and

- national government is responsible for services between provinces and tourism services.

Local regulation of public transport services, subsidy levels and prices (fares) will support the coordination and control necessary for the creation of integrated public transport networks across transport modes. This scope of control is a vital element of the National Land Transport Act, specifically during the initial phase of its implementation. In this phase municipalities are required to negotiate with existing transport operators on compensation for losses they may suffer due to the introduction of new technologies, transport modes and routes, as well as negotiate modifications to the subsidy system.

The responsibility for the planning, operation and subsidisation of rail public transport services currently lies with national government in the form of the Passenger Rail Agency of South Africa (PRASA). To provide for improved integrated planning, the National Land Transport Act provides for local government to support the planning of regional commuter services. To improve accountability for rail public transport services, processes are under way to create integrated planning committees as required by the Act to support local planning and operational subsidisation of rail. PRASA will remain the provider of passenger rail services and be funded for their capital and operational needs, but cities will over time enter into agreements with the agency for services, specify their preferred level of services and ensure alignment with their integrated public transport networks. Ultimately, local government will also need to play a key role in the determination of ticket prices for rail services.

*Local government should take responsibility for setting subsidies to facilitate better land use management and the performance of the municipal public transport function*

Centralised subsidisation limits the extent to which urban development objectives relating to densification, infrastructure efficiency and transport efficiency can be reached. To allow for more flexible local responses to urban design and spatial development, local government should take responsibility for setting subsidies and use specific forms of subsidisation to facilitate better land use management and the performance of the municipal public transport function. This includes the operational subsidisation of bus rapid transit systems, bus and rail operational subsidies, as well as other capital support in the form of taxi recapitalisation.

Internationally, public transport is a subsidised service, even in densely populated metropolitan areas in developed and developing countries. The subsidisation of public transport in South Africa intends both to address the market failure that exists due to long distances between settlements and work opportunities and provide for a social wage to reduce the burden of transport on low income earners. Fare revenue is therefore not intended to cover operational costs because of the low densities of South African cities and low levels of affordability in most communities using the services.

Government's 2007 public transport strategy provides for public transport services to be provided on a per km basis or gross cost basis. Therefore, the ridership risk for the services lies with the city. This approach, compared to leaving the ridership risk with operators, ensures better outcomes through reduced speeding and less overcrowding. To correct the misalignment between public transport operational risks and the ability to mitigate these risks, it may be necessary for provision to be made for a local revenue source to provide sufficient funds to continue to expand public transport services and cover operational shortfalls over the long term. As indicated above, increasing fares to address operational shortfalls will work against the policy objective of keeping transport costs at below 10 per cent of household expenditure. Balancing funding contributions in this area between local and national government will improve local accountability, increase value for money and support transit based development. Significant policy work is necessary in this area to guide the way forward.

### Strengthening own revenue potential and effort

*The process of reviewing the local government fiscal framework will need to consider whether there is a need to expand own revenue sources for cities*

Cities have significant but underutilised own revenue potential. Enhanced revenue administration can increase receipts, improved engagement with private lenders can lower the rate and lengthen the tenure of borrowing, while opportunities exist to strengthen current sources of capital finance, such as development charges. The process of reviewing the local government fiscal framework will need to carefully consider whether there is a need to expand own revenue sources for cities.

The financial impact of current measures to support free basic services needs to be evaluated. There is a need to understand the extent to which they are being subsidised by the local government equitable share or by cross-subsidies embedded in the rates and service tariffs charged to different customer groups. There is also a need to evaluate whether the free services are actually reaching the intended beneficiaries or whether non-poor households are benefitting disproportionately. There is concern that municipal expenditures on free services is crowding out other expenditure priorities.

In other developing countries no households receive free services – all citizens are expected to pay even a very basic amount regardless of income level as a statement of citizenship. As observed elsewhere in the Review, extending the service-revenue link to more households has the potential to enhance municipal accountability and sustainability.

## Conclusion

South Africa’s large urban municipalities are vastly different from their more rural counterparts in terms of demographic, economic and spatial trends. Contexts are rapidly diverging and cities (and rural areas) increasingly require a different policy treatment to allow a focus on their specific contexts and challenges, as well as to account for the institutional capacity they have and are capable of developing.

Like in many countries, cities face the challenges of managing growth in population, physical size, levels of poverty and demands for economic infrastructure. Failure to adequately manage these pressures within the resources available leads to declining levels of access to services, congestion of infrastructure networks, slum developments and growing bottlenecks to economic growth.

The assignment of the housing and public transport functions to large urban municipalities will facilitate better management of the urban built environment, especially when the regulatory and subsidy-setting powers associated with these functions are also assigned to cities. This will provide these municipalities with the flexibility and the discretion to address their specific needs and improve accountability to citizens. Housing and transport play a major part in any citizen's life and ensuring that accountability is at the local level will allow improved public participation in the planning of housing developments and public transport routes and ensure direct feedback on the services provided.

Balancing the provision of amenities with the provision of public transport requires competent city planning units that are able to develop a long term vision of city spatial development and balance both the short term provision of amenities with the provision of public transport. For example, transit-based development approaches offer the prospect of encouraging housing and economic opportunities along transport networks and provides for reduced transport costs, travel times and carbon emissions.

# ANNEXURES

## Summary data of all municipalities

In addition to the material published in the *2011 Local Government Budget and Expenditure Review* detailed information on municipal budgets and annual financial statements, as well as their section 71 in-year quarterly financial reports are available at www.treasury.gov.za

