



**Equitable Share Formula and fiscal capacity in
municipalities with particular reference to Msunduzi
Municipality**

by

Xolile Mpumela

Student Number: 201294791

A dissertation submitted in partial fulfilment of the requirements for the

Degree of

Master of Public Administration

at the

College of Law and Management Studies

School of Management, Information Technology and Governance

Supervisor: Dr M Subban

2015

DECLARATION

I Xolile Mpumela declare that

- (i) The research reported in this dissertation/thesis, except where otherwise indicated, is my original research.
- (ii) This dissertation/thesis has not been submitted for any degree or examination at any other university.
- (iii) This dissertation/thesis does not contain other persons' data, pictures, graphs or other information, unless specifically acknowledged as being sourced from other persons.
- (iv) This dissertation/thesis does not contain other persons' writing, unless specifically acknowledged as being sourced from other researchers. Where other written sources have been quoted, then:
 - a) their words have been re-written but the general information attributed to them has been referenced:
 - b) where their exact words have been used, their writing has been placed inside quotation marks, and referenced.
- (v) This dissertation/thesis does not contain text, graphics or tables copied and pasted from the Internet, unless specifically acknowledged, and the source being detailed in the dissertation/thesis and in the References sections.

Signature:

ACKNOWLEDGEMENTS

Firstly, I would like to give thanks to the Almighty for He is good and His love endures forever.

My sincere gratitude goes to Dr Subban for her academic mentoring and guidance throughout this process. It has been a long journey but, you made each and every step worthwhile. It has been such a pleasure to work under your supervision.

To Ms Angela Pearce who has contributed to this project in more ways than one. Thank you for being patient with me and for always been available to assist from the post graduate office.

I would also like to thank the senior management of Msunduzi Municipality, National Treasury and SALGA who agreed to participate in this study and for giving me access to their respective organisations. This study would not have been possible without your participation and support.

A special thanks goes to my loving mother and my brothers for being my greatest supporters. I am so blessed to have you in my life and I love every single one of you so dearly. I hope that this work is an inspiration to you to continue learning and growing in your respective fields.

To my dear friends who inspired me to pursue this degree and who have been in the winds from the beginning. I'm truly grateful that our paths crossed. May we continue to grow into strong influential women.

Lastly, I would like to thank my husband and friend (of fourteen years). Your love and support has "kept me steady in the winds" Thank you Donga for believing in me even when I did not believe in myself.

ABSTRACT

The apartheid regime left its imprint on South Africa's municipalities with systematic under-investment in municipal infrastructure in black areas. Deprivation of communities with limited access to basic services including water, sanitation, refuse collection and roads created skewed settlement patterns as one of 'enduring planned and deliberate' poverty. The Constitution of the Republic of South Africa, 1996 established 'wall-to-wall' local government with municipalities to address past inequalities. There was no equally corresponding increase in the tax base of communities within municipalities. As a result, they are faced with fiscal imbalances in raising adequate funds to meet mandated functions with municipalities heavily dependent on intergovernmental transfers from national government. Twenty one years into democracy, municipalities continue facing infrastructural disparities evidenced by significant increases in service delivery protests. A suitable redistributive approach is envisaged as current local government funding arrangements may not be addressing objectives of development and redistribution adequately. National Treasury recently completed a review of the 2008 LGES formula and introduced a new formula for the equitable distribution of funds to municipalities. The purpose of the study was to assess the appropriateness of the new LGES formula as a resource allocation and mechanism for equitable resource sharing in government, deemed a focal point in addressing municipal fiscal challenges, using Msunduzi Municipality as reference. Underpinned by the pragmatic paradigm or philosophical worldview, the study used mixed methods research design which included review of documented data, as well as questionnaires for empirical data. The key research question was if the current Local Government Equitable Share formula fiscally capacitates municipalities such that they are able to provide basic services to communities? The study revealed that there is insufficient data available at the local government level to support the design of an appropriate LGES formula. The formula is unable to accurately quantify fiscal structural gaps in municipalities, and therefore fails to respond to basic service needs of municipalities. Furthermore, the LGES formula cannot be effective if the restraints on municipal own revenue sources are unresolved. National government must identify constraints to revenue generation and collection in municipalities to provide appropriate and sustainable financial support whilst promoting economic development, good governance and social progress for all financially 'ailing' municipalities.

List of Acronyms

COGTA	Cooperative Governance and Traditional Affairs
FFC	Financial Fiscal Commission
GRP	Gross Regional Product
LGBER	Local Government Budget and Expenditure Review
LGES	Local Government Equitable Share
MFMA	Municipal Finance Management Act
MGD	Millennium Developmental Goals
NDP	National Development Plan
NPM	New Public Management
OECD	Organisation for Economic Cooperation and Development
RTS	Representative Tax System
SALGA	South African Local Government Association
StatsSA	Statistics South Africa

Table of Contents

	TITLE	PAGE
	Title Page	
	Declaration	i
	Acknowledgements	ii
	Abstract	iii
	List of Acronyms	iv
	List of Figures	viii
	List of Tables	x
	CHAPTER ONE: INTRODUCTION AND OVERVIEW OF THE STUDY	
1.1	Introduction	1
1.2	Background and Outline of Research Problem	2
1.3	Research Problem	3
1.4	Study Objectives	5
1.5	Research Questions	5
1.6	Philosophical Worldview and Research Design Methods	6
1.7	Outline of the Chapters	6
1.8	Conclusion	7
	CHAPTER TWO: MUNICIPAL FISCAL GOVERNANCE VIS-A-VIS PUBLIC ADMINISTRATION	
2.1	Introduction	8
2.2	Post New Public Management Reforms and its Impact on Municipal Finance	9
2.3	Relationship between Public Administration and Developmental Local Government	13
2.4	Interface of Municipal Finance and Public Administration	16
2.5	Conceptual Framework for the Horizontal Allocation of Intergovernmental Transfers	20
2.5.1	Normative Public Sector Theory	21
2.5.2	Public Choice Theory	23

2.6	Formula-Based System of Transfers	25
2.6.1	Principles of a Good System of Transfers	26
2.7	Fiscal Capacity of Municipalities in South Africa	27
2.7.1	Definition of Fiscal Capacity	28
2.7.2	Exploring the Fiscal Capacity of Local Government	29
2.7.3	Fiscal Capacity and Fiscal Effort	35
2.8	Conclusion	36

CHAPTER THREE: EQUITABLE RESOURCE ALLOCATION IN LOCAL GOVERNMENT IN SOUTH AFRICA

3.1	Introduction	37
3.2	South African Federal System of Governance	38
3.3	Municipal Finance System in South Africa	39
3.3.1	Overview of Statutory Measures Underpinning Municipal Financing	41
3.4	Local Government Expenditure Assignment	43
3.5	Local Government Revenue Assignment (Fiscal Framework)	45
3.6	Vertical and Horizontal Fiscal Imbalance	49
3.7	An overview of the Intergovernmental Transfer System in South Africa	50
3.8	Evolution of the Local Government Equitable Share Formula	55
3.8.1	Local Government Equitable Share formula (1998-2004)	55
3.8.1.1	Challenges with the Local Government Equitable Share formula (1998-2004)	56
3.8.2	Local Government Equitable Share formula (2005-2012)	56
3.8.2.1	Challenges with the Local Government Equitable Share formula (2005-2012)	58
3.8.3	Local Government Equitable Share formula 2013	60
3.9	Conclusion	63

CHAPTER FOUR: RESEARCH DESIGN AND METHODS

4.1	Introduction	65
4.2	Significance of the Study	65
4.3	Philosophical Worldview	66

4.4	Research Design	67
4.5	Sampling	68
4.6	Data Collection Tools	70
4.6.1	Documentation	70
4.6.2	Questionnaires	70
4.7	Ethical Considerations	72
4.8	Data Analysis	73
4.9	Limitations of the Study	73
4.10	Conclusion	74

CHAPTER FIVE: FINDINGS AND ANALYSIS OF DATA

5.1	Introduction	75
5.2	Sample	76
5.3	The Research Instrument	76
5.4	Reliability Statistics	76
5.5	Section A: Biographical Data	78
5.6	Section B: Practical Context	80
5.7	Section C: Principles and Structures of the Equitable Share Formula	82
5.8	Section D: The Equitable Share Formula and Service Delivery	88
5.9	Conclusion	92

CHAPTER SIX: CONCLUSION AND RECOMMENDATIONS

6.1	Conclusion	93
6.2	Recommendations	93

7.	REFERENCES	98
----	------------	----

8.	ANNEXURES	
	Ethical Clearance	109
	Gatekeepers Letters	110
	Language Practitioner's Letter	113
	Informed Consent	114
	Questionnaires	115

Table of Figures:

Figure 2.1	Diagrammatic Representation of Literature Review	9
Figure 2.2	An illustration of the link between Public Administration and Public Finance	16
Figure 2.3	Municipal Finance and Service Delivery Model	18
Figure 2.4	Determinants of the horizontal allocation of intergovernmental transfers	21
Figure 2.5	Features of a good transfer system	26
Figure 2.6	Aspects to the Fiscal Capacity of Municipalities	30
Figure 3.1	Composition of the South African Local Government Fiscal Framework	45
Figure 3.2	Sources of Local Government funding per municipal category	48
Figure 3.3	Breakdown of the basic services component	62
Figure 4.1	Features of the Pragmatic Worldview	67
Figure 5.1	Number of years that respondents have been in the organisation	78
Figure 5.2	Designation of the respondents	79
Figure 5.3	Analysis of the respondents' understanding of the process of division of revenue	80
Figure 5.4	Rating of the effectiveness and efficiency in spending LGES allocations in Municipalities	81
Figure 5.5	Respondents view of the LGES formula providing for the total cost of basic services	81
Figure 5.6	Analysis of the objectiveness and fairness of the new LGES formula	82
Figure 5.7	Analysis of the transparency and simplicity of the new LGES formula	83
Figure 5.8	Respondents view on the new LGES formula being immune to political influence	84
Figure 5.9	Respondents view on the LGES formula being informed by municipal fiscal conditions	85
Figure 5.10	Respondents view on the LGES formula accurately capturing the cost of providing basic services	85

Figure 5.11	Respondents view on the LGES creating fiscal dependency in municipalities	89
Figure 5.12	Respondents view on the LGES formula applying different costing for basic services	90
Figure 5.13	Respondents view on the appropriateness of LGES formula for fiscally capacitating municipalities	91

List of Tables:

Table 3.1	Priority Functions for Local Government	44
Table 3.2	International Practices in Intergovernmental Transfers	50
Table 3.3	Division of Nationally Raised Revenue (2010/11-2016/17)	53
Table 3.4	Average LGES Allocation per Component for each type of Municipality	58
Table 3.5	Design of the South African Local Government Equitable Share Formula	61
Table 4.1	Research Paradigms	66
Table 4.2	Sampling per Institution and Employment Category	69
Table 5.1	Response Rate	76
Table 5.2	Reliability Statistics	77
Table 5.3	Results of Kaiser-Meyer-Olkin and Bartlett's Test	78
Table 5.4	Difference between LGES allocation and actual cost of basic services provided	86
Table 5.5	Summary of comments by respondents on components of the LGES formula that require further enhancement	87

CHAPTER ONE

INTRODUCTION AND OVERVIEW OF THE STUDY

1.1 Introduction

The strength of any government lies in its ability to meet the needs of its constituencies in a responsive and sustainable manner. Being at the forefront of service delivery, municipalities are tasked with the responsibility of enabling development at local government level (Haque) (in Pooë and Mafini, 2012:90). Thus, the fiscal capacity of local government is critical in ensuring that local government has adequate revenue sources to deliver public services in a viable and competent way and therefore enhancing the lives of its communities.

Hollands and Mageza (2010:6), state that the legacy of apartheid is still evident in South Africa's municipal institutions. Apartheid laws ensured that there was under-investment in black municipal areas thus denying millions of black people access to basic services. Through the homeland system, the apartheid government influenced the living arrangements in a severe and discriminatory way resulting in 'persistent and deliberate' poverty which is still evident in South African society today.

In 1994, the country witnessed a transition in government. A new democratic administration was elected which substituted the apartheid administration. The enactment of Constitution of the Republic of South Africa, 1996 facilitated the establishment of a border to border system of government by prescribing that local authorities be formed for the entire area of the country to address the inequalities of past policies and to enhance the welfare of all citizens. The creation of municipalities for the whole geographic area of the country increased the population which municipalities must serve. This was done without a matching increase in the income streams of communities which municipalities must service. As a result, municipalities have been faced with fiscal imbalances due to challenges in raising adequate funds to meet their assigned functions leaving a significant number of these municipalities heavily dependent on intergovernmental transfers from national government to meet their operational costs (CoGTA, 2009:59).

Twenty one years into democracy, municipalities still face vast infrastructural disproportions and developmental challenges. The consequences of past apartheid laws has left a notable segment of the residents without access to priority services such as electricity, sanitation and water. The rapid rate of urbanisation has also placed pressure on municipal services.

The challenges facing local government require the matching fiscal capacity in municipalities to enable them to effectively address the basic requirements of their constituencies and to enhance the living conditions of all South Africans.

This study was therefore, undertaken primarily to assess the appropriateness of the funding model for local government in ensuring that municipalities are fiscally capacitated to perform their obligation of providing basic public services to their people. It was also undertaken to contribute to the reservoir of knowledge relating to the use of formula-based resource allocation as a mechanism for equitable resource sharing in government, deemed a focal point in addressing fiscal capacity challenges in municipalities. This study is also seen as a significant addition to the literature on municipal financing of the sub-field of Local Government Management and Development within the study and paradigm of Public Administration and Governance.

1.2 Background and Outline of Research Problem

The study was conducted in Msunduzi Municipality, which is one of seven local authorities within the UMgungundlovu District Municipality. The Municipality is located in Pietermaritzburg, the second largest city in the Province of KwaZulu-Natal, and the administrative and legislative capital of the Province. It covers an area of 634km² and has a total population of 618 536 and 163 993 households (Statistics South Africa (StatsSA), Community Survey: 2011:96).

The Msunduzi Municipality area is a major contributor to the district channels of investment within the provincial spatial framework for economic development and growth. The Municipality trades in a number of goods and services and has a particularly strong industrial sector that is thriving in cross border trade of aluminum products, cut flowers, automotive components and furniture (uMgungundlovu Annual Report, 2013:15). Other economic activities undertaken by the Municipality include animal and crop farming (cane, cattle, fruit, dairy and timber) as well as tourism (botanic gardens, historical buildings and architecture and dams).

Notwithstanding the above-mentioned accolades, the Municipality still faces high rates poverty, unemployment, and varying levels of development and municipal infrastructure backlogs resulting from spatial planning in the urban, semi-urban and non-urban regions. The unemployment rate in the Municipality is 33% (StatsSA, Community Survey, 2011:159), which is higher than the country rate of 25%. According to the StatsSA Community Survey (2011:170 and 172), 73.7 % of households in the Municipality are formal dwellings with

47.9% of the households having access to piped water inside the dwelling, 91.9% of these households use electricity for lighting and 51.6 % have access to a flush toilet.

In terms of finances, in 2009/10, the Municipality reported a budget deficit of more than R200 million and was in a brink of bankruptcy. This, according to the Municipality, was mainly attributed to a culture of non-payment in the communities (50% collection rate), non-compliance with various governance regulations including the Municipal Finance Management Act and the absence of a realistic budget to cover expenditure assignments (Msunduzi Municipality Annual Report, 2010:2). As a result, provincial government placed the Municipality under administration in accordance with Section 139 of the Constitution, by the KwaZulu-Natal Provincial Government.

Following the appointment of an administrator, a financial recovery, revenue improvement and cost containment strategy was developed and is currently implemented by the Municipality. This strategy was developed mainly to enhance the organisation of finances and governance systems of the authority (Msunduzi Municipality Annual Report, 2010:4).

Despite the implementation of the improvement strategy in 2009/10, the Municipality has continued to face challenges. In 2012/13, Msunduzi Municipality received a qualified audit opinion. The basis for the opinion was primarily the Municipality's inability to provide sufficient and appropriate audit evidence for revenue generated through service charges. In the same financial year, the Municipality reported material losses relating to water of R92.4 million (15 701 747kl) and electricity of R122.3 million (202 469 552 kWh) as well as consumer debts amounting to R801.8 million wherein recoverability was doubtful (Auditor-General Report, 2013:1). In addition, the audit found that the Municipality significantly underspent its grant funding and its capital budget by R170.5 million and R33.6 million, respectively (Auditor-General Report, 2013:1). As a result, the authority did not achieve its obligations of availing basic public services and priority infrastructure to the residents of the authority.

The sections below outline the research problem underpinning the study, the objectives of the research, research questions and the outline of the chapters that follow.

1.3 Research Problem

The history of inequity in South Africa has resulted in a significant number of South Africans living in poor conditions with limited financial and social growth despite more than a decade of reparation. The redress has been pursued through an intergovernmental fiscal support, which is founded on redistribution using a system of grants. Although there are a number of

cases that indicate remarkable efforts and exceptional successes of specific authorities, the municipal system is still perceived as failing to provide basic services in a responsible and responsive manner. Over the last number of years, national government has made available considerable funding to local government for capacity building. However, there is very slight indication that this funding and government expenditure has produced the envisioned outcomes, such as increased capacity and performance of municipalities (Republic of South Africa National Treasury, 2014:2). This statement is evidenced by the substantial rise service delivery protests in the last decade. Cronje (2014:1) states that records from the Department of Police show that the country is averaging 4 to 5 violent anti-government protests a day. “The growing levels of protests are a cautionary signal that the challenges of indigent people in South Africa should to be addressed” (Grant, 2014:1)

Moreover, there has been notable failure by government to develop a suitable redistributive approach, that is sustainable and that provides for the increasing demand for public services, without compromising the strength of the economy. This failure by government has created an impression that the model of the redistributive formula for local government is inappropriate and has resulted in the underfunding for some municipalities. This is viewed as compromising the fiscal capability of municipalities to perform their primary mandate which is to provide basic services to its communities. The Cooperative Governance and Traditional Affairs department (COGTA) report on the State of Local Government in South Africa, (2009: 9) admits that “the national government may have created expectations that local government cannot fulfil, or placed a burden on municipalities that perhaps only the strongest amongst them can carry”. The 2008 Division of Revenue Bill cited (in Mahabir, 2010: 157) states “the redistributive capacity of the model proved to be limited, due to the fact that the model is not designed for this purpose”.

On 22 April 2010, during a Budget Vote speech, the former CoGTA Minister, Mr S Shiceka, said “One of the key observations is that the intergovernmental fiscal relations is based on outdated approaches wherein the baseline used for financing of municipalities is not aligned to their income, revenue base and the tasks at hand” (CoGTA Budget Vote speech, 2010: 1). The 2011 Local Government Budget and Expenditure Review (LGBER) stated that “there is an increasing view that the municipal funding provisions might not be effectively responding the objects of growth and redistribution which demands a new method to be applied for the administration and funding of local authorities’ (Republic of South Africa National Treasury, 2011:20). It is for this reason that this study is undertaken, to assess the appropriateness of the funding model for local government in ensuring that municipalities

are fiscally capacitated to satisfy their mandate of delivering priority services to their communities and thus enhancing the quality of lives of South Africans.

1.4 Study Objectives

The purpose of this study was to assess the appropriateness of the current Local Government Equitable Share (LGES) formula in fiscally capacitating local government to provide basic services to poor communities. Accordingly, the study focused on the following objectives:

- Investigate the alignment of the LGES formula to the principles outlined in the Constitution and the White Paper on Local Government;
- Determine if the current range of goods funded through the LGES formula reflects the constitutionally mandated basic services;
- Investigate the extent to which the formula accounts for the fiscal capacity of the Municipality;
- Examine the acceptability of the new formula by the Municipality; and
- Recommend areas in the formula that can be further improved.

1.5 Research Questions

In focusing on the key questions, the research sets out to address an important aspect: does the current LGES formula fiscally capacitate municipalities such that they are able to provide basic services to communities? Therefore, the following questions informed the study:

- Is the structure of the LGES formula aligned to the principles outlined in the Constitution and the White Paper on Local Government?
- Is the current range of goods funded through the LGES formula reflecting the constitutionally mandated basic services?
- To what extent does the LGES formula fiscally capacitate the Municipality to provide basic services?
- How is the recent structural change of the LGES formula going to impact on the funding of the Municipality?
- What are the Municipalities' perceptions and attitudes towards the new LGES formula in addressing the challenge of service delivery?

1.6 Philosophical Worldview and Research Design Methods

A philosophical worldview refers to a general orientation of the researcher about the world. It is a set of norms on the techniques that the researcher employs to gain knowledge and what knowledge they gain through the enquiry (Creswell, 2009:6). The author further advances that, there are four distinct ideologies regarding claims to knowledge which include; constructivism, post positivism, pragmatism as well as advocacy or participatory.

The study's claim to knowledge was through the Pragmatic Approach. In this approach the researcher believes that the ways of learning are a result of actions, circumstances and consequences as opposed to preexisting situations (Creswell, 2009:10). Rather than concentrating on methods, the study places emphasis on the research problem and uses all methods at its disposal to fully comprehend the research problem. This approach is a theoretical basis for the use of mixed methods studies in social science research and conveys the significance of directing focus on the research problem and then applying multiple methods to gain knowledge about the problem (Creswell, 2009:10).

Accordingly, the study used both qualitative and quantitative approaches and multiple sources of data were collected. The data collecting techniques included secondary documented data and administering questionnaires. The questionnaires were targeted at senior, middle and lower level managers working at the Msunduzi Municipality (Finance unit), National Treasury (Municipal Finance and Intergovernmental Relations units) and the National South African Local Government Association (Intergovernmental Fiscal Relations unit) for triangulation purposes. A sample of 113 senior, middle and lower level managers was drawn from a population of 124 from the three institutions mentioned above, each working with a different aspect of the LGES. The details of this are provided in Chapter Four which outlines the research methodology and data analysis techniques employed in the study.

1.7 Outline of the Chapters

The dissertation is structured as follows:

Chapter One focuses on the introduction and overview and provides the context for which the study is based and outlines the research problem. It also presents the research objectives and the research questions that the study intends to provide answers to.

Chapter Two links municipal fiscal governance *vis-à-vis* the paradigm of Public Administration. It presents the philosophical foundation for the research and also presents

a summary of literature collected from various documented data sources. It presents an evaluation of literature pertaining to the evolution of the study of Public Management and the emergence of public governance which represents a new paradigm shift in public administration. The chapter also presents an elaborate discussion on the relationship between Public Administration and municipal finance thus locating this study within literature on municipal financing as a sub-field of Local Government Management and Development within the broader study of Public Administration and Governance.

Chapter Three discusses equitable resource allocation in the South African local government. The chapter discusses the main features on the new federal system of governance in South Africa. It also presents an outline of the South African municipal finance system and the statutory measures underpinning municipal financing and local government's expenditure and revenue assignments. The chapter will also discuss the evolution of the Local Government Equitable Share from its inception in 1998 to date.

Chapter Four highlights the methodology used in this research. It presents the details of the selection of philosophical worldview, research design, research strategy and data analysis techniques. The selection of the sample, data collection tools and limitation of the study will be discussed in this section.

Chapter Five reflects the data presentation and analysis. Data that have been collected through the questionnaire will be presented in this chapter using tables and graphs. This chapter will also discuss the statistical significance amongst key variables that will be used in the empirical stage of the study.

Chapter Six will provide the summary findings, conclusions and recommendations emerging from the research.

1.8 Conclusion

This chapter presented the background and context of the study. It detailed the research problem and discussed the objectives that the study aims to achieve and the research questions the study is intended to provide answers to. The chapter was concluded with the outline of the structure of the dissertation. The next chapter provides the theoretical context on which the study is premised.

