

**2023 DIVISION OF REVENUE AMENDMENT BILL**

**Responses to recommendations contained in the Negotiating Mandates from Provincial Legislatures**

The Select Committee on Appropriations held a virtual meeting on 27 November 2023 to consider the negotiating mandates on the Division of Revenue Amendment Bill, 2023, that were submitted by provincial legislatures. Representatives of National Treasury participated in the meeting and gave verbal comments on some of the recommendations made and also undertook to provide brief written replies on the recommendations raised by provincial legislatures in their negotiating mandates. These written comments are provided below.

Where recommendations fall within the mandate of other departments, National Treasury will refer these to the relevant stakeholders.

**EASTERN CAPE**

**We must reiterate the concern with respect to the equitable share formula which does not take into account more of rural parts in the Province. Secondly, the absence of equitable share formula amongst the three spheres of government is still a concern.**

We recognise the challenges that come with delivering services in rural areas, and the current review of the Provincial Equitable Share Formula is exploring ways to address these concerns. The task team includes provincial treasuries, and the formula already takes into account the initial costs incurred by provinces in running a provincial government through the Institutional Component. The health component has also been reviewed with considerations for the concerns raised by provinces, and a new variable for sparsity has been included in the redesigned risk-adjusted index.

Although no formula exists for the vertical division of revenue amongst the three spheres of government, section 214(1) of the Constitution outlines 10 key principles that are considered when determining the Division of Revenue, which includes reducing economic disparities and promoting stability and predictability. These principles ensure that the revenue allocations take into account government spending priorities and each sphere's revenue-raising capacity and responsibilities. Municipalities have the ability to raise substantial own revenues through property rates and service charges, which is accounted for in the 2023 Division of Revenue Bill. We remain committed to addressing the concerns raised and finding ways to ensure that resources are efficiently allocated to meet the needs of all South Africans. Annexure W1 to the 2023 Division of Revenue Bill further outlined in detail how these considerations were taken into account in the 2023 division of revenue. None of the adjustments in this Bill alter the constitutional considerations that informed the 2023 division of revenue, which is why this detail is not part of the 2023 Division of Revenue Amendment Bill.

**With regard to sections 18 and 19 of the Division of Revenue Act of 2023 which refers to the stopping and reallocation of funds, the shifting of conditional grants needs to be reconsidered to make sure that the funding is not taken from provinces without the conditional grants funding having addressed the purpose it was allocated for in the particular year.**

**When funds are re-allocated away from provinces it will deprive the province in speedily addressing service delivery issues such as the emergencies in cases of the disaster grant. The funds that are underspent on conditional grants should be rescheduled to the following year to allow for the projects to be completed especially these projects that are committed for completion by departments. In addition, it is unclear how the funds are utilised by other provinces that receive the unspent conditional grant funds given the late transfer of funds which is late in the financial year.**

With respect to the use of unspent conditional grants to respond to disasters, conditional grants are not envisaged to be the primary funding source for disaster response, nor can provinces and municipalities use conditional grants for disaster response without a recommendation from the relevant transferring officer and the National Disaster Management Centre. The Disaster Management Act makes clear that the first port of call for disaster response is reprioritisation of own budgets. Only if there isn’t capacity to fully fund the response can provinces and municipalities request funding from the national fiscus. Section 25 of the DoRA allows for the immediate release of funds from the immediate response grants in Schedule 7 of the DoRA, while section 19(6) allows for the reprioritization of conditional grants.

With respect to unspent funds being rescheduled to the following year to allow for the projects to be completed, roll-overs are already provided in section 21(2) of the DoRA. Approval of a roll-over request requires that unspent funds be committed to identifiable projects.

With respect to the capacity of receiving officers to spend reallocated amounts received, section 19(3) of the DoRA requires consultation with anticipated receiving officers. Receiving officers are given 14 days to comment and propose changes to what has been proposed by the relevant transferring officer.

**Similarly, for public transportation, the conditional grant funding has favoured the metropolitan councils, for example the Bus Rapid Transit System (BRT). National Treasury should review the grant funding model and consider local municipalities as there is increasing demand of public transport in these municipalities.**

Currently, the Public Transport Network grant is allocated to metropolitan municipalities and secondary/intermediate cities. However, we understand the importance of considering local municipalities, given the increasing demand for public transport in those areas. This issue will be considered as part of the ongoing conditional grants review.

**Regarding unspent conditional grants at local government level and in particular, the Municipal Infrastructure Grant (MIG), it is recommended that the funds should be transferred or redirected within the district (for local municipalities) whereby the current expenditure is in line with projections or planned service delivery.**

The stopping and reallocation process already allows for such arrangements if the relevant local and district municipalities agree to it. However, it's important to consider the "potential receiving municipality's" spending and implementation capacity, in this case, the district municipality, as it is one of the key factors. While the reallocation process is not solely based on the feasibility of the district municipality taking over from the local municipality, the ability of the receiving municipality to spend the reallocated funds by the end of the financial year is another critical condition outlined in section 19(1) of the 2023 Division of Revenue Act (DoRA). Therefore, unspent conditional grants cannot be automatically redirected to the district municipality without considering all the conditions listed in section 19 of the 2023 DoRA. In the case where the district municipality is unable to take over the funds, the Department of Cooperative Governance may implement projects on behalf of the municipalities by converting allocations to allocations in-kind.