## Annexure A: Aggregate municipal operating and capital budgets and expenditures, 2006/07 – 2012/13

| R thousands | 2006-07 Original budget | 2006-07 Revised budget | 2006-07 Outcome | 2006-07 Outcome as % of Revised budget | 2007-08 Original budget | 2007-08 Revised budget | 2007-08 Outcome | 2007-08 Outcome as % of Revised budget |
|---|---|---|---|---|---|---|---|---|
| **Operating Revenue and Expenditure** | | | | | | | | |
| **Operating Revenue** | **107 370 496** | **103 388 028** | **108 780 602** | **105.2%** | **118 494 978** | **120 825 790** | **127 507 949** | **105.5%** |
| Property rates | 18 631 341 | 18 737 436 | 18 737 170 | 100.0% | 21 486 122 | 21 325 496 | 21 450 760 | 100.6% |
| Service charges | 44 798 419 | 45 579 611 | 45 553 301 | 99.9% | 49 223 013 | 49 494 983 | 49 968 125 | 101.0% |
| Regional Service Levies | 649 269 | 649 869 | 330 300 | 50.8% | 95 188 | 117 721 | 29 743 | 25.3% |
| Investment revenue | 3 351 597 | 2 283 993 | 3 216 937 | 140.8% | 3 672 391 | 2 306 496 | 3 997 806 | 173.3% |
| Government grants | 26 451 537 | 25 817 148 | 28 970 491 | 112.2% | 26 660 968 | 34 625 260 | 39 321 622 | 113.6% |
| Public contributions and donations | - | 146 888 | 678 846 | 462.2% | - | 155 000 | 1 300 027 | 838.7% |
| Other own revenue | 13 488 334 | 10 173 083 | 11 293 558 | 111.0% | 17 357 296 | 12 800 834 | 11 439 866 | 89.4% |
| **Operating Expenditure** | **99 018 901** | **96 832 806** | **99 707 328** | **103.0%** | **117 558 385** | **111 322 087** | **114 449 986** | **102.8%** |
| Employee costs | 30 816 405 | 30 616 799 | 29 057 205 | 94.9% | 34 819 794 | 34 771 052 | 32 672 270 | 94.0% |
| Remuneration of Councillors | - | 271 772 | 1 556 634 | 572.8% | - | 146 460 | 1 671 023 | 1140.9% |
| Repairs and maintenance | 7 190 324 | 7 258 394 | 5 953 438 | 82.0% | 8 532 106 | 8 633 225 | 7 083 170 | 82.0% |
| Depreciation and amortisation | - | 2 458 136 | 5 365 295 | 218.3% | - | 1 813 080 | 6 228 786 | 343.5% |
| Finance charges | 6 709 941 | 4 078 322 | 3 502 849 | 85.9% | 7 482 523 | 5 035 948 | 3 474 865 | 69.0% |
| Materials and bulk purchases | 21 544 703 | 21 519 293 | 22 138 724 | 102.9% | 23 804 514 | 23 279 924 | 23 925 581 | 102.8% |
| Grants and subsidies | - | 1 162 215 | 2 513 787 | 216.3% | - | 1 480 798 | 3 747 756 | 253.1% |
| Other expenditure | 32 757 528 | 29 467 876 | 29 619 396 | 100.5% | 42 919 448 | 36 161 600 | 35 646 534 | 98.6% |
| **Surplus/(Deficit)** | **8 351 595** | **6 555 222** | **9 073 275** | | **936 593** | **9 503 703** | **13 057 964** | |

| R thousands | 2006-07 Original budget | 2006-07 Revised budget | 2006-07 Outcome | 2006-07 Outcome as % of Revised budget | 2007-08 Original budget | 2007-08 Revised budget | 2007-08 Outcome | 2007-08 Outcome as % of Revised budget |
|---|---|---|---|---|---|---|---|---|
| **Capital Revenue and Expenditure** | | | | | | | | |
| **Source of Finance** | **29 087 422** | **28 879 368** | **21 339 380** | **73.9%** | **37 959 164** | **38 170 488** | **29 964 002** | **78.5%** |
| External Loans | 5 286 629 | 6 390 899 | 5 314 823 | 83.2% | 7 252 998 | 9 641 235 | 7 087 508 | 73.5% |
| Public Contributions and Donations | 1 210 581 | 248 009 | 105 058 | 42.4% | 1 777 611 | 1 599 838 | 175 065 | 10.9% |
| Grants and subsidies | 14 651 300 | 14 580 049 | 9 463 237 | 64.9% | 20 051 256 | 19 872 950 | 13 469 077 | 67.8% |
| Other | 7 938 912 | 7 660 410 | 6 456 263 | 84.3% | 8 877 299 | 7 056 465 | 9 232 352 | 130.8% |
| **Capital Expenditure** | **29 087 422** | **28 876 366** | **21 310 065** | **73.8%** | **37 965 167** | **38 198 368** | **29 958 124** | **78.4%** |
| Water and Sanitation | 7 273 319 | 7 148 026 | 5 813 781 | 81.3% | 10 329 349 | 10 621 684 | 7 397 628 | 69.6% |
| Electricity | 3 333 347 | 3 525 139 | 3 093 122 | 87.7% | 4 006 429 | 4 338 182 | 3 832 561 | 88.3% |
| Housing | 4 038 712 | 3 664 287 | 978 526 | 26.7% | 3 337 372 | 3 091 914 | 1 865 774 | 60.3% |
| Roads and storm water | 4 465 212 | 4 313 567 | 3 177 801 | 73.7% | 5 232 722 | 5 239 788 | 4 017 486 | 76.7% |
| Other | 9 976 832 | 10 225 348 | 8 246 835 | 80.7% | 15 059 295 | 14 906 800 | 12 844 675 | 86.2% |

| R thousands | 2006-07 Original budget | 2006-07 Revised budget | 2006-07 Outcome | 2006-07 Outcome as % of Revised budget | 2007-08 Original budget | 2007-08 Revised budget | 2007-08 Outcome | 2007-08 Outcome as % of Revised budget |
|---|---|---|---|---|---|---|---|---|
| **Capital and Operating Expenditure** | | | | | | | | |
| Operating Expenditure | 99 018 901 | 96 832 806 | 99 707 328 | 957.8% | 117 558 385 | 111 322 087 | 114 449 986 | 1004.6% |
| Capital Expenditure | 29 087 422 | 28 876 366 | 21 310 065 | 603.7% | 37 965 167 | 38 198 368 | 29 958 124 | 647.2% |
| **Total** | **128 106 323** | **125 709 172** | **121 017 393** | **96.3%** | **155 523 552** | **149 520 455** | **144 408 110** | **96.6%** |

