The end of the road

A CRITICAL REVIEW OF THE LOCAL GOVERNMENT FISCAL FRAMEWORK

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NOTE:

This working paper draws on work undertaken with the University of Johannesburg (UJ) and the South African Local Government Association (SALGA) in 2018. A central part of that work was a series of interviews with municipal officials undertaken by the PARI research team. Where reference is made in this working paper to the views of municipal officials, it is to those interviews that we are referring, and their words that we are quoting. The method used to conduct those interviews and the selection of municipalities for that 2018 study is summarised in Annexure A.

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[There is] a financial cul-de-sac that many of the local municipalities and districts have already reached across the whole country, with a few and limited exceptions

Auditor-General of South Africa, July 2020

THE BOTTOM LINE

In post-1994 South Africa, a central role for local government was envisaged in the new developmental state that would deliver the promised *better life for all*. Some 25 years later, it is clear that in many respects local government has failed to meet expectations – to be at the forefront of delivering transformative service delivery to all South Africans, and to contribute directly to meaningful and sustainable improvements in the standard of living. Many municipalities are in a state of financial distress, and universal access to affordable, quality services has not materialised.

Both structural and organisational factors contribute to the financial (and operational) outcomes of a municipality, but comparatively little attention is paid to structural factors. The most important contributing structural factor in our assessment is the overarching fiscal framework within which a municipality is located. The post-1994 fiscal framework for local government was designed to ensure that there was sufficient revenue available to pay for the extended range of services and responsibilities that municipalities would have. The foundation of the framework was the assumed ability of municipalities to raise significant amounts of own revenue: The White Paper on Local Government assumed that 73 per cent of all operating expenditure requirements in local government could be funded through property rates and service charges. Our research suggests that in aggregate, local government is probably only able to fund less than 50 per cent of (current budgeted) operating expenditure from property rates and service charges, with the funding gap being greatest outside of the metro areas.

At the same time, the social wage is being eroded: affordable and subsidised access to basic services is an important part of the state's strategy to reduce the cost of living for poor households, and thereby compensate them in part for their lack of income. The current form and operation of the local government fiscal framework (which requires constant increases in services tariffs to fill the funding gap) is eroding the social wage to an alarming extent, and thus contributing to increasing poverty and deepening inequality.

We are in an unsustainable situation that is threatening the entire developmental agenda. Our specific assertion in this paper is that the central underlying cause of the current situation is the structure of local government: current expenditure requirements simply cannot be covered by local government's revenue-raising arrangements, and the gap between the two would be even greater if free and subsidised basic services were delivered as required to address household poverty and inequality. Concurrently, the amount of money that could be saved via the reduction of expenditure 'leakages' from the system is insufficient to fill the funding gap, and there is no realistic prospect of national transfers making up the shortfall.

Our only option is to go back to the drawing board – to the basic design of local government. We are currently in a very different and much more privileged position than those who drafted the 1998 White Paper on Local Government. We have 20 years of empirical data in respect of the optimal pricing of services to ensure household affordability targets are met, much better (albeit not complete) information around the actual costs of delivering those services, and a clearer understanding of the limits of inter-governmental transfers to make good any shortfall. We must use that information to develop an empirical basis to clarify our options in respect of the operating and financial structure of local government, so that we are no longer having these debates on a partisan or partial information basis.

CHAPTER 1

INTRODUCTION

[...] the lack of fiscal space for the local government sector is placing its sustainability and viability at risk.

Financial and Fiscal Commission (FFC), 2019

1.1. Background

In post-1994 South Africa, a central role for local government was envisaged in the new developmental state that would deliver the promised 'better life for all'. The blueprint for this new form of local government was laid out in the 1998 White Paper on Local Government (RSA, 1998). The envisaged changes to the structure and operation of local government under the new Constitution were both considerable and radical: an entirely new form of municipality was imagined, with radically different authorities and obligations. In order to meet the goal of universal democratic representation, South Africa would (for the first time) have wall-to-wall municipalities. Local government would now deliver far more services and wider range of services to many, many more people.

South Africa has been given a rare and historic opportunity to transform local government to meet the challenges of the next century. [...] the existing local government system will be radically transformed [...] into a system of local government which is centrally concerned with working with local citizens and communities to find sustainable ways to meet their needs and improve the quality of their lives.

White Paper on Local Government, 1998

An important focus of policies to address household poverty under this new system would be the provision of free or subsidised basic services (electricity, water and sanitation) to poor households that could not otherwise afford these services. Affordable access to services for households is a key component of the social wage; in effect it supplements the incomes of poor households and thereby contributes to reducing inequality. When services become unaffordable to poorer households, the value of the social wage is eroded, as is its role as a redistributive mechanism. 'Affordable' in this context does not mean households are only able to pay for these services if they reduce other basic expenditure, such as on food, housing or transport; this would exacerbate inequality by effectively erasing any positive social wage impact.

Some 25 years later, it is clear that in many respects local government has failed to meet expectations – to be at the forefront of providing transformative service delivery to all South Africans, and to contribute directly to meaningful and sustainable improvements in the standard of living. Many municipalities appear to be in financial distress, unable to meet their basic services expenditure requirements out of their current income. In the 2013/14 financial year, 86 municipalities were considered by National Treasury to be in a state of financial distress. That number rose to 125 in the 2017/18 financial year (representing almost half of all municipalities), and it is very likely that the number has increased further under the pressure of the Covid-19 economic impact.

The quality of municipal services is declining in many locations, as is the overall state of local basic infrastructure (Watermeyer and Philips, 2020), due in part to a lack of expenditure on maintenance by local government. At the same time, the cost of the basket of basic services provided by local government has increased at an average rate that exceeds inflation over the past five years.[1] In July 2019, municipalities instituted an average[2] 15.6 per cent increase in electricity tariffs, and metros introduced water tariff increases of between 9 and 14 per cent. There are growing indications that poorer households cannot afford to pay for the services they require. This is potentially creating a vicious circle of more and more financially distressed municipalities coexisting alongside more and more households that are unable to access services – either because they cannot afford to pay for them, or because the municipality does not have sufficient resources to provide the services at an acceptable standard.

The debate around the reasons for these failures is heated, and extensive. There are those who contend that local government's poor performance and financial problems are a result of poor financial management (such as excessive spending on inflated salaries, luxury vehicles and vanity infrastructure projects) and widespread corruption, such as the investments in VBS Bank. Others maintain that the problem is a lack of skills and capacity to effectively manage the delivery of services.

PARI's position is that multiple factors contribute to local government outcomes, and that the mix of causal factors varies considerably from municipality to municipality. Both structural and organisational factors contribute to the financial (and operational) outcomes of a municipality. Organisational factors include issues such as the quality of budgeting and prioritisation of expenditure, and financial oversight. Comparatively little attention is paid to structural factors; in our assessment the most important of these is the overarching fiscal framework within which a municipality is located.

This paper focuses on the linkages between the fiscal framework of local government and the twin problems of increasing municipal financial distress, and erosion of the basic services social wage. We have focused specifically on assumptions in the 1998 White Paper on Local Government about the form and operation of the fiscal framework, and actual outcomes over the past 25 years. We believe that a close examination of these issues will reveal important findings about how to structure a sustainable, long-term solution to the current state of local government.

1 https://www.dailymaverick.co.za/article/2020-07-01-property-managers-claim-municipal-rates-are-now-extortionate-municipalities-dont-see-a-problem/

2 Municipalities have discretion with respect to the pricing of municipal rates and services, subject to certain maximums.

1.2. The local government fiscal framework

The local government fiscal framework (LGFF) is the structure that should ensure that all of local government's service delivery obligations are adequately funded and is thus

> *[...] the aggregate revenue arrangement or funding framework of local government relative to the aggregate expenditure mandates and responsibilities of the sphere. In essence, the LGFF is the funding arrangement required to ensure that local government and individual municipalities are financed sufficiently to fulfil their constitutional mandates so that adequate services are rendered to communities.*
>
> **FFC, 2011**

In effect, the LGFF determines how much money is available to local government (and to each individual municipality). As with its operating structure, post-1994 local government had a radically new fiscal framework, designed with the goal of ensuring that municipalities would have access to sufficient resources to deliver their ambitious new mandates.

The developmental outcomes of local government are intricately interconnected with the details and operation of the fiscal framework. Most obviously, expenditure is limited by available financial resources. A municipality cannot invest in new infrastructure, fund infrastructure maintenance, or support socioeconomic programmes without the money these require. But there are other linkages between the fiscal framework and socioeconomic development; although the tariffs charged for municipal services are an important source of municipal revenue, if the cost of services such as electricity or water become unaffordable to poor households, this will have the effect of reducing the social wage and deepening poverty by reducing household income available for other basic necessities. If these service costs rise beyond a certain level, poor households may no longer be able to afford to purchase them, and will effectively be deprived of access. Such an outcome would clearly be contrary to the developmental aims of the post-1994 local government.

Additionally, municipalities are buyers of bulk services (particularly electricity) and their ability to pay for those services is critical to the financial stability of the bulk service providers, most notably Eskom. Local government is also a key employer and procurer of goods and services. In more remote rural areas, they are often the biggest component of the local economy. There are thus multiple and important linkages between the state of local government finances, the wider macro economy and socioeconomic development.

A generally deteriorating state of local government finances is, therefore, a matter of grave concern, something much more important than just a local government problem. The current state of municipal finances is certainly cause for such concern, and is likely to be worsened considerably by the Covid-19 pandemic and associated expected dramatic slow-down in economic activity.

1.3. The current state of local government finances

The financial position of local government in aggregate appears to be under increasing pressure: at the beginning of the 2019/2020 financial year, 126 municipalities (49 per cent of the total) adopted unfunded budgets – that is, a budget where "realistically anticipated revenue is insufficient to meet planned spending". This is a significant increase from the 74 municipalities that adopted unfunded budgets at the beginning of the 2016/17 financial year (National Treasury, 2019a). After an intervention by National Treasury, the 126 municipalities was reduced to 66. The fact remains, however, that almost half of all municipalities were planning to spend money they could not reasonably expect to collect, and almost a quarter still had unfunded budgets *after* Treasury's intervention.

