Intergovernmental Fiscal Relations in the South African Context

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ABSTRACT

South African legislation prescribes the structures and process through which national revenue is raised and distributed. The South African national government determines the formula through which the nationally collected revenue is appropriated. However, currently a horizontal fiscal mismatch exists amongst provinces and also amongst localities within provinces, and these have some implications for fiscal relations on governance which will be analysed in this article.

INTRODUCTION

Fiscal relations between national and sub-national governments have over the years, emerged as one of the fundamental issues for governance, development and policy debates. They are the key to unlocking a country’s developmental potential as the financial capacity of a country is a global indicator of its developmental standing.

In a decentralised government system, fiscal relations are the essential tenet for government success. Sound fiscal relations between the national and sub-national governments promote development and growth whereas, poor fiscal relations renege development and growth.

In South Africa, the national government raises the bulk of revenue while provincial and local governments have their own prescribed fiscal capabilities. However, because of the socio-economic inequalities in the country and the variant levels of governmental institutional capacity (national, provinces and local governments), these fiscal capabilities are fragmented horizontally (within a sphere) and vertically (between spheres). In fact, clear distinctions can be made between high, medium and low capacity governmental institutions in terms of fiscal capacity.

The fragmented fiscal capacities between and among spheres of government in South Africa is attributed to its past, where the country implemented separated development
policies. Therefore, at the time of consolidating the country under a democratic government, the new structures and boundaries of the country inherited the disparities of the previous regime and the socio-economic inequalities and service delivery backlogs were enormous.

Therefore, today, South Africa is a dual economy, on one hand, portraying characteristics of the ‘so-called’ 1st world, which has been dubbed the ‘1st economy’, while on the other hand, it has characteristics of the ‘so-called 3rd world’, which has also been dubbed the ‘2nd economy’. From a developmental perspective, the 1st economy is characterised by a formal market economy with high growth and development in terms of public and private investments and job creation, while the 2nd economy is characterised by a predominantly informal and rural economy which bears the brunt of high unemployment and poverty and it carries the majority of the population.

Within the backdrop of socio-economic inequalities and fragmented developmental levels, sound fiscal relations between the national and sub-national governments are essential for a more isomorphic approach to development and governance in South Africa. Therefore, within the theoretical and pragmatic framework of a decentralisation, this paper discusses the interpolation between fiscal relations and intergovernmental relations.

**DECENTRALISATION**

Mathebula (2004:33) states that, ‘...decentralisation is understood in the science of public law as the establishment of legally autonomous administrative institutions that fulfil their functions autonomously and free from outside directives and are subject to oversight regarding the legality of their actions.’ It is the process of devolving political, fiscal and administrative powers to sub-national units of government (Burki et al., in Mathebula, 2004: 33-34).

Kroon (1986:347), argues that, ‘...decentralisation is defined as the delegation, devolution, deconcentration or transfer of power and decision-making authority to lower levels of government, offices or people’. It is the transfer of public authority, fiscal and human resources from national level to sub-national jurisdictions (Buthelezi, 2004:17). Three forms of decentralisation can be distinguished,

- Deconcentration;
- Delegation; and
- Devolution.

**Deconcentration** involves the redistribution of administrative mandates only within the national administration through field administration away from the capital (Buthelezi, 2004:18). Field administration implies the transfer of some decision-making discretion to field staff, allowing them some latitude to plan, make decisions, and adjust the execution of national directives to local conditions, within guidelines set by the national state department. Deconcentration is therefore the manner in which national (central) governments increase the autonomy of sub-national whilst preserving the right to give directives and full oversight.

The term **delegation** is etymologically derived from the Latin word delegare, which means to hand down or to give to (Roux et al., 1997:95). In practice, delegation refers to an institutionalised activity whereby certain activities and responsibilities are handed down from one hierarchical level to subordinate levels (Botes in Roux et al., 1996:95).
Devolution seeks to create or strengthen independent levels or units of government by which the central government relinquishes certain functions or creates new units of government that are outside its direct control (Roux et al., 1996:95).

In South Africa, the phenomenon of decentralisation is enshrined as a constitutional principle which is aimed at ensuring that the organs of the state are designed to render effective and efficient service delivery to the general populace. The Constitution of the Republic of South Africa, 1996 establishes three spheres of government, national, provincial and local, in a hierarchical manner and assigns powers, functions and responsibilities of each sphere in a decentralised approach. The Constitution further establishes the principles of cooperative government and intergovernmental relations as the enabling mechanisms for effective decentralisation.