| 2008-09 | | | | 2009-10 | | | | 2010-11 | 2011-12 | 2012-13 |
|---|---|---|---|---|---|---|---|---|---|---|
| Original budget | Revised budget | Outcome | Outcome as % of Revised budget | Original budget | Revised budget | Outcome | Outcome as % of Revised budget | Medium-term estimates | | |
| **135 930 415** | **135 955 552** | **149 480 278** | **109.9%** | **162 324 440** | **179 559 906** | **176 342 259** | **98.2%** | **204 534 902** | **220 529 470** | **246 537 445** |
| 26 956 190 | 27 036 225 | 22 305 133 | 82.5% | 27 677 481 | 28 467 230 | 26 293 955 | 92.4% | 31 280 529 | 33 205 592 | 35 822 711 |
| 57 708 059 | 60 032 928 | 58 286 020 | 97.1% | 74 149 054 | 73 180 022 | 72 255 150 | 98.7% | 88 734 901 | 100 309 891 | 118 345 124 |
| 20 000 | 31 366 | 2 719 | 8.7% | - | - | 356 | 0.0% | - | - | - |
| - | - | 4 503 800 | 0.0% | - | 34 800 | 2 829 221 | 8129.9% | - | - | - |
| 33 689 439 | 29 983 046 | 49 519 053 | 165.2% | 32 254 262 | 47 000 913 | 57 474 232 | 122.3% | 52 896 125 | 54 948 200 | 58 258 703 |
| - | - | 493 773 | 0.0% | - | 20 000 | 412 979 | 2064.9% | - | - | - |
| 17 556 727 | 18 871 987 | 14 369 779 | 76.1% | 28 243 643 | 30 856 940 | 17 076 367 | 55.3% | 31 623 347 | 32 065 786 | 34 110 906 |
| **130 123 179** | **131 228 602** | **139 336 656** | **106.2%** | **153 013 003** | **168 589 239** | **163 177 044** | **96.8%** | **191 441 226** | **205 083 526** | **229 131 886** |
| 40 903 670 | 40 587 083 | 38 306 910 | 94.4% | 46 465 014 | 44 641 299 | 44 678 224 | 100.1% | 51 183 113 | 53 043 135 | 57 289 086 |
| - | - | 1 876 354 | 0.0% | - | 32 372 | 2 012 903 | 6218.0% | - | - | - |
| 10 287 318 | 10 499 622 | 7 842 673 | 74.7% | 10 052 546 | 228 740 | 9 323 401 | 4076.0% | - | - | - |
| - | - | 10 375 550 | 0.0% | - | 195 953 | 13 233 228 | 6753.3% | - | - | - |
| 6 845 585 | 6 971 130 | 4 265 192 | 61.2% | 5 773 016 | 4 950 052 | 4 881 959 | 98.6% | 5 612 162 | 6 007 818 | 6 363 833 |
| 27 325 457 | 29 459 819 | 30 181 872 | 102.5% | 39 758 562 | 38 506 371 | 38 107 824 | 99.0% | 48 245 576 | 57 111 044 | 70 166 752 |
| - | - | 3 297 323 | 0.0% | - | 56 256 | 3 698 892 | 6575.1% | - | - | - |
| 44 761 149 | 43 710 948 | 43 190 782 | 98.8% | 50 963 865 | 79 978 196 | 47 240 615 | 59.1% | 86 400 375 | 88 921 528 | 95 312 215 |
| **5 807 236** | **4 726 950** | **10 143 621** | | **9 311 437** | **10 970 667** | **13 165 216** | | **13 093 675** | **15 445 944** | **17 405 559** |

| 2008-09 | | | | 2009-10 | | | | 2010-11 | 2011-12 | 2012-13 |
|---|---|---|---|---|---|---|---|---|---|---|
| Original budget | Revised budget | Outcome | Outcome as % of Revised budget | Original budget | Revised budget | Outcome | Outcome as % of Revised budget | Medium-term estimates | | |
| **46 093 429** | **48 832 009** | **41 640 465** | **85.3%** | **49 946 470** | **45 267 062** | **40 994 819** | **90.6%** | **38 892 671** | **37 990 055** | **39 194 871** |
| 11 622 978 | 11 719 551 | 9 934 788 | 84.8% | 10 085 151 | 10 066 614 | 8 987 929 | 89.3% | 8 052 513 | 7 294 706 | 8 515 578 |
| 1 453 480 | 1 455 770 | 532 345 | 36.6% | 1 125 874 | 644 106 | 301 251 | 46.8% | 504 155 | 370 104 | 365 705 |
| 23 891 697 | 26 420 724 | 19 917 334 | 75.4% | 25 505 555 | 23 025 267 | 19 534 712 | 84.8% | 21 001 915 | 22 018 553 | 22 839 302 |
| 9 125 274 | 9 235 964 | 11 255 998 | 121.9% | 13 229 890 | 11 531 075 | 12 170 927 | 105.5% | 9 334 087 | 8 306 692 | 7 474 285 |
| **46 093 446** | **48 843 894** | **41 669 365** | **85.3%** | **49 946 470** | **47 963 576** | **40 938 752** | **85.4%** | **41 190 190** | **39 316 427** | **40 553 160** |
| 11 185 543 | 11 255 679 | 9 115 368 | 81.0% | 13 057 474 | 11 352 258 | 8 966 236 | 79.0% | 11 682 114 | 12 311 052 | 13 341 585 |
| 5 231 496 | 5 231 340 | 4 747 841 | 90.8% | 6 787 286 | 5 367 429 | 4 784 068 | 89.1% | 5 723 614 | 5 106 886 | 4 898 233 |
| 4 136 121 | 3 979 593 | 1 525 529 | 38.3% | 2 997 590 | 3 122 110 | 1 437 849 | 46.1% | 2 853 215 | 2 876 345 | 3 048 967 |
| 8 615 262 | 9 554 981 | 7 334 755 | 76.8% | 10 147 894 | 10 592 320 | 10 548 003 | 99.6% | 7 902 643 | 9 011 880 | 8 617 753 |
| 16 925 024 | 18 822 301 | 18 945 871 | 100.7% | 16 956 226 | 17 529 459 | 15 202 596 | 86.7% | 13 028 603 | 10 010 265 | 10 646 623 |

| 2008-09 | | | | 2009-10 | | | | 2010-11 | 2011-12 | 2012-13 |
|---|---|---|---|---|---|---|---|---|---|---|
| Original budget | Revised budget | Outcome | Outcome as % of Revised budget | Original budget | Revised budget | Outcome | Outcome as % of Revised budget | Medium-term estimates | | |
| 130 123 179 | 131 228 602 | 139 336 656 | 1007.5% | 153 013 003 | 168 589 239 | 163 177 044 | 941.8% | 191 441 226 | 205 083 526 | 229 131 886 |
| 46 093 446 | 48 843 894 | 41 669 365 | 712.2% | 49 946 470 | 47 963 576 | 40 938 752 | 717.0% | 41 190 190 | 39 316 427 | 40 553 160 |
| **176 216 625** | **180 072 496** | **181 006 021** | **100.5%** | **202 959 473** | **216 552 815** | **204 115 796** | **94.3%** | **232 631 416** | **244 399 953** | **269 685 046** |