CHAPTER TWO

MUNICIPAL FISCAL GOVERNANCE *VIS-À-VIS* PUBLIC ADMINISTRATION

2.1 Introduction

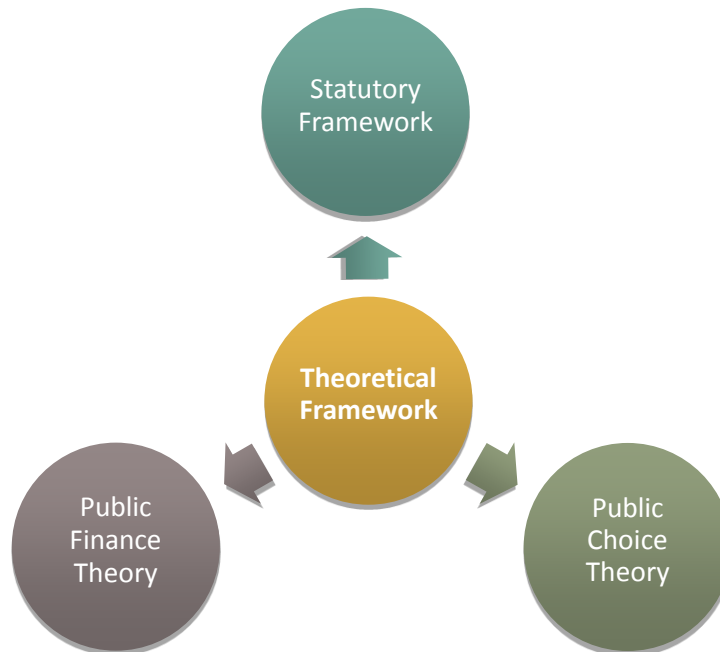
It is accepted that academic theory allows one to understand, explain and predict actions within a specific frame of reference. Mafunisa and Dzengwa (2007:766), assert that knowledge is generated through the discovery of facts, drafting, analysing and interpreting legislation and policies. This chapter presents the formulation of the theoretical framework for understanding the equitable sharing of resources between national government and local government authorities by examining theories and literature from prior studies related to the research topic. The review of literature assisted in gaining a deeper understanding of the incidence of the LGES allocation in the South African fiscal framework.

The chapter begins by discussing the evolution of public administration from the traditional public administration models to the recent emergence of a new era of public administration termed “public governance” which embodies a change in paradigm in the study and practice of Public Administration. The discussion moves to public finance as a sub-field of public administration, thus locating the study within the sub-field of Local Government Management and Development in the field of Public Administration and Governance. Following this discussion, the chapter provides an outline of the use of public finance by government as an instrument for achieving its developmental objectives. Lastly, the chapter highlights the use of Public Economics and Public Choice models that provide conflicting views on the determinants of intergovernmental transfers. The study will use these models deductively with the objective of testing and verifying the principles which they are grounded on.

The focus on local government as a driver of the South African developmental agenda has necessitated a paradigm shift in modernising systems of municipal financial management, processes and policies to reinforce their capacity to operate effectively. Municipal finance is a key component of developmental local government as it used as a tool to addresses disparities, unlocks local government economic activity and facilitates a more sustainable service delivery agenda. This chapter will present a detailed discussion on the role of municipal financing in driving the developmental agenda and creating sustainable communities through effective financial governance.

Figure 2.1 below illustrates the different aspects of literature that the study draws from to develop a theoretical framework for the research. The discussions that follow are an expansion of the illustration below.

Figure 2.1: Diagrammatic Representation of Literature Review



Source: Author's perspective

2.2 Post New Public Management Reforms and its Impact on Municipal Finance

Public administration continuously evolves, taking on contemporary approaches and adjusting practices in line with the technological and social progress, thereby influencing the way government delivers public services (Basheka, 2012:61). The traditional models of public administration dominated for most of the Twentieth Century. Embedded on the work of Max Weber, Frederick Taylor's one-best-way scientific management principle and Wilson Woodrow's theory on politics and administration dichotomy, traditional models are the longest standing theories of Public Administration (Hughes, 2003:1). However, the inefficiencies of the traditional models resulted in public administration reviews with the purpose of correcting what was viewed as the failures of traditional models.

A noteworthy review is that of the late eighties led by the Organisation for Economic Co-operation and Development (OECD) countries as well as selected developing countries. The OECD embarked on a process of reviewing the administration of their public sectors which came as a response to the economic and social realities confronted by governments

which included: bulky and expensive public sectors; the call for quality services by the public; the demand to utilise information technology to improve administrative efficiencies; the fall of centralised economic systems; and the demand for personal development and job gratification by employees in the public sector (Hope, 2001:121). At the time, the private sector was thought to be more effective and efficient. Thus, governments reviewed their public administration and adopted a number of private sector principles with the objective of improving what was posited to be an inefficient public administration (Hughes, 2009:3). The reviews led to the introduction of the of the New Public Administration (NPM) dimension which represented a change from traditional administration to a new public management paradigm founded on economic and private management theoretical principles. The features of NPM comprises a lean administration, decentralisation, de-bureaucratisation, private sector alignment, privatisation, outsourcing of services and performance management (Engida and Bardill, 2012:3). According to Cloete (in Nel, 2015:75), the introduction of these NPM features in the South African government administration occurred in the year 1991. Hope (2001:121) states that the NPM was intended to create an environment based on productivity and a decentralised public sector and is identified by:

- Focusing on output and the competence in delivering output;
- Substitution of centralised organisations by decentralised structures where decisions regarding service delivery and allocation of resources are taken at the site of delivery, and which create an environment for feedback from end users and other relevant groups;
- Exploring opportunities to guide public directives and delivery to achieve cost-effective policy results;
- Focusing on the competence in the delivery of public services, developing performance targets and encouraging competitiveness in the public sector; and
- Reinforcing tactical abilities at the core of government to lead the advancement of the government and to support it to be dynamic so that it is able to effectively respond to exogenous factors in a cost effective manner.

(Hope, 2001:121)

These features signify the divergence from the traditional models of administration, which embodied a hierarchical structure of organisation and centralisation of public administration. Despite the adoption and implementation of NPM, public administration continued to be characterised by poor management of public resources, lack of acceptable accountability mechanisms, opaqueness and lack of access. These failures in administration structures

led to a new focus by governments to what is termed Public Governance. Fourie (2012:80) notes that the prevalent awareness that a lack of good governance, transparency and accountability in government processes hindered progress towards sustainable development led to the change in approach in public administration. Although, governance is a new “buzz” word in public administration, scholars agree that it is an old concept in public administration that has only received attention recently. Nzimakwe (2005:18) argues that ‘the concept of governance is not new. It is as old as human civilisation. This is supported by Nkuna (2013: 139) who posits that the concept of governance is not new to academic and political discourses. Lee (2003:2) also shares the same view and asserts that governance has existed for a long time but, recently it has been rejuvenated and has become an appreciated concept in the public administration arena.

The concept of governance comes as a result of communities being dissatisfied with government’s inability to address social problems and thus putting government under pressure to develop new concepts to improve efficiencies in the delivery of public services. It is against this observation that Nzimakwe (2005:13) asserts that “the theory of governance is government’s response to market and state failures, governance is therefore part of the fight back”. This is confirmed by Lee (2003:5), who notes that public governance has been implemented in many developing countries primarily as an instrument for resolving common public problems.

It is interesting to note that Public Administration literature reveals that scholars have not been able to agree on one single definition for the concept of governance, mainly due to its multidimensional nature. As a result, there are a number of definitions provided in literature each focusing on a specific aspect of governance. The World Bank for example (in Ladi, 2008:11), highlights the following features of governance: a) the organisation of the political administration b) the manner in which social and financial resources are administered and c) the ability of the administration to conceptualise, develop and implement public policies. Matheson (in Siswana, 2007:180) notes that the theory of governance takes into account the manner in which choices are made, the accountability of managers and politicians in relation to the choices made, the balance of rule and institutions, and the environment in which development and implementation of public policy occurs. Holtzhausen and Naidoo (2011:741) define governance as the legal and organisational provisions used by local authorities to apply control and the associated accountability processes, clarity in government processes, enforcement of laws and public involvement. Pierre, 2000 (in Lee,

2003:15) argues that the concept of governance is an endeavor to understand government and its administration using a new outlook of governance that includes various systems of public organisation, including steering, that are likely to substitute intransigent policies and procedures. Hyden (in Nkuna, 2013:141) asserts that, using the governance approach requires an innovative stance of politics where leaders have the ability to rise above the current structures to change the rules of the game and to motivate others to participate in efforts to move society forward in new and productive ways.

Based on these definitions it can be deduced that the concept of governance is multi-faceted and can be used in any type of action as means to a desired outcome. Holtzhausen and Naidoo (2011:738) note that governance is not just about finding the direction to a desired outcome but, it is also provides means of getting to the desired outcome. It further provides details on the required participants as well as their roles in the journey towards achieving the agreed outcome. Therefore, it can be summarised as a process in which government organises itself and its processes in order to effectively implement its programmes thus improving delivery of public services and the welfare of the residents. Vyas-Doorgapersad and Ababio (2010:413) provide the following ten principles of good governance specifically as it relates to local government:

- *Involvement*: to promote engagement and participation of residents in government processes. Encourage them to use their right to directly and indirectly communicate their views in all decision making processes that concern public interest;
- *Rule of Law*: to ensure that laws is applied in a manner that is just and unbiased for all, without exemption, while promoting the basic privileges of humans and respecting societal standards;
- *Transparency*: to develop shared trust amongst the public and government through the sharing of facts and accessibility of accurate and complete information (including transparency in the resource allocation mechanisms);
- *Impartiality*: to create an environment where citizens have equal opportunities to advance their wellbeing;
- *Receptiveness*: to improve the compassion of government administrators to the ambitions of the communities that that serve (through a responsive system of resource allocation);
- *Vision*: to develop a transparent vision and tactic, involving the citizenry in all the development processes so that they are accountable for the advancement of their communities;

- *Responsibility*: to improve the answerability of government in terms of pronouncements in all areas that pertain to the advancement of community priorities (there must be a dichotomy between the political and administrative powers within a municipality);
- *Oversight*: to improve the efforts of monitoring the functioning of the public sector and the application of policies by using resources from the private and public sectors;
- *Effectiveness and Efficiency*: to ensure service delivery by using available resources in an optimal and responsible manner; and
- *Proficiency*: to improve the knowledge and morals of government administrators so that public services are affordable and are delivered in a competent and economic manner.

The United Nations Development Programme, Vyas-Doorgapersad, Subban and Pillay (in Vyas-Doorgapersad and Ababio, 2010:413) state that the above-mentioned elements are necessary for achieving good municipal governance.

These post-modernist era reforms have also transformed the manner in which public funds are managed, particularly in local government. The introduction of the MFMA in 2003 is regarded as a cornerstone of government's reform agenda (Republic of South Africa National Treasury, 2011:17). It represents an aspect of the broader local government reforms as prescribed in the White Paper for Local Government and has created a basis for establishing a framework for sound and sustainable financial governance in municipalities that promotes transparency and accountability in the governance of municipal financial affairs.

2.3 Relationship between Public Administration and Developmental Local Government

The preceding section discussed the evolution of the study and practice of Public Administration and the adoption of governance principles by governments in developing countries. This was done to increase the participation of communities in governance, improve the manner in which government delivers public services to its communities and ultimately improving the living conditions of communities. These principles are also evident in the concept of a developmental local government discussed in the section to follow.

A reactive, competent, answerable and transparent public governance is not just important for the effective running of government but it is also a system in which governments can achieve the Millennium Development Goals (MGDs) through the implementation of

developmental programmes. The South African development programme is embedded on the objectives of the MDGs. The South African government has been using the MDGs as a foundation for the many of its policies and programmes that have been implemented to address the obstacles of high rates of unemployment, poverty and inequality in the country (StatsSA, 2013:18). In the current context, the MDGs are apparent in the Republic's development programme captured in the National Development Plan (NDP) of South Africa. The NDP (2011:2) recognises South Africa as a developmental state and articulates that a developmental state is one that confronts the root causes of poverty and inequality and progressively eradicates them. "It encompasses redress and development, increasing yield and revenue and creating an all-encompassing and equitable community " (Minister of Finance, 2014). Republic of South Africa National Treasury (in Peters, 2013:155) asserts that the provision of basic services to indigent households and investing in economic infrastructure is a significant contributor to poverty relief and increases economic growth and other services that are essential for economic development.

Callanan and Keogan (in Hollands and Mageza, 2010:10) argue that the strength of local government as a democratic tool lies in its nearness to the constituency and its ease of access and the opportunities it presents to its communities to participate in the democratic process. Oates (1999:120) affirms this view and states that, local authorities, being nearer to communities, is going to be more sensitive to the choices of the people they service and are well positioned to identify enhanced means of delivering public services. Robinson (in Boschman, 2009:16) also argues that the key justification for administrative federalism is that local authorities are well positioned to understand the needs and inclinations of communities and are therefore better equipped to effectively respond to these needs by implementing appropriate policies. The White Paper on Local Government further confirms this view and notes that municipalities are strategically located to examine and appreciate the balance of forces in a community, and make sure that community groups that are likely to be sidelined and excluded are included in all governance processes and that they actively participate in the advancement of the communities in which they reside.

Accordingly, the Constitution elevates local government to a separate level of government with a mandate to provide for the basic requirements of the people, and to stimulate growth and wellbeing of communities. The Constitution protects the human rights of all citizens and obligates government to make rational choices, within available resources, to make sure that citizens have access to sufficient priority services. Section 153 of the Constitution

prescribes that a municipality must have a good control over its finances and governance and give priority to the basic requirements of citizens, promote growth in local economies and social progress and participate in development programmes implemented by other spheres of government.

Similarly, the White Paper on Local Government places an emphasis on local government's developmental role. It prescribes this sphere of government to be answerable, sensitive and devoted to work with the community to explore approaches of achieving their developmental objectives as well as enhance their livelihoods. The White Paper recognises four key features of a local government that is focused on development, which are key aspects in addressing local government financial issues, and these are:

- *Capitalising on economic growth and social development* – The authority and role of local authorities must be implemented in a manner that has the greatest effect on the wellbeing of communities, specifically with regard to responding to the basic priorities of indigents as well as the reviving the local economy.
- *Coordinating and Integrating* – Municipalities should provide a clear direction towards achieving local prosperity. Lack of coordination among service providers has a potential of undermining the development effort. Accordingly, local government should create methods to maximize yields from investments and resources from all sectors in order to achieve its growth objectives.
- *Democratising development*- Councils perform a vital role in encouraging democracy in municipalities and advancing the priorities of its communities. Councilors must heighten citizen participation in the strategy and implementation of municipal programmes.
- *Learning and Leading*- Municipalities must be forward looking and provide strategic direction to its constituencies. They should be knowledgeable and credible in the manner in which they function.

Republic of South Africa White Paper on Local Government (1998:25).

In addition, the White Paper on Local Government outlines the key outcomes for local government that is developmental in focus, and is highlighted as follows:

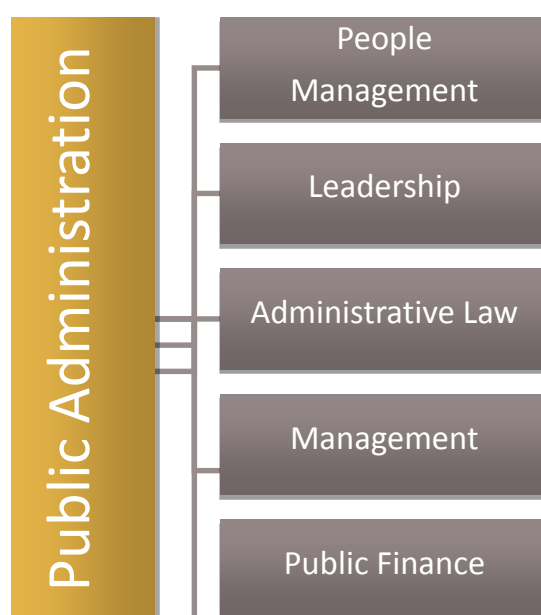
- Delivery of services and municipal infrastructure;
- Establishment of integrated and working cities, townships and rural regions;
- Development of municipal economies; and
- Emancipation of communities and redistribution.

In order to perform its developmental role effectively and to achieve the key development outcomes as defined in the White Paper on Local Government, local authorities must be adequately funded. In this regard, municipal finance is central to the South African developmental agenda. The developmental needs of South African communities are recognised in the decision process of dividing revenue which explains national government's responsibility to continuously increase the municipal share of the nationally raised revenue and b) in the decisions relating to the horizontal allocation among municipalities through the use of formula to allot the LGES (Republic of South Africa Division of Revenue Bill, 2013:61). Funding for development programmes is channeled through the LGES formula for local authorities and in conditional allocations specifically, the infrastructure budgets and grants which are aimed at stimulating growth and development in municipalities in line with the provisions of the White Paper on Local Government. The section below provides a detailed discussion on municipal financing in the context of public administration.

2.4 Interface of Municipal Finance and Public Administration

As mentioned in the previous section, the study of Public Administration is multi-dimensional and multidisciplinary in its approach. It entails many diverse components which include: human resource management, management, leadership, administrative law and finance which are building blocks of Public Administration, as highlighted by Siswana, (2007:97). Figure 2.2 below illustrates the inter-relationship between Public Administration and Public Finance.

Figure 2.2: An illustration of the link between Public Administration and Public Finance



Adapted from: Siswana, 2007:97

It is recognised that finance is central to public management reforms mainly because it supports the implementation of government's developmental vision and is the cornerstone of service delivery. Dewett (1996: 539) notes that in a growing economy, government has an obligation of stimulating economic growth; and finance is a powerful mechanism used by governments to bring about the desired social and economic changes. Boex (2009:12) shares the same view and asserts that a strong public economy and administration should be supported by public investment make sure that there is harmony between the available budget and government policy priorities as well as with the intended government policy outcomes. Thus, public finance has been used to accelerate development and to break the cycle of poverty and income inequalities.

Musgrave and Musgrave (1989:6) state that the three key functions of finance in the public sector are:

- *Allocative* - the course by which the budget is split among public and private goods and by which a combination of social goods is selected through a budgetary policy process.
- *Distributive* - distribution of revenue collected to communities. Revenue and expenditure processes are implemented in such a manner that they change the distribution of resources with the objective of reducing economic disparities (the LGES formula is one mechanism used by government to redistribute nationally-raised revenue to address disparities in local government).
- *Stabilisation* - maintaining a good level of prices, employment rate, productivity and economic growth.

Musgrave and Musgrave (1989:6)

The above functions are critical in public finance. However, in their current form, they are mostly applicable for the national government. Notwithstanding this, these functions can be seen as important elements informing the funding decisions for local authorities.

In the context of local government, municipal finance is an instrument used by local governments to meet the expectations of the local communities. It is an aspect of finance that focuses on revenue generation, spending and the overall utilisation of government wealth to impact communities in greatest way possible (Sunday, Ocheni and Okechukwu, 2014:84). It is used to reduce poverty levels by enabling municipal governments to embark on effective pro-poor programmes to develop their communities. Furthermore, municipal finance promotes economic development through provision of municipal services required for local economic development.

In the South African context, municipal spending contributes towards the provision of free basic services to indigent communities and the provision of local infrastructure thus promoting local economic development (Republic of South Africa National Treasury, 2011:16). It can therefore be deduced from this discussion that municipal finance is essential for delivery of municipal services and improving the livelihoods of local communities. The relationship between municipal expenditure and the delivery of services to communities by local government is demonstrated in Figure 2.3 below.

Figure 2.3 below illustrates the relationship between municipal expenditure and delivery of services.

Figure 2.3: Municipal Finance and Service Delivery Model



Adapted from: Republic of South Africa National Treasury, 2011:46

The municipal finance and service delivery model is adapted from a model developed by the Republic of South Africa National Treasury, and provides a conceptual context for explaining the relationship between municipal finance and municipal service delivery. The adapted model provides four main components that are essential for addressing community needs in an effective and responsive manner thus enhancing the quality of their lives which has relevance for the discussions in this study.

Component 1: *Strong Fiscal Framework*- relates to the relationship between the community’s demand for services and the municipal fiscal framework. The Constitution assigns specific tasks to municipalities and the municipal fiscal framework provides municipalities with different revenue streams which they can use to fund these expenditure

functions. However, in most cases there is a misalignment between available revenue and the demand for basic services. As a result delivery of basic services is often compromised. The model notes that the factors that impact on the amount of revenue that can be generated by a municipality is the vertical distribution of resources from national government, the design of the LGES formula and the taxes that a municipality is allowed to charge (Republic of South Africa National Treasury, 2011:46). There are other internal factors which are within a municipality's control that affect the amount of revenue generated by municipalities and thus impact on the level of services delivered to communities. These, according to the model, include: poor debt management within the municipalities, inaccurate and unreliable billing systems and the problem on non-payment for municipal services (Republic of South Africa National Treasury, 2011:47).

Component 2: *Strong Municipal Governance Structures*- captures the relationship between municipal governance systems and service delivery. The model assumes that good management and governance systems leads to enhanced service delivery whilst inefficient governance systems can have the adverse effect. The model identifies factors that erode good governance in municipalities which include corruption, poor leadership, and lack of capacity to spend available resources which results in underspending of budgets as well as inefficient financial management (Republic of South Africa National Treasury, 2011:47).

Component 3: *Good Expenditure Choices*- focuses on the relationship between community needs and budget choices made by government officials in order to fund these needs. According to Republic of South Africa National Treasury (2011:47), there are a number of functions that municipalities must deliver on; these include municipal mandates, community needs as well as functions assigned to local government by the other two spheres of government. However, often, the said functions are not always complemented by matching resources. Therefore, local government must make tough decisions in prioritising or ranking these functions and proposing the most appropriate allocation of resources to fund these competing needs. The model assumes that good expenditure choices will enhance service delivery and bad choices will have the adverse effect.

Component 4: *Actual Service Delivery*- highlights the relationship between the actual services delivered and the benefit these bring to the communities. It looks at whether there has been equitable distribution of services delivered if the communities receive Value-for-

Money and the impact of the services delivered in enhancing the quality of the lives of the communities.

The municipal finance and service delivery model identifies the misalignment of expenditure functions and revenue capacity and highlights the need to focus on ensuring that intergovernmental transfers cover the “structural gap” which is the variance between the basic requirements of the community and the available own source revenue generated by municipalities. The “structural gap” can be closed by national government through the provision of adequate intergovernmental transfers. Kenyon (2012:20) notes that the space between the structural and actual gaps must be covered by improved revenue performance by municipalities and improved implementation of services. The model therefore provides that a strong municipal fiscal framework must be supported by good municipal governance structures for the economic, efficient and effective allocation of resources for the provision of services, and the ultimate promotion of the quality of life of communities. Good governance and competent leadership plays a significance role in making sure a local authority is progressive in provision of services (Republic of South Africa National Treasury, 2011:4). This is currently one of the major challenges in several municipalities in this country.

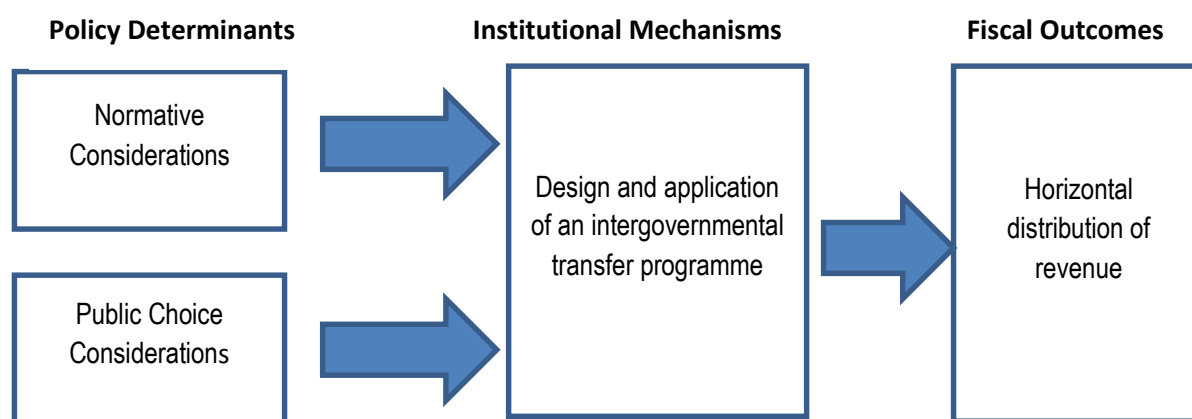
Effective municipal financial management is also essential in ensuring that there are sufficient financial resources (fiscal framework) available to provide adequate services to communities and to sustain municipal institutions. The comprehensive municipal legislative framework is a foundation of the reforms implemented by the South African government to strengthen financial management systems in municipalities. The legal framework calls for strong municipal governance structures and promotes accountability, and the efficient, effective and economic utilisation of municipal finances necessary for the sustainability of municipalities and, most importantly, to generate more and better services for the citizens.