**Reduction of Municipal Infrastructure Grant (MIG) direct grant by R244 million is affecting all municipalities in the province except metros. Though we understand the Fiscal consolidation being the main reason, it should be noted that Eastern Cape is one of the poorest provinces and requires funding to address service delivery.**

The Municipal Infrastructure Grant (MIG) is not allocated to the eight metros, as the Urban Settlements Development Grant (USDG) is the equivalent grant for metros. Unfortunately, the USDG was reduced by R553 million, which equates to 6.8% of the baseline. Similarly, the MIG faced a similar 6.8% reduction in baseline.

Regarding the service delivery needs in the Eastern Cape, we understand and share your concerns. The National Treasury remains focused on the province's underspending on municipal conditional grants. Despite the capacity building support embedded in several of the grants provided to municipalities in the province, there has been a persistent under-expenditure issue. In the last three audit periods, Eastern Cape municipalities have only spent an average of 70% of their conditional grants, which is worrying. We are dedicated to working towards addressing this issue and increasing the effectiveness of our grant allocation systems so that the communities receive the services they need and deserve.

**FREE STATE**

**District Development Model - the Portfolio Committee was made aware that National Treasury, Provincial Treasury and Local Government will be responsible for the funding of the model and that CoGTA and Provincial Treasury will respectively facilitate and guide local municipalities on how to implement the model, however there is still uncertainty on how this process will unfold.**

Over the past three years, funding has been allocated through the Municipal Systems Improvement Grant to develop diagnostic studies that establish the foundation for the One Plans of the 44 districts and 8 metropolitan spaces. Furthermore, there is funding available for the institutionalisation of the District Development Model (DDM) approach model during the 2023/24 financial year and over the upcoming MTEF period.

As the sector department responsible for the DDM model, the Department of Cooperative Governance is in the best position to provide guidance on the implementation process of the DDM. We will forward the recommendation to clarify the roles and responsibilities of each sphere of government in supporting municipalities with the implementation of the DDM model to the Department of Cooperative Governance for action.

**Global Economic outlook and its ramifications – the National Government must develop a comprehensive social security programme to protect municipalities and communities that are in distress.**

Acknowledging the vital role social protection plays in advancing government's key priorities, government continues to prioritise social spending despite the mandatory fiscal consolidation reductions. Specifically, health, education, and social protections remain key areas of focus, with 61.3 percent of non-interest spending in the 2023/24 fiscal year already directed towards the social wage. This expenditure pattern is set to continue across the 2024 MTEF period, with an average of 61 percent of non-interest spending dedicated to social wage.

Additionally, we recognise the need for dedicated support to municipalities in distress. Currently, appropriate structures and processes are in place to render such support. Firstly, the Eskom Debt Relief Programme aims to guarantee uninterrupted access to electricity for citizens in affected municipalities. Secondly, the review of the capacity building system for local government is ongoing and emphasises collaboration, a problem-led approach, and a whole-municipality approach. This new framework is designed to enhance municipal capability development sustainability, resulting in stronger municipal capacity to perform their delegated functions and improve service delivery.

**Loadshedding- National Treasury must take into serious consideration the financial impact of power outages and must consider compensating municipalities for unforeseeable costs associated with energy crisis.**

We recognise that the impact of loadshedding has been felt widespread across the provinces, municipalities, national government, and the private sector. As a result, we must acknowledge that the fiscus may have limited capacity to accommodate requests due to the significant downtime resulting from loadshedding. This downtime has had a substantial impact on the functioning of several sectors of the economy, leading to a negative effect on revenue generation.

Furthermore, we must acknowledge that energy-intensive industries such as mining, quarrying, and manufacturing have been particularly affected by loadshedding. These sectors continue to face significant challenges in their operations while loadshedding persists. The negative effects of loadshedding will be compounded by ongoing logistical challenges such as constraints in rail infrastructure.

**Local business in distress: National Treasury must also include the local businesses in their economic recovery strategy to assist those businesses**

The recommendation is noted. The economic recovery plan focuses on providing a range of support for local businesses affected by the pandemic to ensure they can recover, sustain and contribute to the post-pandemic economy. For instance, in response to the income losses that farmers and agribusinesses are facing, the economic recovery plan aims to provide targeted support for the agricultural sector. This support will enable farmers and producers to recapitalise their businesses, market their produce, and improve their income to strengthen the sector's contribution to the economy. In addition, a number of programmes are in place to support small businesses through national initiatives, managed by departments like Department of Small Business Development and the National Youth Development Agency.