## Annexure B: Aggregate national transfers and conditional grants to local government, 2006/07 – 2012/13

| | | 2006-07 | | | | | 2007-08 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | National Financial Year | | | | | National Financial Year | | | | |
| Sch. | Grant | *Original allocation* | *Adjustment* | *Revised allocation* | *Amounts received or transferred* | *Actual Expenditure* | *Original allocation* | *Adjustment* | *Revised allocation* | *Amounts received or transferred* | *Actual Expenditure* |
| | **Equitable share and related** | **18 557 940** | **50 257** | **18 608 197** | **18 520 387** | **18 508 144** | **21 225 620** | **71 744** | **21 297 364** | **21 290 257** | **21 255 877** |
| 3 | Equitable Share | 18 057 940 | - | 18 057 940 | 18 057 940 | 18 057 940 | 20 675 620 | - | 20 675 620 | 20 675 620 | 20 675 620 |
| 6 | Water Services Operating and Transfer Subsidy Grant (Augmentation to the Water Trading Account) | 500 000 | 50 257 | 550 257 | 462 447 | 450 204 | 550 000 | 71 744 | 621 744 | 614 637 | 580 257 |
| | **Infrastructure** | **8 637 395** | **454 116** | **9 091 511** | **7 318 372** | **7 286 183** | **13 758 616** | **3 550 878** | **17 309 494** | **15 126 774** | **14 981 143** |
| | *Direct transfers* | | | | | | | | | | |
| 4 | Urban Settlement Development Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Municipal Infrastructure Grant | 6 265 300 | -12 617 | 6 252 683 | 5 809 379 | 5 800 817 | 7 548 564 | 713 224 | 8 261 788 | 8 261 788 | 8 238 214 |
| 6 | Local Economic Development Programme Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Community Based Public Works Programme Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Urban Transport Fund Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Consolidated Municipal Infrastructure Programme Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Building for Sports and Recreation Programme Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | National Electrification Programme (Municipal) Grant | 391 130 | - | 391 130 | 390 973 | 383 662 | 467 827 | - | 467 827 | 462 492 | 453 292 |
| 6 | Public Transport Infrastructure and Systems Grant | 519 000 | - | 519 000 | 518 020 | 505 704 | 1 174 000 | - | 1 174 000 | 1 174 000 | 1 148 605 |
| 6 | Neighbourhood Development Partnership Grant | - | - | - | - | - | - | 231 200 | 231 200 | 41 242 | 41 242 |
| 6 | 2010 FIFA World Cup Stadiums Development Grant | - | 600 000 | 600 000 | 600 000 | 596 000 | 2 700 000 | 1 905 000 | 4 605 000 | 4 604 999 | 4 576 523 |
| 6 | Municipal Drought Relied funds (DWAF) | - | - | - | - | - | - | 100 000 | 100 000 | 89 900 | 69 303 |
| 6 | Disaster funds: dplg | - | - | - | - | - | - | 492 352 | 492 352 | 492 353 | 453 964 |
| 6 | Rural Transport Services and Infrastructure Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Electricity Demand Side Management (Municipal) Grant | - | - | - | - | - | - | - | - | - | - |
| 6 | Implementation of Water Services Projects (Capital) | - | - | - | - | - | - | - | - | - | - |
| | *Indirect transfers* | | | | | | | | | | |
| 7 | Water Services Operating Subsidy Grant | 490 500 | -50 257 | 440 243 | - | - | 490 025 | 6 714 | 496 739 | - | - |
| 7 | Community Based Public Works Programme Grant (indirect grant) | - | - | - | - | - | - | - | - | - | - |
| 7 | Integrated National Electrification Programme (Eskom) Grant | 971 465 | -83 010 | 888 455 | - | - | 930 200 | 39 027 | 969 227 | - | - |
| 7 | Regional Bulk Infrastructure Grant | - | - | - | - | - | 300 000 | - | 300 000 | - | - |
| 7 | Backlogs in Water and Sanitation at Clinics and Schools Grant | - | - | - | - | - | 103 000 | -439 | 102 561 | - | - |
| 7 | Backlogs in the Electrification of Clinics and Schools Grant | - | - | - | - | - | 45 000 | - | 45 000 | - | - |
| 7 | Neighbourhood Development Partnership Grant (Technical assistance) | - | - | - | - | - | - | 63 800 | 63 800 | - | - |
| 7 | Electricity Demand Side Management (Eskom) Grant | - | - | - | - | - | - | - | - | - | - |
| 7 | Rural Households Infrastructure Grant (Schedule 7) | - | - | - | - | - | - | - | - | - | - |
| | **Capacity building** | **748 657** | **95 000** | **843 657** | **610 250** | **577 010** | **748 657** | **180 000** | **928 657** | **874 750** | **863 186** |
| | *Direct transfers* | | | | | | | | | | |
| 6 | Municipal Systems Improvement Programme Grant | 200 000 | - | 200 000 | 200 000 | 192 487 | 200 000 | - | 200 000 | 200 000 | 193 079 |
| 6 | Local Government Restructuring Grant | 350 000 | 95 000 | 445 000 | 265 000 | 246 766 | 350 000 | 180 000 | 530 000 | 530 000 | 530 000 |
| 6 | Local Government Financial Management Grant | 145 250 | - | 145 250 | 145 250 | 137 757 | 145 250 | - | 145 250 | 144 750 | 140 106 |
| | *Indirect transfers* | | | | | | | | | | |
| 7 | Financial Management Grant: DBSA | 53 407 | - | 53 407 | - | - | 53 407 | - | 53 407 | - | - |
| | **Other** | | | | | | | | | | |
| 6 | 2010 FIFA World Cup Host City Operating Grant | - | - | - | - | - | - | - | - | - | - |
| 8 | Expanded Pubic Works Programme Incentive Grant for Municipalities | - | - | - | - | - | - | - | - | - | - |
| | | **27 943 992** | **599 373** | **28 543 365** | **26 449 009** | **26 371 337** | **35 732 893** | **3 802 622** | **39 535 515** | **37 291 781** | **37 100 206** |