2.5 Conceptual Framework for the Horizontal Allocation of Intergovernmental Transfers

The discussion above provided elements that national government should consider in determining the appropriate transfer programme to municipalities. From the discussions it is evident that developing a suitable transfer system that considers the intricate composition of each municipality is a daunting task.

The section below presents two distinct arguments emanating from literature that underpin the conceptual framework for horizontal allocation of intergovernmental transfers. The Public Finance literature provides normative explanation of intergovernmental grants allocations based on the promotion of efficient and equitable distribution of public resources. Public Choice literature provides an explanation for politicians or national government influencing fiscal decisions reacting to the demands of voters for government services (Boex and Martinez-Vazquez, 2004:457). Figure 2.4 is a diagrammatic view of these two main policy determinants for horizontal allocation of revenue that drive national governments in pursuing their economic role through the system of intergovernmental transfers. These policy determinants provide a basis for the choices relating to the design of the intergovernmental grant programme and ultimately the horizontal distribution of nationally raised revenues to municipalities.

Figure 2.4: Determinants of the horizontal allocation of intergovernmental transfers



Adapted from: Boex and Martinez-Vazquez, 2004:458

2.5.1 Normative Public Sector Theory

The first policy determinant for horizontal intergovernmental transfers is the normative theory of public finance. Normative public finance or public sector economics consist of a body of theory set to describe, analyse, and interpret government operations particularly those relating to public finance. Cordes (2003:169) states that the normative theory tries to describe how government should utilise economic and legal mechanisms available to it to correct the allocation resources and distribution wealth to its communities. It is concerned with social interest, and considers what government should be doing in terms of the standards that are broadly accepted by a community asserts, Tresch (2002:4).

Boadway and Shah (in Mahabir, 2010:160) state that the normative considerations assume that the main function of local government is to service communities with public goods and

services and the community must be prepared to pay for these services provided to them. Slack in (Mahabir, 2010:160) argues that in the normative approach, this is usually done to improve efficiencies in the delivery of public services due to the changing needs of society and the levels of services required to fulfil such needs. Pinho and Veiga (2005:2) agree with these views and affirm that the normative considerations assume that at national level, government is mainly driven by impartiality, efficacy and stabilisation in quest of maximisation of the prosperity of the citizenry (Boex and Martinez-Vazquez, 2004: 458). The normative consideration is explained using three fundamental views discussed below.

- The first view in the normative considerations relates to efficiencies in the provision of public services to communities. In this perspective, the distribution of intergovernmental transfers is usually done by means of a formula which uses the needs of the communities and the local fiscal capacity as indicators to inform the distribution of resources. Accordingly, it would be expected that greater intergovernmental grants are disbursed to municipalities that have more pressing needs or those with lower levels of fiscal capacity.
- The second view in the normative considerations is concerned with striking a good balance between revenue and expenditure obligations at all government levels. Pinho and Veiga (2005:3) state that if equity is the overarching objective, then the process of allocating revenue should be conducted in a manner that more resources are allotted to the areas with limited revenue streams to enable them to deliver the required level of services. Thus, the intergovernmental transfer programme ought to be developed and implemented in manner that it achieves fiscal equalisation among the different municipalities.
- The third and final view in the normative considerations relates to economic stabilisation of government. In most governments, the policy objective of achieving macroeconomic stability or a stable economic environment is pursued at the national sphere of government. One way of achieving this objective is to make sure that there is competent horizontal allocation of resources to municipalities thus guaranteeing an efficient delivery of public services to communities.

The views discussed above emphasize the intentions of national government being that of promoting impartiality, effectiveness or stabilisation objectives pursuing the maximisation of

the prosperity of its constituents. However, critiques of this theory argue national government is not concerned with improving efficiencies and addressing the needs of its constituents but is rather concerned with maximising the prospect of its electoral success. These views are captured in the Public Choice theories discussed below.

2.5.2 Public Choice Theory

The second policy determinant for horizontal intergovernmental transfers is founded on the Public Choice Theory. The Public Choice Theory provided a contrasting view to the normative considerations discussed in the previous section. Hughes (2003:10) asserts that Public Choice is a sub-discipline of economic ideology which applies microeconomics principles in social science and politics. Ulbrich (2011:6) articulates that it is a partly distinct field of economics that analyses the behaviour of elected officials and administrators in the public service, and explores the policy inferences of government failure.

The Public Choice Theory has its origins in the series of publications by Duncan Black dating back to 1948. The rationale behind Public Choice Theory is that government is an economic problem which restricts economic growth and the freedom of individuals (Hughes, 2003:10). The theory further asserts that government control should be reduced by providing the communities with more choice which will lead to individual freedom and efficiency in the provision of public services. Ostrom and Ostrom (1971:205), provide the following assumptions which the Public Choice theories are based:

- Individuals are self-interested;
- Individuals are rational;
- Individuals adopt maximizing strategies; and
- Individuals are knowledgeable.

From the preceding discussion, it can be noted that the Public Choice Theory views politicians as self-interested individuals who are motivated by salaries, power and patronage. Literature suggests that when the above-mentioned assumptions are applied, politicians elected through a democratic process are likely to maximise their prospect of returning to office by implementing the fiscal choices of the voters. Alperovich (1984:286) supports this statement and asserts that central to the Public Choice Theory is the assumption that that rational behaviour of democratic governments can be viewed as resulting from government's efforts to maximise the prospect of electoral success. A government confronted with a decision-making situation in which one or more actions or

policies have to be selected from among several probable alternatives, will select policies or actions that will increase its chances of being re-elected (Alperovich, 1984:286).

Accordingly, in the Public Choice consideration, intergovernmental transfers are a strategic tool for national government targeted at re-election. If this principle is applied in the context, the division of resources to municipalities by national government (politicians) will be aligned to the fiscal preferences of the majority voters asserts Boex and Martinez-Vazquez, (2004:460). For example, in South Africa the majority of the voters live in the Gauteng Province, the Public Choice view suggests that the national government of South Africa would ensure a greater allocation of intergovernmental grants to municipalities in the Gauteng province where the majority of voters reside to maximise its prospects for re-election.

Critiques of the Public Choice Theory argue that the theory lacks empirical support and that it fails to explain and predict political behaviour. It is also argued that Public Choice Theory cannot explain why politicians would vote against the interests of their constituents and why politicians would promote higher taxes, fewer benefits and smaller government (Pressman 2004:9). In addition, the Public Choice Theory fails to predict or explain why wealthy individuals would seek public office (Pressman 2004:11). Another limitation to the theory, according to Levin and Milgrom (2004:22), is that in the real world, choices seem to be vastly situational or context dependent. Factors such as: the manner in which a choice is presented, the feelings of the decision-maker when the decision is made; the social background informing the decision as well as many other environmental variables that influence choices. Therefore, these factors cannot be discounted in the process of decision making.

Notwithstanding the above discussion, it is worth mentioning that in spite of the shortcomings of the Public Choice Theory, it remains a powerful instrument in the public sector policy analysis. The Public Finance and Public Choice theories are critical considerations provided in a body of literature that has pursued to understand the relationship between government policy and the horizontal allocation of nationally raised revenue to local government. These two perspectives present conflicting views of government's intentions with regard to allocation of resources to local government. The Public Choice consideration is based on an assumption that public actions are informed by the behaviour of self-interested citizens, interest groups, government officials and politicians

who interact with one another in political institutions asserts Buchanan, Johnson and Halcombe (in Cordes, 2003:169). To the contrary, the normative theory argues that government's overarching objective is to enhance efficiencies in the delivery of services and to fulfil the changing needs of the citizens. The study tested the validity of these arguments by conducting an empirical investigation on the determinants of the South African LGES. The findings are discussed in detailed in Chapter Five.

2.6 Formula-Based System of Transfers

The section above has provided a conceptual framework for the determination of a transfer programme to local government. This section provided the quantitative and qualitative determinants of local government transfers. The quantitative determinants include the fiscal capacity and fiscal effort indicators used by national governments to determine transfer programmes to local government. The qualitative determinants comprised of normative considerations (which are based on public finance theories) and Public Choice theories that are conceptual policy determinants for the horizontal allocation of revenue to local government. These discussions have presented a range of factors involved in designing a system of intergovernmental transfers as well as elements that influence national government choices regarding allocation of funds to municipalities.

In trying to bring objectivity to the design of intergovernmental transfers, a number of governments have opted to use a mathematical formula to allocate funds to municipalities. The section below discusses the rationale for government's using a formula to allocate funds specifically to local governments and the principles of a good transfer system.

An allocation formula is one of many mechanisms used by governments to distribute funds to local governments. Formula-based intergovernmental transfers are distributed according to a set of criteria determined by national government (Ulbrich, 2011:285). A LGES allotted using formulae are progressively becoming common mainly because they meet a range of assessment standards such as sufficiency of revenue, growth, certainty, uncomplicatedness, transparency, allocative efficacy, equitability, and are an incentive for sound fiscal management (Boex, 2009:12). Kirigia (2009:84) states that a common purpose for developing and using a formula for intergovernmental transfers is to ensure that financial resources are allocated in the greatest equitable and effective way probable. This is supported by Boex (2009:12) who states that in developed countries, the underlying philosophy surrounding formula based allocations is the logical reasoning that formulae are responsive to the priorities of government and embody the principles namely: efficacy,

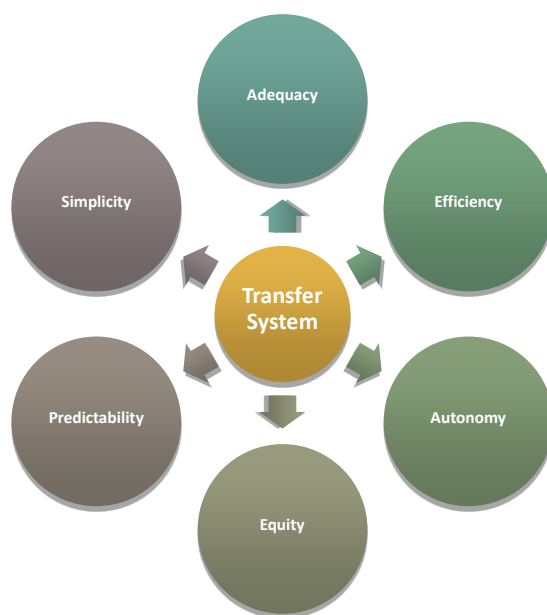
impartiality and efficiency in the delivery of services to the voting citizenry. Moreover, formula based allocations are appealing in public sector budgeting since they make it easier for government to account for decisions relating to resource allocation (Bird and Smart, 2002:4).

2.6.1 Principles of a Good System of Transfers

The method in which a transfer system is developed is often based on a complex combination of political choice, economic principles, historical reasons and contextual factors. As a result, the design of intergovernmental fiscal transfers is recognised as being one of the most challenging tasks within Public Finance. Public economic literature identifies a set of principles that intergovernmental transfers should adhere to which include: transparency of grant design, equity, clear grant objectives, accountability and autonomy.

Similarly, Smoke and Schroeder (in Ncube, 2013:297) provide the principles of a good transfer system as presented in Figure 2.5 below.

Figure 2.5: Features of a good transfer system



Adapted from: Smoke and Schroeder (in Ncube, 2013:298)

In South Africa, the White Paper on Local Government adopted the set of principles, similar to those provided in public economics literature. It prescribed that a transparent, formula-based system is introduced to achieve equity, efficiency and transparency in the distribution of resources to municipalities (Republic of South Africa White Paper on Local Government, 1998:11). The Paper further notes that a formula-based mechanism is essential as it eliminates subjectivity in distribution of resources thus reducing discrepancies and

inequalities (Republic of South Africa White Paper on Local Government, 1998:11). It is on this basis that in 1998 the Department of Finance (now National Treasury) proposed that the horizontal allocation of revenue by national government to municipalities be done using a formula-based mechanism (Republic of South Africa National Treasury, 2012:3). Subsequently, the first LGES formula was developed and officially launched in 1998 in accordance with the prescripts of the Constitution and principles prescribed in the White Paper on Local Government.

Similar to other developing countries using a formula-based approach to allocate funds to local government, the South African government has been confronted with a difficult task of developing a suitable redistributive formula that addresses local government inequalities while taking into account the principles prescribed in the White Paper on Local Government. As a result, the South African national government has conducted several reviews of the formula which include two major reviews in 2005/06 and 2012/13 financial years. These reviews were primarily to address the redistributive challenges in the formula and to develop a suitable mechanism that responds to the needs of local communities in an effective, efficient and economic manner. The details of these Reviews are discussed at length in Chapter Three.

2.7 Fiscal Capacity of Municipalities in South Africa

The discussion in the preceding section highlighted the significance of municipal finance in achieving the objectives of a developmental local government and in delivering services in an effective and viable manner. However, the existing imbalances between municipal areas mean that the level of services delivered to local government differs from one municipal area to the other. Thus, in order to address the imbalances between municipal areas, national government must develop an appropriate measure of these imbalances in order to implement a suitable intergovernmental equalisation programme.

In principle, a suitably designed intergovernmental equalisation transfer programme rectifies biases that may create fiscally based cross border movements between municipalities by equalising benefits among municipalities. An evaluation of the expenditure and benefits of delivering basic services in the different municipalities is important in determining a municipality's net fiscal benefits. The intergovernmental equalisation programme may well be advanced by designing a level of equalisation and developing a method of funding the intergovernmental transfers (grants).

The following section is a significant focal point of the study and presents an argument on the fiscal capacity in municipalities with particular reference to South Africa. The section also elaborates on the relevance in equitable resource allocation and more specifically to the development of an intergovernmental transfers programme for local government. In addition, the section explores the measurement of municipal fiscal capacity in the South African context, and how this measurement is aligned to international standards.

Martinez-Vasquez and Boex (in Nikolov and Josifov, 2006:3) note that fiscal capacity can be defined as the potential capacity of local government authorities to generate revenues from their own revenue streams.

2.7.1 Definition of Fiscal Capacity

The South African Local Government Association (SALGA) (2010: iii) argues that the wealth of a municipality can be best measured by its ability to generate revenue from its community and the extent of this capability to generate own income is known as fiscal capacity. Chitinga-Mabungu and Monkam (2013:2) explain fiscal capacity as a quantity of a municipal area's capability to generate revenue comparative to its expenditure requirements. Yilmaz, Hoo, Nagowski and Rueben (2006:2) argue that low fiscal capacity municipalities will typically have a comparatively low revenue base, high expenditure requirements or a mixture of the two. Therefore, the concept of fiscal capacity is posited to be an inherent feature of local government's economy. It is determined by the municipality's economic resources, economic activities and revenue sources and reflects the economic and financial revenue bases from which municipalities can draw (Barro, 2002:1). This observation is shared by Chernick (1998:531) who argues that any description of fiscal capacity should begin with quantifying the level of economic activity which include: level of income generated, income received by residents in the community and the value of property in that municipal area.

There are a number of reasons for governments measuring the fiscal capacity of municipalities. Yilmaz (2002:2) states that a measure of fiscal capacity provides information on a municipality's financial strengths and deficiencies which may be utilised to: compare and evaluate economic conditions and assess the strength of a municipality's economy and to guide national government in providing assistance to local governments through grant funding. The Advisory Commission on Intergovernmental Relations (1986: 23) identifies four primary uses for fiscal capacity measurements which are closely related to those noted by Yilmaz. These include:

- analysis of regional economic disparities;
- development of regional policy;
- analysis of comparative fiscal policy; and
- development of fiscal equalisation policy.

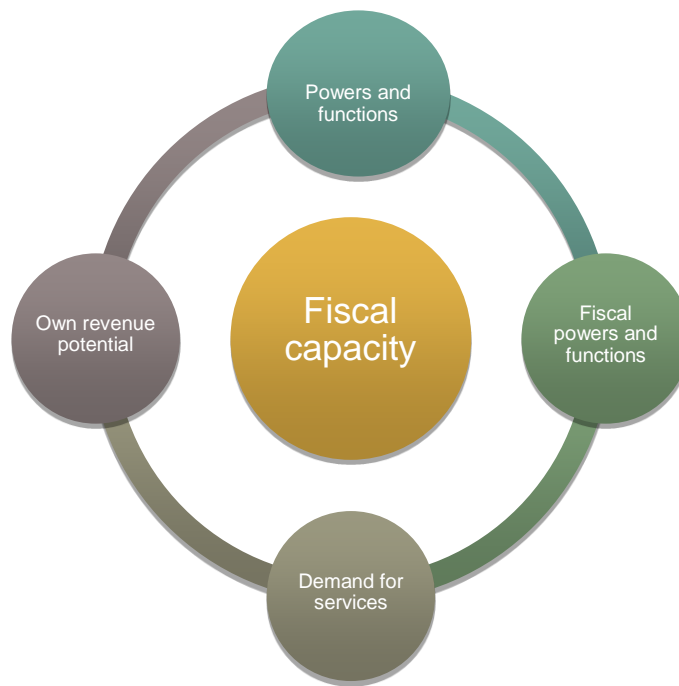
It is clear from the discussion above that fiscal capacity is fundamental in the process of developing an intergovernmental transfer programme for local government. It provides critical information relating to the potential revenue bases for municipalities which is essential for determining a suitable fiscal equalisation programme for local government. The section below provides a discussion on the measures of fiscal capacity in the municipal context.

2.7.2 Exploring the Fiscal Capacity of Local Government

Literature provides a number of elements that influence the level of fiscal capacity of a municipality. These elements encompass geographic and demographic factors that make each municipality unique. For an example, the settlement patterns of each municipal area and the different levels of economic activity and poverty all have a degree of influence in the size of revenue that a municipality can collect. Bahl and Smoke (2003) (in Amusa, Mabunda and Mabungu, 2008:2) posit that differences in the number of the inhabitants, income sharing, size of the revenue base, the different levels of organisational capacity and urbanisation and the manner in which distribution of revenue collection and responsibilities varies extensively within and among municipalities. As a result, each municipality has its distinctive revenue raising ability making it unique and different to other municipalities.

The Republic of South Africa National Treasury (2011:38) summarises the dynamics that influence the fiscal capacity of municipalities' into four distinct aspects shown in Figure 2.6 on the page to follow.

Figure 2.6: Aspects to the fiscal capacity of a municipality



Adapted from: (LGBR, 2011: 38)

- *Fiscal powers and functions*

Municipalities receive their revenue raising mandate from the Constitution and other national legislation. Section 229 of the Constitution assigns fiscal authority and tasks to local governments authorising them to raise their own revenue. The Municipal Property Rates Act (No.6 of 2004) prescribes that local authorities levy taxes on properties, surcharges for services delivered by or for municipalities. Municipalities are only authorised to generate own revenues from the sources specified by these pieces in the legislation. This implies that municipalities cannot expand their revenue powers beyond those prescribed in national legislation. Therefore, the nationally imposed limitations on municipalities' fiscal powers and functions decrease municipalities' overall revenue potential.

- *Own revenue potential*

Local authorities can only generate income proportionate to the earnings of the residents, households and businesses located within their municipal area, provided that they have the fiscal powers and functions to do so. According to SALGA (2011:iii), metropolitan municipalities have revenue potential that is nine times greater than that of a rural municipality and large city municipalities have revenue potential five times greater than a rural municipality. This implies that a municipal area with an affluent population is more likely to finance service delivery when compared to other poorer municipal areas because they can generate income from their bases effortlessly. The customers' ability to pay for

municipal services is another important factor for a municipality's revenue potential. A municipality with a significant number of indigents is more likely to have a low revenue potential due to the inability of its customers to pay for municipal services. The justification used to describe non-payment is the incapacity for consumers to pay owing to poverty (Booyesen, 2001; Botes and Pelsler, 2001; Burger, 2001) (in Peters, 2013:157). This assertion is also shared by Ngxoxo (2003:60), who argue that customers are willing to pay for municipal services they receive; however they have no financial means to do so. This is mainly as a result of high rates of unemployment in poorer municipalities which impacts on the local authority's revenue potential and ultimately its fiscal capacity.

- *Powers and functions*

The service charges and surcharges levied by a municipality can only be in accordance with the functions that it is authorised to deliver (LGBR, 2011:38). Different categories of municipalities are allotted categories of functions and authority and thus have different service offerings and revenue sources. A municipality that is authorised to offer a diverse set of services is likely to have greater revenue potential when compared with a municipality that is authorised to deliver a limited range of municipal services.

- *Community demand for municipal services*

The level of a local authority's service responsibilities gives the basis for its revenue potential. A community's demand for a municipal service is influenced by a range of elements comprising the level of backlogs and the quantity of indigent households and businesses in that municipal area. A municipality with a high demand for municipal services has greater revenue potential compared to an area with low demand, provided that the consumers are prepared and capable to pay for those services. The population density of the area also impacts on the level of service delivery demand in a municipal area. A highly populated municipality will have a higher demand for municipal services compared to a sparsely populated municipality.

It is imperative for national government to have a good appreciation of these factors and how each impacts on each municipality to be able to develop an appropriate intergovernmental transfer programme. It is also worth noting that fiscal capacity is not the same as a municipality's own-revenue generated. Equally, its inability to generate its own income does not equal to a deficiency of fiscal capacity. Therefore, this implies that a local authority's fiscal capacity cannot be measured in isolation of its fiscal effort (LGBR,

2011:38). Parker (in Teko, Nkote and Jannat, 2014:57) advances the notion that municipal areas with the similar fiscal capacities can still raise different quantities of income owing to a number of factors such as: using different tax rates, inconsistencies in the revenue collection effort and different levels of taxpayer compliance. However, Bird (in Bird and Smart, 2002:6) warns that assigning excessive weight on fiscal effort in allocating intergovernmental transfers can improperly penalise poorer municipalities whereby a percentage rise in effort is more challenging to attain when compared to urban municipalities. The challenge for national government is striking a balance between promoting fiscal effort by penalising municipalities that do not demonstrate good fiscal effort and compromising service delivery as a result of under-allocation of grants to poor municipalities that lack fiscal effort due to their demographics.

While scholars agree on the definition of fiscal capacity and its uses, literature indicates that there is no solid agreement between scholars on the measures of fiscal capacity. Yilmaz (2002:3) argues that there is a debate around quantifying fiscal capacity. Boardway and Shah (2007:20) state that estimating fiscal capacity is conceptually and empirically difficult. As a result, there are a number of methods that have been used in a range of empirical studies to measure fiscal capacity some of which are discussed below.

Recently, a body of empirical studies have been conducted and they are centred on the different methods used to measure the fiscal capacity of municipal areas. This has been particularly observed in the work of Martinez-Vazquez and Boex (1997); Yilmaz (2002); Yilmaz *et al* (2006); and recently Chitinga-Mabungu and Monkam (2013). In their work, these scholars identify a selection of approaches that are currently used to quantify fiscal capacity of a municipal area and they also propose alternative measures that can be used to determine the fiscal capacity of a municipal area. These methods include, *inter alia*, revenue collections method, per capita income method, gross value product method and the representative tax system.

- *Revenue Collection method*

The revenue collection method uses the current collection of revenue or collections from a base year to measure fiscal capacity. Martinez-Vazquez and Boex (1997:2) argue that the regional revenue collection measure of fiscal capacity is simple yet poor. They further note that, while the data for this approach is always readily available from the national revenue services, the disadvantage of using it is that actual revenue collected can be influenced by

different levels of enforcement, compliance, tax rates and the discretion of the local government authority (Martinez-Vazquez and Boex, 1997:2).

- *Per Capita Personal Income method*

Per Capita Personal Income approach is the most commonly used measure of fiscal capacity due to its simplicity. This method measures revenue generating ability as the per capita amount of income a region's population could generate if they forced a standard tax obligation on itself (Allers and Ishemoui, 2011:3). However, the citizens' income is increased by the region's ability to distribute a share of its revenues to non-citizens (Chernick, 1998:533). Liddo, Longobardi and Porcelli (2014:10) state that this method is a good measure of the citizens' ability to pay taxes. However, literature notes that the accuracy of current and complete data on per capita income is a concern.