**Funding for rehabilitation of roads: funding must be allocated to local government to address the rehabilitation of roads due to the collapse of rail systems which puts more pressure on the over usage of roads which results in damage of road infrastructure.**

Funding for refurbishment and maintenance of these roads is already provided for in the Municipal Infrastructure Grant (MIG) and Integrated Urban Development Grant (IUDG) allocated to local municipalities and intermediate cities, respectively.

On average, the MIG and IUDG allocate R3 billion per annum towards road maintenance and refurbishment. However, it has been noted that municipalities often spend double this amount. Thus, the issue pertaining to the state of municipal roads, particularly those in rural areas, does not likely stem from a lack of funds but rather from how and on what these funds are spent.

The Department of Cooperative Governance, which administers the MIG and IUDG, has been made aware of this issue, and the Department of Transport is also playing a role in providing support and oversight of the road projects funded from these grants.

**School infrastructure backlog: the Committee is concerned that under School Infrastructure Grant that the Free State Department of Education had been consistently achieving Matric results with distinction but have not been favourably considered under this Grant to address the backlogs within Free State schools.**

There are two conditional grants available for this purpose, which are the Education Infrastructure Grant and the School Infrastructure Backlogs Grant. The Free State province, unfortunately, does not benefit from the implementation of the School Infrastructure Backlogs Grant. However, the province does receive allocations from the Education Infrastructure Grant. This particular grant is designed to provide supplementary funding for ongoing infrastructure programmes in provinces. Its goal is to maintain existing infrastructure and build new infrastructure that meets the required norms and standards for school buildings.

For the financial year 2023/24, the Free State province has been allocated a budget of R1 billion from the Education Infrastructure Grant. Government is determined to ensure that these funds are used appropriately, effectively, and efficiently to achieve our goals.

**Conditional Grants reduction: - given limited revenue resources, most provinces are reliant on conditional grants which have been reduced and will result in the inability of provinces to provide services and infrastructure to poor households including the delivery of houses and implementation of National Health Insurance.**

The National Treasury understands and acknowledges the challenges and pressures faced by provinces. However, the current fiscal challenges require adjustments to be made to expenditure levels across all government programmes in order to achieve the targets set out for fiscal consolidation.

These reductions have been necessary and extensive, affecting all aspects of government programmes, including national departments' baselines. All of these efforts have been undertaken to ensure the most effective and sustainable allocation of funds.

In order to mitigate the potential impact on service delivery, no reductions in year were made to the provincial equitable share allocations. Furthermore, the national departments took a careful approach towards the conditional grant allocations affected by the reductions, assessing the spending patterns of the grant allocations and considering the implications of the cuts on the overall operational activities of the grants.

Government’s priority is to minimise the impact on service delivery and ensure that necessary needs are met, while at the same time minimising underspending on programmes.

**Municipal Debt Relief: if a municipality fails to comply with the conditions of the debt relief, the National Treasury must take over the electricity license of that municipality or alternatively CoGTA in collaboration with SALGA should ensure that the credit control systems of ESKOM and municipalities are aligned by means of a Memorandum of Understanding (MoU) and that ESKOM must assist municipalities with credit controls through electricity disconnections.**

While the revocation of licenses is an existing measure for non-compliant municipalities, it is important to note that the National Treasury is not legally authorised to take over such licenses.

It is critical to ensure that non-compliant municipalities are held accountable for their actions, and the National Treasury will support efforts to achieve this goal. National Treasury takes note of the recommendation regarding the involvement of the Department of Cooperative Governance and SALGA in this matter, and we will refer the matter to them for consideration.

**GAUTENG**

**That National Treasury should capacitate all spheres of government, to enable them to spend funds allocated to them for service delivery to avoid surrendering funds.**

There is an issue with spending capacity amongst government institutions. There are various programmes designed to assist with this problem. It has been demonstrated by National Treasury's study that individual departmental efforts alone are insufficient to address the issue of state incapacity. A collaborative approach, embedded in the capability development framework, is more likely to be successful if there is co-creation between organs of state.

Collaboration between sectors and across organs of state is vital for improving the efficiency and effectiveness of government programmes. By co-creating solutions to address issues of state incapacity, government can ensure that limited resources are used responsibly and that critical services are delivered effectively.

**That National Treasury should ensure that the fiscal framework is redistributive in light of the programmes affected by reductions meant for the poor.**

The National Treasury fully recognises and supports the principle of redistribution as a fundamental guiding principle in the division of revenue. It is essential in ensuring equitable distribution of resources across different provinces and municipalities.

The allocation of resources is determined by the demand for public services in each province and municipality based on poverty levels, backlogs in access to services, and other demographics that reflect the needs of the population. This process ensures that higher per capita or household amounts are allocated to poorer and more rural provinces and municipalities. This approach is based on the principle of redistribution, which is central to achieving equity in the delivery of public services. Therefore, the reductions implemented do not change this all important principle of the division of revenue.