The annual local government audit reports prepared by the Auditor General of South Africa (AGSA) signal rising concern about the state of local government finances. For the 2017/18 financial year[3] the AGSA made this observation:

> *There are increasing indicators of a collapse in local government finances – we assessed 76% of the municipalities to have a financial health status that was either concerning or requiring urgent intervention. Almost a third of the municipalities were in a particularly vulnerable financial position.*
>
> **AGSA 2019a, p9**

A growing number of municipalities appeared to the AGSA to be unable to operate financially as going concerns, and the inability of many to fund infrastructure maintenance was also flagged as a serious problem. As just one outcome of this lack of maintenance, the AGSA (ibid, p10) noted that "[…] *39% of the municipalities that disclosed their water losses reported losses of more than 30%, resulting in an overall loss of R2,6 billion*".

In the 2018/2019 financial year, things got even worse: both financial governance and financial outcomes deteriorated in most provinces. Only 20 (of 257 municipalities) received a clean audit. Despite an aggregate expenditure of R1.26 billion on consultants to assist with the preparation of financial statements, fewer than half of all municipalities were able to submit statements that did not contain material misstatements.[4] Thirty-three received a disclaimer (an audit opinion which means the auditor could not find sufficient financial records to come to any conclusions about the municipality's financial statements). Of greatest concern was that 28 municipalities (more than 10 per cent) had outstanding audits, due mostly to their inability to compile their own financial statements in good time.

Some provinces are in much worse shape than others. In the Free State, no municipality received a clean audit and only three (out of 23) managed an unqualified with findings opinion. In the North West, not a single municipality could manage even that outcome: the province distinguished itself with eight qualified audits, nine disclaimers and three municipalities with outstanding audits. These outcomes are depressingly familiar – some of these municipalities have had disclaimer outcomes for the last three or even four years in a row.

The AGSA found that in the 2018/19 financial year:

- 79 per cent of municipalities had a financial health status that was "*either concerning or requiring urgent intervention*".
- 31 per cent of municipalities were considered to be in a "*particularly vulnerable*" financial position.
- 34 per cent of municipalities ended the year with a deficit (involving an aggregate amount of R6.3 billion of unfunded expenditure).

This represents a deterioration from the previous year, and led the AGSA to conclude that there clearly exists "*a financial cul-de-sac that many of the local municipalities and districts have already reached*". This was based in part on an estimate by the AGSA that only about 60 per cent of the revenue on local government's balance sheet will ever be collected (which implies an uncollectable amount of some 80 to 85 billion rand).

Probably the most disconcerting part of the 2018/19 audit report is that these dire outcomes reflect the state of local government finances *before* the impact of the coronavirus pandemic lockdown and subsequent sharp decline in economic activity.

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3 The local government financial year runs from 01 July of one year to 30 June of the next year.

4 A material misstatement is information in the financial statements that is sufficiently incorrect that it may impact the economic decisions of someone relying on those statements. https://www.accountingtools.com/articles/2018/5/19/material-misstatement

Outstanding debt owed to local government has risen steadily over the past few years, from just under R130 billion at the end of the 2016/17, to just over R181 billion at the end of March 2020. Most of this debt (almost R150 billion) has been owed for more than 90 days, and 70 per cent is owed by households. The debt owed to municipalities is indicated in the table below. Note that the figure to March 2020 represents only nine months of the financial year and reflects the debt situation before any impact of the Covid-19 national lockdown.

TABLE 1: Local government debtors: Total (percentage change from previous period)

	March 2020*	June 2019	June 2018	June 2017
Total	R181.3bn (+9,5%)	R165.5bn (+15.6%)	R143.2bn (+11.6%)	R128.3bn
Owing for more than 90 days	R146.7bn (+7.9%)	R135.9bn (+17.1%)	R116bn (+13.7%)	R102bn
Owed by households	R127.7bn (+7.7%)	R118.6bn (+16.4%)	R101.9bn (+26.3%)	R80.7bn

* Data are for nine months of the financial year

Source: *National Treasury Section 71 in-year reporting data (www.mfma.treasury.gov.za)*

One important point to make is that although an improvement in financial and operational governance is obviously required to minimise financial leakages from the system – these range from irregular expenditure to losses incurred in the distribution of water and electricity – there are a growing number of municipalities where financial distress coexists alongside relatively good governance outcomes (discussed in greater detail in Chapter 3). It is very likely that the coronavirus pandemic and associated economic slowdown has increased the number of municipalities in financial distress which suggests that good governance on its own is not sufficient to address financial distress, although it is certainly a necessary condition.

In addition, although there is some positive correlation between the audit outcome and the quality of service delivery and the value of the social wage, that relationship is also impacted by local factors, and cannot be guaranteed. Most notably, a clean audit gives no indication of the extent to which poor households are actually able to afford (and thus access) basic services. If there are not enough resources to address basic service needs (particularly in respect of indigent households) the quality of the audit outcome will not change that.

These observations are certainly not intended to suggest that financial governance outcomes are unimportant. Greater accountability for the use of public funds in the delivery of the developmental mandate is essential to achieving that developmental mandate, and there is enormous room for improvement in this area. However, we believe that the challenges facing the local government fiscal framework exceed non-compliance with legislation, and will not disappear with an improvement in audit outcomes. Instead, there is a far more serious structural problem with the design of that fiscal framework.

Clearly, the current situation with respect to municipal finances cannot continue for much longer without threatening the integrity of the entire structure. The Covid-19 pandemic will definitely make things worse; it is just a question of how much worse. Rapidly rising unemployment and a likely deep recession will greatly reduce municipal revenue while the demand for subsidised services from households that can no longer afford to pay their municipal accounts will increase. Many more municipalities are likely to become functionally bankrupt over the medium-term, which will further undermine the role of local government in socioeconomic development, at a time when that role is more important than ever. The wider national economic situation and rapidly deteriorating public finances mean there is probably no possibility at all that the national fiscus will be able to compensate fully for deteriorating municipal finances through greater transfers from the centre. However, Covid-19 should not be seen as the cause of the current financial crisis in local government: it is merely the latest (albeit very possibly unbearable) burden on a fiscal structure that (we believe) is fundamentally unsound.

1.4. Looking for solutions

The debate over the root causes (and thus the remedies for) of municipal financial distress is not new, and it is also increasingly heated. There is one group (mostly inside local government) who contends that municipalities (especially smaller and more rural municipalities) simply do not have enough financial resources at their disposal to deliver the services required of them. For this group, the solution to the problem is to increase local government's share of national revenue.

A related – and overlapping – group (largely representing local government, and the Department of Cooperative Governance and Traditional Affairs [COGTA]) believes the root cause of the problem is lack of capacity in local government, particularly in respect of operational and financial management. For this group, the solution is to provide more support to local government. However, we cannot ignore the fact that tens of billions of rands have already been spent on supporting municipalities over the past ten years, with little improvement recorded in either governance or financial resilience indicators.

There is another group (mostly within oversight institutions such as National Treasury and the AGSA, and the wider public) that makes two main assertions. The first is that if municipalities actually collected all the revenue they are authorised to collect (and priced services to reflect the actual cost of their provision), they would have far fewer financial constraints. The group's second assertion is that municipalities fail to manage their finances properly, and/or do not prioritise what they regard as the 'right' things in their budgets in respect of the funds over which they have discretion. For this group, the solution is for municipalities to improve revenue collection, reduce corrupt and/or wasteful expenditure and improve the way they prioritise expenditure.

Our research[5] suggests that both the first and third points of view have some merit, although the third does not, in our assessment, take sufficient account of the social wage function of affordable municipal services. Even so, neither of them presents a comprehensive picture of the underlying structural reasons for municipal financial distress – why revenue is not being collected, why there are so many unfunded mandates, and why maintenance is so poorly funded, etc. – or a comprehensive set of possible solutions.

We propose that a more detailed picture of the causes and possible solutions can be obtained through a closer examination of the local government fiscal framework: how it has evolved, how it is implemented, and its 'fit' (or lack thereof) with the current actual requirements of local government and the prevailing (and expected) fiscal reality of South Africa. We are not alone in this view; the Financial and Fiscal Commission (FFC) has stated its belief that

> ***[...] the Local Government Fiscal Framework is not in synchronization with the constitutional mandate of the sphere and requires renewal and rebuilding.***
>
> **FFC 2019, p7**

To date, however, their concerns have received little attention and no real action.

This paper investigates how well the fiscal framework envisaged in the 1998 White Paper matches the fiscal reality faced by local government in 2020.

Chapter 2 provides an overview of the local government fiscal framework that was envisaged – and described in considerable detail – in the 1998 White Paper. ***Chapter 3*** details the current state of local government finances, with particular reference to that envisaged fiscal: what has worked, what has not worked, and what was either never implemented, or not implemented as envisaged. ***The final chapter*** sets out our conclusions about the role of the fiscal framework in the current financial crisis in local government, and our recommendations for what could be done to address this in a sustainable manner.

5 A detailed investigation commissioned by SALGA of the structure of the local government equitable share and the financial challenges faced by municipalities undertaken in 2018/2019.


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CHAPTER 2

THE THEORY: THE ENVISAGED LOCAL GOVERNMENT FISCAL FRAMEWORK

2.1. Introduction

An ideal local government fiscal framework (LGFF) is, in summary, one that ensures sufficient revenue to meet all mandated expenditure requirements (while taking into consideration that the requirements of delivering a social wage set limits to service charges, and thus, income). This integrated relationship between revenue arrangements and expenditure responsibilities was emphasised in the 1998 White Paper:

> *Municipalities need to have access to adequate sources of revenue – either own resources or intergovernmental transfers – to enable them to carry out the functions that have been assigned to them.*
>
> **White Paper on Local Government, 1998**

This may seem obvious – available revenue needs to match required expenditure – but attaining this equilibrium has been very difficult in practice.