- *Gross Regional Product (GRP) method*

The GRP method measures the worth of goods and services produced using the municipalities' financial resources over a given period of time. It sums the value added by all economic wealth in the municipality. The disadvantage of this measurement is that the computation of GRP data is comprehensive and the required data is not always accessible for individual municipal areas (Allers and Ishemoui, 2011:4). Even though gross product data is accessible at a national level (as gross domestic product), it is not always obtainable at municipal level.

- *Representative Tax System(RTS) method*

The RTS method was developed as early as 1962 by the United States Advisory Commission on Intergovernmental Relations and is one of the most conventional approaches to measuring fiscal capacity in public finance literature (Yilmaz, 2006:3). The RTS method is a tax arrangement that is indicative of the sum of all taxes imposed by local governments of a country (Yilmaz, 2002:4). It comprises five components; description of tax streams, finding average tax rates, measuring revenue exposure, grouping of tax income into bases and measuring fiscal capacity assert Martinez-Vazquez and Boex (in Teko *et al*, 2014:57). This method uses statistical data collected from national surveys to estimate the revenue capacity index which measures the relative ability of a municipality to raise revenue. It is grounded on a calculation of per capita tax quantities that a region can generate applied as national average of the total tax bases that could be taxed regardless of whether they are actually taxed (Chervin, 2007:3).

Telo *et al.* (2014:57) notes that the main advantage of the RTS method as a measure of fiscal capacity is its precision. Yet, there are scholars that have criticised the RTS methodology mainly due to its calculation. The calculation uses data from national surveys which are mostly conducted in five year intervals. As a result, interpolation for the missing years is inevitable. This reduces the independence of between-year estimations. Furthermore, an increase in a region's tax rate causes an increase in overall fiscal capacity indices which is not necessarily related to the actual improvements in fiscal capacity.

In the South African context, to show for the different fiscal capacities across local authorities, a revenue adjustment factor is factored to the institutional and community services components of the LGES formula (Republic of South Africa Division of Revenue Bill, 2015:97).

The revenue adjustment factor is founded on a per capita index that is based on the variables below:

- Sum of income of all residents and family units in a local authority (as a quantity of income and economic activity);
- Unemployment rate;
- Property values;
- Sum of indigent family units as a proportion of the quantity of family units in the local authority; and
- Sum of family units on traditional land

Using this index, local authorities are ordered based on their per capita revenue-generating prospective. The upper 10% of authorities that are allocated a revenue adjustment factor of zero. This implies that they do not get a provision from the institutional and community services components. The lower 25% of local authorities are allocated a 100% revenue adjustment factor. This implies that they get the whole provision from the institutional and community services components. Authorities that are placed in the range of bottom 25 % and top 10 % are allotted a revenue adjustment factor effected on a descending scale, such that the municipalities with a greater per capita revenue-generating prospective get a lower revenue adjustment factor and those that have a lower revenue generating prospective get a greater revenue adjustment factor (Republic of South Africa Division of Revenue Bill, 2015:97).

With regard to district municipalities, the revenue adjustment factor originates from the RSC/JSB levies replacement grant which replaced own revenue source since district municipalities do not generate their incomes from property taxes. Similar to the methodology used for local and metropolitan municipalities, district municipalities are allocated revenue adjustment factors on a descending scale based on their ranking.

Often, fiscal capacity data is not accessible at municipal level especially in developing countries due to data limitation. Rao (2003:20) notes that the scarcity of information makes it difficult to get a clear picture of the differences in fiscal capacity across municipalities, the structure and operation of property rates and the ability of municipalities to collect user charges on electricity and water from the consumers. As a result, most developing countries use the Gross Product Value to offer a detailed, but incomplete, indicator of the revenue produced in a region as it is a quantity of earnings, incomes and wages.

2.7.3 Fiscal Capacity and Fiscal Effort

The above section has provided a discussion of the different methods used to measure fiscal capacity and the shortcomings of these methods. It further provided factors that impact on the degree of the fiscal capacity of a local authority. It is essential that these factors are accounted for in the process of measuring the fiscal capacity of a region. When measuring the fiscal capacity of a municipal area, in addition, is also important to investigate the fiscal effort of that region. Often, fiscal capacity is confused with fiscal effort. As defined in the preceding section, the fiscal capacity of a municipality is its ability to generate income from its own streams to pay for public goods and services and fiscal effort is the extent to which a municipality uses the revenue streams assigned to it (Teko *et al.* 2014:56). Section 227 of the Constitution assigns that national government grants to local government may not reward local authorities that fail to generate own income proportionate to their fiscal capacity. Accordingly, local authorities are expected to demonstrate some degree of fiscal effort before they can receive a transfer from government.

While the level of revenue collection is widely considered as good measure of fiscal capacity, in actuality, the sum of income collected is not entirely suitable for measuring fiscal capacity. Determining fiscal effort of a region provides a more complete measure of fiscal capacity. The meaning of fiscal effort is the degree to which a municipality uses its fiscal capacity to generate income.

The equation below explains how fiscal effort of a region is calculated, where: e =Local effort, L= Local own-source revenue and B = Local tax base.

$$e = \frac{L}{B}$$

Yilmaz *et al.* (2006:2)

Local effort (e) is the quotient of Local own source revenue (L) and the Local tax base (B).

2.8 Conclusion

The traditional models of public administration gave a basis for the study of Public Administration and remain the most successful and long standing theories of management in the public sector (Hughes, 2003:17). However, the rapidly changing society and the reconfiguration of the public sector necessitated the review of public administration and the introduction of more contemporary approaches in Public Governance discussed in the chapter.

The chapter has presented a discussion on the multidimensional nature of Public Administration. Human resource management, leadership and public finance are amongst the range of topics encompassed within the study of Public Administration. The latter has been discussed in greater detail in the chapter as it is central to this study. The chapter also presented two arguments emanating from the Public Economics and Public Choice theories that seek to explain the relationship between national government decision making and the policies relating to intergovernmental transfers. These theories provide a conceptual framework aimed at increasing the knowledge of the system of local government intergovernmental transfers and their validity is tested in Chapter Five.

CHAPTER THREE

EQUITABLE RESOURCE ALLOCATION IN LOCAL GOVERNMENT IN SOUTH AFRICA

3.1 Introduction

The structure of the new South African government system is established in the Constitution. Every level of government is allocated its unique authority, tasks and responsibilities and the underlying principle underpinning the government system is cooperative governance. In 1994, a democratic administration substituted the apartheid government. This change in administration created an opportunity for the new government to restructure and change the administrative system and the apartheid laws. Between 1994 and 2000, local government went through a comprehensive restructuring process. The former four provinces and nine homelands of the former administration were replaced by nine provinces. Furthermore, the 1200 race based local authorities were reconfigured in two stages: in 1995, 843 provisional municipalities were established and in the second stage, in 2000, urban and rural areas were merged which reduced the number of local municipalities to 284 (Derichs and Einfeldt, 2006:3). In the recent years, local government has continued to reconfigure which has led to a further decrease in the number of local authorities in South Africa to reach 278 in 2014.

The strong legislative framework has been unable to fully address the challenges faced by local government. Twenty years into democracy, local government is still confronted with a number of interrelated challenges which include poor capacity, weak administration systems, undue political interference in technical and administrative decision making and uneven fiscal capacity.

The chapter begins by discussing the main features of the federal system of governance in South Africa. This is followed by an overview of the South African municipal finance system and the statutory measures underpinning municipal finance. The chapter also provides an elaborate discussion on the expenditure assignment and the local government fiscal framework and the cause of vertical and horizontal imbalance in federal system of government and the system of intergovernmental transfers as government's strategy to address these imbalances. The chapter concludes with a discussion of the evolution of the LGES formula and the two major reviews that were conducted by national government to address the shortcomings of the formula.

3.2 South African Federal System of Governance

The Constitution of the Republic of South Africa, Act 108 of 1996, establishes three distinct, codependent and interconnected levels of government with each level allocated its own authority, tasks and responsibilities. National government is accountable for leadership, policy making, regulation and oversight; provinces are mainly responsible for social delivery (health and education) and municipalities are mainly responsible for delivering basic services. Chapter 3 of the Constitution sets out the principles within which the three spheres should work together to improve lives of citizens through provision of effective and efficient services. A relationship of co-operative governance among the different spheres of government is defined and requires that local authorities be capacitated to be developmental, competent, answerable, democratic and viable to make sure that the welfare of the citizens of South Africa.

The Constitution democratises local government and elevates it as a separate level of government with a task of prioritising basic requirements of the citizens and to stimulate growth and prosperity in communities. Therefore, municipalities have the right to administer the local government undertakings of their constituencies on their own initiative independently.

Local government in South Africa is characterised by high levels of economic inequality as a result of a long history of systematic under investment in black areas under the pre 1994 government. Moreover, there are distinct demographic and geographic features that make each municipal area unique. Thus, a coherent approach to local government cannot be a one-size fits all approach (NDP, 2011:387). Accordingly, the South African government has then taken a differentiated approach in the treatment of municipalities in line with Section 155 of the Constitution which distinguishes the different categories of municipalities each with its own distinct powers and functions. The three categories of municipalities as classified in the Constitution are:

- Category A (Metropolitan): has an exclusive municipal executive and a legislature in its jurisdiction.
- Category B (Local municipality): shares municipal executive and legislature in its jurisdiction with a category C municipality located within the said jurisdiction.
- Category C (District municipality): has municipal executive and a legislature in the jurisdiction and included more than one municipality.

Section 152 of the Constitution further sets out the following objectives for local government:

- to deliver an answerable and self-governing local authority to citizens;
- to make sure that there is sustainable delivery of public services to citizens;
- to stimulate and encourage growth in local economies and society;
- to encourage a healthy and safe environment, and
- to promote the involvement of citizens and community groups in all municipal undertakings.

The Constitution provides that the South African government implements public management reforms to devolve powers and functions to local government thus bringing government and service delivery closer to the people.

3.3 Municipal Finance System in South Africa

The section above has presented a discussion of the structure of government in South Africa with a specific focus on local government. Local government is given a distinct role of promoting development through the provision of services to communities. To meet this objective, local government must have adequate matching resources at its disposal. This section provides the legislative framework underpinning local government finance in South Africa. It further presents a discussion on the local government expenditure assignments and revenue assignments and the fiscal gaps arising from the mismatch between these two assignments.

The reorganisation of government in South Africa to three distinct spheres led to a substantial increase in the roles and responsibilities of local government in delivering basic services. The decentralisation of powers and functions to local government was followed by expenditure assignment to local government which relates to the provision of basic public goods and services (electricity and water). This necessitated the need to build capacity to raise revenue and to implement expenditure decisions at municipal level.

The intergovernmental system as outlined in the Constitution is based on seven principles. Legislation, policy, and practice must be in line with these principles to protect the stability of the intergovernmental system. The Constitution sets the intergovernmental principles as follows:

- *Distinctiveness and Accountability:* All three spheres of governments are unique and accountable in their own right, each with its own specified powers and responsibilities. This makes each level of government accountable to its legislature,

consents each level of government to develop its own priorities. However, these priorities must be aligned to constitutional and other nationally-legislated obligations and ensure that, being a government and not just an administration; each level of government is fully responsible for its actions or failure to act. Furthermore, intergovernmental relations must be just, and promote good governance.

- *Cooperative Governance*: Each sphere of government should not undertake any powers or functions except for those assigned by the Constitution. All three spheres are obliged to cooperate with each other and should respect the functional, geographical and institutional integrity of other levels of governments. There should be consultation on any legislation that will impact other levels of government and should contribute in developing capacity of other levels.
- *Good Governance*: Accountability is an important aspect of good governance. The relationship between councillors and officials and their accountability to their constituencies is key principle of good governance. There must be accountability and transparency in all reporting mechanisms within and between the three levels of government.
- *Increased access to services*: The Constitution and the White Paper on Local Government prioritised provision of basic services to all South Africans. This principle sets that access to services must be extended to reach all communities at affordable costs. This also entails designing of apposite levels of service to meet community needs economically and leveraging in additional resources to enhance efficiency.
- *Equitable vertical and horizontal sharing of resources*: The Constitution sets out a revenue sharing system, which accounts for the fiscal capacity and functions allotted to each level of government. It entitles the provincial and local governments to an equitable share of nationally generated revenue in a form of intergovernmental grant. The Constitution further prescribes that the system of intergovernmental transfers must be comprehensive and simple. The system should comprise conditional grants for infrastructure, the equitable share, and capacity building and reform.
- *A single process for vertical division*: This principle recognises that there are trade-offs in determining allocations to each level (the vertical division). Thus, the process of allocation of resources to the different levels of government should be inclusive and driven by set political priorities and must accommodate all facets of service delivery and local governance. The risk of consenting to unstructured and ad hoc funding requests is that it can fragment the process of resource allocation and also undermines the process of political prioritisation.

- *Delivery effectiveness and efficiency:* There is a direct relationship between the government's macro-economic policy and its provision of public services. Government expenditure is aimed at the delivering public goods and services whilst stimulating economic growth in order to address inequalities and alleviate poverty in communities. Hence, it is imperative that government performs its functions of delivering public goods and services and manages its expenditures in an effective and efficient manner in order to achieve the objectives on the macroeconomic policy.

(Girishankar, DeGroot and Pillay, 2006:46)

3.1 Overview of Statutory Measures Underpinning Municipal Financing

There is a range of other legislation that governs the system of intergovernmental fiscal relations in South Africa and municipal finance. The following are some of the many pieces of legislation that establish intergovernmental fiscal relations and that govern municipal finance in South Africa.

3.3.1.1 Constitutional imperatives

As discussed in preceding sections, the Constitution of the Republic of South Africa (1996) is the supreme law of the Republic and provides the basis for public financial management. Chapter 13 of the Constitution provides for general financial matters of government and includes prescripts for local government financing. Section 214 (1) (a) of the Constitution prescribes that an Act of Parliament must provide for the equitable division of revenue generated nationally between the national, provincial and local spheres of government. In addition, Section 227 (1)(a) prescribes that local government and all provinces are entitled to an equitable share of revenue generated nationally to empower them to provide basic services and execute the functions assigned to them. It is on the basis of these prescripts that the model of equitable sharing of revenue was first introduced in South Africa in 1998.

3.3.1.2 The Intergovernmental Fiscal Relations Act (No.97 of 1997)

This Intergovernmental Fiscal Relations Act prescribes the process for the division of revenue between the national, provincial and local spheres of government. It also promotes co-operation between the three spheres of government on budgetary, fiscal and financial matters.

3.3.1.3 Division of Revenue Act

The Division of Revenue Act (DORA) is an Act of Parliament referred to in Section 214 (1) (a) of the Constitution. It is enacted on an annual basis and provides for the annual equitable division of revenue generated nationally amongst all three spheres of government and stipulates the responsibilities of each sphere of government.

3.3.1.4 Intergovernmental Relations Framework Act (No 13 of 2005)

The Intergovernmental Relations Framework Act (No.13 of 2005) promotes and facilitates intergovernmental relations by providing a framework for the creation of intergovernmental forums and provides for mechanisms and procedures for facilitating the settlement of intergovernmental disagreements.

3.3.1.5 Municipal Finance Management Act (No 56 of 2003)

The Municipal Finance Management Act (No.56 of 2003) (MFMA) is a key component of the broader legislative framework governing local government authorities and forms a major part of the reform packaged to bring about financial management reforms in municipalities. The MFMA aims to support municipalities by strengthening their financial management systems thus moving them towards an even more sustainable future.

3.3.1.6 Municipal Systems Act (No 32 of 2000)

The Act provides the processes, mechanisms and principles for municipalities to enable them to provide economic and social enhancement of communities and complete access to affordable basic services. The Act ensures that municipalities introduce tariffs for services and policies for credit control and provide a framework for the delivery of services and service delivery agreements.

3.3.1.7 Municipal Property Rates Act (No.6 of 2004)

The Act regulates the powers of a municipality to impose taxes on properties and surcharges on fees for services delivered by or on behalf of the municipality. In addition, the Act provides for: reductions and rebates through their rating policies, transparent and fair systems of exemption, fair and equitable assessment methods for properties as well a process for objections and appeals.

3.3.1.8 Municipal Fiscal Powers and Functions Act (No.12 of 2007)

Municipal Fiscal Powers and Functions Act (No.12 of 2007) regulates municipalities' powers to impose surcharges on fees for municipal services provided.

3.3.1.9 White Paper on Local Government (1998)

The White Paper on Local Government creates a foundation for a system of local government that is developmental. It calls for a local government that is dedicated to working with its communities towards building sustainable settlement opportunities enhance the quality of life of communities. It further promotes a local government that responds to the economic, social and material needs of its communities in an inclusive manner. The White Paper on Local government also provides the principles for the local government fiscal framework.

This body of legislation forms a legal framework for local government financing. It is established through the Constitution of the Republic of South Africa, 1996 and is grounded on the understanding that redistribution of resources is a challenge that must be resolved mostly through a system of transfers (CoGTA, 2009:57). This framework also ensures that the intergovernmental fiscal system in South Africa is designed to address the challenge of redistribution of resources. This is done through the Constitutional assignment of powers and functions to all three spheres of government.

3.4 Local Government Expenditure Assignment

The assignment system in South African appears to mostly agree with the principles of revenue and expenditure assignment captured in the public finance literature according to Boadway (in Yemek, 2005:6). The main objective of the South African assignments system is to reduce interregional disparities and advance social indicators inherited from past policies through the provision of public services.

The Constitution allocates functions into two categories: concurrent functions (shared among the spheres) and exclusive functions (performed by only one sphere). Schedule 4 of the Constitution provides a list of the functional areas of concurrent national and provincial legislative capability. These comprise health services, social welfare, school education, agriculture and housing. With regard to these functions, national government is responsible for policy formulation, developing a regulatory frameworks, establishing norms and standards as well as monitoring and evaluation of implementation of policies (Republic of South Africa National Treasury, 2011:31). Provinces are primarily responsible for implementation in accordance with the national regulatory frameworks. This implies that the

size of the budget at provincial level is generally larger than that of the relevant national department due to the assignment of functions.

The other category is exclusive functions. A function falls into the exclusive category if it is only performed by one sphere of government. That sphere would be responsible for developing legislation or policies and its administration as well as monitoring performance in relation to that function (Republic of South Africa National Treasury, 2011:31). The Constitution does not outline the exclusive functions of national government mainly because national government takes on the responsibility for all government functions that have not been specifically allocated to the other spheres of government. Therefore, national government is responsible for the following exclusive functions: fiscal policy, defence, criminal justice system (safety and security, courts), foreign affairs, higher education and other administrative functions (Derichs and Einfeldt, 2006:4). These functions account for a significant share of national government's budget. Provinces are assigned the following exclusive functions: ambulance services and provincial planning as well as legislative competence over provincial roads. However, national government has the powers to regulate the above-mentioned functions if it is deemed appropriate to maintain critical national standards or for reasons related to the overall security of the country (Republic of South Africa National Treasury, 2011:31). Table 3.1 below illustrates the devolution of priority functions to local government.

Table 3.1: Priority functions for local government

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

Source: *Budget Review, 2011:33*

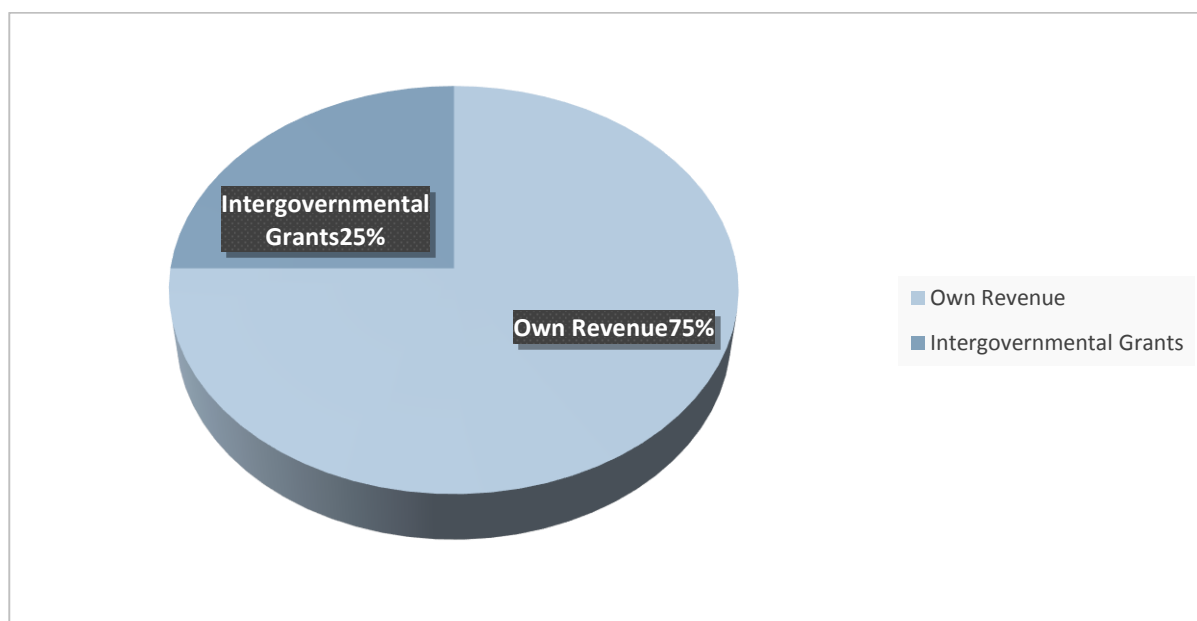
The expenditure assignment in South Africa is designed to achieve meet three objectives: firstly, an efficient resource allocation through a government system that is accountable and responsive; secondly, equitable delivery of services to communities in the different municipal areas; and lastly, sustaining economic growth and macroeconomic stability (Yemek, 2005:6). To meet these objectives, municipalities are assigned a range of fiscal instruments through Section 229 of the Constitution. These include own source revenues (user charges, surcharges), intergovernmental transfers and other locally raised taxes. This implies that the different priorities of local government can be funded through the different sources of revenue assigned to local government which are discussed in the section to follow.

3.5 Local Government Revenue Assignment (Fiscal Framework)

The South African Intergovernmental Fiscal Framework stems from the intergovernmental system founded on a principle of cooperation among the three spheres of government. It is a funding arrangement that ensures municipalities are adequately resourced financially to fulfil their Constitutional mandate which is to provide basic services (Financial and Fiscal Commission, 2013:8). The Fiscal Framework refers to all available income streams that local government can access to meet its expenditure assignment and functions.

These income streams mainly include: own revenue sources, intergovernmental transfers as well as borrowing. Figure 3.1 below illustrates the composition of the South African Local Government Fiscal Framework in the 2012/13 financial year.

Figure 3.1: Composition of the South African Local Government Fiscal Framework



Adapted from: Kenyon (2012:4)

3.5.1 Own Revenues

Section 229 of the Constitution assigns fiscal powers and functions to municipalities. In conjunction with the Municipal Property Rates Act (No.6 of 2004), the Constitution allots powers to municipalities to raise their own revenues by imposing rates on property, surcharges of fees for services provided by or on behalf of the municipality. Own revenues account for the bulk of the Local Government Fiscal Framework. Kenyon (2012:4), notes that in 2012/13, 75% of the total Local Government Fiscal Framework was own revenue and intergovernmental transfers accounted for 25%. Schoeman (2011:4) states that data indicates that most municipalities have little or no borrowing power to fund deficits, with the exception of metropolitan municipalities. Therefore, borrowing accounts for a marginal partition of the fiscal framework for local government.

In terms of own revenues, municipalities generate revenue by imposing user charges, rates and taxes as well as borrowing, which are discussed below.

- *User charges*

According to CoGTA (2009:60), user charges are the primary source of municipal own revenue. Municipalities charge tariffs for provision of basic services to households. These services include provision of water, electricity, sanitation, fines and penalties (traffic fines or late payments), specialised services (approval of building plans), and interest charged on arrears. In the 2012/13, Msunduzi Municipality generated R1,9 billion from user charges of which R1,4 billion was from sale of electricity (Msunduzi Municipality Annual Report, 2013: 296). This accounts for 58% of the Municipality's total revenue at the end of t 2012/13

In view of service charges being the main income stream for municipalities it is important that there are proper payment enforcement measures in place to ensure effective collection which is currently a challenge in many municipalities.