INTERGOVERNMENTAL RELATIONS

According to Thornhill (2002:8), Intergovernmental relations encompass all the interdependent relations amongst the various tiers, spheres or levels of government. It includes the co-ordination of public policies determined by the legislative and executive bodies of the various governmental structures. Thornhill (2002:8) further argues that, ‘…Intergovernmental relations also refer to the actions and transactions of political office bearers and officials on any level or sphere of government that have bearing on the decisions and actions of another level, tier or sphere of government’.

Tulloch in Mathebula (2004:15) states that the concept of intergovernmental relations has two words, ‘intergovernmental’ and ‘relations’, where the former is an adjective meaning that ‘…which concerns or is conducted between two or more governments’, while the latter is a noun meaning, ‘…the way in which a person, thing or entity is associated, connected and linked to another’.

In South Africa, the Constitution is the premise through which intergovernmental relations derives it nature and character. Section 40 (1) of the Constitution of the Republic of South Africa Act, 1996 states that, “…in the Republic government is constituted as national, provincial and local spheres of government, which are distinctive interdependent and interrelated”. Levy and Tapscott (2001:248) expound on the constitutional definition, working definitions of the concepts, distinctive, interdependence, and interrelatedness, as follows:

Distinctive: The distinctiveness of each sphere is the degree of legislative and executive autonomy entrenched by the Constitution of the Republic of South Africa Act, 1996.

Thus, each sphere is distinguishable from the other in its powers to make laws and execute them. For example, the national government makes laws to govern the whole country, in the form of White papers, Bills and Acts of Parliament, whereas the provincial governments can make laws to govern the provinces in the form of Proclamations and Provincial Ordinances, while the local governments have got powers to make by-laws to govern their municipalities.

Interdependent: The interdependence of the sphere of government is the degree to which one sphere depends upon another for the proper fulfilment of its constitutional obligations. Two interrelated aspects of this dependency are mentioned. Firstly, the provincial
and local spheres of government are entitled to assistance from the national and provincial governments respectively in order to fulfil their constitutional functions. Secondly, it is the constitutional duty of the national and provincial sphere to supervise the provincial and local spheres respectively to ensure that they fulfil their constitutional obligations. Hence section 100 (1) and section 139 (1) (a) and (b) of the Constitution of the Republic of South Africa Act, 1996, emphasizes on the need for national supervision of local government respectively.

**Interrelated:** The interrelatedness of the spheres of government is the duty of each sphere of government to cooperate with one another in mutual trust and good faith, for the greater good of the country as a whole. For example, projects undertaken at local government spheres such as housing have got higher chance to be successful if the local government works in cooperation with either the provincial government or the national government, or both, as compared to working in isolation.

The Intergovernmental Relations Framework Act, 2005 (Act 13 of 2005) was also enacted to give meaning to the constitutional dictates on intergovernmental relations. This Act formalises the relations between (and within) the three spheres of government. It mandated the establishment and functioning of national, provincial and municipal intergovernmental forums. It also laid out protocols for the conduct of intergovernmental relations as well as intergovernmental dispute resolution procedures.

The effectiveness and efficiency of public service delivery by public institutions will largely be dependent on the relationships amongst the different institutions involved in related activities (Thornhill, 2001:8). In fact, effective intergovernmental relations are a key requirement for effective and efficient public service delivery. Bird (1990:281), confirms this assertion by stating that, ‘...it is the workings of the myriad of intergovernmental relations that constitute the essence of the public sector in all countries’.

**INTERGOVERNMENTAL FISCAL RELATIONS IN SOUTH AFRICA**

The objective of decentralisation and intergovernmental relations in government is to facilitate effective service delivery. Intergovernmental fiscal relations are a facet of intergovernmental relations. In line with the functions of public administration such as policy making, planning, staffing, finance, work methods and control, one critical area for decentralisation and defined in the Constitution of the Republic of South Africa (1996), is finance. Van der Waldt and Du Toit (1997:167) argue that the availability of money and the division of revenue are two of the most important criteria for obtaining government objectives and therefore the national government should create a fiscal relationship with the other two spheres of government by placing limitations on expenditure by means of the budget.

From a constitutional model, South Africa is a quasi – unitary and quasi-federal state, characterised by three spheres of government; national, provincial and local governments. The national government has a macro responsibility over all government activities (unitary) and provincial and local governments have distinctive responsibilities assigned to them in terms of the constitution (federalism). Each of these spheres of government is allocated certain powers, functions and financial capabilities; each of which may be exclusive, concurrent or shared.
Fjeldstad (2000:8) states that, ‘…Governments rely on a wide variety of tax instruments for their revenue needs, including direct and indirect taxes, general and specific taxes, business and individual taxes’. He further argues that there is no ideal assignment of taxes between central and lower levels of government. Boadway et al., in Fjeldstad (2000:8) further states that, a set of ‘tax-assignment rules’ has been developed in the traditional fiscal federalism theory. These principles relate to the respective responsibilities of central and lower spheres, tiers or levels of government in macroeconomic stabilisation, income redistribution and resource allocation.