What does this integrated (i.e., revenue and expenditure) view of a fiscal framework imply? Firstly, a fiscal framework cannot be assessed based solely on its revenue component – in other words, how much funding it makes available for local government. Instead, these funding arrangements must be assessed in context – the context of what exactly that funding is intended (required) to purchase, as well as how affordable services are. The framework must be fit for purpose and generate sufficient revenue – in the required format – to meet the *actual* expenditure requirements and operational reality of local government, not some set of assumed requirements and operational reality.

Secondly, the integrated approach suggests that we can potentially improve the revenue–expenditure fit by adjusting the equation: we can either adjust the amount of money available (by increasing revenue inflows and/or by reducing expenditure leakages), or we can adjust the list of things that have to be purchased with that money (or the way in which they are purchased). The combination selected – revenue and/or expenditure interventions – will be determined by a number of factors, including limits on revenue generation, potential to reduce leakages, and the ability to adjust the mandate and/or operating structure of local government (which in many cases is regulated by statute and/or the Constitution).

The LGFF is located within the post-1994 national inter-governmental fiscal framework. The key component of that national framework is the *equitable division of revenue* among the three spheres of governmentnational, provincial and local. During negotiations for South Africa's new Constitution, there was considerable debate around the decentralisation of the tax-raising authority. Local government already had some own-revenue-raising capacity (property taxes and service charges being the main items) but provinces had hardly any (apart from vehicle licensing). All income, and value-added and related taxes were levied at national level. To counter demands for a federal fiscal system (whereby provinces would have greater own-revenue-raising capacity), the system agreed upon ensured equitable distribution of nationally raised revenue to attain a fiscal balance between revenue and expenditure of the three spheres of government. Provinces and municipalities would be entitled to keep the revenue they raised under their own powers, and were not obliged to contribute these funds to the national revenue pot.

Under the current system, national revenue is allocated among the three spheres (the vertical allocation) and then among the various parts of those three spheres (the horizontal allocation of each vertical allocation). This is based on a detailed formula, reviewed and revised periodically,[6] and contained in

6 The Financial and Fiscal Commission has the primary responsibility for coordinating this task (www.ffc.co.za).

the annual Division of Revenue Act (DORA). Revenue is allocated in the form of both unconditional and conditional transfers. Total revenue available to local government is thus made up of both own and equitable share revenue, and the latter is made up of both unconditional and conditional transfers.

The critical document in establishing the post-1994 LGFF in South Africa was the 1998 White Paper, which dealt extensively with the responsibilities of the new form of local government; how municipalities would access the revenue they required to deliver those responsibilities; and, the rules that would be applied to how that revenue could be spent. In the next section we first discuss the details of the White Paper in this respect, followed by the main events that impacted the LGFF after 2000, when the current structure of local government was fully implemented.

2.2. The White Paper

The 1998 White Paper on Local Government envisaged a radically new form of local government for South Africa, with the capacity to deliver a much wider range of goods and services to far more people, in a very different way than in the past. No longer would municipalities be responsible only for the delivery of a limited number of basic services to a small group of people. Instead, they would be central to delivering the long-term developmental mandate of the post-apartheid state. In particular, the new municipalities would carry most of the responsibility for addressing the country's huge basic infrastructure and services backlog, and delivering universal access to services.

In order for these ambitious goals to be achieved, a just-as-radical new fiscal framework was required, to ensure that all municipalities had access to sufficient resources to discharge their mandates. Designing such a fiscal framework was not an easy task: decades of inequality and the neglect of millions of South Africans had caused enormous service delivery backlogs, very poor local populations, and small local economies across much of the country, which reflected the spatially skewed distribution of economic activity in South Africa.

Municipalities in these areas could not reasonably be expected to raise significant amounts of money through service charges and property rates to address long lists of service delivery and development obligations. How were all these obligations to be funded in these places? How should services such as electricity and water be priced to balance the revenue requirements of local government with the ability of poor households to pay for them? These were only some of the complex questions that required an answer in the new LGFF.

The drafters of the White Paper were aware of the enormity of the task of designing an appropriate fiscal framework; they were also aware that there was only a very limited empirical basis for that design. The new form of local government represented such an enormous departure from the status quo that a range of assumptions had to be made about both sides of the new frameworkexpenditure and revenue.

On the expenditure side, although there was a long-term commitment to equitable service delivery, affordable services for all households and a central socioeconomic developmental role for local government, it was not known how much money would actually be required for these purposes over the next ten, twenty or thirty years. What would it actually cost to deliver, say, a water connection to a rural household in Bushbuckridge compared to a water connection to an informal dwelling in Cape Town? Since there had been so little quality service delivery to many poor urban areas, or to remote rural areas, there was no basis on which these costs could be accurately calculated. They had to be estimated as well as possible, along with household numbers and population and the poverty demographics that would determine the long-term level of demand for new infrastructure and services.

Similarly, there was not much empirical data available on the revenue side of the future local government balance sheet. Pre-1994 local government had the authority to raise revenue from a variety of sources, although a limited number of households were included in this tax and service-delivery regime. In white urban areas, local government raised revenue by levying property taxes, and selling services such as electricity and water (often on-sold from bulk service providers). Municipalities had relatively few infrastructure investment obligations, and limited development planning responsibilities. Most local municipalities were in a relatively good financial position since they serviced only relatively wealthy (white) areas, where most residents could easily afford to pay their municipal accounts. They also had relatively small service delivery obligations, reflecting the low number of households that they serviced. At that time, South Africa also had low bulk electricity prices (some of the lowest in the world) which allowed the municipalities to earn a healthy margin on electricity sales, making such sales the single biggest contributor (41.4 per cent) to municipal revenue. As a result of these factors, in aggregate, municipalities that serviced white urban areas were able to generate most of their operating expenditure requirements from their own property rates and municipal services charges.

On the basis of the existing financial affairs of this relatively small group of municipalities, the White Paper drew the important conclusion that "… [the] aggregate size of the (current) municipal budget in South Africa is substantial". When this starting point was augmented by the additional assumptions that (1) municipalities would in future be able to levy property taxes on millions of households that had never paid such taxes before; (2) most of the money for the infrastructure investment required to address the service delivery delivery backlog would be transferred from national government via the equitable share; and, (3) additional operational funding would also be available from the equitable share, the critical conclusion was drawn that local government in aggregate would have sufficient resources to meet all its expenditure obligations.

The real funding challenge was thus conceptualised as ensuring that this pool of resources was allocated among municipalities (the horizontal allocation of funds) to ensure that poorer areas had access to sufficient funds to compensate for their lower own-revenue generation potential.

There was a clear commitment in the White Paper to ensuring that households received services at a price they could afford, not only in the interests of promoting universal access to such services (as part of the social wage package), but also in the interests of ensuring that municipalities would get paid for those services. At the same time, there was an expectation that tariffs would be set at a rate that accurately reflected the costs of providing those services: "[…] services (should be) provided at levels which are affordable, and that municipalities are able to recover the costs of service delivery". There was thus a clear assumption that the following two goals were compatible: it would be possible for local government to charge fees that were affordable, and that those fees would meet cost recovery requirements.

It was acknowledged that there would always be some very poor households that would be unable to pay for services and thus "[…] a need for subsidisation to ensure that poor households, who are unable to pay even a proportion of service costs, have access to basic services".

It is important to note that at the time the White Paper was being written there was a general expectation that over the medium- to longer-term the post-apartheid economy would grow in real terms, a significant number of employment opportunities would be created, inequality would decline, and household poverty levels would consequently fall. The implication was that, over the long term, the relative number of households that would require subsidisation would be comparatively low.

The details of the White Paper's funding model are set out below. In Chapter 3, we have analysed the current state of local government finances against the background of this funding model and its key assumptions.

2.3. The White Paper funding model

In summary, the new structure of local government would have access to the following funding sources:

a. Own revenue
b. An equitable share of nationally raised revenue
c. Other funding streams

A key foundational component of the White Paper's municipal funding model was that own revenue would make up a significant portion of local government's funding requirements, an assumption reflected in this key statement:

> *Municipalities do generally have sufficient revenue-raising powers to fund most of their expenditure [...]. On average they finance 90% of their recurrent expenditure (operational or running costs) out of their own revenue, and in particular from property rates and user charges (for services).*[7]

This was a critical assumption: if local government *in aggregate* could finance 90 per cent of its operating expenditure requirements – which included all its employee costs together with key operating expenses such as infrastructure and asset maintenance – then its main additional funding requirements would be limited to a 10 per cent top-up for operating expenditure (most notably the subsidisation of the free basic services), and funding for new infrastructure development to address the service delivery backlog. This assumption was central to how the rest of the funding model was envisaged and enacted, and it is the basis of the current position that local government would have enough money if it only worked harder to collect revenue.

> *National transfers account for a relatively small proportion of the local government fiscal framework, with the majority of local government revenues being raised by municipalities themselves through their substantial revenue-raising powers.*
>
> **DORA, 2020**

The White Paper proceeded on the assumption that the main sources of own revenue for the new local government structure would be property rates and service charges: it was assumed that these items would be able to make up just over 81 per cent of total own revenue (with the balance – 19 per cent – coming from items such as rentals and other charges). That, in turn, implied that income from property rates and services charges would be sufficient to finance 73 per cent of all local government operating expenditure requirements (i.e., 81 of 90 per cent).

These optimistic forecasts reflected in part the fact that municipal income would be raised from a far greater number of households than before, as previously excluded households would now fall under the property rates tax regime of a municipality. Additional revenue would also be generated through the purchase of bulk services (such as water or electricity) and the on-selling[8] of these to (a larger group of) consumers. This was envisaged as a *margin income*, the quantum of which would be determined by the difference between the purchase (bulk) price and the consumer tariff, as well as the quantity demanded.