**That National Treasury should consider changing the equitable share formula in favour of local government in view of the provisions of the White Paper on Local Government on revenue-raising powers not yielding the intended results.**

The current share of nationally raised revenue allocated to local government takes into account the ability of municipalities to raise substantial own revenue, which for example, is not the case for provincial governments that largely provide social services, such as health care and basic education. Local government does however not currently fully optimise the revenue raising and cost recovery abilities at its disposal and is inefficiently utilising its current transfers and own revenues. These concerns need to be addressed as increasing the local government share cannot be done to compensate for municipal inefficiencies. The (local government equitable share (LGES)'s unconditional nature poses a challenge, as local governments continue to use a significant portion of the funds for purposes other than providing Free Basic Services (FBS).

Based on this reality and in a constrained fiscal environment, it is extremely difficult to make a case that local government is underfunded, when one considers its expenditure capacity and what transfers from the fiscus are spent on. Analysis of expenditure of the local government equitable share in the table below indicates that the cost of providing free basic services incurred by municipalities is significantly lower than the subsidies for free basic services in the LGES. This means that funds intended to support core functions and provide free basic services to poor households are not used for those purposes.

**Figure 1: Cost of Free Basic Services incurred as % of LGES subsidies**

A graph of a number of people

Description automatically generatedA similar observation is made with respect to conditional grant expenditure over the last 3 audit periods. During this period, municipalities spent an average of 73.6 per cent of their direct conditional grant allocations. This suggests that municipalities do not have the capacity to spend more grant funds than currently allocated to them.

**Table 1: Conditional Grants Expenditure, 2019/20 - 2021/22**

A screenshot of a computer

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Notwithstanding the above, it is important to note that government is dedicated to reviewing various components of the local government fiscal framework to address these concerns. Government looking at a balanced approach that safeguards local government interests while also holding the sector accountable for allocation and productive inefficiencies. This is evident in ongoing consultations. These consultations aim to address the impact of various factors on municipal revenues, including addressing fiscal leakages, improving current spending patterns and inefficiencies.

The development of national norms and standards to regulate municipal surcharges on electricity and identify alternative revenue sources is a crucial step towards reviewing the local government fiscal framework. The draft report is currently under review, and stakeholders will be consulted for recommendations.

**That National Treasury in conjunction with the Department of Social Development should ensure that there is comprehensive social security programme, to protect those segments of the population particularly exposed to the negative impact of rising inflation, including higher energy, fuel and food prices.**

National Treasury appreciates the committee’s suggestion, and it will be referred to the appropriate forum for deliberation. The proposed measure would require collaboration between various government departments and stakeholders, including the Department of Social Development, The Presidency and National Treasury.

**KWAZULU-NATAL**

No recommendations.

**LIMPOPO**

No recommendations.

**MPUMALANGA**

**The Department of Cooperative Governance and Traditional Affairs must ensure that municipalities implement their approved APPs to the latter, to avoid further under-expenditure.**

The recommendation is noted and will be referred to the Department of Cooperative Governance.

**The Department of Cooperative Governance and Traditional Affairs must strengthen its monitoring systems in the Provincial municipalities and have strict accountability tools since no reduction was made in Local Government.**

Direct municipal conditional grants are reduced by R3.4 billion and the reductions to allocations for municipalities in the Mpumalanga account for 6.8 per cent of this. The former part of this recommendation will however be referred to the Department of Cooperative Governance for purposes of provincial oversight however the primary responsibility to monitor grant funds lies with the relevant transferring officers of conditional grants.

**The Department of Cooperative Governance and Traditional Affairs must draw a list of all damaged properties and be submitted for approval to the National Disaster Management Centre (NDMC) so they can access the rehabilitation budget.**

The framework for the funding for post disaster recovery and rehabilitation is provided for in sections 56 and 57 of the Disaster Management Act. The guiding principle outlined in section 56 is that national, provincial and local government may financially contribute to response efforts and post-disaster recovery and rehabilitation. There is therefore an expectation that the cost of repairing or replacing public sector infrastructure should be borne by the organ of state responsible for the maintenance of such infrastructure.

Notwithstanding the above, R159 million is allocated to several municipalities in Mpumalanga to fund the repair and recovery of municipal infrastructure damaged by floods that occurred between February and March 2023. This amount is more than the R149 million that the NDMC recommended for municipalities in the province in 2023/24. The NDMC's recommendation for funding submitted to the National Treasury included amounts for the outer years (R112 million for each year). These will be provided for in the 2024 Budget.

Should this recommendation be speaking to events post the February-March floods, affected provincial departments and municipalities should, with the assistance of the provincial disaster management centre (PDMC), assess the costs of the damages and put together a funding application that the PDMC has to submit to the NDMC. The NDMC will then undertake its assessment and verification process and only once this is done will it submit to the National Treasury, funding recommendations for National Treasury's approval.