| 2008-09 | | | | | 2009-10 | | | | | 2010-11 | 2011-12 | 2012-13 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| National Financial Year | | | | | National Financial Year | | | | | | MTREF | |
| *Original allocation* | *Adjustment* | *Revised allocation* | *Amounts received or transferred* | *Actual Expenditure* | *Original allocation* | *Adjustment* | *Revised allocation* | *Amounts received or transferred* | *Actual Expenditure* | *Original allocation* | *Original allocation* | *Original allocation* |
| **25 750 152** | **795 154** | **26 545 306** | **25 873 846** | **25 852 962** | **24 825 081** | **401 699** | **25 226 780** | **25 095 352** | **24 952 553** | **30 829 410** | **34 319 891** | **37 633 396** |
| 24 888 685 | 670 995 | 25 559 680 | 24 888 692 | 24 888 692 | 23 846 502 | 509 000 | 24 355 502 | 24 246 618 | 24 246 618 | 30 167 706 | 33 939 901 | 37 234 396 |
| 861 467 | 124 159 | 985 626 | 985 154 | 964 270 | 978 579 | -107 301 | 871 278 | 848 734 | 705 935 | 661 704 | 379 990 | 399 000 |
| **18 002 806** | **1 537 445** | **19 540 251** | **17 112 417** | **16 823 437** | **19 729 876** | **509 635** | **20 239 512** | **17 041 411** | **14 296 279** | **22 164 150** | **26 555 655** | **29 400 703** |
| - | - | - | - | - | - | - | - | - | - | 2 604 083 | 3 131 944 | 3 808 158 |
| 8 653 919 | 437 145 | 9 091 064 | 9 089 582 | 8 912 006 | 11 084 860 | 348 634 | 11 433 494 | 11 303 301 | 9 370 673 | 9 924 800 | 11 936 607 | 14 513 821 |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| - | 8 900 | 8 900 | 8 900 | 5 993 | - | - | - | - | - | - | - | - |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| 595 637 | - | 595 637 | 590 639 | 534 007 | 932 957 | - | 932 957 | 914 414 | 766 666 | 1 020 104 | 1 096 612 | 1 151 443 |
| 3 170 000 | -250 169 | 2 919 831 | 2 919 831 | 2 873 372 | 2 418 177 | - | 2 418 177 | 2 418 177 | 1 933 481 | 3 699 462 | 4 425 000 | 4 125 000 |
| 407 015 | -118 015 | 289 000 | 182 148 | 177 150 | 582 000 | -30 606 | 551 394 | 505 912 | 422 777 | 1 030 000 | 1 190 440 | 1 182 462 |
| 2 895 000 | 1 400 000 | 4 295 000 | 4 295 000 | 4 294 994 | 1 661 107 | - | 1 661 107 | 1 661 107 | 1 648 840 | 302 286 | - | - |
| - | 9 000 | 9 000 | 9 000 | 8 598 | - | 53 700 | 53 700 | 53 700 | 53 700 | 228 357 | - | - |
| - | 17 317 | 17 317 | 17 317 | 17 317 | - | - | - | - | - | - | 470 000 | - |
| - | - | - | - | - | 9 800 | - | 9 800 | 9 800 | 4 180 | 10 400 | 11 100 | 11 655 |
| - | - | - | - | - | 175 000 | - | 175 000 | 175 000 | 95 962 | 220 000 | 280 000 | - |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| 269 040 | 59 601 | 328 641 | - | - | 135 199 | 107 301 | 242 500 | - | - | 145 978 | - | - |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| 1 140 759 | 9 999 | 1 150 758 | - | - | 1 467 366 | 0 | 1 467 367 | - | - | 1 751 780 | 1 769 812 | 1 914 057 |
| 450 000 | - | 450 000 | - | - | 611 500 | - | 611 500 | - | - | 893 000 | 1 675 340 | 1 849 107 |
| 208 451 | 1 652 | 210 103 | - | - | 348 567 | - | 348 567 | - | - | - | - | - |
| 90 000 | - | 90 000 | - | - | 148 950 | - | 148 950 | - | - | - | - | - |
| 122 985 | -37 985 | 85 000 | - | - | 79 394 | 30 606 | 110 000 | - | - | 125 000 | 100 000 | 105 000 |
| - | - | - | - | - | 75 000 | - | 75 000 | - | - | 108 900 | 118 800 | - |
| - | - | - | - | - | - | - | - | - | - | 100 000 | 350 000 | 740 000 |
| **430 000** | **-** | **430 000** | **380 000** | **358 159** | **499 990** | **-** | **499 990** | **469 490** | **378 465** | **576 589** | **609 361** | **639 829** |
| 200 000 | - | 200 000 | 200 000 | 188 128 | 200 000 | - | 200 000 | 200 000 | 159 078 | 212 000 | 224 720 | 235 956 |
| - | - | - | - | - | - | - | - | - | - | - | - | - |
| 180 000 | - | 180 000 | 180 000 | 170 031 | 299 990 | - | 299 990 | 269 490 | 219 387 | 364 589 | 384 641 | 403 873 |
| 50 000 | - | 50 000 | - | - | - | - | - | - | - | - | - | - |
| - | - | - | - | - | 507 557 | - | 507 557 | 507 557 | 465 231 | 210 280 | - | - |
| - | - | - | - | - | 201 748 | - | 201 748 | - | - | 682 415 | 1 108 000 | 1 163 400 |
| **44 182 958** | **2 332 599** | **46 515 557** | **43 366 263** | **43 034 558** | **45 764 253** | **911 334** | **46 675 587** | **43 113 810** | **40 092 528** | **54 462 844** | **62 592 908** | **68 837 328** |