Within the overall revenue contribution assumptions, the White Paper also contained detailed assumptions about how much revenue local government could raise from the sale of these various municipal services, and thus what the contribution of each of these would be to operating expenditure requirements. These assumptions are summarised in Table 2.

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7 1998 White Paper on Local Government.

8 It should be noted that almost all electricity is purchased by municipalities from the bulk service provider (Eskom) while the water situation is more mixed. Some municipalities purchase from the water boards, but there are many that provide the bulk water themselves, and thus do not pay a bulk provider.

TABLE 2: White paper assumptions of the contribution of various income sources to own revenue and operating expenditure*

Income source	Assumed contribution to own revenue (%)	Assumed contribution to operating expenditure (%)
Property rates and taxes	19.9	17.91
Electricity sales	41.4	37.26
Water	11.8	10.62
Sewerage & refuse removal	8.2	7.38

*Based in turn on the assumption that own revenue would make up 90% of total operating expenditure

The most important discrete category of revenue was assumed to be electricity income, which would be sufficient to finance more than a third of all operating expenditure requirements.

> *The assumed ability of local government to finance most of its expenditure requirements out of own revenue (while still keeping the cost of those services 'affordable') is not just critical to the local government fiscal framework but is the foundation of the entire national fiscal framework and the state's developmental agenda. The national fiscal framework is based on the assumption that almost 100 per cent of national and provincial budgets can be financed from nationally raised revenue, because local government only requires a relatively small share of that revenue. In turn, the bulk of the state's programme to deliver basic services and to maintain local infrastructure is intended to be financed by local government's own revenue. The integrity of the local government fiscal framework – and most notably the own revenue portion – is, therefore, not a local government problem, but a national one.*

The White Paper recognised the importance of an effective revenue management function in achieving these targets – ensuring that municipal customers actually paid their accounts if they could afford to do so. (The revenue collection target is currently set by National Treasury at a minimum of 95 per cent). The implied position (as described above) was that the cost of municipal services would be set at a rate that was generally affordable. Therefore, effective revenue management would be determined mostly by robust debt management systems (i.e., by making customers pay their 'affordable' accounts). The White Paper made the following recommendations in this respect:

> *[...] municipalities must keep a proper record of outstanding debtors, and must take action against them after a given notice period. Such action can include cutting off services or court action to recover debts.*

And what, according to the White Paper was the most effective way to compel customers to pay their outstanding accounts?

> *It is fundamentally important that local government is able to retain the power to cut off electricity[9] to consumers as a credit control measure, and amendments to the Electricity Act will be promulgated in this regard.*

9 This was even more so the case after the Constitutional Court effectively ruled that water could not be disconnected because of an outstanding municipal account, although the pressure could be reduced.

In addition to own revenue, local government would have access to an equitable share of nationally raised revenue. Local government has always received the lowest share of that revenue (around 8.5 per cent of non-interest allocations[10] for the original 2020/21 budget estimates, compared to approximately 42 per cent for provinces and almost 50 per cent for national)[11] because of its ability to raise its own revenue. The central feature of the new fiscal framework was its conceptualisation of the equitable share as a fiscal balancing mechanism. That is, the underlying assumption was that any shortfall in the aggregate local government budget due to insufficient own-revenue collection could always be filled by the equitable share:

> *When fully operational, the new system of intergovernmental transfers will enable all municipalities to deliver a package of basic services to all low-income **and** indigent households in their areas.*
>
> (The emphasis we have added here highlights that the White Paper assumed some form of subsidised services to both low income households and indigent households. This would not only have a significant pro-poor impact but would also create a significant financial obligation for the local government fiscal framework to deliver.)

This assumption of the guaranteed availability of funds via the equitable share transfer mechanism was so strongly held that it has dictated the municipal demarcation process: projected own-financial viability of a demarcated municipality (i.e., the ability of a municipality to be a financially viable unit without an equitable share or similar transfer mechanism) was never intended to be the *primary* factor determining demarcation (i.e., that a municipality would only be demarcated as such if it was financially viable because of its own revenue). Many municipalities were demarcated *despite* limited own-revenue-raising capabilities, in the greater interest of promoting democratic and accountable government, and on the clear assumption that the equitable share would always make up any own-revenue shortfall. Dependency on such transfers has not been envisaged as a reason to declare a municipality 'non-viable' and it is only *one* of the criteria taken into account in the demarcation of municipalities, rather than a critical variable (Khumalo and Ncube, 2016).

The equitable share is made up of two components: operational transfers and conditional grants. The former are, in theory, to be spent at the municipality's own discretion in line with local priorities, but in reality are meant to be allocated to particular purposes, although there is little oversight of this. (The details of the current operational transfer structure is set out in 2.4. below).

Conditional transfers (conditional grants) are, as the name suggests, funds that may only be spent for specified purposes, and in line with strict rules. Failure to spend the funds as indicated can cause them to be reclaimed by the national fiscus. The aim of the conditional transfers is to try and ensure that municipalities direct their spending in line with national priorities, most notably in respect of infrastructure investment and spatial development. Most of the conditional grants are in respect of capital expenditure, and the most significant of these is the Municipal Infrastructure Grant (MIG), intended to address the significant backlog in the provision of basic services inherited in 1994. In the original 2020/21 Division of Revenue Act (DORA), conditional grants constituted some 31 per cent of total transfers (both direct and indirect) to local government.

10 Excluding indirect transfers

11 Numbers do not add up to exactly 100 per cent.

The White Paper was clear that municipalities would need additional funding in addition to operational transfers and conditional grants – not least to address the huge infrastructure backlog and to support local economic development. Additional funding would come from various forms of credit (borrowing) and other means of leveraging alternative funding sources. The White Paper clearly envisaged that "[…] a vibrant and innovative primary and secondary market for short and long term municipal debt should emerge" and, in the interests of supporting the development of such a market, recommended that national government investigate a range of supportive mechanisms, including the following:[12]

- Municipal bond insurance
- Treasury trusts
- Interception of intergovernmental transfers
- Debt syndication
- Bond banking

On top of the possibilities for expanded municipal credit markets, the White Paper made a number of recommendations about the creation of alternative financing models, the use of which would allow municipalities to leverage additional resources, by mobilising off-budget resources "via partnerships with businesses and non-profit organisations".

12 There has always been a very clear view that national government would never provide sovereign guarantees for municipal debt.

2.4. Key developments after 2000

What were the main factors that impacted the LGFF after 2000, the year most components of the current local government structure came into operation? In 2001 the policy in respect of free basic services was adopted and gave effect to the White Paper's requirement that very poor households could still receive a minimum level of services. The free basic services are offered to households classified as 'indigent', a narrower group of beneficiaries than the one envisaged by the White Paper (as discussed above). In this respect, each municipality is required to have an indigent household policy that sets the local criteria for a household to qualify (these are largely around a maximum household income, although other conditions may also apply).[13] Households are required to register with their municipality (and regularly re-register, mostly each year) to receive the free basic services plus the rates rebate. The minimum level of free basic services to qualifying households is six kilolitres of water and 50 kilowatt hours of electricity per month, together with subsidised sewerage, sanitation and solid waste management.

The calculation of the vertical and horizontal equitable share has been restructured on more than one occasion, in an attempt to better reflect the actual funding requirements of local government, as well as to try and control how those funds are allocated. The latest restructuring was undertaken in 2012, and implemented in 2013. The new formula deals in large part with the horizontal allocation of the non-conditional portion of the equitable share (i.e., the allocation of the local government share among municipalities), and was designed in large part to address the funding gap in those municipalities that have the lowest own-revenue generation capacity. The allocation formula now contains the following:

- **The basic services grant** to compensate municipalities for the subsidisation of free basic services. The current amount is R435.04 per household for the full package of free services. The allocation is not made on the basis of actual indigent households in each municipality, but on estimates based on the 2011 census.
- **The municipal institution grant** to enable municipalities with limited resources to pay for basic administration and governance, as well as unfunded community services. This is weighted to favour municipalities with the lowest ability to finance these functions themselves.
- **The tax base equalisation grant** (revenue adjustment factor)
- **The matching grant** (correction and stabilisation)

In summary: **LGES = BS + (I+CS) X RA +/- C**

Where

LGES is the local government equitable share

BS is the basic services component

I is the institutional component

CS is the community services component

RA is the revenue adjustment factor

C is the correction and stabilisation factor

Source: *DORA, 2020*

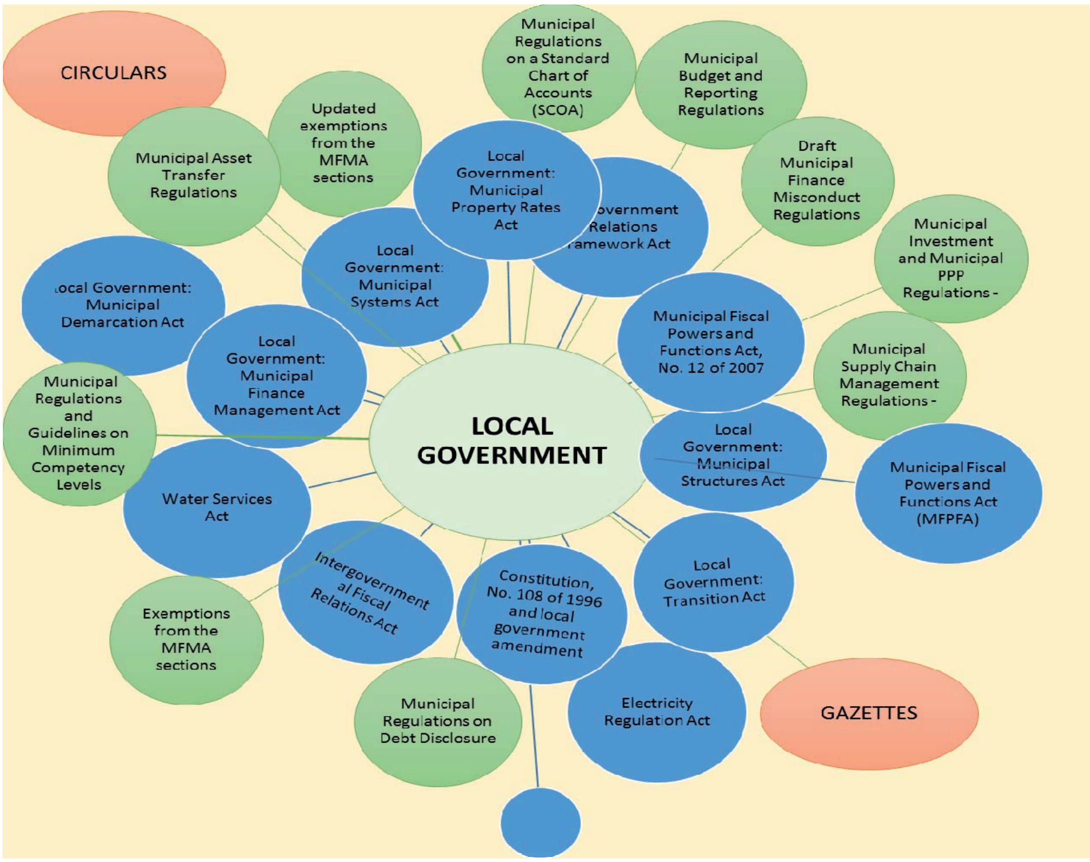
Because the allocation formula is intended to benefit municipalities on the basis of their estimated own revenue generating capacity, the value of transfers per household to most rural municipalities is more than double that made to the metros.