**NOTHERN CAPE**

**It is thus recommended that National Treasury in future, absolve struggling Provinces like the Northern Cape from any further reductions on any allocations, and especially Conditional Grants that will ensure better economic conditions for a very disadvantaged Province. The Northern Cape must furthermore be seriously considered for better allocations considering the challenges that the Province face in this vast landscape. Consequence management must also be implemented against sector Departments that do not spend Conditional Grants optimally.**

While we do acknowledge the challenges faced by the Northern Cape, the current fiscal challenges require that adjustments be made fairly to ensure fiscal consolidation targets are met. Reductions have been made across all government programmes, including national departments' baselines. However, the Provincial Equitable Share allocations have been spared from any in year reductions.

In addition, the Provincial Equitable Share Formula is currently under review, looking at ways to address challenges faced by all provinces, including the vastness and rurality of each province. Furthermore, transferring officers are responsible for monitoring grant allocations and ensuring compliance with conditions, and National Treasury supports implementing consequences for violations. However, it is important to note that at times, inefficiencies in spending and capacity issues may mean that even if the province were to be spared from reduction, funds may still be unlikely to be spent in full. Government will continue to work towards ensuring that all provinces receive the necessary support to address their unique challenges.

**The wage bill is one of the contributors impacting negatively on the fiscus, with challenges of unqualified incumbents, redundant and duplicate positions impacting negatively on service delivery. It is recommended that requisitely qualified persons must be appointed or capacitate incumbents to ensure that there is better service delivery and phasing out redundant and duplicate positions at all spheres of government.**

The concerns regarding the wage bill crowding out service delivery and its impact on the fiscus is supported. In response to these concerns, Various initiatives are underway to assist in the professionalisation of the public service across all three spheres of government and bringing the wage bill down to more manageable levels. National Treasury has issued the 2024 MTEF Guidelines for Costing and Budgeting for Compensation of Employees to address these concerns. Additionally, the Minister for the Public Service and Administration has issued a Directive outlining control measures for implementation on PERSAL/PERSOL. These measures aim to assist Executive Authorities in adhering to MTEF and financial ceilings when creating and filling vacant positions within their departments. These initiatives are intended to ensure that only requisitely qualified persons are appointed or capacitated to ensure better service delivery, as well as phasing out redundant and duplicate positions at all spheres of government.

**Debt service cost has the biggest impact on the total budget, causing even less available funding for service delivery. It is recommended that debt service cost be managed properly also by considering addressing the wage bill.**

The recommendation is supported. The fiscal strategy aims to continue rebuilding the public finances by narrowing the budget deficit and stabilising debt. The balanced approach to fiscal consolidation includes targeted spending reductions based on policy priorities, efficiency measures across government, and moderate tax revenue measures.

**NORTH WEST**

**The portfolio committee voted in favour of the bill with the following proposed amendments:**

**Prioritisation of basic services, water and electricity and all blocked projects**

Ensuring the provision of basic services and protecting the most vulnerable are fundamental policy priorities despite the current constraints in the fiscal environment. It is for this reason that for the 2023/24 financial year, there were no reductions in both the local government and the provincial equitable shares.

While prioritising blocked or stalled projects, the relevant accounting officers remain responsible for their implementation and oversight. We appreciate your recommendation and will raise it with the relevant sector departments during appropriate bilateral meetings and structures.

**Proposed retainment of funds for upgrading and improvement of school infrastructure and amenities**

The National Treasury is well aware of the pressing infrastructure needs in the education sector. However, the current fiscal challenges require us to adjust expenditure levels across government programmes at national, provincial, and local levels. Several factors considered when making these adjustments, including mitigating the potential impact of reductions on provinces. As a result, for the 2023/24 financial year, there were no reductions for Provincial Equitable Share allocations, while some reductions were made to provincial conditional grants.

Regarding the conditional grants, reductions were not made to crucial programmes like the National School Nutrition Grant, with the Early Childhood Development Grant experiencing lesser reductions. In light of these considerations, programmes such as the Education Infrastructure Grant and the School Infrastructure Backlogs Grant had to absorb a higher share of the reductions for the conditional grants.

While we appreciate the infrastructure needs in education, it's vital to highlight the need for some adjustment in response to the current fiscal constraints. Government will continue to work on addressing the pressing infrastructure needs and to ensure that reductions in certain areas do not compromise service delivery.

**Prioritisation of all farms that were affected by veld fires within the province**

National Treasury does not have enough information to provide a comprehensive response to the recommendation made. However, we would like to point out that in South Africa, farms affected by fire are assisted through several measures aimed at mitigating loss and providing support to affected farmers. In the event of a fire incident, the South African government mobilises the National Disaster Management Centre (NDMC) to assess the damage's extent and coordinate relief efforts while classifying the disaster. The province and the Centre works with affected farmers to develop a plan to address the damage and losses incurred. Government would then provide emergency funding to affected farmers to cover immediate needs such as food, shelter, and medication. The funding is aimed at ensuring that farmers can begin rebuilding their lives and livelihoods as soon as possible. Additionally, the Comprehensive Agricultural Support Programme (CASP) grant is also repurposed to assist in such emergencies. Nevertheless, as the National Treasury has not received any recommendation from NDMC, we would encourage the committee to raise this issue with the provincial treasury to obtain a more informed response.