# Annexure C: Aggregate municipal personnel spending, 2006/07 – 2012/13

| Summary of Employee and Councillor Remuneration | 2006/07 | 2007/08 | 2008/09 | Current year 2009/10 | | | 2010/11 Medium Term Revenue & Expenditure Framework | | |
|---|---|---|---|---|---|---|---|---|---|
| R thousands | Audited Outcome | Audited Outcome | Audited Outcome | Original Budget | Adjusted Budget | Full Year Forecast | Budget Year 2010/11 | Budget Year 2011/12 | Budget Year 2012/13 |
| | A | B | C | D | E | F | G | H | I |
| ***Councillors (Political Office Bearers plus Other)*** | | | | | | | | | |
| Salary | 921 345 | 1 162 752 | 1 172 254 | 1 375 380 | 1 227 165 | 1 280 577 | 1 532 807 | 1 648 577 | 1 738 526 |
| Pension Contributions | 85 863 | 95 064 | 102 998 | 122 638 | 118 074 | 116 527 | 112 655 | 131 726 | 141 665 |
| Medical Aid Contributions | 18 013 | 20 322 | 24 598 | 39 434 | 35 824 | 38 070 | 44 528 | 47 052 | 50 507 |
| Motor vehicle allowance | 160 197 | 196 445 | 212 314 | 275 651 | 252 682 | 269 696 | 343 833 | 361 441 | 386 140 |
| Cell phone allowance | 17 677 | 26 811 | 31 725 | 53 010 | 49 010 | 48 139 | 69 018 | 71 691 | 76 293 |
| Housing allowance | 9 710 | 9 187 | 7 626 | 7 704 | 6 913 | 7 128 | 8 206 | 8 825 | 9 655 |
| Other benefits or allowances | 37 758 | 56 913 | 91 690 | 112 212 | 97 405 | 106 030 | 109 958 | 105 014 | 112 071 |
| In-kind benefits | 37 | 65 | 149 | 102 | 105 | 106 | 303 | 327 | 191 |
| **Sub Total - Councillors** | **1 250 601** | **1 567 559** | **1 643 353** | **1 986 131** | **1 787 179** | **1 866 272** | **2 221 307** | **2 374 654** | **2 515 048** |
| **% increase** | | **25.3%** | **4.8%** | **20.9%** | **-10.0%** | **4.4%** | **19.0%** | **6.9%** | **5.9%** |
| ***Senior Managers of the Municipality*** | 5 934 | 8 013 | 8 077 | 10 739 | 7 603 | 10 849 | 12 662 | 9 987 | 10 945 |
| Salary | 496 377 | 646 729 | 764 117 | 957 118 | 860 569 | 886 178 | 1 146 656 | 1 212 961 | 1 298 907 |
| Pension Contributions | 31 588 | 35 600 | 42 938 | 55 658 | 50 734 | 53 070 | 73 156 | 76 454 | 85 139 |
| Medical Aid Contributions | 10 095 | 11 682 | 11 438 | 15 320 | 14 476 | 15 669 | 22 140 | 22 473 | 24 211 |
| Motor vehicle allowance | 63 350 | 81 743 | 103 657 | 124 122 | 114 259 | 118 136 | 157 837 | 164 291 | 176 394 |
| Cell phone allowance | 1 937 | 3 474 | 3 076 | 5 340 | 5 119 | 5 323 | 8 922 | 9 135 | 9 993 |
| Housing allowance | 5 062 | 4 851 | 4 743 | 8 689 | 8 357 | 9 037 | 13 984 | 13 363 | 14 678 |
| Performance Bonus | 26 117 | 32 905 | 48 710 | 77 268 | 65 416 | 64 459 | 92 519 | 97 418 | 108 039 |
| Other benefits or allowances | 19 520 | 32 607 | 32 763 | 27 281 | 27 624 | 29 676 | 31 812 | 33 873 | 35 872 |
| In-kind benefits | 8 377 | 12 265 | 14 736 | 15 689 | 9 664 | 15 068 | 18 542 | 14 879 | 15 758 |
| **Sub Total - Senior Managers of Municipality** | **668 356** | **869 870** | **1 034 255** | **1 297 224** | **1 163 821** | **1 207 466** | **1 578 228** | **1 654 834** | **1 779 936** |
| **% increase** | | **30.2%** | **18.9%** | **25.4%** | **-10.3%** | **3.8%** | **30.7%** | **4.9%** | **7.6%** |
| ***Other Municipal Staff*** | 37 667 | 37 169 | 45 858 | 58 273 | 33 997 | 34 146 | 65 659 | 40 790 | 45 581 |
| Basic Salaries and Wages | 15 093 044 | 17 565 621 | 20 305 130 | 25 283 681 | 24 607 177 | 24 740 822 | 29 726 791 | 32 146 803 | 34 599 166 |
| Pension Contributions | 2 760 502 | 3 269 345 | 3 742 461 | 4 715 725 | 4 433 670 | 4 457 598 | 5 464 816 | 5 879 346 | 6 321 138 |
| Medical Aid Contributions | 947 205 | 1 200 740 | 1 393 887 | 1 777 835 | 1 687 504 | 1 736 607 | 2 169 355 | 2 355 247 | 2 527 997 |
| Motor vehicle allowance | 920 961 | 1 096 762 | 1 169 001 | 1 327 023 | 1 242 751 | 1 238 208 | 1 439 535 | 1 531 643 | 1 634 199 |
| Cell phone allowance | 44 281 | 34 430 | 54 564 | 58 171 | 44 324 | 56 246 | 71 491 | 74 265 | 80 168 |
| Housing allowance | 221 221 | 279 684 | 297 042 | 365 532 | 333 266 | 339 022 | 393 641 | 413 864 | 438 150 |
| Overtime | 1 227 261 | 1 445 938 | 1 993 507 | 1 444 705 | 1 531 920 | 1 584 466 | 1 860 690 | 2 003 256 | 2 142 237 |
| Performance Bonus | 115 651 | 184 940 | 252 371 | 393 368 | 427 699 | 440 160 | 626 571 | 580 465 | 630 589 |
| Other benefits or allowances | 2 274 464 | 1 995 016 | 2 412 117 | 2 462 542 | 2 200 641 | 2 482 593 | 3 038 733 | 3 041 996 | 3 283 173 |
| In-kind benefits | 239 557 | 292 715 | 378 548 | 498 803 | 70 133 | 40 620 | 75 873 | 79 788 | 90 954 |
| **Sub Total - Other Municipal Staff** | **23 881 814** | **27 402 361** | **32 044 485** | **38 385 659** | **36 613 083** | **37 150 487** | **44 933 154** | **48 147 463** | **51 793 350** |
| **% increase** | | **14.7%** | **16.9%** | **19.8%** | **-4.6%** | **1.5%** | **20.9%** | **7.2%** | **7.6%** |
| **Total Parent Municipality** | **25 800 771** | **29 839 789** | **34 722 093** | **41 669 015** | **39 564 084** | **40 224 225** | **48 732 690** | **52 176 951** | **56 088 334** |
| **% Increase** | | **15.7%** | **16.4%** | **20.0%** | **-5.1%** | **1.7%** | **21.2%** | **7.1%** | **7.5%** |
| **Board Members of Entities** | | | (0) | | | | | | |
| Salary | 2 356 | 15 132 | 16 401 | 24 045 | 22 580 | 22 572 | 22 102 | 23 368 | 24 646 |
| Pension Contributions | | 18 286 | | 30 805 | 30 805 | 30 704 | 34 176 | 35 789 | 36 614 |
| Medical Aid Contributions | | | (0) | | | | 167 | 178 | 189 |
| Motor vehicle allowance | | 427 | 483 | 497 | 481 | 490 | 623 | 667 | 710 |
| Cell phone allowances | | | | | | | | | |
| Housing allowance | | | | | 535 | 535 | 469 | 501 | 530 |
| Board Fees | 1 443 | 6 295 | 2 038 | 2 940 | 4 928 | 2 818 | 4 949 | 5 363 | 5 711 |
| Other benefits and allowances | 13 | 61 | 66 | | | | 2 | 2 | 2 |
| In-kind benefits | 6 061 | 8 339 | 7 521 | 9 724 | 7 657 | 7 847 | 12 015 | 12 796 | 12 225 |
| **Sub Total - Board Members of Entities** | **9 873** | **48 539** | **26 509** | **68 011** | **66 986** | **64 966** | **74 501** | **78 663** | **80 626** |
| **% increase** | | **391.6%** | **-45.4%** | **156.6%** | **-1.5%** | **-3.0%** | **14.7%** | **5.6%** | **2.5%** |
| **Senior Managers of Entities** | | | | | | | | | |
| Salary | 75 504 | 91 613 | 78 231 | 111 766 | 100 685 | 105 870 | 140 044 | 148 750 | 160 341 |
| Pension Contributions | 4 842 | 5 250 | 5 695 | 6 710 | 22 616 | 23 459 | 26 396 | 28 228 | 29 947 |
| Medical Aid Contributions | 1 843 | 1 772 | 1 784 | 2 289 | 13 072 | 13 359 | 14 435 | 15 427 | 16 343 |
| Motor vehicle allowance | 5 617 | 5 453 | 6 780 | 1 688 | 7 027 | 6 895 | 9 734 | 10 511 | 11 277 |
| Cell phone allowances | | | 1 071 | 6 543 | 260 | 1 304 | 1 656 | 1 790 | 1 941 |
| Housing allowance | 142 | 732 | 1 143 | 44 | 12 340 | 12 346 | 13 626 | 14 567 | 15 404 |
| Performance Bonus | 8 342 | 8 193 | 8 493 | 13 490 | 19 427 | 19 323 | 24 636 | 26 580 | 28 222 |
| Other benefits or allowances | 2 370 | 3 714 | 1 590 | 2 002 | 668 | 809 | 1 127 | 1 070 | 1 152 |
| In-kind benefits | | | | | | | | 1 | |
| **Sub Total - Senior Managers of Entities** | **98 660** | **116 727** | **104 788** | **144 532** | **176 096** | **183 366** | **231 654** | **246 923** | **264 626** |
| **% increase** | | **18.3%** | **-10.2%** | **37.9%** | **21.8%** | **4.1%** | **26.3%** | **6.6%** | **7.2%** |
| **Other Staff of Entities** | | | | | | | | | |
| Basic Salaries and Wages | 1 237 062 | 1 401 686 | 1 587 034 | 1 817 658 | 1 937 785 | 1 990 018 | 1 872 817 | 2 031 622 | 2 177 560 |
| Pension Contributions | 165 031 | 211 934 | 243 316 | 277 857 | 232 263 | 244 930 | 282 479 | 318 181 | 341 711 |
| Medical Aid Contributions | 96 272 | 111 263 | 134 615 | 158 953 | 136 474 | 144 163 | 163 743 | 183 410 | 198 009 |
| Motor vehicle allowance | 95 122 | 84 279 | 104 785 | 123 144 | 133 142 | 129 531 | 136 401 | 158 869 | 169 915 |
| Cell phone allowances | | | 7 412 | 8 733 | 9 356 | 6 470 | 11 041 | 12 894 | 14 007 |
| Housing allowance | 13 709 | 13 776 | 16 912 | 22 617 | 17 414 | 18 612 | 23 593 | 25 969 | 27 852 |
| Overtime | 82 496 | 97 444 | 104 578 | 124 676 | 169 037 | 168 854 | 147 883 | 167 443 | 181 152 |
| Performance Bonus | 319 910 | 359 492 | 516 980 | 562 587 | 338 590 | 521 884 | 608 141 | 428 135 | 464 077 |
| Other benefits or allowances | 179 333 | 190 914 | 181 199 | 209 767 | 152 269 | 154 726 | 179 767 | 193 879 | 214 163 |
| In-kind benefits | 142 222 | 158 662 | 196 939 | 242 447 | 223 134 | 217 529 | 271 299 | 294 541 | 321 335 |
| **Sub Total - Other Staff of Entities** | **2 331 158** | **2 629 450** | **3 093 770** | **3 548 440** | **3 349 462** | **3 596 717** | **3 697 163** | **3 814 942** | **4 109 782** |
| **% increase** | | **12.8%** | **17.7%** | **14.7%** | **-5.6%** | **7.4%** | **2.8%** | **3.2%** | **7.7%** |
| **Total Municipal Entities** | **2 439 691** | **2 794 716** | **3 225 066** | **3 760 983** | **3 592 544** | **3 845 049** | **4 003 318** | **4 140 528** | **4 455 034** |
| **TOTAL SALARY, ALLOWANCES & BENEFITS** | **28 240 462** | **32 634 505** | **37 947 159** | **45 429 998** | **43 156 628** | **44 069 274** | **52 736 008** | **56 317 479** | **60 543 368** |
| **% increase** | | **15.6%** | **16.3%** | **19.7%** | **-5.0%** | **2.1%** | **19.7%** | **6.8%** | **7.5%** |
| **TOTAL MANAGERS AND STAFF** | **26 979 989** | **31 018 408** | **36 277 297** | **43 375 855** | **41 302 462** | **42 138 035** | **50 440 199** | **53 864 162** | **57 947 694** |