The proliferation of conditional grants since 2000 has mostly impacted the larger, more urban municipalities; many smaller municipalities tend to receive the MIG and only one or two other grants. Despite its recommendations that grants be consolidated for administrative reasons, the FFC reported in

13 For example, we know of at least one municipality where a household is excluded from the free basic services if any kind of business activity is conducted from their home, even if household income is below the threshold.

2013 that there had been a five-fold increase in the number of conditional grants to provinces and local government between the 2005/06 financial year and the 2013/14 financial year (FFC, 2013). The number of grants allocated to local government has grown particularly significantly (FFC, 2013). The real challenge is that qualifying for each different grant requires both significant administrative and management time, resulting in "overlapping programmes with competing objectives and complex reporting requirements" (FFC, 2013, p1). The increase in the number of narrow grants also results in municipalities effectively structuring their capital expenditure to suit the requirements of the grants, rather than local conditions and requirements (PARI, forthcoming); it is precisely this local adaptability that was one of the initial and chief justifications for the current structure of local government.

In addition to the increased administrative and reporting costs associated with the proliferation of grants, there has been a general increase in the regulatory burden on local government. Research conducted by the FFC in 2014 concluded that local government is the most regulated sphere of government. The FFC illustrated the regulatory burden on local government in the following diagram:



Source: *FFC 2014*

In the intervening six years there have been some notable increases in that regulatory burden, certainly not what the White Paper envisaged when it stated:

> *National government should provide a coherent framework to ensure that the reporting requirements placed on municipalities are reasonable, and should also ensure the rationalisation and standardisation of the current multiplicity of local government surveys into a coherent annualised national*

data collection system.

The most likely effects of this excessive regulatory burden are:

i. To redirect (already scarce) resources towards regulatory compliance, instead of direct service delivery;

ii. "To delay service delivery and development because of the need to meet the requirements of several different pieces of legislation. The relevant provisions of the different pieces of legislation are sometimes duplication and at other times contradictory" (SALRC, 2019, p1); and,

iii. To effectively make it more difficult to exercise oversight over local government, due to the sheer volume of reporting data that is generated.

There is no empirical evidence to suggest that the additional regulation burden has resulted in a commensurate improvement in local government's operational and/or financial management. In contrast, a great deal of anecdotal evidence suggests that the main outcome is the diversion of resources from direct line functions. The impact is most likely to be the greatest in the smaller municipalities because of their generally constrained resource environment. There is little differentiation in regulatory obligations based on the size of the municipality or its revenue base.

Several of the municipal officials interviewed for the 2018 research that this working paper is based on, voiced their general view that most of the increased reporting burden had little organisational value:

> *All this regulation has actually made things worse because the reality is that no one can work out what is actually going on. Do you really think that (national) Treasury reads in detail every single report that is sent to them?*
>
> *There are more and more reports, but no one did anything when this municipality was in big trouble, so what's the point?*

In 2019, the South African Law Reform Commission (SALRC) announced a project to review the regulatory, compliance and reporting burdens imposed on local government by legislation. The project issue report (SALRC, 2019) included the following as initial evidence of an excessive reporting burden:

> *The Local Government Data Collection Forum, whose main purpose was to address multiple reporting (a burden created when local government is required to provide data, sometimes the same data, to multiple entities), established early on in its investigation that:*
>
> > *(i) the barrage of requests for information came from four organs of state with statutory authority to collect data imposed financial and administrative burden on municipalities;*
> >
> > *(ii) there was a great deal of duplication in the data requested by three of these entities namely Stats SA, National Treasury, the Department of Provincial and Local Government;*
> >
> > *(iii) 95% of municipalities received questionnaires from provincial governments for information similar to that asked for by national government; and that*
> >
> > *(iv) 60% of municipalities do not complete all the questionnaires, among other things, due to lack of adequate resources.*

As at the date of this report, the SALRC had yet to publish its final findings or recommendations.

In the next chapter we have discussed the current state of local government against the assumptions and expectations contained in the White Paper. How well does the current reality match up against those assumptions?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CHAPTER 3

THE REALITY: THE CURRENT STATE OF LOCAL GOVERNMENT

The current state of local government is certainly not what was envisaged in the White Paper more than 20 years ago. A significant contributing factor to many of these disappointing outcomes is, we believe, the failure of the local government fiscal framework to deliver what was expected. In particular, assumptions about the ability of local government to raise own revenue from rates and services charges – while still contributing to the social wage in the form of affordable services – have failed to materialise, for multiple reasons. Combined with significant leakages from the system (poorly managed finances, irregular and wasteful expenditure, and distribution losses) the effective impact is that we currently have a system of local government that is inherently financially unsustainable in its current structure and operation.

3.1. Local government finances are in a precarious – and deteriorating – state

In the 2018/19 local government audit report the Auditor-General of South Africa (AGSA) highlighted the precarious financial state of local government: it was concluded that 79 per cent of all municipalities had a financial health status that was "either concerning or requiring urgent intervention", that 31 per cent of municipalities were considered to be in a "particularly vulnerable" financial position. In addition, just over a third of municipalities ended the year with a deficit – an aggregate amount of 6.3 billion rand (AGSA, 2020a).

Although poor financial governance certainly contributes to financial distress, we cannot conclude that good governance is a panacea: the 2018/19 AGSA report for local government indicated that three of the municipalities and municipal entities that received a clean audit, and 27 of those that received an unqualified audit ended the year in deficit. In terms of current liabilities exceeding current assets (i.e., a state of technical insolvency) two that received a clean audit and 35 with an unqualified audit ended the year in such a position (AGSA 2020b).

3.2. Local government own revenue has failed to meet White Paper estimates

The current fiscal framework of local government is based on one key assumption: local government in aggregate is capable of financing 73 per cent of total operating expenditure requirements by property rates and income from the trading of municipal services. The assumed contributions of aggregate (i.e., across all municipalities) own-revenue categories to aggregate operating expenditure are summarised below:

TABLE 3: White Paper assumptions of the contribution of own income to operating expenditure (aggregate)

Income source	Assumed contribution to operating expenditure (%)
Property rates and taxes	17.91
Electricity sales	37.26
Water	10.62
Sewerage and refuse removal	7.38

How has this assumption turned out in practice? The evidence suggests that in aggregate it has not materialised, and that, outside of the major metros, the shortfall between assumption and reality is considerable – that is, only the metros are close to matching these assumptions, but cannot compensate for the shortfall in other places. An accurate assessment of the situation (how much own revenue contributes to operating expenditure) is made difficult by the fact that municipalities must match revenue and expenditure for a balanced budget – the lower the anticipated revenue, the lower the budgeted operating expenditure and the better the 'fit' between the two will seem. However, the White Paper was clear that own revenue would be sufficient to meet operating expenditure requirements, that is, own revenue would be sufficient to cover 90% of what a municipality *should* be spending on operating expenditure to cover its constitutional obligations, without undermining the social wage. Because that figure (the ideal level of operating expenditure) is not available, we have assessed actual own revenue against *budgeted* operating expenditure on the assumption that the original budget is an (imperfect) proxy for required operating expenditure. Almost all municipalities end the year with operating expenditure below what was budgeted, in part because actual revenue falls short of budgeted revenue.

We have examined the period from 2016/2017 to the third quarter of the 2019/20 financial year in order to obtain a better picture of the relationship between own revenue and operating expenditure. The methods used to calculate this data and the data sets used are set out in Annexure B. We acknowledge that there are some data-quality issues (reflecting poor financial record keeping in many municipalities), but the reporting errors in aggregate tend to overstate revenue (that is, actual revenue is more likely to be lower than the figures we used for our calculations). Data quality is the reason we have not extended our analysis to the period prior to 2016/17, and also why we have only examined a limited number of data sets. Data quality also explains some of the more apparently anomalous data sets, such as those from North West. (The issue of data quality is discussed in more detail in Annexure B.)

Our findings are summarised in Table 4 which shows the various categories of own revenue as percentages of budgeted operating expenditure, both the budgeted revenue figure and the actual revenue figure. For example, the Property Rates column indicates first the percentage contribution of budgeted property rates to budgeted operating expenditure (i.e., its anticipated contribution) and second, the percentage contribution of actual property rates to budgeted operating expenditure (i.e., the actual 'contribution' to budgeted operating expenditure). The 'actual' column thus serves as a proxy for the contribution of the various own-revenue categories to operating expenditure. A comparison of 'budget' and 'actual' serves as an indication of the budgeting gap – what municipalities are estimating they can bill, and what they are actually able to bill.