**WESTERN CAPE**

**The R1.7 billion increase in the Western Cape’s Provincial Equitable Share allocation is not sufficient to cover the cost of the centrally agreed public sector wage increase for the province by the national government, which amounts to R2.9 billion. Service delivery is being crowded out by the public wage increase, which means that the provincial government will have to cut frontline services to cover the shortfall of the centrally agreed increase. It is recommended that the national government must fully fund the public sector wage increase agreement in the current Bill for all provinces. By not fully funding the public sector wage increase agreement for all provinces, the national government is forcing provincial governments to cut provincial budgets in order to fund the shortfall for the centrally agreed public sector wage increase agreement.**

The National Treasury acknowledges the concerns raised by the committee, and we understand the challenges faced by the province. However, it is crucial to note that we need to balance compensation demands with the broader needs of society and the economy.

Due to the current constrained fiscal environment, we have tried to be strategic in making additional allocations for the implementation of the 2023 wage agreement. These allocations were specifically targeted at personnel-heavy departments, with the aim of mitigating the possible impact on frontline services.

For the provincial government, the allocations were focused on the health and education sectors, which are among the sectors that contribute the most to frontline services. While it is possible that these allocations will not cover the total cost of the wage agreement, we anticipate that they will help provinces to reduce the impact of resource reductions on frontline services.

**The cuts to conditional grants for provincial and local governments are excessive and damaging to the service delivery capabilities of these governments. It is recommended that conditional grants are not cut in-year; and that the National Treasury should instead source these funds from the national governmental budget instead of cutting local government and provincial government budgets. Further, it is recommended not to cut conditional to the City of Cape Town, and in particular increase the City of Cape Town’s Urban Settlements Development Grant, Informal Settlements Development Grant, and fuel levy allocation. Not cutting conditional grants in-year is also in line with public participation comments received in committee.**

The current fiscal challenges faced by the country require adjustments to expenditure levels for all government programmes, including programmes to provinces and municipalities. The reductions were necessary to achieve our targets for fiscal consolidation, and the scale of these reductions required cuts to be made across all government programmes.

To mitigate the potential impact of these reductions, no in-year reductions were made to the provincial and local government Equitable Share allocations and the sharing of the general fuel levy with metropolitan municipalities. Reductions were however made to municipal conditional grants in order to achieve the fiscal consolidation targets, which included the need to reduce conditional grants specifically targeted at metropolitan municipalities (including the City of Cape Town).

**Cuts to infrastructure grants, such as the Education Infrastructure Grant, are especially worrying, as infrastructure represents an investment in the future of the province. Infrastructure projects often take place over a number of financial years, with projects needing stability over a number of years to be completed successfully. The cuts to these grants means that there is a risk of some projects that are already in progress not being completed. The long life-cycle of infrastructure-related grants must be taken into account. It is recommended that National Treasury do not make any in-year budget cuts to conditional grants affecting infrastructure as this risks halting projects midway; and that these funds should be sourced from the national governmental budget instead of cutting local government and provincial government budgets. In particular, given that rights such as the Right to Basic Education (Section 29 of the Constitution) is an immediately realisable right; there is currently no justification for cutting the budgets for Education Infrastructure Grant and the Early Childhood Grant. This is also in line with public participation comments received in committee.**

The National Treasury appreciates and acknowledges the concerns raised by the committee, especially with regard to the reductions in the infrastructure conditional grants. We understand the importance of these grants in facilitating critical infrastructure development across the country.

As we have previously mentioned, the size and scale of the reductions required that we make tough decisions regarding how these reductions should be effected. In making these decisions, we sought to spare critical programmes such as the Provincial Equitable Share and the National School Nutrition Grant. Additionally, we made lesser reductions to programmes like the Early Childhood Development Grant.

However, this meant that some programmes had to bear a greater proportion of the reductions, especially the Education Infrastructure Grant and the School Infrastructure Backlogs Grant. While we recognise the impact these reductions may have on infrastructure projects, as well as the delivery of public services, we must balance these realities with fiscal constraints.

**Certain conditional grants have been around for years, with the result that provinces and local governments depend on these grants when they set up their budgets and plan their programmes for the financial year. It is recommended that the conditional grants directly linked to provincial government mandates should rather be incorporated into the Provincial Equitable Share formula, and form part of the Provincial Equitable Share division of revenue for provinces. In particular, conditional grants related to Education, Health and Social Sector mandates should not be cut; and this is in line with public participation comments received in committee.**

This recommendation has been referred to the grants review process.