- *Rates and taxes*

In many democratic countries including South Africa, property rates are a key income source for municipalities. Rates are defined as property taxes that a municipality can impose from individuals and businesses that own fixed property in the municipal area. Municipal rates account for a substantial share of own revenue for local government in South Africa (Ngxongo, 2003:26). In 2012/13, Msunduzi Municipality collected R589,8 million from property rates which includes penalties imposed (Msunduzi Municipality Annual Report, 2013:296). This represents 32% of total revenue collected over this period. The rates charged are calculated as an estimated value of

that property. The Rate in the Rand is set each year by council, as the percentage of the property value that the owner must pay to the municipality. Rates are usually paid either annually or in twelve monthly instalments. The municipality keeps a valuation roll which lists all the fixed properties in the municipal area with details of the property owner and the official value of the land and building. It is important that these values are updated regularly because as the area develops and the price of the building or land changes. Therefore, the rate must be revised regularly such that if this is not done the municipality may lose out on revenue.

3.5.2 Borrowing

Section 230 (a) of the Constitution assigns powers to municipalities to raise loans in order to finance their capital budget. This is done through an external or an internal loan. An external loan is a loan from a bank or a financial service provider. This is regarded as a costly option of financing the municipalities' capital budget due to exorbitant interest rates. External loans should ideally be used only to finance the procurement or construction of large capital projects such as construction of buildings, roads, water systems and sewerage works. According to the MFMA, the municipality must publish its plans to enter into a long-term debt instrument.

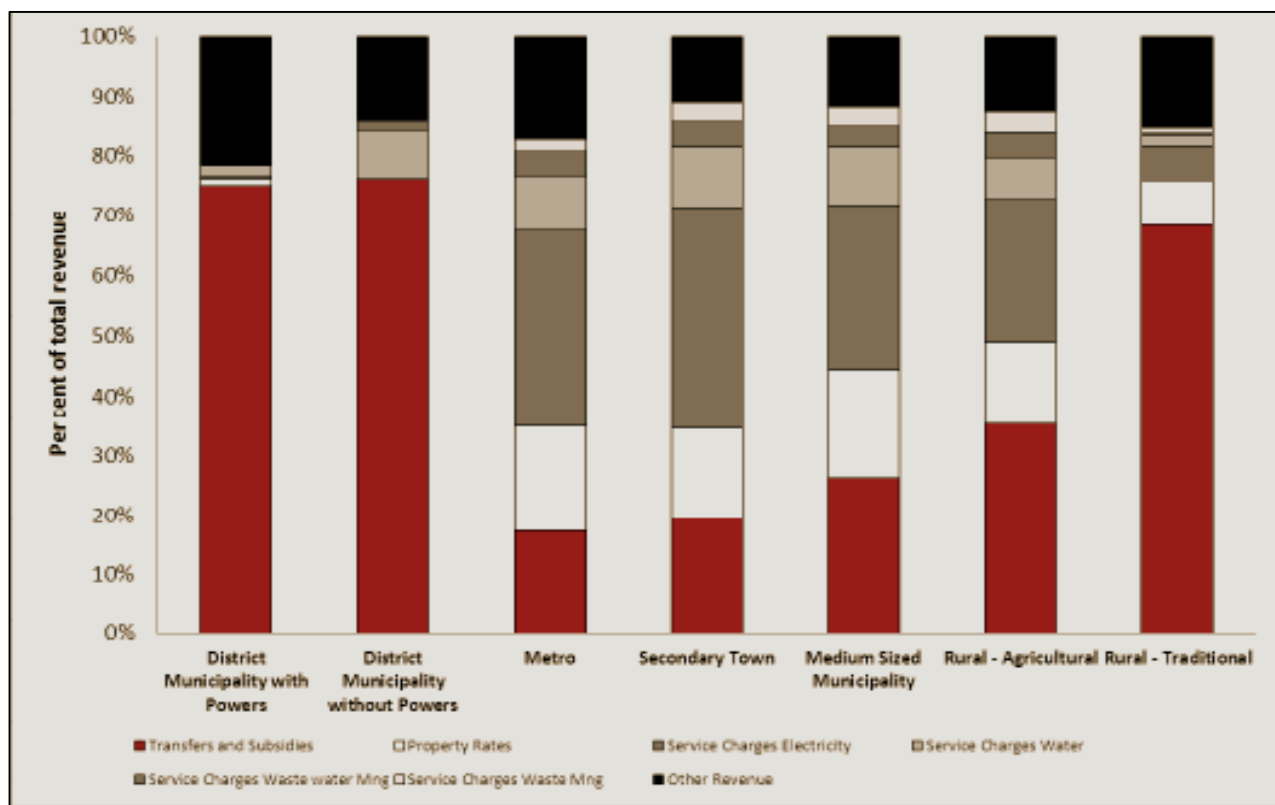
Internal loans are internal savings or funds that a municipality retains; these include Consolidated Loan Funds or Capital Development Funds. These Funds can lend internal loans to the municipality for the procurement or construction of capital items. These internal loans generally impose a lower rate of interest when compared with external loans. The municipality pays the interest back to its own savings fund which can later be used for another capital project. However, in South Africa, a significant percentage of the total municipal borrowing is focused on a few larger municipalities that are alleged to be creditworthy. Many smaller municipalities cannot access private capital owing to their balance sheets (Liebig, 2008:74). This creates a challenge for smaller municipalities, especially rural municipalities as they have a greater need for financial assistance to enable them to adequately provide services to their communities. It is observed that municipal borrowing has been declining especially since the beginning of the recession of 2008/2009 FFC (in Chitinga-Mabungu and Monkam, 2013:8).

3.5.3 Intergovernmental grants

Intergovernmental grants are one of the revenue sources for local governments. Oates (1999:112) asserts that intergovernmental grants are a unique and important policy instrument in fiscal decentralisation that can address a number of different functions. Literature emphasises three possible roles for intergovernmental grants in federal government: deterrence of spillover benefits to other municipal areas, fiscal equalisation across municipalities and a better tax system. Ncube (2013:296) states that an effective system of intergovernmental transfers is critical for poverty alleviation, reducing disparities, economic growth and overall national development.

Municipalities receive a number of intergovernmental grants to finance their operational and capital functions. Ulbrich (2011:183) states that one central function of intergovernmental grants is to balance revenue with service responsibilities among the three levels of government and across the same level of government. They are designed to encourage horizontal equalization and to reduce the resource disparities between municipal areas. According to Kenyon, (2012:4), in 2012/13, intergovernmental transfers accounted for 25% of the Fiscal Framework.

Figure 3.2: Sources of local government funding per municipal category



Source: Kenyon (2012:7)

Owing to the substantial inequalities in municipal fiscal capacities, intergovernmental grants are mostly important for indigent and municipalities in rural areas. South Africa's eight metropolitan municipalities had proposed budgets totalling R196.9 billion in 2014/15, of which 17% is funded through intergovernmental transfers. On the contrary, in the same year, 70 of the most rural municipalities had a total projected budget of R17.1 billion, 73% of which is funded by intergovernmental transfers (Republic of South Africa National Treasury, 2014 [b]:100).

3.6 Vertical and Horizontal Fiscal Imbalance

Despite decades of the fiscal decentralisation in South Africa, there is still relative control of allocation of financial resources by national government. Yemek (2005: 22) states that fiscal decentralisation in South Africa discloses two important features. Firstly, the national government is assigned a responsibility of leading and developing a strong policy framework, while local government has a critical role to meet the needs of local communities through the provision of basic services. Secondly, the allocation of revenue-raising capacity among municipalities is uneven. Brand (2007: 4) affirms this when it is stated that, in South Africa, there is a concentration of financial resources at national level while, the expenditure assignment for most public services is at the provincial and local spheres of government. The misalignment between funding and functions creates a vertical fiscal gap that requires a revenue sharing mechanism or an equalisation programme, holds Brand (2007: 4). Mahabir (2010:160) asserts that the total revenue that each municipality is expected to generate from its own sources differs significantly across the different types of municipalities.

Mahabir (2010:160) notes that such discrepancies are most likely to result in certain municipalities being able to raise enough revenues to cover or even exceed their expenditure responsibilities while others are likely not to. Another source of inequity between municipalities arises from the variances in the unit cost of providing public services (Rao, 2003:16). Economic theory refers to cases where a municipality's expenditure responsibilities exceed its own revenue raising capacity as a "horizontal fiscal gap", asserts Reschovsky (in Mahabir 2010:160). In addressing the challenge of the horizontal fiscal gaps in local government, Section 214 of Constitution makes a provision for the equitable division of nationally raised revenue to the three spheres of government. According to the Republic of South Africa National Treasury (2013:110), the process of division of revenue at national government level provides for appropriate funding for each sphere of government and accounts for the service-delivery responsibilities as well as sources of revenue assigned to

them. It is for this reason that intergovernmental transfers are pivotal component of the South African intergovernmental system to ensure that the Constitutional obligation of local government, which is to provide basic services, is achieved in addition to addressing the high degree of vertical and horizontal imbalances that exist in the assignment system. However, it is equally important to develop an appropriate design and administration of a system of intergovernmental transfers to achieve the above-mentioned objectives.

3.7 An overview of the Intergovernmental Transfer System in South Africa

The discussion above has presented the different sources of local government finance including intergovernmental grants. Literature reveals that intergovernmental fiscal transfers have been a key characteristic of public finance in a number of countries for a number of years. They are instruments used by most countries, including South Africa, primarily to address problems of fiscal balances between regions in the same level of government. The imbalances between the revenue and expenditure needs between municipalities in South Africa called for national government to provide intergovernmental transfers to municipalities with relatively low fiscal capacity and those with relatively high fiscal needs. This policy decision was to ensure that all South Africans have access to comparable levels of basic services at a reasonable cost.

Table 3.2 below displays other uses of intergovernmental transfers taken from different country examples. What is interesting from this country comparison is that even though the ultimate goal for most governments is to derive some form of equity among different regions, the element of inequality that each transfer programme addresses differs from country to country.

Table 3.2: International Practices in Intergovernmental transfers

Enable similar levels of service affordability	Equalising difference in expenditure needs as measured by indicators (e.g. population), by historical cost, or by national expenditure norms	India, Italy and Spain
Enable similar levels of fiscal resource availability	Equalising differences in fiscal capacity as measured by indicators (e.g. gross regional product per capita) or a representative revenue system	Canada
Enable similar levels of service at similar levels of taxation	Reducing the fiscal gap (equalising fiscal capacity and expenditure needs)	Australia, China, Germany, Japan, Korea, Latvia, Russia and the United Kingdom

Source: Almand Martinez-Vazquez (2009:19)

In the case of South Africa, the revenue raised by the national sphere of government, minus the contingency reserve and interest paid on state debts, is divided between the three spheres of government; this is identified as the vertical division of revenue. Vertical transfers from the national sphere are mostly implemented using two instruments: conditional and unconditional grants. The structure or form of a grant is often dictated by its purpose. For example, a conditional grant must be spent for a specific use, such as putting more police guards on the street or providing free or reduced price lunches to school children. Whereas, a pure equalisation grant such as state aid to local governments does not place many limitations on how the funds may be spent. This type of grant is referred to as an unconditional grant. The aspects mentioned briefly in this paragraph are developed more fully in the following subsections.

3.7.1 Conditional grants

Conditional grants are funds allocated from one level of government to another. They are attached to specific conditions that provide that certain services be delivered on compliance with a set of requirements (Republic of South Africa National Treasury, 2013: 203). They are allocated from national government to the provincial and local levels of government, and may only be used for the specified purposes as outlined by the transferring national department and are subject to conditions set out in the grant framework (Republic of South Africa National Treasury, 2013: 203). Conditional grants are used to meet national redistribution objectives, address inter-municipal spillovers, and ensure the implementation of set national priorities and policies linked to socio-economic services provided by local governments (Amusa *et al.* 2008:6). These grants are mainly aimed at the allocated functions such as education and health and are also used to support national priorities which include provision of housing and municipal infrastructure to poor households, and capital grants to reduce service delivery backlogs and addressing other local deficiencies. They are appropriated in the national, provincial and municipal budgets and are legislated annually in the Division of Revenue Act (Momoniat, 2001:11).

3.7.2 Unconditional grants (Equitable Share)

An unconditional grant is an equitable share from national government that enables both provinces and local government to deliver basic services and to perform functions assigned to them (Republic of South Africa National Treasury, 2011:43). Contrary to conditional grants, the equitable share may be used at the discretion of the recipient province or municipality (Oates, 1999:1107). This funding instrument is used in many countries

particularly in OECD countries and is believed to be the appropriate funding instrument for fiscal equalisation across jurisdictions by channelling funds from wealthy municipalities to poorer ones (Oates, 1999:1107). Amusa *et al.* (2008:6) state that unconditional grants that are intended to decrease fiscal inequities resulting from the misalignment of revenue and expenditure functions and to enable local governments to provide basic services and perform functions allotted to them.

In South Africa, the main unconditional grant is the LGES grant, which gives a municipality its share of nationally collected revenue using an allocation formula. The main objective of the LGES is to enable local government to provide basic services and to execute its allocated function by augmenting the revenue that municipalities can generate themselves (Republic of South Africa Division of Revenue Bill, 2014: 90). The Republic of South Africa National Treasury (2011:52) states that the LGES is designed to balance the uneven distribution of fiscal capacity among the three spheres of government and across municipalities.

The LGES is distributed using a formula which divides the equitable share (unconditional grant) among the country's 278 municipalities. This distributive process is called the horizontal division of revenue. This formula takes into account a number of factors such as the specific social, economic and institutional needs of the different municipalities (Derichs and Einfeldt, 2006:5). These allocations are not appropriated in the national budget but in the municipal budget as they are considered to be a direct charge legislated in the annual Division of Revenue Act.

Table.3.3: Division of nationally raised revenue (2010/11-2016/17)

R million	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
	Outcome			Revised estimate	Medium-term estimates		
Division of available funds							
National departments	356 027	382 712	412 706	449 251	489 424	522 257	522 983
Provinces	322 822	362 488	388 238	414 932	444 423	477 639	508 254
Equitable share	265 139	291 736	313 016	338 937	362 468	387 967	412 039
Conditional grants	57 682	70 753	75 222	75 995	81 955	89 672	96 215
Local government	60 904	68 251	76 430	83 670	90 815	100 047	105 187
Equitable share	30 541	33 173	37 139	39 789	44 490	50 208	52 869
Conditional grants	22 821	26 505	30 251	34 268	36 135	39 181	41 094
General fuel levy sharing with	7 542	8 573	9 040	9 613	10 190	10 659	11 224
Non-interest expenditure	739 752	813 451	877 374	947 853	1 024 662	1 099 943	1 166 424
<i>Percentage increase</i>	7.2%	10.0%	7.9%	8.0%	8.1%	7.3%	6.0%
Debt-service costs	66 277	76 460	88 121	101 256	114 901	126 647	139 201
Contingency reserve	-	-	-	-	3 000	6 000	18 000
Main Budget Expenditure	805 979	889 911	965 496	1 049 109	1 142 562	1 232 590	1 323 624
<i>Percentage increase</i>	7.9%	10.4%	8.5%	8.7%	8.9%	7.9%	7.4%
Percentage shares							
National departments	48.1%	47.0%	47.0%	47.4%	47.8%	47.5%	47.4%
Provinces	13.6%	44.6%	44.2%	43.8%	43.4%	43.4%	43.6%
Local government	8.2%	8.4%	8.7%	8.8%	8.9%	9.1%	9.0%

Source: Republic of South Africa National Treasury, (2014b:95)

Table 3.3 above presents the vertical division of revenue between the three spheres of government. In this division, the national share comprises all conditional grants allocated to provinces and local government in accordance with section 214(1) of the Constitution. As illustrated on the table above, the bulk of the revenue share is allocated to the national departments which received 47.8% in 2014/15. The provincial government receives the second largest allocation, (43.4%) mainly to provide for health, education and social welfare, and local government received 8.9% of the revenue share mainly to provide basic services. Local government received the least of the allocation mainly because unlike provinces, municipalities have legislated powers to generate their own revenues to augment their budget and to meet their expenditure requirements and should not be completely dependent on intergovernmental transfers as a funding source.

Local authorities are entitled to an equitable share of revenue generated nationally to empower them to deliver priority services and execute the tasks assigned to them in

accordance the Constitution. The White Paper on Local Government states that the framework for municipal finance is to be obligated to establish a system of formula-based intergovernmental grants which to include an LGES of national revenue. According to Boschmann (2009:8), transfers should be determined using a transparent and simple formula. The White Paper on Local Government further states that, the LGES will be designed in a way that empowers all local authorities to deliver a basic level of services to indigent family units within their areas of authority in an economic manner. Furthermore, the White Paper on Local Government, provides five main objectives that must be drive the process of horizontal division of the LGES among municipalities. These objectives are: probability; fairness; competence; making sure that basic administrative capacity specifically for poor local authorities and incentives for good financial management at municipal level.

In summary, the White Paper on Local Government, 1998 identifies equity as the underlying principle of the horizontal division of revenue and that the LGES should empower municipalities to provide basic services to indigent communities economically. It further notes that the second principle is effective administrative infrastructure. The system must make sure that the even the poorest local authority is empowered to establish a simple administrative structure that will enable it to administer its area in an effective manner.

It is on this basis that unconditional grants are allocated using a formula that utilises unbiased statistics so that the division cannot be subjectively influenced to benefit a specific local authority at the detriment of another. The formula takes into the account factors such as the size of the population in that municipality, as well as the number of people living below the poverty line. The LGES is the second main source of funding for municipalities. According to the Republic of South Africa Division of Revenue Bill (2013:91) over the 2013 medium term framework, the LGES, including the RSC/JSB levies replacement grant and special funding for councillor remuneration and ward committees, amounts to R135.3 billion (R40.6 billion in 2013/14, R44.5 billion in 2014/15 and R50.2 billion in 2015/16). It is founded on an impartial measure of the expenditure and needs related to the assigned functions and these components are translated into a transfer formula and are the only unconditional grant to local government designed to provide for a number of municipal functions. However, provision of free basic services is its main purpose.

The following section presents an overview of how the LGES formula has transformed since its inception in 1998 until the 2012 when the current formula was introduced. The

discussions will also provide challenges with previous formulae and how the current LGES formula has attempted to address these challenges.

3.8 Evolution of the Local Government Equitable Share Formula

The original LGES formula was introduced in 1998. However, over time many of the formula's components were no longer applicable to the then context of local government as they had been when the formula was initially introduced. The constant alterations in the organisation of local government necessitated the two comprehensive LGES reviews which were conducted in 2004 and 2012.

3.8.1 Local Government Equitable Share formula (1998-2004)

As mentioned above, the sharing of nationally raised revenue with local government commenced in 1998. The government made a decision to use a component based formula to allocate the local equitable share (Mahabir, 2010:161). The author further notes that this formula took into consideration the service, development and backlog expenditure need of the municipalities. The formula was based on demographic and service data which was transparent, objective and independently collected by StatsSA. The original formula comprised four separate formulae namely:

- basic service grant (funded the provision of basic services to poor households);
- tax base equalisation grant (reduce disparities within a municipality);
- municipal institution grant (funded the basic administrative and political structure of the Municipality and;
- matching grant (promote positive externalities across municipalities)

According to Mahabir (2010:161), in the 1998/9 financial year, the basic services and the municipal institutional grants were used to allot funding. The tax-based equalisation and the matching grants were not applied and as a result, were taken out of the formula as the former became obsolete owing to modifications in the organisation of metropolitan municipalities while the latter grant could not be implemented owing to the absence of a reliable measure for inter-municipal externalities (Republic of South Africa National Treasury, 2012:3). Accordingly, it was the basic services grant and the municipal institution grant that determined the bulk of the horizontal allocations in the period between 1998 and 2004.

This was called the “window” approach since the funds for each component were allocated using different formula mechanisms (Republic of South Africa National Treasury, 2012:3). The window approach continued to fund the shifting of former R293 towns from provinces to municipalities in their former homelands. It was also used to provide additional funding for additional personnel subsidies to R293 towns. Following the implementation of government’s policy on the provision of free basic services to poor households, additional funding was allocated for these services using the “window” approach. Republic of South Africa National Treasury (2012:4) states that, at the end of 2004/5 there was a total of six different windows (R293 allocations, S-grant, I-grant, nodal allocations, free basic services and free basic electricity/ energy). Each of these windows had its own structure.

3.8.1.1 Challenges with the Local Government Equitable Share formula (1998-2004)

There was a general concern from a number of stakeholders with the “window” approach to funding municipalities, particularly the Financial Fiscal Commission (FFC). The numerous funding windows in the formula were said to be inefficient and needed to be removed. The windows created complication in their implementation and their objectivity was reduced (Republic of South Africa National Treasury, 2013:7). Stakeholders raised concerns regarding the formula not being transparent and simple enough to examine (Republic of South Africa National Treasury, 2013:7). The number of windows also continued to increase as local government transformed. This meant that the structure of the formula was not flexible enough to incorporate the changes that were being implemented in municipalities. It was for these reasons that the FFC, among other stakeholders, called for a robust, impartial and transparent measure of fiscal capacity that would improve the equalisation framework and redistribution in the formula. National Government accepted that there were many flaws in the formula and that it needed to be improved. As a result, the formula was used for the last time to allocate the LGES in 2004/05 (Republic of South Africa National Treasury, 2012:4). Thereafter, a comprehensive review of the formula was conducted which resulted in a new LGES formula being introduced in 2005.

3.8.2 Local Government Equitable Share formula (2005-2012)

The new LGES formula introduced in the 2004/5 financial year was to address the shortcomings of the original 1998 LGES formula. The new formula took the following four important aspects into account to ensure that the LGES supports the municipalities’ capacity in providing services: a) provision for basic services and other municipal functions assigned to them; b) fiscal capacity and fiscal efficiency of municipalities; c) developmental needs of municipalities; and d) the degree that information is accessible, the extent of backlogs and

poverty in municipalities (Amusa *et al.* 2008:6). These key factors were translated into the five components constituting the structure formula:

- Basic Services Component (BS) - for the provision of basic services;
- Institutional Component (I) – for the provision of fiscal capacity and efficacy of local authorities;
- Development Component (D) – for the provision of the priority and other requirements of local authorities;
- Revenue Raising Capacity Correction Component (RRC)- for the provision of fiscal capacity and efficiency for local authorities and;
- Correction and Stabilisation Factor (C) - for stability and predictability of allocations of revenue shares.

(Republic of South Africa National Treasury, 2012:30)

The five components were used to formulate the LGES formula, and it was structured as follows:

$$LES = BS + I + D - RRC \pm C$$

The total of the *BS*, *I* and *D* components measured the expenditure needs of a municipality for provision of services. The *RRC* component measured the fiscal capacity of a municipality, the difference of which constituted the fiscal gap that the LGES was to fund (Mahabir, 2010:163). The *D* component of the formula was inactive and did not contribute to the allocation of grants to municipalities. It was introduced into the formula mainly to respond to provision in 214 (2) (f) of the Constitution, which sets that *an Act of Parliament must take into account the developmental and other priorities of provinces and municipalities*. However, government and other stakeholders could not agree on how or what should be measured and subsequently funded through this component.

This LGES formula did not allocate funds to all municipalities such that they balance back to the total amount allocated to municipalities through the vertical division of revenue (Republic of South Africa National Treasury, 2012:11). Therefore, to ensure that all available funds were allocated through the horizontal allocation, the formula allowed for an adjustment factor to be applied. According to Republic of South Africa National Treasury (2012:11), the

simplest way to ensure that the system balances was to rescale the *BS*, *I* and the *D* components to the available budget. Thus, the formulas then became:

$$LES = \text{Adjustment Factor} \times (BS+I+D) - RRC \pm C$$

This rescaling had a significant effect on the size of LGES allocations. For instance; in the 2012/13 financial year, the value of the adjustment factor was 4.95 which implied that the allocations in the *BS*, *I* and *D* components were multiplied approximately five times before having the *RRC* and *C* components applied to them.