In South Africa, the national government raises the bulk of the country’s revenue through tax instruments such as corporate tax, pay as you earn, value added tax, fuel levy, customs and excise duties. The provinces have very limited tax instruments such as gambling licencing, tourism levies and toll roads levies. Municipalities have a more significant tax instrument base where they can raise revenue from municipal rates and tariffs and property taxes.

A National Revenue Fund is provided for in section 213 and 214 of the Constitution of the Republic of South Africa, 1996, into which all money received by the national government must be paid (Malan, 2000:29). Nationally collected revenue is distributed through an Act of Parliament that is passed annually, the Division of Revenue Act (DoRA). According to the Fiscal and Financial Commission (FFC), the division of revenue between national, provincial and local government entails an unconditional equitable share to which the three spheres are entitled (www.ffc.co.za). This is supplemented by conditional grants, transferred from the national sphere to the other spheres, for specific purposes.

A host of intergovernmental processes are implemented to enhance co-operative governance around policy and budget decisions. The Cabinet makes final budget allocations after consultation with the FFC, the provinces and organised local government. The Intergovernmental Fiscal Relations Act, 1997 (Act 97 of 1997), formalises this consultative process.

The Intergovernmental Fiscal Relations Act empowers the three intergovernmental bodies to strengthen cooperation on budgeting between the Executive and Parliament, and between spheres of government. The Act helps to clarify the roles of the FFC, Budget Council and Budget Forum in the budget cycle (www.ffc.co.za).

Financial and Fiscal Commission

The FFC is an independent body established in terms of section 220 of the Constitution of the Republic of South Africa, 1996. It was created to be an expert, advisory body which would serve as a resource for constructing the budget. Its stated purpose is to make recommendations on the budget and intergovernmental financial issues to Parliament, the provincial legislatures, and the Budget Council.

According to section 5 – 7 of the Financial and Fiscal Commission Act, 1997 (Act 99 of 1997) the FFC is composed of 22 members, with serving terms of 5 years. They include:

- Nine persons, each of whom is nominated by the Executive Council of a province;
- Two persons nominated by South Africa Local Government Association (SALGA); and
- Eleven members appointed by the President.
According to Section 9 of the *Intergovernmental Fiscal Relations Act*, the FFC is to make recommendations to the Minister, Parliament and the Provincial Legislatures on the division of revenue in May of each year, ten months prior to the tabling of the budget.

**Budget Council**

According to the National Treasury’s Medium Term Expenditure Framework Treasury Guidelines for preparing budget submissions (2001:3), the Budget Council is a consultative body of political office-bearers from the national and provincial spheres which make recommendations to the Cabinet on the budget. Over the years, the council has become a quite cohesive working group and the principal forum for consultation and debate in the months leading up to the official tabling of the budget in Parliament.

The core members of the Budget Council are as follows:

- The Finance MinMEC (the Minister and Deputy Minister of Finance and the nine provincial MECs for Finance);
- Treasury advisors;
- Director General of Finance and Heads of Treasury; and
- The FFC can attend as observers.

According to sections 2-4 of the *Intergovernmental Fiscal Relations Act*, the Budget Council was formalised and given specific functions and requires the Ministry of Finance to convene the Council at least twice a year. The Council is consulted on fiscal and financial matters affecting provincial government.

**Budget Forum**

The Budget Forum is a consultative forum pertaining to local government. In addition to the Budget Council, it also includes five members of SALGA and one representative from each of the provincial associations (National Treasury’s Medium Term Expenditure Framework Treasury Guidelines for preparing budget submissions, 2001:3 and *Intergovernmental Fiscal Relations Act*, 1997). Similar to the Budget Council’s concentration on the provinces, the Budget Forum looks at fiscal and financial matters revolving around local government.

The Minister of Provincial and Local Government (dplg) is invited to attend meetings, but is not a member of the Forum. Legislation requires the Minister of Finance to convene the Local Government Budget Forum at least once a year.