**The population data that was used to calculate the Provincial Equitable Share is outdated. As was confirmed in the latest Census date released this year, the Western Cape has moved from the 5th most populated province, to the 3rd most populated. The Western Cape also objects to the admission from National Treasury that the newest data will not be used for the next Main Budget, due in February next year. It is recommended that the incorporation of the data, particularly the population statistics should be incorporated for the main budget for implementation in February 2024.**

Allocation methodologies that use population data to determine allocations will not be updated to use the 2022 census data for the 2024 Division of Revenue Bill. This was agreed to by the Technical Committee on Finance (TCF), Technical Budget Forum (TBF), Budget Council and Budget Forum. The reasons for not using the 2022 Census in 2024 include the following:

* The Census data was released too late into the budget process and as such the data could not be used for the allocation.
* The 2022 Census data is being released in parts and not all data that is required to make updates to both equitable share formulae is available.
* Where data is available, it has not yet been disaggregated to a level that is needed to make the updates in the 2024 Division of Revenue

Once all data has been received, the technical working groups will assess the information to determine the potential impact and develop proposals on how to manage it. As has been done in the past, phasing in any changes over the course of several years may be necessary to avoid major disruptions to established baselines.

**The Provincial Equitable Share per capita also shows favour towards more rural provinces, and while this is understandable to an extent, it is does not differentiate between areas where poorer persons reside and areas which are considered rural in more geographical terms. The majority of poor people that rely on government services are based in urban areas, and this current favour does not seem to be properly take this into account in the Provincial Equitable Share formula. It is thus recommended that this metric is reviewed to instead take into account where the most poor persons in a province reside.**

This recommendation will be considered as part of the ongoing review process.

**In terms of the R1.4 billion declared underspending in the local government equitable share, it is recommended to reallocated these back to local governments in South Africa to relief local municipalities of the impact of budget cuts in this Bill.**

Monies were set aside for higher tariff increases approval by NERSA that never realised. The R1.4b was set aside and not allocated in the February 2023 budget, and the reverting of these funds will have no negative impact on individual municipalities as it do not impact on their existing allocations.

Debt-service costs are projected to be higher in 2023/24 by R14.1 billion due to a combination of the predicted widening of the main budget deficit, higher interest rates, and depreciation of foreign exchange rates compared to the 2023 Budget. It, therefore, became necessary for all spheres of government to contribute towards stabilising the growth in debt.

Reallocating the R1.4 billion to local government would inevitably result in a cut equivalent to this amount from local government conditional grants. This outcome could have unintended consequences for projects that are in various stages of implementation.

**In line with public participation comments received, it is recommended that the budget system, budget process and budget legislation on both a national and provincial sphere of government level is made more child-friendly to understand and engage with (for example: more infographics, TikTok posts and Instagram reels to explain the respective line items of budgets and implications thereof in simple terms that children would understand).**

The recommendation is noted. National Treasury conducts a budget outreach programme which is intended to make the budgets as user friendly as possible.

**In line with public participation comments received, it is recommended that the National Treasury includes experts in respective sectors to comment on the human rights legal impact of cutting respective conditional grants.**

The recommendation is noted.

**It is recommended that National Treasury address the unsustainable budget and fiscal deficits within the Medium-Term Expenditure Framework (MTEF) through effective budgeting strategies.**

The committee's recommendation is consistent with the existing fiscal strategy outlined in the 2024 Medium-Term Expenditure Framework (MTEF). Throughout this period, government’s fiscal strategy aims to rebuild public finances by narrowing the budget deficit and stabilising debt, while at the same time protecting vulnerable households through safeguarding the social wage. To achieve this, we are pursuing fiscal consolidation through implementing spending reductions, efficiency measures across the government.

By stabilising debt by 2025/26, even at a higher level than initially projected in the 2023 Budget, we will be creating a positive chain reaction on public finances. Such multiplier effects include creating additional fiscal space, providing the government with the necessary room to respond to emerging priorities effectively.

Furthermore, to ensure value for money, there will be a comprehensive restructuring of the state over the medium term to enhance efficiency. This restructuring includes implementing the recommendations highlighted in the spending reviews, which may involve actions such as closing or merging underperforming entities.

**It is recommended that National Treasury encourages fiscal decentralisation to empower provinces and municipalities for more effective service delivery instead of promoting centralised fiscal control.**

The recommendation is noted. The National Treasury is on record supporting the devolution of rail, housing, and bus services functions in a responsible and sustainable manner where capacity constraints are considered. We believe that where possible, local governments should have greater fiscal control to better manage the resources available to them and enhance their ability to provide essential services.

**It is recommended that the National Government manage the energy crisis effectively at the national level to alleviate budget pressures on provinces and municipalities, allowing them to focus on essential services without seeking alternative funding sources.**

We understand the budget pressures on provinces and municipalities to deliver essential services to citizens. Since the 2023 Budget, the integrated national electrification programme (INEP) grants now fund alternative energy sources, which was welcomed in the sector, given that these grants underspend and the 2022 Census showing 94.7% access to electricity.

However, the fiscus is under pressure, and we support alternative funding sources to find sustainable solutions to the energy crisis. The grant system promotes private sector resources and PPPs, which has shown success in energy efficiency and demand-side sectors. The National Treasury encourages efficient use of funds through grants to support service delivery, innovative solutions, and alleviate budget pressures. We value a multifaceted approach with all relevant stakeholders to address the energy crisis holistically while ensuring sound financial management practices.