Table 3.4: Average LGES allocation per component for each type of municipality

Metros	1 422 677	27 469	-220 472	-328	1 229 346
Secondary cities	233 304	12 809	-10 520	-63	235 530
Large towns	78 963	8 992	-3 400	-23	84 532
Small towns	39 048	5 936	-570	-12	44 402
Rural municipalities	82 142	12 206	-78	-25	94 245
Unauthorised districts	13 682	8 549	-6 022	387	16 596
Authorised districts	232 299	11 245	-4 070	-64	239 410

Republic of South Africa National Treasury, 2012:11

Table 3.4 above depicts that the bulk of the allocation in the 2012/13 financial year is under the *BS* component, with metropolitan municipalities receiving the biggest allocation. The Unauthorised District Municipalities receive the least allocation based on the formula, mainly because they are not authorised to perform some of the basic services functions such as sanitation and provision of water. Accordingly, their *BS* component will be relatively low. The *D* component does not appear on the Table above, owing to this component being inactive and accounts for 0% of allocations. It is also for this reason that it has not been included in the equation.

3.8.2.1 Challenges with the Local Government Equitable Share formula (2005-2012)

Despite the use of the 2004 formula to allocate funding to municipalities for almost a decade, there were a number of apprehensions regarding its inappropriateness and particularly its shortfall in addressing the needs of municipalities and their communities. Accordingly, CoGTA, SALGA, FFC and selected municipalities called for a review of the 2004 LGES formula to address deficiencies that had been identified over the period between 2004 and 2012. The common deficiencies identified in the 2004 formula are as follows:

- Availability of current data - the Census information collected by StatsSA is not completely consistent due to *inter alia*, the frequently fluctuating migration patterns, the large number of informal settlements and the high levels of poverty and illiteracy;
- The alignment of the composition of the formula to the legal and theoretical principles were not indicative of the national policy priorities;
- The formula was technically ineffective at ensuring that the needs of different municipalities were accounted for;
- The existing range of municipal services that were funded using the formula were not aligned to the Constitutionally mandated basic services; and
- The formula did not adequately account for the larger fiscal capacities and revenue-generation capacities of metropolitan municipalities and other municipalities in urban areas, so that the LGES allocation is shared and distributed equitably.

CoGTA (2009:58) and Republic of South Africa National Treasury (2012:30)

The challenge for National Government has been its inability to strike a balance between a suitable LGES formula that takes into consideration the developmental needs of local government and a formula that will not reduce the ability of these municipalities to generate their own revenue. This point is one of the focal points of this research study.

Boschmann, (2009:8) mentions that the experience of numerous countries has revealed that the design of an equalisation formula that is perfect is an impossible task. As cited in the earlier discussions, the South African intergovernmental fiscal framework has also had its fair share of challenges in this regard. It has been almost impossible for a simple allocative formula to take all the country's needs into account, while intricate formulae are challenging to understand. Furthermore, efforts in undeveloped states have revealed that even simple formulae may still depend on current data, which is always difficult to produce (Boschman, 2009:8). Another challenge in South Africa is the substantial increase in intergovernmental transfers in the period between 1998 and 2012 while own revenue generated is declining thus creating grant dependency in many municipalities.

The stakeholders (CoGTA, SALGA and the FFC) recommended for a Review of the 2004 LGES formula and for the creation of a new formula that will effectively respond to the contemporary needs of local government, and one that will not create dependency on national government transfers. Again, this important point is integral to fiscal capacity and sustainability for municipalities in the current dispensation. There is agreement between

officials that the guidelines of a grant systems must be transparent and clear, and must inspire behaviour that is consistent with good management practices and incentivise good fiscal performance and discourage municipalities from remaining poor and transfer dependent.

3.8.3 Local Government Equitable Share formula 2013

In response to the concerns raised by the stakeholders and other fiscal experts National Treasury, CoGTA and SALGA, with the assistance of the FFC and StatsSA, conducted a review of the LGES formula in 2012. The aim of the review was to introduce an improved structure for an LGES formula for use in the 2013 Budget. However, the review did not comprise an evaluation of the RSC/JSB charges replacement grant or the special support for councillor compensation and ward committees, which are both allocated with the LGES, but assessed independently (Republic of South Africa National Treasury, 2013:92).

The 2012 LGES Review involved a series of engagements and consultations with municipalities and other relevant stakeholders. This consultative process was done in three phases and involved presentations, workshops and two comprehensive discussion papers presented to municipalities. The proposed structure of the formula was authorised by the Budget Forum in October 2012. Thereafter, the Review team developed a new formula utilising data from the 2011 Census. This new formula was used for the first time in the 2013 Budget.

The main objectives for the new formula as endorsed by the Budget Forum are to:

- *Empower local authorities to deliver basic services indigent households*

The LGES should supplement municipal own revenue collection to enable the municipalities to increasingly deliver free basic services to indigent communities consistent with policy, regulations and standards set nationally. It should promote efficient provision of services, promote alternative approaches to service delivery and create positive benefits for local authorities that deliver services to reach a greater number of family units (Division of Revenue, 2013:93).

- *Enable municipalities with limited own resources to perform core municipal functions and meet the expense of basic administrative and governance capacity*

The LGES should provide funding to enable municipalities with low fiscal capacity to afford a basic level of governance and administrative capacity and to allocate funds for costs relating to performing critical functions in municipalities with limited own-revenue sources. Furthermore, the LGES should account for the capacity of some local authorities to cross-

subsidise the provision of administrative and other important municipal services using their own income, consider the diverse fiscal capacities in local authorities and ensure that allocations do not impede the municipality's own-revenue-raising efforts (Republic of South Africa Division of Revenue, 2013:93).

The new formula is based on the following principles. The LGES formula must:

- Be transparent and simple
- Be fair and objective;
- Account for inequality between municipalities;
- Use only good quality, credible and verifiable data;
- Be dynamic and able to responsive to changes; and
- Provide for stability and predictability.

These principles resonate with the principles of good governance and are underpinned by the White Paper on Local government which advocates transparency and accountability in the process of resource allocation.

Contrary to the 2004 formula, the current formula comprises three parts which are made up of five components discussed below.

Table 3.5: Design of the South African Local Government Equitable Share Formula

Basic Services (BS)	provides for the cost of free basic services for indigent households	2011 Census
Institutional component (I)	offers a subsidy for basic municipal administrative expenses.	Department of Cooperative Governance and Traditional Affairs
Community Services (CS)	provides core municipal services that are not included under basic service component	n/a
Revenue Adjustment (RA)	makes sure that funds from this component of the formula are only channeled to local authorities with inadequate fiscal capacity	2011 Census
Correction and Stabilisation (C)	makes sure that all of the formula's assurances can be achieved	n/a

Source: Republic of South Africa National Treasury (2013:92)

The **basic services component** share is determined by multiplying the monthly subsidy (R275.17 per household per month, including R27.5 for maintenance) by the sum of family units that fall below the affordability threshold in each local authority (CoGTA, 2012: 3). This component only includes indigent households in the calculation as households that fall above the affordability threshold must be empowered so that they are able to pay for their own basic services. Funding for each service is distributed to the local authority that is authorised to provide that service (Republic of South Africa National Treasury, 2013:92).

Figure 3.3: Breakdown of the basic services component



Adopted: from Republic of South Africa National Treasury, 2013:92

The **institutional component** entails of a base allocation of R5.3 million, which is allocated to each of the 278 municipalities and an additional amount that is determined by the size of the municipality's administration (Republic of South Africa Division of Revenue Bill, 2014:94). This component is not designed to completely provide for the administrative expenses of local authorities but provides for basic administrative costs. The formula uses the sum of council seats in each local authority as a base for the size of administration for each municipality.

The **community services component** provides funding for municipal graveyards, health services, municipal infrastructure, fire services, planning, storm water management, street lights and parks (CoGTA, 2012:3). Similar to the institutional component, this component is not planned to entirely provide these services. The formula applies a revenue adjustment factor to this component so that a greater share of the allocation is allocated to municipalities with less revenue potential. The community services component is calculated as follows: $CS = [\text{municipal health and associated services provision} \times \text{sum of households}] + [\text{other services allocation} \times \text{sum of households}]$.

The **revenue adjustment factor** is applied to the institutional and community services components of the formula to guarantee that funds are channeled towards local authorities

that have the smallest revenue potential and are able to provide for these functions using their own income. This is achieved through the creation of a capita index that accounts for the following elements: Sum of earnings of all residents or family units in a local authority (as an index of revenue and economic activity), recorded property prices, sum of family units on traditional land, proportion of unemployment, sum of indigent family units as a proportion of the sum of family units in the local authority. Municipalities are ranked using this index to determine the size of their revenue adjustment factor which ranges between 0% and 100%. The revenue adjustment factor is not designed on the real revenues collected by municipalities. This component is not intended to create any perverse incentive for municipalities to collect own revenue below its potential to receive a higher equitable share (Republic of South Africa Division of Revenue Bill, 2014:94).

The **correction factor** is a general stabilisation and correction factor.

The formula is a combination of all these components, and is structured as follows:

$$LGES = BS + (I + CS) \times RA \pm C$$

There are a number of similarities between the current LGES formula and the 2004 formula. The *BS*, *I* and *C* components were present in the 2004 formula and have been included in the current formula. However, there are also significant changes that have been effected to the formula. For example, the previous formula subtracts the *R* component from the overall formula, but the new LGES formula factors a *RA* factor to the *I* and the *CS* components only. There is also an addition of a *C* component which was not present in the previous formula. The *D* component has also been removed in the new formula as it was never activated in the previous formula and therefore did not contribute to the allocations (Republic of South Africa National Treasury, 2013:92).

3.9 Conclusion

The change in South African politics and the democratisation of the state in 1994 formed a basis for transformation in the public administration of the day. The change in government provided the new administration an opportunity to restructure and implement key reforms aimed at addressing the inequalities resulting from past policies and improving the delivery of services to communities. The advancement of the South African public administration is captured in the Constitution which decentralised government by establishing three levels of governments and prescribing a set of principles within which these three spheres should work together to improve lives of citizens through the provision of effective and efficient services. This significant change in the organisation of government necessitated transformation in governance structures and approach. Transformation in local government

has not come without challenges. The imbalances between different municipal areas have persisted despite twenty one years of redress. To address these disparities government has reviewed its funding instrument to local government and introduced a new local government redistributive mechanism. The study therefore investigates the appropriateness of this redistributive system in addressing the needs of local communities in the fuller context of local government.

CHAPTER FOUR

RESEARCH DESIGN AND METHODS

4.1 Introduction

The validity of the knowledge generated from a research study is dependent on its methodology, that is, the manner in which data is collected (Leedy and Ormrod, 2005:93). Research methodology is a procedure by which an investigator uses in explaining, clarifying and envisaging a phenomena (Rajasekar, Philominathan and Chinnathambi, 2013:5). This chapter provides a discussion on the methodology employed in the study. The chapter commences with a summary on the significance of the study which is followed by an explanation of the philosophical worldview underpinning the study. The third section provides a discussion on the different research methods and an explanation for selecting mixed methods employed in this study. This section will be followed by a discussion on the data gathering techniques used in the research and how the information was analysed. Following this, the chapter will provide a discussion on the ethical issues that had to be taken into account during the course of the study and the limitations of the study. The last section of this chapter presents the conclusion.

4.2 Significance of the Study

Local government is the key location for delivery of government services and is therefore fundamental to government's priority of improving of the quality of life of all South Africans. Hence, this study is relevant for a number of reasons. Firstly, the growing number of service delivery protests has brought significant attention to local government and has evoked conflicting views on the local government fiscal framework and its ability to provide adequate resources for the provision of basic services. Secondly, the National Treasury has recently completed an evaluation of the LGES formula and introduced a new formula which was implemented in the 2013 National Budget. This study provides primary feedback on the appropriateness of this new formula in addressing the challenges of service delivery in municipalities, as well as the perception and attitudes of the relevant government stakeholders on the structure of the new formula. Lastly, this research study will add to the well of knowledge relating to the use of formula-based resource allocation as a mechanism for equitable resource sharing in government, deemed a focal point in addressing fiscal capacity challenges in municipalities. It will also be a significant addition to the literature on local government financing of the sub-field of Local Government Management and Development within the study of Public Administration and Governance.

4.3 Philosophical Worldview

Mouton (in Wessels, 2010:534) argues that a researcher’s selection of a research methodology is determined by a particular research ideology defined as a means of understanding the world or a philosophical worldview. Creswell (2009:6) contends that a philosophical worldview is a set of conventions about how the researcher will know and what they will know during the enquiry. Creswell (2009:6) further advances the view that there are four paradigms in which knowledge claims can be characterised namely: post positivism, constructivism, and advocacy or participatory and pragmatism. Table 4.1 displays these four paradigms and their definitions.

Table 4.1: Research Paradigms

Experimental	Realistic	Critical theory	Mixed methods
Semi-experimental	Phenomenological	Neo-Marxist	Mixed models
Correlational	Hermeneutic	Feminist theories	Participatory
Causal comparative	Symbolic interaction	Critical race theory	
Quantitative	Ethnographic	Participatory	
Randomised control trials	Qualitative	Emancipatory	
	Participatory action research	Postcolonial/indigenous	
		Queer theory	
		Disability theories	
		Action research	
		Critical theory	

Adapted from: Wessels (2010:534) and Creswell (2009:6)

The paradigm or philosophical worldview underpinning the study is the pragmatic paradigm. The pragmatic worldview believes that claim to knowledge is a result of actions, conditions and consequences rather than originator conditions (Wessels, 2010:534). Instead of concentrating on methods, the researcher emphasises the research problem and uses all methods obtainable to gain knowledge on the problem. This worldview is a philosophical basis for mixed methods studies and articulates the significance of focusing attention on the research problem and then using multiple methods to develop knowledge about the problem (Creswell, 2009:10).

Figure 4.1 below illustrates the characteristics of a pragmatic worldview.

Figure 4.1: Features of the pragmatic worldview



Adapted from: Creswell (2009:6)

4.4 Research Design

The preceding section provided a discussion on the philosophical worldview underpinning the study. Creswell (2009:5) contends that the philosophical worldview of the researcher influences the choice of research design used in the study. The study used mixed methods which combines both qualitative and quantitative methods in research. Du Plessis and Majam (2010:456) state that mixed methods signifies a research method that comprises gathering, examining, and interpreting qualitative and quantitative information in one study or a sequence of studies that explore one fundamental phenomenon. It includes a variety of theoretical assumptions, philosophical paradigms, methodological traditions, data collection and analysis methods and adapted considerations and value commitments Greene (in Du Plessis and Majam, 2010:456).

Greene, Cradelli and Graham (in Du Plessis and Majam, 2010:469) highlight the following elements as explanations for using mixed methods in research:

- *Triangulation*- pursues corroboration, convergence and correspondence of findings from using different methods;

- *Complementary*- pursues improvement, explanation, design and clearing up findings from one technique with the results from another technique;
- *Development*- utilises findings from one technique to assist, inform or develop the other technique, where development is largely interpreted to consist of sampling and implementation and quantifying decisions;
- *Initiation*- pursues to determine the inconsistencies, the reorganising of questions or findings from one technique with questions or findings from another technique; and
- *Extension*- tries to widen the degree and extent of the investigation by utilising a range of methods for variable investigation elements.

Cakata (2011:3) argues that the main strength of using mixed method in research is that it allows research to advance in a more holistic manner when compared to a single method where the area of investigation is less likely to be limited by the method itself. Du Plessis and Majam (2010:457) state that the strengths of individual methods are utilised to overcome the shortcomings of the other to enhance and deepen the research of a phenomenon. Therefore, the use of mixed methods design was appropriate for this research as it allowed the researcher to use multiple sources of data (primary and secondary) to investigate the complex research question. The objective of the research was to investigate appropriateness of the current LGES formula in fiscally capacitating municipalities, such that they are capable of delivering basic services to communities. This objective could not have been addressed by using either a qualitative or a quantitative method alone; hence the decision to combine the methods. The study did not only rely on documented secondary data from the National Treasury local government databases, but considered the views of officials who work closely with the subject matter which were obtained through the use of questionnaires. Employing this strategy, allowed for the study to gain a more holistic insight into the subject matter.

4.5 Sampling

Sampling is explained as choosing a specific section of the population, in a study area, which will be a representation of the entire population (Yulianti and Tung, 2013:104). Barreiro and Albandoz (2001:4) state that there are different methods in research used to select a sample from a population. The two main sample designs used in research are probability and non-probability. In the probability design the selection process indicates that each unit in the population has a fair and independent probability selection. The main methods used to select a sample in this design are: simple random, stratified random, cluster and systematic (Creswell, 2009:217). In the non-probability design, the elements are

selected using non-random methods. The three main methods used to select a sample using non-probability design are: convenience, quota and purposive.

The study used non-probability design and purposive sampling method. In this sampling procedure, specific participants from the population who are experienced in the key concept being explored for the research are recruited or selected (Creswell and Clark, 2011:173). This method was employed mainly to ensure that the participants work directly with the LGES and have an in-depth understanding of the composition of the LGES formula and its allocative function. Accordingly, a sample was selected purposefully and focused on officials in supervisory and management positions who interact with the LGES and that were able to provide an informed opinion of this funding mechanism whilst addressing the research questions.

A sample of 113 senior, middle and lower level managers was drawn from a population of 124 from the National Treasury, Msunduzi Municipality and the SALGA. Table 4.2 below provides a breakdown of the population and sample per institution, division and management level.

Table 4.2: Sampling per Institution and Employment Category

Institution	Target group	Population Size	Sample Size
Msunduzi Municipality	Senior , middle and lower level managers (Finance unit)	67	60
SALGA	Senior , middle and lower level managers (Intergovernmental Relations and Municipal Finance units)	21	18
National Treasury	Senior , middle and lower level managers (Intergovernmental Relations unit)	36	35
Total		124	113

All 113 participants were informed prior to their participation in the study that their involvement was on a voluntary basis, and that they had a right to withdraw their involvement at any given time during the course of the research. Their confidentiality was protected throughout the different stages of the study.

4.6 Data Collection Tools

As mentioned in the preceding discussion, the mixed methods research design was used in the study. Accordingly, qualitative and quantitative methods were used to collect data. The study used two data collection tools; questionnaires for the collection of empirical data and documentation for gathering secondary data. These two data collection methods are discussed in more detail in the section below.

4.6.1 Documentation

The qualitative data collection tool employed in the study was documentation. This process of data collection entailed an examination of literature with the aim of exploring information on the current LGES formula. In this regard, a variation of literature, document, reports, published and applied findings were utilised, specifically the recent discussion documents compiled by the National Treasury and CoGTA on the recent review of the LGES formula. In addition, data reviewed also includes; notes, policies, legislation, circulars and journals which were used in the data analysis stage.

Using data from the National Treasury's municipal budget database, an analysis of the growth and distribution of the LGES allocation between 2002 and 2013 was undertaken. This data was used to assess the changes in the LGES formula influencing the growth and distribution of the equitable share to municipalities over a 10 year period. Yin (2009:103) cites that documents play an explicit role in data collection and are important in any data collection plan to corroborate and augment evidence of effective resource utilisation.

4.6.2 Questionnaires

An empirical approach was used to determine the acceptability of the new LGES formula by municipalities using Msunduzi Municipality as a case study. A questionnaire of structured closed-ended questions was used to gather data from a purposefully selected sample. Auriacombe (2010:478) argues that structured questionnaires have little flexibility as respondents are given several questions accompanied with a number of possible answers from which to select. However, structured questionnaires are often used in research as they are understood to enhance data quality by reducing measurement error. This view is supported by Babbie (in Creswell, 2009:10) who cites that the standardised nature of questionnaires allows for more accurate measurements, and data collected from different participants can be interpreted comparatively.

With regards to this study, three sets of questionnaires were developed and customised for each of the institutions participating in the study (National Treasury, CoGTA and SALGA). Similar to many questionnaires, the questionnaire for this study made use of the Likert scale to measure responses. The Likert scale had five levels: strongly agree, agree, neutral, disagree, and strongly disagree. This type scale was primarily used to measure intensity of the respondents' views towards specific statements. Although the questionnaires were customised for each individual institution, there are specific questions that are similar across all three questionnaires which were developed strategically to be used for triangulation purposes. In addition specific theoretical statements were included in the questionnaires to determine whether the empirical data confirms the theoretical data collected during the literature review.

Prior to distribution of questionnaires to the purposefully-selected sample, the questionnaires were reviewed by a statistician and several other people. This was done to eliminate errors; link statements to the research objects and research questions; and to evaluate the correctness of the scales used. The feedback provided from the review process was used to enhance the questionnaires ensuring that the statements and scales used in all three questionnaires are appropriate for providing answers to the research questions and addressing the research objectives.

Following this empirical reasoning, a total of 113 questionnaires were distributed manually and electronically to all three participating institutions. Each questionnaire was accompanied by a cover letter and an informed consent form. The cover letter introduced the researcher, described the purpose of the questionnaire, requested a response from the participant, provided assurances of confidentiality and an estimated time it will take to complete the questionnaire and appreciation for the respondent's time was expressed in the cover letter. The informed consent form was for participants to sign before they complete the questionnaire. The form assures the participant's rights to confidentiality during the course of the study. Completed questionnaires (electronic and hard copies) received were recorded, scanned and saved as an electronic file and a hard copy was also stored. The return rates among respondents were also recorded on a regular basis to monitor the progress on data collection.

4.7 Ethical Considerations

Hesse-Bieber and Leavey (in Creswell, 2009:87) state that researchers need to identify the ethical issues that may arise during their studies. Schurink, (2010:432) cites that practical ethics captured in ethical codes can be utilised as a guide to do ethical research. These ethical considerations include the following:

- Respecting the interests and rights of the individuals participating in the research;
- Contributing to new knowledge in the area of study and towards problem solving;
- Does not do harm when intruding into a participant's personal space; and
- Qualifying the significance of the research.

These guidelines were taken into account when approaching this study. Prior the commencement of the study, formal letters were written to each of the three institutions that had been selected to participate in the study. The objective of these letters was primarily to request for permission to access the relevant units within the institutions for purposes of data collection. The letters were also used to introduce the researcher, the purpose of the study and the relevance of the institution's participation in the study. Data collection did not commence until all three institutions had responded in writing granting permission for the researcher to conduct research in the identified sites.

Furthermore, the researcher had to obtain ethical clearance from the University's ethics committee before commencing with the study. This process included submitting a research proposal, copies of the questionnaires to be used in the study and gatekeepers letters from all three institutions participating in the study confirming their participation and granting access to the research sites. Following this, the application to conduct the study was granted full approval by the ethics committee and an ethical clearance certificate was issued. This gave the research permission and data collection could commence.

As mentioned in the preceding section, through the cover letter, all participants were informed prior to their participation in the study that it is purely on a voluntary basis, and that they are free to withdraw their involvement at any given time throughout the course of the research should they wish to do so. In addition, the letter assured the participants that their anonymity and confidentiality would be protected throughout the different stages of the study. All information gained from the research was treated with caution and the study strictly adhered to confidentiality and anonymity.

4.8 Data Analysis

In mixed methods research, analysis of data comprises individually studying the qualitative information applying qualitative approaches and the quantitative information applying quantitative approaches (Creswell and Clark, 2011:203). These authors further state that, there are a variety of analytical techniques that a researcher can use to represent, interpret and validate the data and results.

The challenge with analysing qualitative data is that it is unstructured and raw as it is collected from multiple sources with varying depths. Therefore, the starting point was to create a database which was used to store all collected and reviewed data. The data was labelled according to each participating institution. The next step was to organise and index the data such that data with common themes are grouped together for systematic analysis and comment. The various themes were colour coded to create a collage of themes that emanate from the data to highlight the statistical significance.

In the data analysis process, the completed questionnaires were evaluated and errors in the entries were eliminated. This was followed by converting the raw data into a scientific format using the statistical software. This process included creating and assigning numeric values for each of the 5 possible answers (on a Likert scale) in the questionnaires. This data was then computed into a Statistical Programme for Social Sciences (SPSS) for analysis. Cronbach's Alpha was applied to examine the reliability of design and data for statistical significance.

4.9 Limitations of the Study

The scope of the research was to assess the appropriateness of the current LGES formula for fiscal capacity of municipalities to provide basic services with particular reference to Msunduzi Municipality. This meant that the study was limited to Msunduzi Municipality, and did not extend to the rest of the municipalities in the province and the country. Therefore, the findings could not be generalisable; however similar studies could be replicated and extended to other municipalities to determine the full extent of the appropriateness of the LGES formula for fiscally capacitating municipalities in South Africa through further research.