Note the following in respect of 2020: The budgeted data are for the full year, while the actual revenue data are for the first three quarters of the financial year, compared to the full year budgeted operating expenditure; that is, the 'actual' column for 2020 indicates billed revenue for the first three quarters, compared to budgeted operating expenditure for the full year (to 30 June, 2020).

TABLE 4: Contribution of main own revenue items to budgeted operating expenditure (2016/17 to Q3/2020)

Province	Property rates (%)		Electricity (%)		Water (%)		All services and rates actual (%)
	Budget	Actual	Budget	Actual	Budget	Actual	
Eastern Cape							
Q3/2020	15.02	14.77	51.03	8.62	7.71	3.80	
2018/19	14.86	14.08	24.08	21.39	7.49	7.26	48.1
2017/18	13.76	11.30	22.85	19.05	8.16	7.04	46.6
2016/17	12.46	11.42	23.52	21.97	6.20	6.14	44.2
Free State							
Q3/2020	12.89	9.62	26.94	18.01	11.95	10.18	
2018/19	12.66	12.93	27.44	24.39	12.13	11.43	60.1
2017/18	13.10	15.36	27.62	24.62	12.46	12.22	60.5
2016/17	12.49	11.92	30.97	24.44	11.94	11.70	55.3
Gauteng							
Q3/2020	18.97	13.69	33.79	23.29	13.80	9.19	
2018/19	19.21	19.92	34.25	32.19	13.17	12.67	74.3
2017/18	18.42	19.07	35.32	33.57	13.28	11.65	73.1
2016/17	17.22	16.25	36.71	35.49	13.02	11.45	71.7
KwaZulu-Natal							
Q3/2020	18.80	13.37	31.23	19.22	11.29	7.20	
2018/19	18.42	14.52	30.94	23.33	10.48	8.12	49.9
2017/18	18.30	3.86	32.08	6.66	10.11	1.67	13.5
2016/17	17.59	18.82	34.23	32.65	9.66	8.63	63.1
Limpopo							
Q3/2020	10.39	7.32	18.82	11.54	6.14	4.19	
2018/19	8.75	8.57	17.11	15.57	4.85	4.85	31.9
2017/18	8.79	5.17	18.56	7.35	4.62	3.48	17.7
2016/17	9.08	8.02	19.00	17.24	5.84	4.74	33.0
Mpumalanga							
Q3/2020	13.94	10.00	23.07	15.26	8.48	6.09	
2018/19	13.90	13.35	21.44	20.00	8.06	7.32	46.2
2017/18	13.79	17.31	24.10	19.45	8.45	8.09	50.2
2016/17	13.36	13.04	25.49	21.35	8.39	7.58	47.4
North West							
Q3/2020	10.88	7.61	26.08	23.83	10.51	7.54	
2018/19	10.35	7.95	24.00	10.49	10.11	7.31	30.0
2017/18	10.35	5.81	26.82	13.97	10.36	3.45	25.6
2016/17	10.03	9.91	28.96	25.88	9.89	9.38	51.0
Northern Cape							
Q3/2020	16.33	14.02	25.95	17.14	8.75	6.41	
2018/19	14.75	12.87	24.56	20.72	9.87	7.28	46.2
2017/18	14.99	10.39	26.27	14.52	10.22	5.52	35.9
2016/17	13.88	19.01	26.75	22.83	10.41	8.65	58.1
Western Cape							
Q3/2020	20.36	15.66	33.50	25.16	7.35	5.61	
2018/19	20.83	20.58	32.84	31.89	8.90	8.18	68.0
2017/18	20.36	17.29	31.98	24.99	7.84	5.80	53.6
2016/17	18.77	19.81	33.11	32.80	8.96	9.36	69.6
Aggregate							
Q3/2020	17.39	13.07	32.73	20.32	10.88	7.37	
2018/19	17.28	16.58	29.99	26.48	10.59	9.60	59.7
2017/18	16.83	13.69	30.73	22.48	10.50	7.50	49.8
2016/17	15.86	15.61	32.25	30.50	10.35	9.51	62.2
Metros*							
2018/19	20.84	20.12	35.02	31.07	11.59	10.57	69.7
2017/18	20.19	21.11	35.73	34.45	11.20	10.39	73.8
2016/17	18.68	18.43	36.79	35.70	11.18	10.32	71.8

* Data for the metros for 2020 were not included because of uncertainty about the quality of the data for some metros (details in Annexure B).

Source: *National Treasury MFMA MBBR Tables and Section 71 in-year reporting data (www.mfma.treasury.gov.za)*

If we compare this table to Table 2 (which summarises the own-revenue generation assumptions of the White Paper) we can draw the following conclusions:

i. In aggregate, local government is nowhere near the target of rates and service charges making up 73 per cent of operating expenditure, although the metros in aggregate are not far off that target. The main reason for the better metro performance is most likely the concentration of wealthier households and commercial enterprises (i.e., those that receive the highest municipal accounts) in those areas. The main reason that Gauteng's outcomes are on or close to target is because of the high concentration of metros in the province. It should also be remembered that the 73 per cent target is an **aggregate** one, implying that the actual outcome in wealthier areas should be higher, to compensate for lower revenue in poorer areas.

ii. General underperformance holds true, even in the Western Cape, the province with the highest number of clean audits and the best overall governance outcomes which further suggests that although there is a relationship between good governance and revenue outcomes, good governance on its own will not guarantee that the White Paper's own-revenue assumptions are met.

iii. The main reason why own revenue falls short of the is that the contribution of electricity falls short of the White Paper's assumptions of 37.26 per cent. Firstly, the key contributor to this situation is Eskom which supplies electricity directly to just over 50 per cent of South African households, and to a large number of commercial and industrial clients. Electricity revenue goes to Eskom, not the local municipality. Secondly, Eskom's governance and operational problems have resulted in well-above inflation increases in electricity tariffs. Since 1998 the dynamics of the electricity sector have changed considerably, and South Africa has gone from having some of the cheapest electricity in the world to a current situation where it is mid-priced on a global comparison. Rising prices have resulted in many municipal customers reducing their electricity usage. In addition, rising electricity tariffs together with load-shedding has encouraged wealthier users (who have higher municipal accounts) to opt out of the system by installing their own generation systems.

In reality, the situation is far worse than this analysis indicates. The 'actual' revenue in Table 4 indicates the revenue *billed* in each period, and not the revenue actually received. Cash-flow data for many municipalities (including some of the metros) are extremely poor, but National Treasury estimates a revenue collection rate in the metros of around 93 per cent, and about 74 per cent in aggregate across local government (these estimates were made before considering the impact on payment rates of the current sharp decline in economic activity). The AGSA is more pessimistic; it estimates that only about 60 per cent of services revenue on the aggregate local government balance sheet will ever actually be collected.

If we assume a revenue collection rate of about 70 per cent (i.e., that 70 per cent of 'actual' revenue will turn into income), then, in aggregate, local government is probably only able to fund **less than 50 per cent of (current budgeted) operating expenditure** from property rates and service charges, with the funding gap being greatest outside of the metro areas.

Low revenue collection rates are reflected in the ever-growing local government debtors' book, which increased from R128 billion in the 2016/17 financial year to R181 billion at the end of March 2020. Over the same period, the debt owed by households increased From R81 billion to R128 billion. Although the non-payment of electricity gets a lot of media attention, the biggest outstanding amounts owed to municipalities are in respect of rates and taxes and water, as indicated below:

TABLE 5: Aggregate municipal debt by type of service: 31 March 2020

Service	Amount owed (R billions)
Property rates	50.21
Water	36.18
Electricity	22.4

Source: *National Treasury S71 in-year reporting (www.mfma.treasury.gov.za)*

One of the critical debates is whether low collection rates (and thus the rising debtors' book) reflect the inability of households to pay, or a lack of effort on the part of municipalities to collect money. Our analysis suggests that both factors are important, together with another that receives little attention – Eskom. The White Paper was clear about what it envisaged on the issue of debt management:

> *[...] municipalities must keep a proper record of outstanding debtors, and must take action against them after a given notice period. Such action can include cutting off services or court action to recover debts.* ***It is fundamentally important that local government is able to retain the power to cut off electricity to consumers as a credit control measure****, and amendments to the Electricity Act will be promulgated in this regard.* (our emphasis)

This critical regulatory tool has effectively never been available to municipalities where Eskom is a major supplier of electricity.

The end result of Eskom's direct participation in the retail supply of electricity is that *almost 50 per cent of municipal households are exempt from electricity disconnection as a credit control tool to enforce the payment of rates and taxes*. Of even greater concern is that this also results in households not paying for water. Payment rates for water have been declining steadily, from 67.3 per cent of households in 2008 to 40.9 per cent in 2018 (StatsSA, 2019). PARI's own research (Ledger and Rampedi, 2019; Ledger, Chilenga and Rampedi, 2016) suggests that payment rates for water are lower in areas where Eskom is the supplier of electricity, since these households are very well aware that the municipality cannot disconnect their water supply to force payment. This issue was emphasised by municipal officials during our 2018 study:

> *People cannot afford to pay their rates and taxes and the prepaid services (electricity) at the same time, so they choose the pre-paid services.*
>
> *We tried a payment campaign to say that if you pay half of your outstanding account then the other half will be written off, but we collected hardly any money from that.*
> (Eskom is the only electricity service provider in this municipality, and household municipal account payment rates are below 20 per cent.)
>
> *Two thirds of our bad debt comes from areas where we cannot disconnect the electricity.*

3.3. The social wage is being eroded

Universal access to basic services at a cost households can afford is a critical part of the state's commitment to deliver a social wage as a tool to reduce both poverty and inequality. The White Paper was clear about the obligations of local government to provide affordable services at a minimum quantity and quality to all households, and to subsidise those who were unable to pay for services. This implies that the goal of raising sufficient revenue to meet operating expenditure requirements cannot result in services becoming increasingly unaffordable, particularly for poorer households. Unfortunately, it appears that this is exactly what has happened, with the development goals of the social wage either minimised or ignored in the national debate around municipal financial distress. A strong narrative in national government posits that consumers must be 'made' to pay their accounts, or be deprived of access to these services. This approach is totally at odds with the fundamental developmental role of local government.