# Annexure D: Aggregate salaries and benefits of councillors and senior managers, 2010/11

| Disclosure of Salaries, Allowances and Benefits<br>Rand per Annum | Number | Salary | Contributions | Allowances | Performance Bonuses | In-kind Benefits | Total package |
|---|---|---|---|---|---|---|---|
| **Councillors** | | | | | | | |
| Speaker | 155 | 78 176 612 | 6 521 115 | 26 259 477 | 124 494 | 17 100 | 110 454 596 |
| Chief Whip | 40 | 31 566 009 | 3 140 171 | 11 079 230 | 55 363 | 17 100 | 45 785 406 |
| Mayor | | 811 858 | 58 638 | 308 624 | | | 1 179 120 |
| Executive Mayor | 93 | 98 122 688 | 8 410 051 | 32 317 819 | 151 338 | 917 100 | 138 226 964 |
| Deputy Executive Mayor | 32 | 28 717 088 | 2 088 507 | 9 430 267 | | | 40 235 862 |
| Additional Councillor after 2011 election (3 months) | 1 | 40 509 | 810 | | | | 41 319 |
| Executive Committee | 405 | 262 881 032 | 22 848 563 | 92 645 285 | 451 993 | 68 400 | 377 330 192 |
| Mayoral Committee | | 5 682 215 | | 2 082 168 | | | 7 764 383 |
| Member of Mayorol committee | 9 | 3 150 777 | | 1 216 477 | | | 4 367 254 |
| Total for all other councillors | 2 604 | 985 656 848 | 82 697 205 | 325 079 916 | 1 416 391 | 554 736 | 1 391 194 768 |
| **Total Councillors** | **3 338** | **1 492 440 050** | **125 765 059** | **499 774 136** | | **674 436** | **2 113 569 015** |
| **Senior Managers of the Municipality** | | | | | | | |
| City Manager | | 2 779 323 | 176 881 | 547 648 | 364 115 | | 3 867 967 |
| Municipal Manager (MM) | 96 | 183 766 849 | 13 679 292 | 36 221 767 | 13 676 433 | 363 022 | 246 821 589 |
| Chief Finance Officer | 85 | 141 600 813 | 14 908 285 | 29 556 884 | 10 186 386 | 223 647 | 195 771 566 |
| Chief Financial Officer | | 827 139 | 19 614 | 354 488 | 160 701 | | 1 361 942 |
| Chief Operating Officer | | 1 238 497 | | | 185 775 | | 1 424 272 |
| Deputy Municipal Manager | 1 | 516 913 | 117 074 | 105 317 | 101 823 | | 841 127 |
| Deputy Municipal Manager (DMM) | 2 | 1 231 062 | 176 734 | 595 470 | 237 767 | | 2 241 033 |
| Director: Finance & Administration | 1 | 328 500 | 6 457 | 84 000 | 57 750 | | 476 707 |
| Executive Director : Economic Development | | 1 396 908 | | 139 992 | 128 023 | | 1 664 923 |
| Manager Finance | 1 | 482 543 | | 180 000 | 84 963 | | 747 506 |
| Other Senior Managers | 396 | 606 068 680 | 448 049 054 | 124 767 564 | 44 638 242 | 1 620 240 | 1 212 220 904 |
| **Total Senior Managers of the Municipality** | **582** | **938 648 480** | **477 111 173** | **192 296 781** | **69 742 923** | **2 206 911** | **1 665 493 207** |
| Polokwane Housing Assosiasion | | | | | | | |
| West Rand Development Agency | | | | | | | |
| Board Member | 9 | 173 372 | | 16 628 | | | 190 000 |
| List each member of board by designation | | | | | | | |
| Chief Executive Officer (CEO) | 1 | 1 509 869 | | 84 691 | | | 1 594 560 |
| Municipal Entities | 1 | 39 827 045 | 3 122 596 | 3 692 896 | 5 452 182 | | 39 895 125 |
| **Total for municipal entities** | **11** | **44 029 811** | **4 300 277** | **5 223 108** | **4 651 007** | | **46 082 644** |
| **TOTAL COST OF COUNCILLOR, DIRECTOR and EXECUTIVE REMUNERATION** | **3 885** | **2 460 240 510** | **604 558 177** | **692 174 504** | **73 815 397** | **2 881 347** | **3 801 919 083** |