**Minister’s Committee on the Budget (MinComBud)**

According to the FFC, the MinComBud is a particularly prominent actor in the drafting of the budget. This is a subcommittee of Cabinet specifically tasked with budget matters. It is a smaller technical subcommittee of the Cabinet, most closely involved in the oversight of the developing budget and its compliance with government goals (http://wwwffc.co.za/mincombud).
Joint MinMecs

Joint MinMecs are basically MinMecs for sectors which are concurrent functions of national and provincial government such as health, education, welfare, and housing. Each committee comprises the national minister and the provincial MECs for that sector. They meet throughout the year to identify trends in the sector, set priorities, and discuss budgetary implications of national policies for provincial service delivery.

Technical Committee on Finance and the Joint Sectoral Technical Committees

According to the MTEF Guidelines (2001), the Technical Committee on Finance and the joint sectoral technical committees (referred to as ‘4x4s’) support the Budget Council. They are teams of officials who discuss policy options for the sector, problems with service delivery, and budget difficulties. These 4x4s are designed to include four national and four provincial representatives, with both treasuries and the line departments present. In practice the composition of the groups may vary. Only a few provinces are represented on a particular 4x4 but each province is involved in at least one 4x4.

The distinguishing element of the 4x4s is that they bring together treasury and line departments, at both the national and provincial levels. The 4x4s are permanent bodies which meet throughout the year and pick up on other sector-wide policy issues beyond budgeting. In addition to 4x4s for health, education, welfare, personnel, and justice, 4x4s have now also been convened to address infrastructure and transport (MTEF Guidelines 2001). However, it should be noted that, the 4x4s are advisory bodies of officials and do not have particular decision-making power.

Treasury Committee

According to the MTEF Guidelines (2001), the Treasury Committee is the body which evaluates requests from provinces and national departments for additional funds to address unforeseen or unavoidable needs. The Committee is chaired by the Minister of Finance and includes a select number of Cabinet ministers. The Committee meets in October and its decisions are then included in the Adjustments Estimate to the original budget which is tabled in Parliament in late October.

Parliamentary Budget Committee

The parliamentary Budget Committee was formed in November 2001. The Committee was established as an ad hoc committee, with the immediate task of holding hearings on the Mid-Term Budget Policy Statement (MTBPS) released in November and tabling a report in Parliament. It was comprised of 15 members from the National Assembly (9 ANC members and 6 members of the opposition) and 8 members of the National Council of Provinces (5 ANC members and 3 opposition members). The intention is for the Budget Committee to be a vehicle for Parliament’s active engagement in the budget process (MTEF Guidelines, 2001).
According to Mase (2003:27), the division of nationally raised revenue based on political judgement and historical expenditure patterns, including fiscal capacity, expenditure efficiency, developmental needs and service backlogs. He further states that, the division also takes into account national priorities that are anticipated to have potential impact on local government, e.g. the provision of free basic services like electricity and water to poor households.

In terms of the political process, the vertical division of revenue is determined through a consultation process involving organised local government, provincial ministers of finance and the consideration of the recommendations from the FFC. It then culminates into the Division of Revenue Act (DoRA) passed by Parliament, giving it a legal and legislative status (Mase, 2003:27).

THE CHALLENGES FOR INTERGOVERNMENTAL FISCAL RELATIONS IN SOUTH AFRICA

There is undoubtedly a mismatch between revenues raised and expenditure responsibilities between national, provincial and local governments. According to the South African Local Government Association (SALGA), South Africa’s fiscal system is based on a revenue sharing model with seven (7) out of nine (9) of the provinces receiving more funds than they can raise by way of taxes. Similarly, except for major urban municipalities, most municipalities are dependent on national transfers (SALGA National Consultative Workshop Discussion Document, 2007:54).

This vertical mismatch is generally known as a vertical fiscal imbalance. Horizontal fiscal imbalance also exists amongst provinces, and also amongst localities within provinces. There are massive relative differences amongst provinces’ expenditure responsibilities, and existing as well as potential revenue sources. Hickey (2002), states that, ‘...the provinces raise 3% of their own revenue, 11% in conditional grants and 86% in equitable share. Municipalities raise 92% of their own revenue mainly from rates, levies and other local taxes.’

Within the backdrop of afore-mentioned scenario, some major implications for fiscal relations on governance will be discussed as follows;

Provincial implications

Provinces have limited revenue raising powers to manage their developmental role. They rely on the national equitable share for their sustenance. In terms of assignment of powers and functions (concurrent functions), provinces have service delivery and local government support responsibilities. Service delivery responsibilities entail such services as health, social development, housing and health while local government support responsibilities entails capacity building and resource facilitation. National departments of government normally channel financial resources for local government (service delivery) through provincial departments. However, in circumstances where provincial departments have inadequate capacity, this protocol results in non-service delivery as the funds remain unspent at provincial government level. Thus, poor coordination of financial resources by provincial
departments can create bottlenecks and lead to non-service delivery. Areas that have been impacted by such bottlenecks in the recent past include housing delivery.