It certainly is the case that there are some municipal customers who are able to pay their accounts but simply refuse to do so (the other parts of government that collectively owed local government R18.7 billion in March 2020 spring to mind). However, household poverty is both real and pervasive. Many households simply cannot afford to pay their municipal accounts. Household poverty rates are high, and have also increased considerably over the past few months. Even before the impact of Covid-19, estimates were that some 40 per cent of all South Africans lived below the Lower-Bound Poverty Line (LBPL).[14] The White Paper did not anticipate a situation where so many poor households would simply be unable to afford to pay for municipal services. Although dominant narrative holds that 'households can afford to pay, they just choose not to', the current economic reality in South Africa suggests that this is not true. Research (Ledger 2016, Jacobs 2009) suggests that 80 per cent of South African households are not able to afford a nutritionally balanced basket of food every month. This is the reality of the household 'choice' of whether or not to pay for municipal services.

> *Households prioritise what they can pay – food and transport – and they don't pay the municipality because there simply isn't money left over.*
>
> *If people have to choose between food for their children and paying the municipality, which one do you think they will choose?*

The free basic services allowance to registered indigent households is an inadequate compensation for this situation. It is important to note that:

- About 40 per cent of all South Africans live below the LBPL – which means they have to sacrifice expenditure on food to be able to afford non-food items.
- There are approximately 16.5 million households in South Africa.
- Only around 3.6 million[15] (22 per cent) are registered as indigent households across all of local government.

To add to this, the free allowance is allocated per household, not per person. The reality in many rural municipalities (supported by our fieldwork findings) is that poor household size is often relatively large. In these circumstances the free basic allowance is nowhere near the amount of (particularly) water or electricity that the household actually requires to maintain minimum hygiene and living standards.

Our 2018 fieldwork repeatedly highlighted the enormous challenges faced by municipalities that are constitutionally obligated to deliver services (notably water) to people who cannot afford to pay for them.

> *You know, people will register as indigents, but the free water allocation just isn't enough for everyone who is living in that household, especially when there are a lot of children living in one house. So they need more water, but they can't pay.*
>
> *People think that when you are bringing them water (to their house) you are doing it so that you can charge them (and they know that they cannot pay). So they give you a false ID, or they damage the meter.*

14 The lower-bound poverty line (LBPL) is calculated from a set of reference households whose total expenditure is close to the food poverty line and who are therefore forced to live on 'survival foods' and to sacrifice some basic food-needs in order to meet their non-food requirements. In 2019, the LBPL was R810 per person per month.

15 For 2018 (StatsSA, 2019).

Subsidised and affordable access to basic services is an important part of the state's strategy to reduce the cost of living for poor households, and thereby compensate them in part for lack of income. The current form and operation of the local government fiscal framework (which requires constant increases to tariffs) is eroding the social wage to an alarming extent, and thus contributing to increasing poverty and deepening inequality.

In this context it is important to note that National Treasury has repeatedly raised the issue of whether or not current services charges actually reflect the cost of delivering those services: their view is that tariff determination processes in many municipalities are not resulting in full cost recovery (National Treasury, 2019b). National Treasury holds that if services were priced on a full cost-recovery basis in many instances they would be higher. The implications is that 'accurate' cost calculation could make municipal services even more unaffordable for more households.

3.4. Thriving municipal debt markets and alternative funding arrangements have not materialised

The White Paper assumed that a 'vibrant' credit market for local government would develop and enable it to raise additional funding, particularly for infrastructure investment. The reality has proven to be very different; almost all lenders only extend credit to the largest municipalities with the best governance outcomes, and only finance the projects deemed to be the most bankable. Even in this group, however, the use of finance for capital projects is limited: consolidated data across all municipalities indicate that borrowing (from all sources, not only the private sector) has historically contributed no more than 15 per cent to the funding of capital expenditure at local government (National Treasury consolidated MBBR table A5).[16]

The White Paper also envisaged a range of alternative and innovative funding and service delivery mechanisms that municipalities could use to leverage additional resources for local development and service delivery. Very few of these have actually materialised at scale, however, particularly in the smaller and poorer municipalities where they are most needed and presents a potential source of municipal funding that is not being utilised to any meaningful extent.

It appears that there are two main obstacles to the use of alternative structures. The first is the limited capacity within most municipalities to conceptualise, design, implement and manage these alternative structures. For this reason, what innovation is seen (such as in the use of community organisations to deliver basic services) is concentrated in the larger municipalities that can afford to hire such expertise, and experiment with alternative structures that make up a very small part of the overall service delivery budget. The second reason is that the overarching regulatory environment – particularly with respect to procurement – has narrowed the space for innovation. Once again, it is the smaller municipalities, which lack the expertise to innovate around these regulations, that are shut out of these options.

16 http://mfma.treasury.gov.za/Media_Releases/mbi/2018/Documents/Forms/AllItems.aspx?RootFolder=%2fMedia%5fReleases%2fmbi%2f2018%2fDocuments%2fl%2e%20Audited%20results%20for%202016%2d17%2fCapital&FolderCTID=&View=%7b48BDEAC8%2d7798%2d4241%2d8F9E%2dDC55A74ABC67%7d

CHAPTER 4

NOW WHAT?

4.1. What are our options?

The current situation cannot continue for much longer: the inability of local government to raise sufficient own revenue to cover 90 per cent of operating expenditure while supporting a social wage, threatens the entire national developmental agenda. If we return to the original description of the fiscal framework –

> *[...] an effective fiscal framework is one where sufficient revenue is available to cover all the expenses that must be incurred to deliver that agenda*

– it appears that we are now in a situation where revenue does not match expenditure (even though the cost of municipal services is unaffordable for millions of households).

Where can we look for solutions? A useful metaphor often heard in respect of local government budgets and finance is 'cut your coat according to your cloth'. The implication is that you can only spend what you can finance: either you cut a smaller coat, or you get a bigger piece of cloth.

Let's start with the latter – a bigger piece of cloth. Although there is some room to **increase revenue collection in local government** – notably from state entities and other customers who can afford to pay – the reality is that the cost of municipal services needs to be lower for a significant number of households, and more households should have access to more free services in order to deliver the requisite social wage component.

We believe that restoring the integrity of the social wage should be non-negotiable when discussing the future of the local government fiscal framework. For too long we have been sacrificing the welfare of poor households to try to balance the books of what is fundamentally an unsound financial model from the point of view of pro-poor development.

A number of organisations have said that to get a bigger piece of cloth **inter-governmental transfers to local government must be increased**. This too is not viable under current fiscal conditions. Increasing transfers to local government will require cuts to key provincial and national budgets, such as health and education, which simply cannot be considered. The level of government debt is forecast to rise above 70 per cent of GDP by the 2022/23 fiscal year, and the national priority is to reduce, not increase, debt, which will require better matching of revenue and expenditure, and will most likely result in a contraction of the overall fiscal envelope.

There are certainly options in respect of **reorganising the current structure of the equitable share**, most notably by making the conditional grant system less complex and more flexible. This would reduce administrative costs and allow local municipalities to use these funds on local priorities, such as infrastructure maintenance. It is unlikely, however, that these adjustments would address all the problems in the fiscal framework, although they could contribute to more effective expenditure allocations.

If we conclude that there is not much prospect of getting a bigger piece of cloth – in fact, we are most likely to end up with a smaller piece if we focus on restoring the social wage – then we are left with looking at the size of the coat.

What are the options for rationalising local government expenditure? If we reorganised the expenditure side of the equation, would it solve our problem? Many people think so. As part of their argument they point to **irregular expenditure of R32 billion and fruitless and wasteful expenditure totalling R2 billion** for the 2017/18 financial year. However, the irregular expenditure figure should be approached with some caution. Because it denotes expenditure that does not comply fully with supply chain management requirements, in many instances the non-compliance is fairly minor, and cannot be taken as a proxy for wasted money; it also does not indicate that goods and services were *not* obtained.

Although the AGSA does not give a detailed breakdown of these issues it indicated in the 2017/18 audit report that payment for goods and services that were not received totalled R11.5 billion of the material irregularities identified in the audit. If we assume that half of all irregular expenditure and all of the fruitless and wasteful expenditure represents an expenditure 'leakage' that could be prevented, we end up with a figure of less than R20 billion. Of course, we cannot afford any misspent money, but it is important to put that figure in context. It represents about 5 per cent of local government operating expenditure and less than 25 per cent of the amount of local government revenue that the AGSA believes will never be collected.

One area of 'leakages' from the system that is important (although it gets much less attention than irregular expenditure) is **distribution losses**, that is, water and electricity that the municipality pays for but never invoices for because it is lost from the system. Accurate data on aggregate water and electricity reticulation losses in local government are not available, but for the 2017/18 financial year water losses of R6.56 billion were disclosed (AGSA, 2020a). A 2012 study by the Water Research Council (McKenzie, Siqalaba and Wegelin, 2012), suggested a distribution loss of 37 per cent across the 132 municipalities covered by the study. In terms of electricity distribution losses, the national average appears to be around 30 per cent, based on data collated by COGTA, but the data should be approached with caution. Reticulation losses are caused by faulty infrastructure (most important in respect of water) and illegal connections (most important in respect of electricity). Local government certainly cannot afford to keep funding these losses, and there should be greater attention placed on how to reduce these. Better maintenance (see below) would address losses, as would more affordable tariffs and wider distribution of free basic services.