**It is recommended that the National Government allow regional autonomy in wage negotiations to prevent disagreements like the Western Cape's stance on above-inflation wage agreements, ensuring accountability for decisions made at regional levels.**

This recommendation will be referred to the national Department of Public Service and Administration (DPSA).

**It is recommended that the National Treasury develop a comprehensive plan, led by the DPSA, to downsize the public service as a crucial step in addressing the ongoing fiscal crisis.**

This recommendation is supported. It is crucial to ensure that the public service is effective and efficient in providing essential services to citizens while managing costs. To address these challenges, The Presidency, DPSA and National Treasury, together with other relevant government entities including the provincial treasuries, are currently working on a comprehensive plan, led by the DPSA, to downsize the public service.

More details about this plan will be provided in the 2024 main budget and the 2024 State of the Nation Address.

**It is recommended that the National Government assess Transnet's borrowing practices to ensure visible improvements align with borrowed funds, particularly in critical sectors like harbours impacting foreign currency earnings.**

This recommendation will be referred to the national Department of Transport/DPE.

**It is recommended that National Treasury creates space for increased private sector participation within budgetary allocations, aligning with public announcements to ease fiscal pressures and enhance overall budget efficiency.**

National Treasury prioritises public-private partnerships to enhance budget efficiency. We have revised our PPP guidelines, updated the local government Borrowing Policy Framework, and engaged private stakeholders through the Urban Finance Working Group. These initiatives aim to assist municipalities in achieving a sustainable debt regime, developing long-term financial strategies, and exploring possibilities of parallel issuances with sovereign bonds. Ultimately, we are committed to delivering positive outcomes that benefit all stakeholders.

**It is recommended that National Treasury re-evaluates outdated public policy choices contributing to the budget and fiscal crisis, seeking alternative approaches to stimulate growth and deviate from anti-growth policies.**

An outline of National Treasury's budget process is contained in various budget documents, such as the MTBPS and BR, that are subject to public scrutiny and parliamentary oversight. The WC participates in these processes through the Budget Council and Budget Forum processes.

**It is recommended that National Treasury embraces subsidiarity and allocative efficiency principles by devolving certain powers to capable provinces and metros, fostering greater operational efficiency not currently forecasted in the Division of Revenue Amendment Bill 2023.**

We acknowledge the potential benefits of devolving certain powers to provinces and metros to achieve efficiency and improve service delivery. We will collaborate with relevant stakeholders to identify areas where this approach could be effective. For instance, we are exploring the devolution of certain provincial bus routes to the City of Cape Town. However, we will proceed cautiously to avoid any potential pitfalls along the way.

**It is recommended that National Treasury considers integration of conditional grants into the Provincial Equitable Share formula to balance flexibility with budget stability.**

The National Treasury is currently undertaking a review of the conditional grants, this recommendation will be considered as part of that process.

**It is recommended that National Treasury advocates for child-friendly budget documentation to make financial information accessible to all ages and foster long-term benefits through youth education on government budgeting.**

The National Treasury welcomes and notes the recommendation.

**It is recommended that National Treasury focuses on current population data for informed budget decisions, ensuring funds are allocated where needed most due to shifts in population distribution.**

Allocation methodologies that use population data to determine allocations will not be updated to use the 2022 census data for the 2024 Division of Revenue Bill. This was agreed to by the Technical Committee on Finance (TCF), Technical Budget Forum (TBF), Budget Council and Budget Forum. The reasons for not using the 2022 Census in 2024 include the following:

* The Census data was released too late into the budget process and as such the data could not be used for the allocation.
* The 2022 Census data is being released in parts and not all data that is required to make updates to both equitable share formulae is available.

Where data is available, it has not yet been disaggregated to a level that is needed to make the updates in the 2024 Division of Revenue.

**It is recommended that National Treasury investigates the causes of underspending before reallocating funds to local governments to ensure effective utilisation.**

The recommendation is noted. The National Treasury remains committed to proactively addressing issues related to understanding and taking necessary measures to enhance the effectiveness of funds by local government. Some of the corrective measures include engagement with relevant stakeholders to address the root causes of underspending.

**It is recommended that National Treasury establishes a formal process for human rights legal impact assessments to uphold human rights standards in budget decisions.**

The recommendation noted.

***The following recommendation should have been considered as part of the fiscal framework that has already been adopted by Select committee on Appropriations. When a fiscal framework has been adopted, it becomes difficult to make changes that deviate significantly from the agreed-upon framework.***

* **It is recommended that National Treasury acknowledges the focus on consumer welfare in VAT recommendations; and suggest a comprehensive economic impact analysis before implementing adjustments.**
* **It is recommended that National Treasury redirects borrowing towards capital expenditure to stimulate job creation in the economy, prioritising it over funding current expenditures.**
* **In line with public participation comments received, it is recommended that the National Treasury does not increase VAT. Further, it is recommended that National Treasury reduces the VAT burden on a larger basket of food items, in order to reduce the impact of the increased cost of living impact on consumers.**