4.10 Conclusion

This chapter has explained the research methodology that was employed in this study. It provided details on how the study was conducted and the research instruments that were used to collect and analyse data. The chapter began with a discussion on the philosophical worldview of the researcher which formed a foundation for which the study is premised. The philosophical worldview underpinning the study is a pragmatic approach which informed the research design employed in the study, which was a mixture of both qualitative and quantitative approaches. To collect data, the study used documentation and questionnaires. The questionnaires were distributed to a purposefully selected sample of officials working at the National Treasury, CoGTA and SALGA. The chapter provided an explanation on the ethical issues that were accounted for during the data collection process. Before the conclusion, the chapter highlighted the limitations of the study.

CHAPTER FIVE

FINDINGS AND ANALYSIS OF DATA

5.1 Introduction

The chapter presents results and discusses the findings obtained from the questionnaires in this research study. The questionnaire was the main data collection tool used and was dispersed to officials at the Msunduzi Municipality Finance Unit, SALGA and the National Treasury. The purpose of this study was to evaluate the appropriateness of the current LGES formula in fiscally capacitating local authorities to provide basic services to indigent communities. The objectives of the research were to:

- Examine the alignment of the LGES formula to the values defined in the Constitution and the White Paper on Local Government;
- Determine if the current range of goods funded through the LGES formula reflects the Constitutionally mandated basic services;
- Investigate the extent to which the formula accounts for the fiscal capacity of the Municipality; and
- Examine the extent and acceptability of the new formula by the Municipality; and Recommend areas in the formula that can be further improved

The information gathered from the responses was studied using the version 22.0 of the Statistical Package for Social Scientists (SPSS). The results are presented in graphic statistics using tables and graphs to illustrate qualitative data that was gathered. Inferential methods used in the study include Chi-Square Test values and correlations which are deduced utilising the p-values. There were three categories of respondents: namely, National Treasury, SALGA and Msunduzi Municipality. The results are presented analysed, and interpreted according to these categories using thematic analysis.

The chapter commences by presenting an overview of the sample and research instrument and the reliability of the study. This section is followed by a presentation, analysis and explanation of the results for the three institutions under the sub-themes: Practical Context; Principles and Structures of the LGES and The LGES formula and Service Delivery. The chapter will conclude by providing a summary of the findings in relation to the above-mentioned sub-themes.

5.2 Sample

Table 5.1: Response Rate

Organisation	Sample	Number of Respondents	Response rate
National Treasury	35	28	80.0%
SALGA	18	9	50.0%
Msunduzi Municipality	60	39	65.0%
Total	113	76	67.3%

In total, 113 questionnaires were distributed and 76 were returned which gave a 67% response rate. Babbie and Mouton (in Maharaj-Sampson and Ferreira: 2015:126) state that a response percentage of 50% is acceptable for analysis and reporting. Thus, a response level of 67% is sufficient for the analysis of this research. However, it should be noted that the response rate was lower than anticipated mainly because of the unavailability of senior managers at Msunduzi Municipality. Questionnaires were also emailed to managers to complete at their convenience. However, despite follow up emails and calls, a number of them did not respond. Other exogenous factors that impacted on the response rate are vacancies within the targeted units as well as staff being on leave during the period of data collection.

5.3 The Research Instrument

The questionnaire contained 62 statements, with a degree of measurement at an ordinal or a nominal level. The research tool was split into 4 distinct segments which measured several research themes as shown below:

Section A: Biographical Data

Section B: Practical Context

Section C: Principles and Structures of the Equitable Share Formula

Section D: The Equitable Share Formula and Service Delivery

5.4 Reliability Statistics

Reliability and validity are the two most central traits of precision. Reliability is calculated by capturing numerous measurements on the same thing. A reliability coefficient of 0.70 or more is seen as “acceptable”.

Table 5.2 below shows the score of Cronbach's Alpha for the items that were in the questionnaire.

Table 5.2: Reliability Statistics

	Number of Items	Cronbach's Alpha
B2	3 of 6	0.741
B3	6 of 6	0.687
C1	15 of 15	0.868
C2	2 of 3	0.914
D1	5 of 7	0.566
D2	3 of 3	0.884

The reliability scores for all sections, except D1, approximate the suggested value of 0.700. This shows a significant overall level of acceptable, constant scoring for the different sections of the study.

5.4.1 Factor Analysis

Factor analysis is a statistical technique with data reduction as its key objective. It is normally utilised in survey based studies, where the researcher wants to present a range of statements with a lower quantity of hypothetical factors. An example of this is when as part of a survey conducted at national level on political perceptions and views, respondents can respond to three different questions relating to an environmental policy, indicating issues at the national, provincial and local government level. Each question, individually, would not be an adequate measure of opinions on the environmental policy. However, when combined they may provide a better measure of the perceptions. Thus, this type of analysis may be applied to find out if the three measures actually measure one object. If they do, then they can be joined to develop a new element, a factor rating element that encompasses scores of every single participant on the factor. These techniques are suitable in a number of circumstances. For example, a researcher may wish to understand the expertise required to be a soccer player may be varied as numerous events, or if a small number of important skills are required to be prosperous soccer player. One must not trust that variables are there to conduct a factor analysis however, in reality variables are typically interpreted, named, and acknowledged as real.

Before the matrix tables, is a table that presents the findings of the Kaiser-Meyer-Olkin (KMO) and Bartlett's Test. The condition is that the KMO Measure of Sampling Adequacy must be more than 0.50 and Bartlett's Test of Sphericity less than 0.05.

In all cases, the requirements of the measure were met which permits for the factor analysis process. Some elements are split into smaller variables. The details of this are explained in relation to the study using the rotated component matrix below.

5.4.2 KMO and Bartlett's Test

Table 5.3: Results of Kaiser-Meyer-Olkin and Bartlett's Test

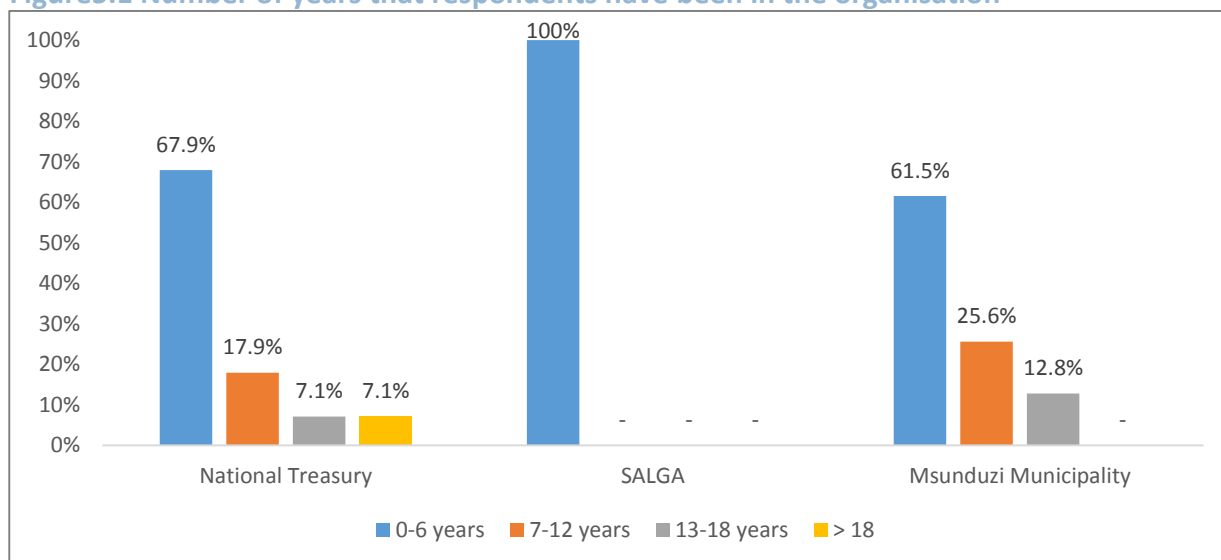
	Kaiser-Meyer-Olkin Measure of Sampling Adequacy.	Bartlett's Test of Sphericity		
		Approx. Chi-Square	df	Sig.
B2	.569	41.393	10	.000
B3	.610	65.274	15	.000
C1	.608	524.316	105	.000
C2	.499	43.303	3	.000
D1	.514	90.389	21	.000
D2	.668	71.979	3	.000

All of the above conditions are satisfied for factor analysis.

5.5 Section A: Biographical Data

This section presents the respondents' characteristics specifically looking at the number of years in the organisation and their designations.

Figure 5.1 Number of years that respondents have been in the organisation



Approximately 68% of the National Treasury respondents have been in the organisation for 6 years or less. The remaining 32% have been in the National Treasury employ for

a period of 7 years or more. All SALGA respondents have been in the organisation for 6 years at the most whilst 62% of the Msunduzi Municipality respondents were employed in the organisation in the same period. Assessing the number of years in the organisation is useful as it indicates that a fair proportion of the respondents have been in the organisation for an adequate period of time. This enhances the quality of the responses as the respondents have reasonable exposure, a background of embedded knowledge and experience having been in the service for a number of years.

Figure 5.2 Designation of the respondents

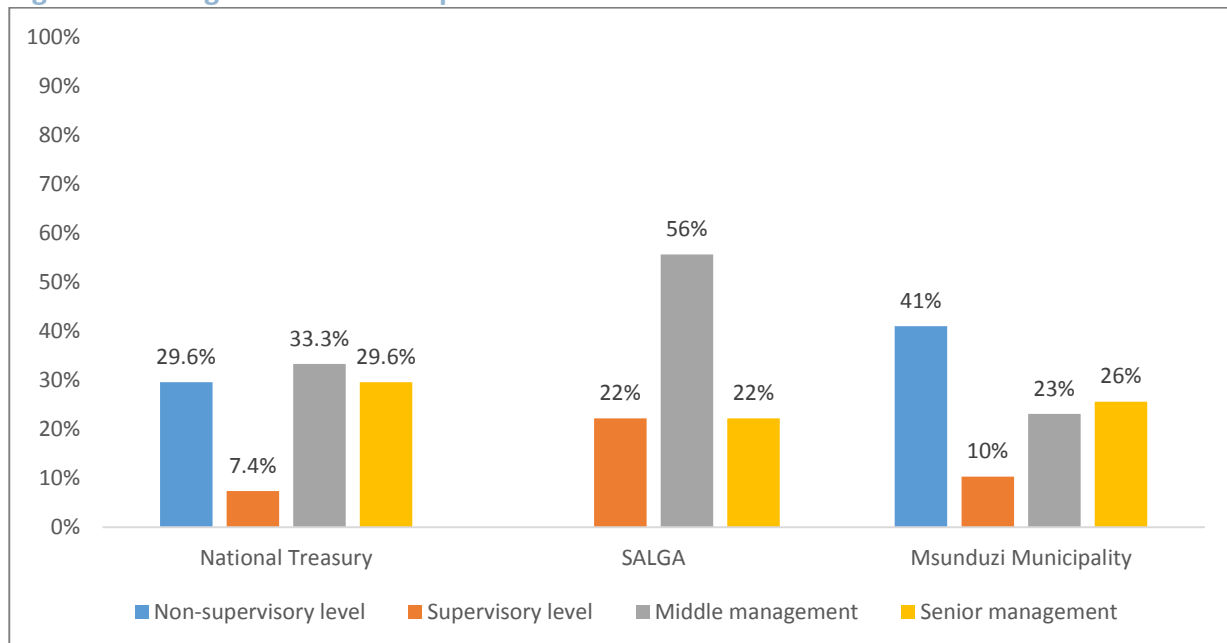


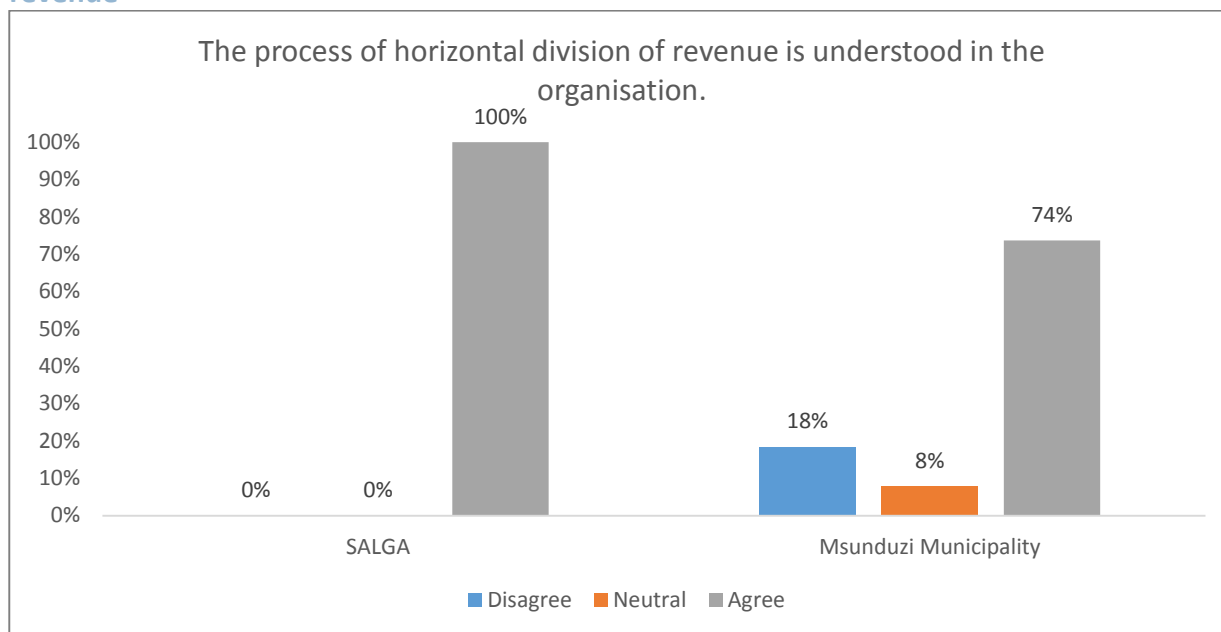
Figure 5.2 above shows that the bulk of the National Treasury respondents are at management level; 41% and 10.3% at non-supervisory level and supervisory level, respectively. The study had targeted senior managers. However, owing to unavailability of some senior managers during the data collection period, the sample was also extended to other lower management staff who also work closely with the LGES. The responses from this segment of staff would not impact negatively on the study.

The section that follows provides an analysis of the scoring patterns of the respondents for selected statements per section. Where relevant, the degree of disagreement (negative statements) were combined to report on one category labelled “Disagree”. Similarly, the degrees of agreement (positive statements) were also collapsed to one category labelled “Agree”. The results below are presented and analysed in accordance with the significance of the statements.

5.6 Section B: Practical Context

This section presents an analysis of the three organisations, that is, SALGA, Msunduzi Municipality and National Treasury, overall understanding of the process of horizontal division of revenue as well as the objectives of the LGES and LGES formula.

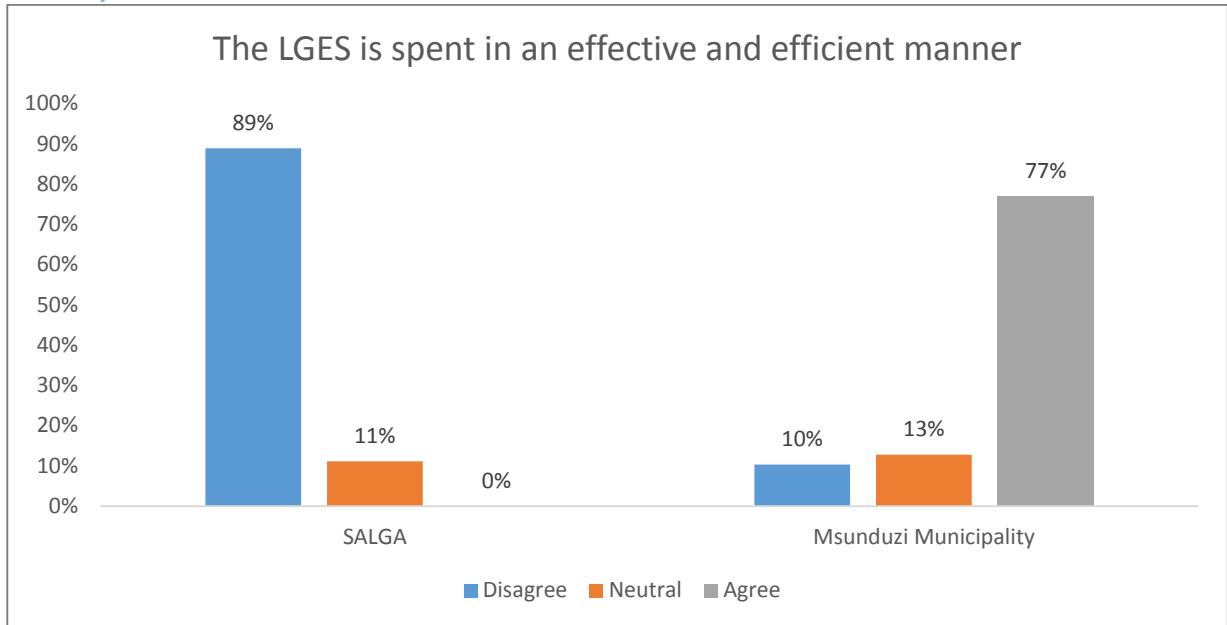
Figure 5.3 Analysis of the respondent's understanding of the process of horizontal division of revenue



A total of 18% of the Municipality's respondents are of the view that the process of resource allocation to local government is not understood within the municipality. This is a critical finding especially because it comes from the senior officials in the municipality. If this processes is not clearly understood at senior management level that there is a high probability that other officials within the municipality also do not understand the process of horizontal division of revenue.

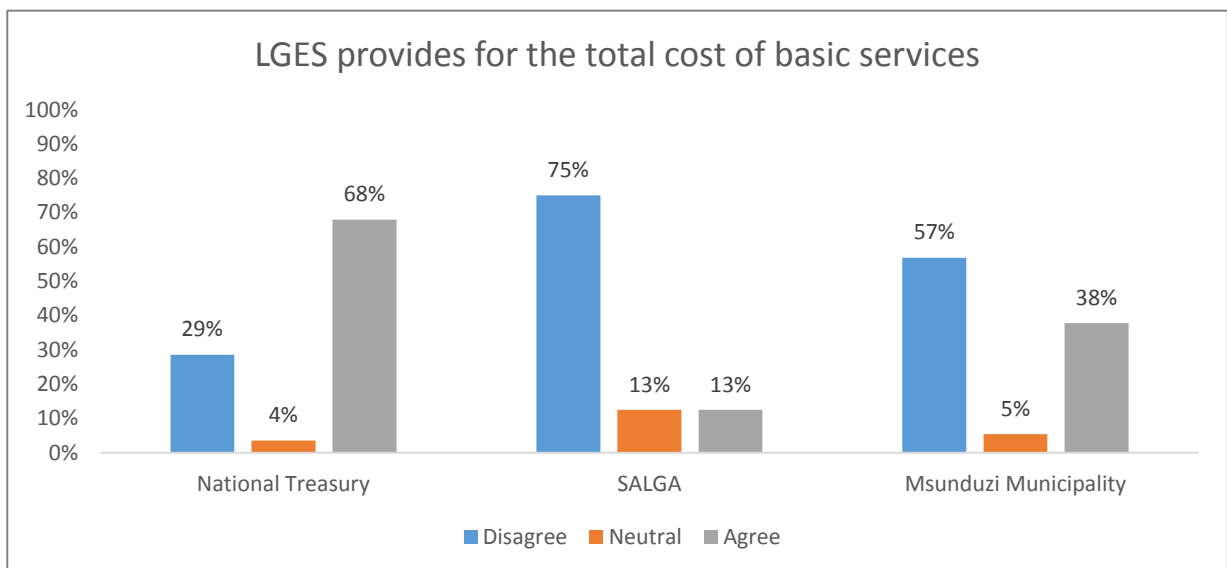
Section 6(g) of the Republic of South Africa Public Finance Management Act (1999) provides that the National Treasury promotes and enforces revenue management in a transparent and effective manner. Therefore, the National Treasury has a responsibility to promote and enforce transparency in the allocation of revenue to municipalities. The credibility of the horizontal allocation of resources lies in its transparency; therefore, it is important that National Treasury develops training programmes and workshops to close the knowledge gap that exists in municipalities on the local government resource allocation process.

Figure 5.4: Rating of the effectiveness and efficiency in spending LGES allocations in Municipalities



An amount of 77% of the municipality respondents agree that the LGES allocated to the municipality is spent in an effective and efficient manner. On the contrary, there is a very high level of disagreement from the SALGA respondents with regard to municipalities spending their equitable share allocations in an effective and efficient manner. This view is also shared by the Auditor- General in the 2013/14 MFMA Report on the Audit Outcomes of Local Government which states that “there are weaknesses in the effective utilisation of grants” (2015:7).

Figure 5.5: Respondents’ view of the LGES formula providing for the total cost of basic services



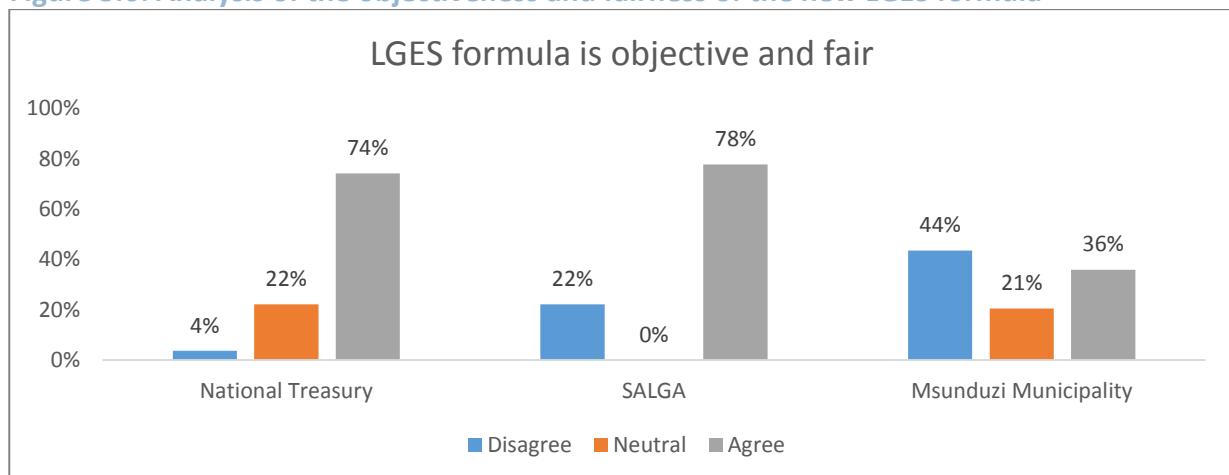
An average of 54% of the respondents disagree that the LGES provides the total cost of providing basic services. This implies that there is a gap between the requirements

of the Municipality to provide basic services in a sustainable manner, and what is allocated to municipalities in the form of the LGES. Internationally, decentralised countries mostly focus on the equalisation of revenue capacities only, and ignore the expenditure weaknesses in the delivery of public services (Wessels, 2010:15). Similar to international decentralised countries, South Africa has not been able to develop a methodology for assessing the cost of providing basic services in different municipalities. The National Treasury has acknowledged the weakness in the LGES formula and noted that there are no comprehensive studies that have recognised and measured the elements that impact on the cost of providing services and the extent to which they influence cost. It is also not clear how such elements can be quantified for each of the 278 municipalities (Republic of South Africa National Treasury, 2012:11); therefore, this calls for further research into this important aspect. The National Treasury further noted that the absence of this data was a critical restriction in designing the basic services component of the LGES formula (Republic of South Africa National Treasury, 2012:11). This is an important point in this study because it reveals some of the technical weaknesses of the LGES formula and the impact on the allocation of the LGES to different municipalities.