Local Government Implications

Municipalities are dependent on a strong revenue base to sustain their viability. However, the majority of municipalities have limited revenue capabilities and are characterised by high levels of poverty and unemployment and have strong elements of rural and informal economies, resulting in increasing demands for subsidisation and welfarism. This is evidenced by the escalation of informal settlements which put pressure on the municipalities to provide free basic services and housing. Municipal areas vary in terms of urban and rural characteristics. This requires them to plan differently. These concerns have been further highlighted by the Department of Provincial and Local Government and they form the essence of the policy process on the system of provincial and local government which was initiated earlier in 2007 and expected to result in the review of the White Paper on Local Government (1998).

Intergovernmental Coordination and Alignment

Planning for service delivery in the country remains a mammoth task. National, provincial and local government planning is not aligned and coordinated and usually results in duplication and wastage of resources. The National Spatial Development Perspective (NSDP), the national development planning tool is prepared at national level and the level at which it addresses grassroots issues at a remote rural scenario is questionable. The NSDP prescribes developmental approaches to predetermined developmental corridors and fails to unlock developmental potential for other areas. As a consequence some areas with potential are neglected. For instance, the Eastern Cape province is generally considered through the NSDP as a ‘social net’ rather than a place with massive investment potential and as such NSDP priorities for that province renege the future prospects of any high growth rates and development.

The provinces have their own Provincial Growth and Development Strategies (PGDS). These are macro plans which are province specific. However, the coordination and implementation of these plans at municipal level remain a challenge. The consultation, cooperation and joint-efforts by provincial departments and municipalities is usually hindered by political and ‘turf’ issues and this results in stifling development and growth.

At local government, the Integrated Development Plans (IDPs) are intended to be an expression of a government-wide commitment to a municipal space. Such a commitment ought to be expressed in terms of resource allocation and capacity building support. However, more often than not, IDPs are prepared and adopted with minimal inputs from provincial and national departments (sector departments). Many IDPs are not aligned to provincial and national priorities and many programmes and projects identified in the IDP process become unfunded.

The various planning approaches as discussed undoubtedly influence the national budgeting process that eventually result in policy decisions such the MTEF and DoRA. If left unattended for longer, the short-comings identified above have a propensity to perpetuate
the inequalities that exist between the 1st and 2nd economy and the country will struggle to bridge the gap of inequalities.

**Intergovernmental relations ignominy**

Although intergovernmental cooperation and integration is defined in terms of the Constitution and the *Intergovernmental Relations Framework Act*, collaboration is still voluntary with minimal authority and accountability. Relations at an intergovernmental perspective are usually reneged by political and human differences. There are superiority and political complexes that normally disrupt the intentions of intergovernmental cooperation leading to counter-productive engagements and non-delivery of services to communities. Such complexes are perpetuated by party-political differences (within a party and between parties), perceived capacities and competencies and in some cases racial and ethnic differences. Therefore, if politicians, political office-bearers and public officials fail to reconcile such differences and execute the functions as a seamless government with a common mandate and voice, the threat to sound intergovernmental and fiscal relations will continue to prevail.

**CONCLUSION**

Within a decentralised system of government, the paper has highlighted the theoretical and pragmatic tenets of intergovernmental relations and intergovernmental fiscal relations. The South African situation and approaches to intergovernmental fiscal relations are influenced by the Constitution and the various pieces of legislation that have been enacted to facilitate this rapport. These include the *Intergovernmental Fiscal Relations Act*, the *Financial and Fiscal Commission Act* and more recently the *Intergovernmental Relations Framework Act*.

Legislation prescribes the structures and processes through which national revenue is raised and distributed. The national government also determines the formula or methodology through which the nationally collected revenue is appropriated. However, whether the final allocations of revenue to provinces and municipalities are equitable remains a subject of much debate.

While strides have been made to facilitate such relations from a policy perspective, the implementation process has been marred by many a challenge. These hindrances range from the fiscal imbalances to intergovernmental cooperation challenges. Furthermore, the implementation of a quasi-federal and unitarist constitutional model, propel some of the challenges associated with intergovernmental and fiscal relations and perhaps it is high time to redefine the constitutional standing of spheres of government.

The country therefore needs to continually review and improve its governance approaches in search for best alternatives to facilitate growth and development. Thus the politicians, political office-bearers and public officials ought to embrace the iterative nature of public administration in time and space, must take risks, and should respond to the change factors in their environments.
SOURCES


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