What about **cutting all the expenses incurred by municipalities that could be considered 'non-essential'**? It appears that operating expenditure could be rationalised when costs are either not directly related to the delivery of services or appear to be inflated. However, in the absence of a local government-wide cost calculation exercise, it is very difficult to speculate about what an 'effective' cost structure would look like. As just one example, allegations are often made that municipalities are overstaffed, but at the same time it is generally acknowledged that there is a shortage of specialist (and expensive) skills in areas such as engineering and infrastructure planning and management. (We do need to acknowledge, however, that having 257 municipalities probably contributes to poor economies of scale and the creation of a high cost base.)

Finally, on the cost side of the equation, we need to consider **costs that *should* be incurred in local government** (i.e., costs that increase the cost base and thus increase the size of the coat) **are currently not being incurred**. The most prominent of these is infrastructure maintenance, a cost item specifically intended to be financed almost entirely out of local government own-revenue. (There is a small infrastructure maintenance component included in the free basic services component of the equitable share, but conditional grants may not be utilised for this general purpose.) The South Africa Institution of Civil Engineering's 2017 Infrastructure Report Card gave an overall grade of D+ ('at risk of failure') to South Africa's infrastructure. Sanitation infrastructure outside of the metros scored an E – 'unfit for purpose' (Watermeyer and Philipps, 2020). A significant percentage of this poorly rated infrastructure is under the authority of local government.

All the officials we interviewed for our 2018 study were clear that their municipal infrastructure was in a precarious state, and desperately in need of proper maintenance, but that there simply was not enough money available in their own revenue account to afford this (in contrast to the view which suggests that low levels of maintenance are a 'planning' problem).

> *We have a huge infrastructure maintenance backlog, but there is no money to fix these things – there is simply no budget.*
>
> *It is a constant battle to find money for maintenance: this is supposed to come from own revenue, but that is just not possible.*
>
> *You can see that this town is falling apart, but where is the money to fix it?*
>
> *You are still expected to maintain your infrastructure even if no one is paying us for the services.*

There is evidence to suggest that current maintenance expenditure is much lower than it ought to be. A study undertaken more than ten years ago suggested that the annual difference between required maintenance in local government and budgeted maintenance amounts to some R6 billion per annum. The 2018 *State of City Finances* report indicated that cities were spending about 60 per cent of what they should be on maintenance. A 2013 study by the FFC found that the difference between what should be spent on maintenance by local government and what was actually being spent was approximately R10 billion per annum (using data from the 2011/2012 financial year). Applying a 6 per cent per annum escalation gives a rough estimate of the current value of that gap of around R14 billion per annum. This is additional expenditure that urgently needs to be incurred, and thus funded.

4.2. Where should we start?

We are in an unsustainable situation that is threatening the entire developmental agenda. Our specific assertion in this paper is that the central underlying cause of the current situation is the structure of the local government fiscal framework: its expenditure requirements simply cannot be covered by its revenue-raising arrangements, and the gap between the two would be even greater if free and subsidised basic services were delivered as required to address household poverty and inequality.

One official point of view is that operational efficiencies (and thus a more cost-effective and efficient operating structure) will be attained if we **increase the capacity of local government**. This supposition is the basis for countless municipal support programmes run by various government departments and agencies, and a host of other non-governmental organisations. It focuses on addressing organisational issues, with the implicit assumption that the overarching structure of local government (including the fiscal framework) is *not* the root cause of the problem. A conservative estimate would be that at least R50 billion has been spent on efforts of this kind over the past fifteen years, with little to show for it. At some point it needs to be acknowledged that the real problems are structural, and that continuing to spend money on capacity building within the limits of a dysfunctional structure is largely a pointless exercise.

It's time to do something different. We need to go back to the drawing board – to the basic design of local government. We are in a very different and much more privileged position than those who drafted the 1998 White Paper on Local Government. We have 20 years of empirical data in respect of the optimal pricing of services to ensure household affordability targets are met, much better (albeit not complete) information around the actual costs of delivering those services, and a clearer understanding of the limits of inter-governmental transfers to make good on any shortfall. We must use this information to **develop an empirical basis to clarify our options in respect of the operating and financial structure of local government**, so that we are no longer forced to have these debates on a partisan or partial information basis.

It is now time to consolidate the information we have and to accurately calculate the limits of the local government fiscal framework – and thus the operating structure of local government – under the current conditions.

An aggregate **zero budgeting exercise** for local government – taking into account the requirements of the social wage, the real cost of delivering quality services and the cost of addressing critical expenditure areas such as maintenance – is the starting point. It will serve to determine the real limits of local government's financial resources – the size of the cloth from which we must cut our coat.

The next task will be to critically consider the existing structure of local government against those financial limits: what demarcation and operating structure will maximise the likelihood of local government meetings its constitutional obligations within these limits?

If we do not focus on addressing these fundamental structural issues as a matter of urgency, we will never improve the state of local government to the extent where it is able fully to meet its developmental mandate.

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ANNEXURE A

SUMMARY OF METHOD UTILISED FOR INITIAL 2018 STUDY

The original research study was undertaken in order to:

- Provide an opinion of the assumptions on revenue raising outlined in the White Paper on Local Government; and
- Provide an opinion on the adequacy of the equitable share amount (proportion) and formula for distributing revenue within the local government system (i.e. vertical and horizontal divisions of revenue).

The research project was divided into three phases, as follows:

Phase 1: Desktop review, quantitative analysis and generation of preliminary findings report:

A desktop review was conducted of current research on the suitability of the current local government equitable share (LGES) formula, the actual cost of providing basic services, and the constraints faced by municipalities in raising their own revenue. Key sources in this respect included research undertaken by the FFC, National Treasury, University of Johannesburg, PARI and others. An analysis of quantitative data on own-revenue generation capacity and the long-term costs of service provision included information on how capacity and costs vary across different types of municipalities and what the data suggest about the factors that shape these variations.

Phase 2: Primary case study research in a purpose sample of five (5) of municipalities.

The municipalities identified for the case study research in Phase 2 were the following:

- uMhlathuze Local Municipality, King Cetshwayo District Municipality, KwaZulu-Natal
- Kannaland Municipality, Garden Route District Municipality, Western Cape
- Bushbuckridge Local Municipality, Ehlanzeni District, Mpumalanga
- Nala Local Municipalit6y, Lejweleputswa District, Free State
- Mogale City Local Municipality, West Rand District Municipality, Gauteng

These municipalities were selected on the basis that they were a good representative sample to provide insight into the following issues:

- The financial challenges faced by rural municipalities with high poverty levels
- The revenue-raising and administration challenges faced by municipalities that have concurrent governance with traditional authorities
- The impact of more flexible conditional grant structure
- The reality that relatively large municipalities with fairly good governance outcomes might still face considerable financial pressure
- The financial viability of smaller municipalities

Phase 3: Preparation of a consolidated report, and stakeholder engagement

This report comprises what is required for Phase 3 – the final report – and is based on the initial findings report (the output from Phase 1), together with the findings from the fieldwork undertaken in Phase 2, which were used to support or change those initial findings, where appropriate.

The report was finalised after a draft version of this report was presented to SALGA for input.

1.2. Method and Approach

Phase 1 of this research was based on a desktop analysis of a wide range of documents, which included policy documents, legislation, and existing research (including PARI's own extensive work around the institutional drivers of performance in local government undertaken over the past five years). In addition, interviews were undertaken with institutional representatives able to provide additional insights. A set of initial findings were collated from this analysis.

For **Phase 2**, each municipality was contacted independently to set up meetings with officials. SALGA assisted with this process. Unfortunately we were unable to obtain appointments with representatives at Nala municipality during the time allocated for this phase of the work. However, we were able to obtain considerable insights from our interviews at the other municipalities, and we do not believe that the unavailability of the Nala officials has undermined the integrity of our findings. Additional insights from the perspective of local government were obtained during the SALGA consultation phase in respect of the draft final report.

ANNEXURE B

DATA METHOD

In order to compile the data tables contained in this report, the following data sources were used:

- For the details of municipal debtors, we used the Section 71 (S71) in-year reports submitted to National Treasury. These data tables are compiled by municipalities and submitted to Treasury. They are not subjected to external audit, and for many municipalities the data are probably not completely accurate. However, the general quality of financial data across local government appears to have improved over the past few years. We used data starting from the 2016/17 financial year; before that date not only are there significant questions around the quality of data but many municipalities also submitted either incomplete data or failed to make S71 submissions at all. Despite these limitations, we have used the S71 reports for this data set because it is the only consolidated source of this data at this level of detail in respect of different categories of debtors.

- In respect of the revenue breakdown (into the various source categories) and operating expenditure, we utilised National Treasury's consolidated MBBR tables, most notably Table A4 – Budgeted Financial Performance. For the 2016/17 and 2017/18 financial years, we have used the audited data. This should guarantee a fairly high level of data integrity, although it should be noted that audited outcomes may be revised in subsequent years, and the data from municipalities with very poor audit outcomes (such as a disclaimer) is obviously suspect. In summary, the data for those two years is likely to have a relatively high degree of accuracy.

- For the revenue and expenditure data for the 2018/19 financial year, we used the pre-audit data submitted by municipalities and consolidated into Table A4 because the audited data was not yet available in this format (due to the later-than-usual completion of the audit because of the Covid-19 lockdown). This data thus has a lower level of integrity than the audited data, even though data quality submission across local government in aggregate has improved over the past five years.

- For the revenue and expenditure data for the 2019/2020 financial year (for the first nine months of that year, to 31 March 2020) we made use of the Section 71 in-year reports, the only consolidated data source offering the requisite level of detail. This data should be approached with some caution, and probably provides no more than a general idea of the actual situation. However, as a general rule, municipalities are more likely to overstate their revenue in preliminary data submissions than to understate it. That is, data errors are more likely to support than to undermine our findings of the inadequacy of municipal revenue.

- Municipalities do submit data to National Treasury in respect of cash flow, and data are captured in MBBR Table A7. However, we did not make use of these tables since an analysis of the individual municipal data indicated a considerable number of gaps – i.e., where no data had been submitted – which in our assessment casts serious doubts on the accuracy of the consolidated data tables.

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