# Annexure E: Aggregate personnel numbers as at 30 June 2010

| Summary of Personnel Numbers | Previous year 2008/09 | | | Current year 2009/10 | | | Next year 2010/11 | | |
|---|---|---|---|---|---|---|---|---|---|
| Number | Positions | Permanent Employees | Contract Employees | Positions | Permanent Employees | Contract Employees | Positions | Permanent Employees | Contract Employees |
| **Municipal Council and Boards of Municipal Entities** | | | | | | | | | |
| Councillors (Political Office Bearers plus Other Councillors | 5 928 | 1 743 | 4 015 | 6 540 | 2 174 | 4 302 | 6 638 | 2 221 | 4 285 |
| Board Members of municipal entities | 87 | 49 | 107 | 192 | 41 | 154 | 185 | 65 | 145 |
| **Municipal employees** | 1 322 | 1 259 | 89 | 293 | 787 | 372 | 329 | 206 | 49 |
| Municipal Manager and Senior Managers | 1 229 | 495 | 926 | 1 432 | 507 | 1 088 | 1 462 | 631 | 1 113 |
| Other Managers | 3 655 | 3 144 | 1 165 | 5 678 | 3 949 | 1 309 | 5 906 | 4 241 | 1 187 |
| Professionals | 13 346 | 13 921 | 1 003 | 17 600 | 17 566 | 1 227 | 18 880 | 17 968 | 2 074 |
| *Finance* | 3 643 | 3 370 | 406 | 4 344 | 3 760 | 460 | 4 591 | 4 065 | 586 |
| *Spatial/town planning* | 748 | 740 | 63 | 1 164 | 937 | 76 | 1 143 | 985 | 253 |
| *Information Technology* | 352 | 302 | 54 | 457 | 381 | 69 | 587 | 516 | 153 |
| *Roads* | 1 063 | 1 249 | 178 | 2 755 | 2 856 | 214 | 2 677 | 2 250 | 182 |
| *Electricity* | 1 284 | 1 522 | 21 | 2 180 | 1 808 | 14 | 2 268 | 1 974 | 403 |
| *Water* | 2 092 | 1 902 | 144 | 2 441 | 2 317 | 155 | 2 616 | 2 581 | 270 |
| *Sanitation* | 772 | 800 | 21 | 897 | 908 | 11 | 939 | 985 | 17 |
| *Refuse* | 1 966 | 2 069 | 59 | 1 812 | 2 346 | 72 | 1 969 | 2 522 | 84 |
| *Other* | 23 770 | 9 972 | 950 | 29 086 | 27 089 | 17 358 | 29 666 | 29 235 | 19 006 |
| Technicians | 12 164 | 12 885 | 1 474 | 19 091 | 16 660 | 615 | 20 531 | 17 064 | 861 |
| *Finance* | 800 | 898 | 100 | 1 408 | 1 166 | 104 | 1 217 | 1 027 | 148 |
| *Spatial/town planning* | 582 | 824 | 79 | 1 318 | 897 | 23 | 1 591 | 1 070 | 27 |
| *Information Technology* | 285 | 283 | 23 | 540 | 462 | 24 | 529 | 474 | 15 |
| *Roads* | 1 538 | 1 452 | 908 | 2 385 | 1 930 | 234 | 2 678 | 2 176 | 253 |
| *Electricity* | 2 383 | 2 414 | 50 | 2 896 | 2 378 | 32 | 2 639 | 2 182 | 27 |
| *Water* | 2 354 | 2 343 | 42 | 2 888 | 2 690 | 54 | 3 732 | 3 509 | 82 |
| *Sanitation* | 1 158 | 1 123 | 63 | 1 390 | 1 261 | 39 | 1 277 | 1 148 | 51 |
| *Refuse* | 1 722 | 1 678 | 33 | 2 281 | 2 130 | 37 | 2 153 | 2 029 | 49 |
| *Other* | 9 833 | 12 957 | 731 | 14 652 | 11 774 | 502 | 16 155 | 12 652 | 505 |
| Clerks (Clerical and administrative) | 23 144 | 25 769 | 1 900 | 35 249 | 29 041 | 2 106 | 36 871 | 29 816 | 2 671 |
| Service and sales workers | 16 579 | 19 978 | 1 247 | 25 687 | 21 788 | 1 530 | 23 725 | 19 850 | 1 484 |
| Skilled agricultural and fishery workers | 910 | 899 | 10 | 1 089 | 1 224 | 17 | 1 088 | 1 161 | 31 |
| Craft and related trades | 5 115 | 5 716 | 42 | 6 858 | 6 528 | 46 | 7 867 | 7 241 | 63 |
| Plant and Machine Operators | 12 239 | 13 901 | 573 | 16 608 | 14 459 | 494 | 16 945 | 14 901 | 293 |
| Elementary Occupations | 40 296 | 38 877 | 3 313 | 53 635 | 41 628 | 6 355 | 55 062 | 39 573 | 8 706 |
| **TOTAL PERSONNEL NUMBERS** | **166 822** | **157 731** | **17 514** | **228 111** | **189 212** | **37 197** | **234 447** | **191 297** | **42 040** |
| **% increase** | | | | **36.7%** | **20.0%** | **112.4%** | **2.8%** | **1.1%** | **13.0%** |
| **Total municipal employees headcount** | **42 492** | **60 381** | **3 070** | **54 796** | **62 962** | **3 662** | **52 565** | **61 649** | **3 581** |
| Finance personnel headcount | 7 380 | 7 933 | 602 | 8 973 | 8 782 | 622 | 8 876 | 8 433 | 640 |
| Human Resources personnel headcount | 2 843 | 3 353 | 456 | 3 873 | 3 672 | 577 | 3 589 | 3 477 | 834 |