5.7 Section C: Principles and Structures of the Equitable Share Formula

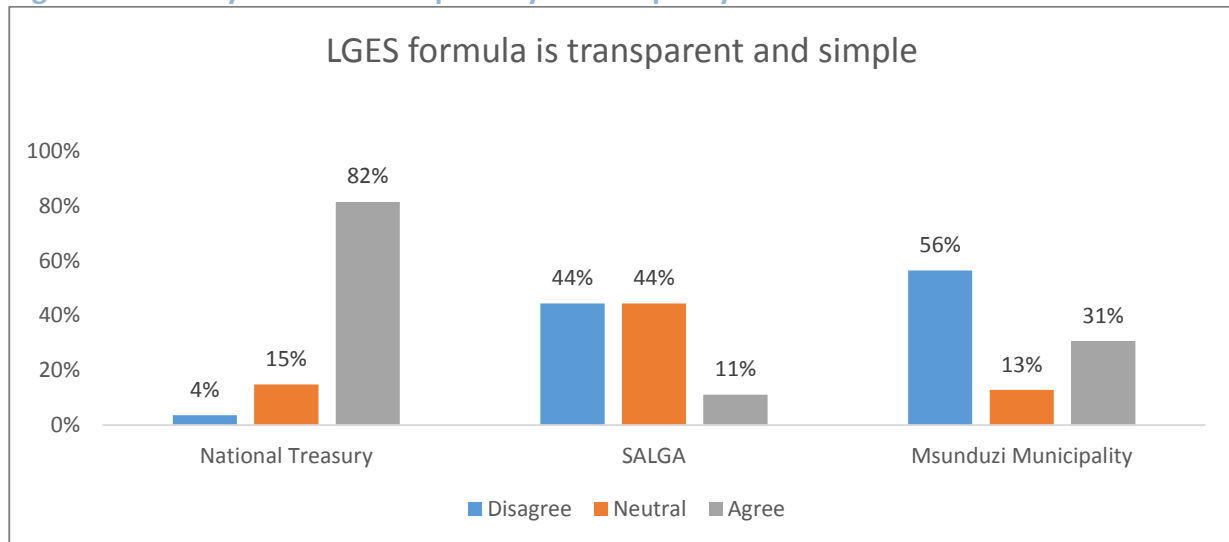
In this section, the analysis of responses is presented from SALGA, National Treasury and Msunduzi Municipality on their understanding of the principles underpinning the structure of the new LGES formula and particularly its alignment to the prescripts of the Constitution and the White Paper on Local Government. The section primarily seeks to provide answers to the research question: *Is the structure of the LGES formula aligned to the principles defined in the Constitution and the White Paper on Local Government?*

Figure 5.6: Analysis of the objectiveness and fairness of the new LGES formula



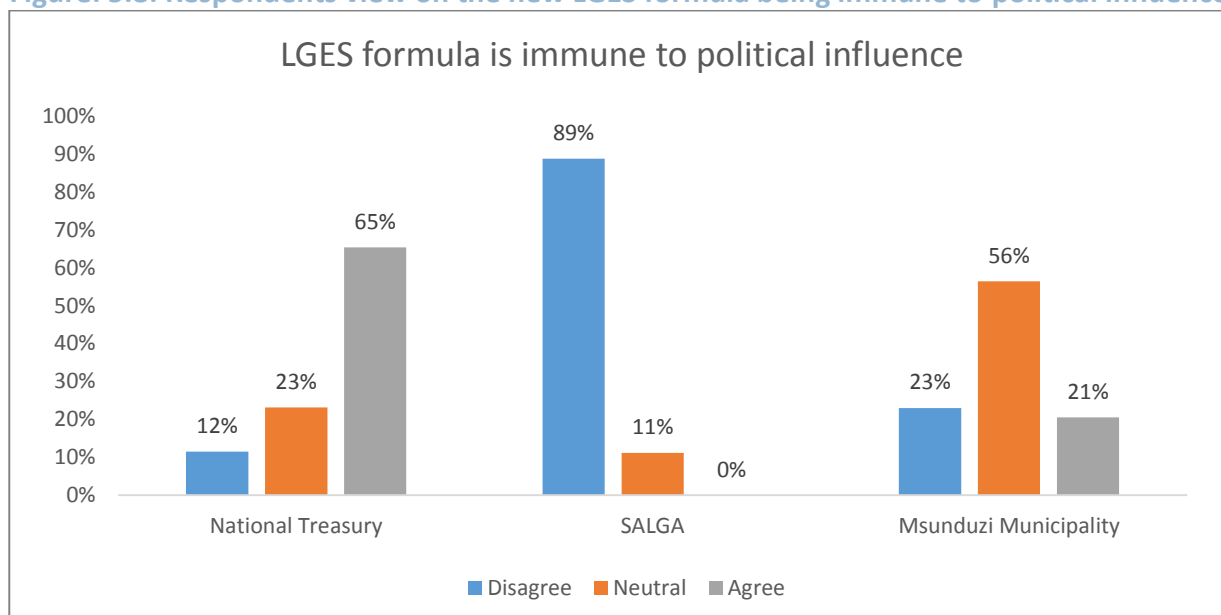
There is a strong view from the National Treasury and SALGA that the new LGES formula is objective and fair. This is consistent with the dictates of the White Paper on Local Government which states that the horizontal division of the equitable share among municipalities should be driven by efficiency and equity (Republic of South Africa White Paper on Local Government, 1998:91). However, it is worth noting that 44% of respondents from Msunduzi Municipality disagree with this statement. The study reveals divergence in views between national government and local government on the objectiveness and fairness of the LGES formula.

Figure 5.7: Analysis of the transparency and simplicity of the new LGES formula



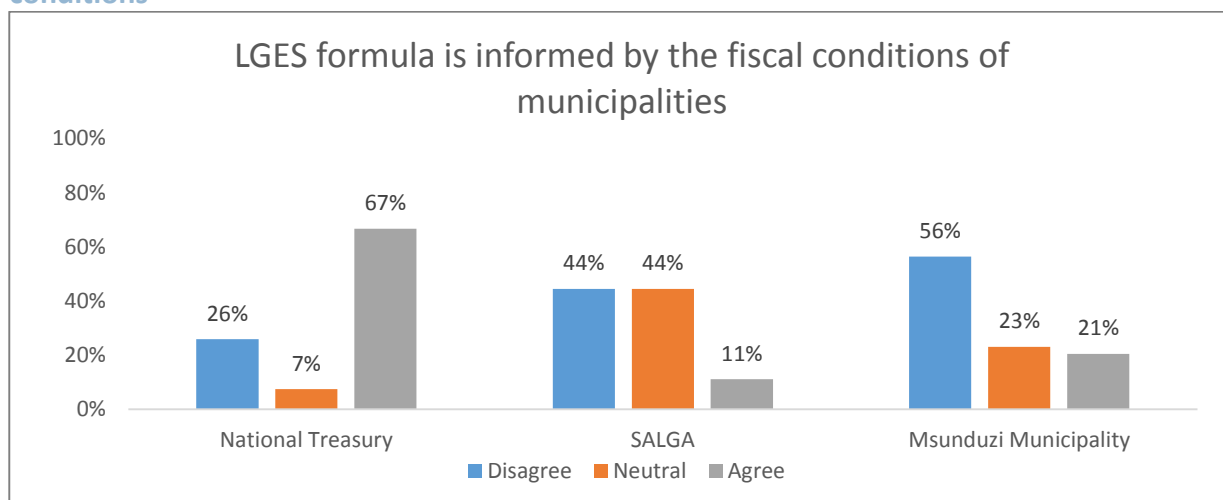
On average, 41% of the respondents agreed that the new LGES formula is transparent and simple. This response is aligned to Wessels (2010:17) argument that a transfer system or an allocation formula that is simple results in the ease of administration and transparency of outcomes. Boschmann (2009:8) also supports this view when he states that a transfer programme should be based on simple and transparent formula. Furthermore, Boex (2009:12) asserts that a formula-based allocation must meet some of the key evaluative principles of financial management which include: predictability, simplicity, and transparency. However, it is worth noting that a significant percentage of respondents from SALGA and Msunduzi Municipality disagreed with this statement. This is an important finding as it reveals that outside the National Treasury, there is a strong view that the LGES formula is not simple and transparent. This finding is a divergence to requirements of a good transfer system as cited by Smoke and Schroeder (in Ncube, 2013:297), which are: simplicity, transparency, equity, accountability and autonomy. This finding shows that there is still a need to further simplify the LGES formula and to ensure that there is a clear understanding of the different components that make up the formula, by other government departments, public entities and most importantly communities.

Figure: 5.8: Respondents view on the new LGES formula being immune to political influence



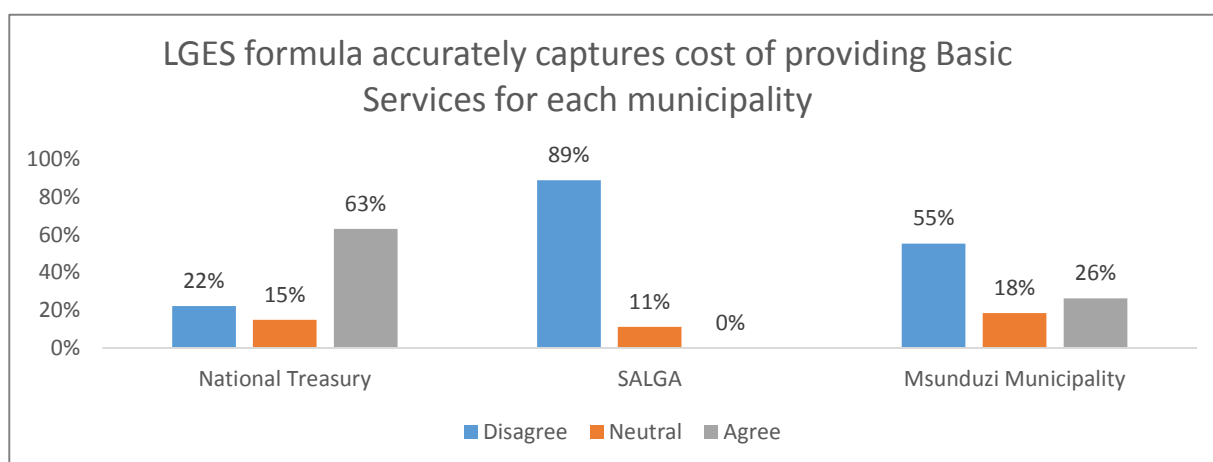
Sixty five percent of National Treasury’s respondents agree that the LGES formula is immune to political influence. This finding challenges the Public Choice Theory which is based on the notion that politicians are self-maximising individuals, and argues that the division of resources to municipalities by national government (politicians) will be fiscal preferences of the majority voters (Boex and Martinez-Vazquez, 2004:460). However, there is a notable (89%) view from SALGA respondents that the formula is not immune to political influence. This response from SALGA is consistent with the work of Banful (2011:2) who argues that allocation of resources using a consistently applied formula centred on fiscal elements does not essentially circumvent politically driven targeting. He further notes that the policy makers of transfer systems that are formula based, such as who decides on the components of the formula, when and how the formula can be adjusted, are significant factors of the extent to which the formula can prevent political manipulation (Banful, 2011:2). This view is also supported by the Public Choice Theory which is founded on the assumption that politicians are self-maximising individuals who use political influence in resource allocation in order to maximise the prospects of electoral success argues Alperovich (1984:286).

Figure: 5.9: Respondents view on the LGES formula being informed by municipal fiscal conditions



An average of 42% of the respondents disagreed that the LGES formula is informed by the fiscal conditions of municipalities. The largest percentage (56%) was recorded under the municipality respondents. This view is shared by Alm and Martinez-Vazquez (2009:68) where it is stated that there is a lack of tradition in South Africa for considering inequalities in fiscal capacity. An equalisation formula that does not account for the disparities in fiscal capacity in municipalities cannot achieve its objective which is to equalise.

Figure 5.10: Respondents view on the LGES formula accurately capturing the cost of providing basic services



Alm and Martinez-Vazquez (2009:10) also argue that there is no standard methodology or an accepted principle in government for how to estimate expenditure needs of local government. The absence of this methodology can result in differing views between local and national government on the extent of a municipality's expenditure needs. As a result, there is a situation where national government is of the view that the LGES

allocation to a municipality is adequate and a municipality holding a different view (Alm and Martinez-Vazquez, 2009:10). This study reveals that this theory exists in the practical context. Almost two-thirds of National Treasury respondents are of the view that the LGES formula captures the total cost of providing basic services while a majority of the respondents from Msunduzi disagreed with that statement.

After the new LGES formula was introduced, the National Treasury confirmed the assertions by Alm and Martinez- Vazquez and stated that “due to the unavailability of countrywide costing data for basic services, the cost of basic services may not be accurate” (Republic of South Africa National Treasury, 2012:11). It can be deduced from this discussion that the LGES does not give greater recognition to the differences among municipalities. Owing to the absence of costing or price index data for provision of basic services, the LGES formula does not adequately capture the diversity among municipalities. Consequently, the funding distributed using the LGES formula to municipalities may not always match the municipalities’ needs, thus making it inappropriate.

Table: 5.4: Difference between LGES allocation and actual cost of basic services provided

R'000	2012/13	2013/14	2014/15
LGES	338,903	354,313	373,541
Total Cost of FBS provided	338,903	363,502	391,529
Difference	-	(9,189)	(17,988)

Source: Msunduzi Municipality draft Budget 2015/16

When comparing the LGES allocation to Msunduzi municipality and the cost of providing free services in the municipality, there is a funding gap of R9.2 million and 18 million for the 2012/14 and 2014/15 financial years, respectively.

The misalignment between intergovernmental transfers and municipal expenditure needs is well articulated by Balh (2001:2) who states that in order to know how much funding is required, national government must assess the difference between the available revenue to municipalities (fiscal capacity), and the expenditure needs of those governments. Bahl further notes that this can be quite subjective since expenditure needs are almost unlimited (Bahl, 2001:2).

5.7.1 Areas of the LGES formula that require further enhancement

Table 5.5: Summary of respondents comments on components of the LGES formula that require further enhancement

Formula component	National Treasury	SALGA	Msunduzi Municipality
Basic Services (BS)	<i>Basic Services components require to be structured more on rural or poor municipality with higher allocation compared to metros and secondary cities</i>	<i>Costing of free basic services for different municipalities given the topographies, density etc.</i>	<i>Treasury must develop a price index for basic services and provide more financial support to poor municipalities.</i>
	<i>Basic services-different costs of services in different areas”.</i>	<i>Basic service component-study is required to determine actual cost of providing free basic services across all municipalities.</i>	<i>The municipality needs more money</i>
	<i>Developing separated costing factors to account for the diverse costs of providing services in different areas.</i>	<i>The cost of basic services must be reviewed.</i>	<i>More money is still needed.</i>
	<i>Allocation should be made to municipalities that provide the function rather than giving it to the authority</i>	-	-
Institutional component (I)	<i>A clear guide on how to measure the institutional component around all municipalities and how this will be affected by political interference.</i>	<i>Governance costs must be reduced in favour of more spend on service delivery, and increased fiscal efficiency should be met with a larger share.</i>	-
	<i>What does an efficient administration cost?</i>	<i>Does it fully provide for capacity development in municipalities?</i>	-
	-	<i>Incentivising performance and improved service delivery and not expenditure, need to be built into the Equitable Share consideration</i>	-
Community Services (CS)	<i>Community services- cost of services and distribute between district and local municipalities.</i>	<i>Commitment to fundamentally alter apartheid spatial paradigm which in its nature was characterised by geo-political emphasis</i>	-
Revenue Adjustment (RA)	-	<i>Investigate need for the revenue adjustment factor to increase fund distribution to municipalities with low fund capacity.</i>	-
Correction and Stabilisation (C)	-	-	-

Table 5.5 shows that there is a strong view from the Municipality that the LGES is not sufficient to provide the full extent of the municipality's needs in so far as basic services is concerned. Subban and Wissink (2015:19) argue that while some funding may be made available by redirecting resources from affluent parts to service historically disadvantaged area, it may not be adequate to address service delivery backlogs. Thus, larger LGES allocations and economic development strategies are necessary (Subban and Wissink, 2015: 49).

Similar to the National Treasury and SALGA, the Municipality has highlighted the need to develop a price index for basic services that will allow the LGES formula to accurately capture the expenditure needs of the municipalities. This will enable the formula to allocate funding that matches the needs of municipalities.

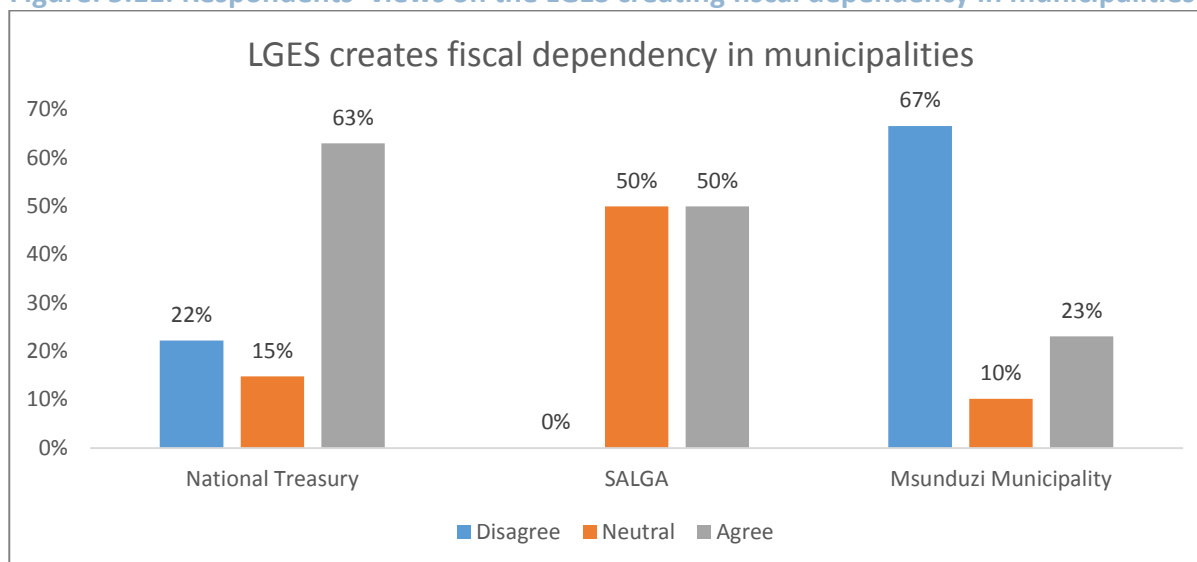
SALGA respondents have highlighted the cost of the basic services component as an area that requires further enhancement in the LGES formula. In this regard, Bahl (2001:17) states that a key constraint to designing a formula grant programme is finding credible data to implement the programme. In the South African context, it is credible costing data that has proved to be a major constraint of the LGES formula.

The respondents also raised an interesting point of including an incentive for good performance and improved service delivery in the formula, and not to only focus on cost of providing services. However, Kenyon (2012:17) warns that the possibility of incentives in the grant system does not always work and this is evidenced by the poorly performing Expanded Public Works Programme incentive grants. Kenyon further notes that incentives can be too intricate to measure and time-consuming, may not be affordable to the fiscus and poorly performing municipalities are too weak to respond to an incentive model (Kenyon, 2012:17). These are concerns that warrant attention.

5.8 Section D: The Equitable Share Formula and Service Delivery

This section provides an analysis of the responses from National Treasury, SALGA and Msunduzi Municipality on the LGES and its ability to empower local authorities to provide public services in a viable manner. This analysis also seeks to provide answers to, *inter alia*, the research question: *What are the perceptions and attitudes towards the new LGES formula in addressing the challenge of service delivery?* In evaluating the link between the municipalities' service delivery obligations of and the LGES, it is important to also assess if the principles of good governance are adhered to.

Figure 5.11: Respondents' views on the LGES creating fiscal dependency in municipalities

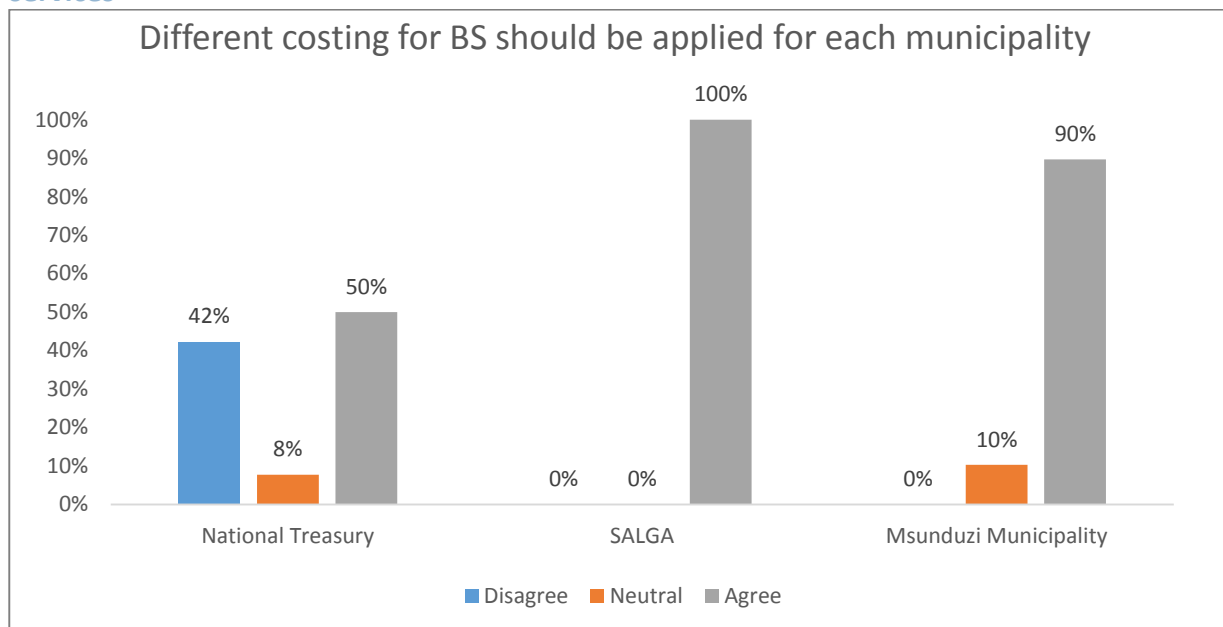


The sustainability of municipalities lies in their ability to fund their expenditure responsibilities from their own sources of revenue. Grant dependency weakens the municipalities' long term viability and sustainability and its capability to meet its service delivery objectives. Figure 5.11 above shows that there is a notable level of disagreement from the Msunduzi Municipality respondents with regard to the LGES creating dependency in municipalities. The municipality is of the view that the LGES does not reduce fiscal effort and thus results in grant dependency. The view from the municipality contradicts municipal finance literature that advances the view that intergovernmental transfers create financial dependency which negatively affects the financial sustainability of municipalities. The 2014 World Bank report (in Republic of South Africa National Treasury, 2014:3) highlights a high level of grants dependency in municipalities as a common global municipal financial management challenge. Furthermore, Republic of South Africa National Treasury (2008:52) notes that municipal dependence on grants as a source of revenue has risen dramatically over the years. The National Treasury's Local government database also shows that grants to municipalities are expected to grow by a faster rate over the medium-term in real terms when compared to municipal own revenue.

Contrary to Msunduzi Municipality respondents, a significant share of the National Treasury respondents agree that the LGES can create fiscal dependency. This view supports the report published by the Republic of South Africa National Treasury (2014:27), which states that in the 2013/14 financial year, 98 of 207 local municipalities received more than 75% of their revenue from national transfers. This represents an increase from 2012/13 where 75 local authorities generated more than 75% of their

income from government grants. The feedback from the National Treasury is also supported by Rodden’s findings which reveal that grant dependence is increasingly common, especially as countries decentralise expenditures by increasing intergovernmental transfers rather than expanding the local tax base (Rodden, 2002:28). Wildasin (2009:21) also supports Rodden and argues that municipal finances are heavily dependent on intergovernmental transfers, particularly from national governments. In the South African context, the increase in grant dependence has been cited as one of the main issues in horizontal division of revenue for local government (Republic of South Africa National Treasury, 2008:62). The rising levels of grant dependence is particularly problematic because it is associated with a decline in revenue collection efforts by municipalities.

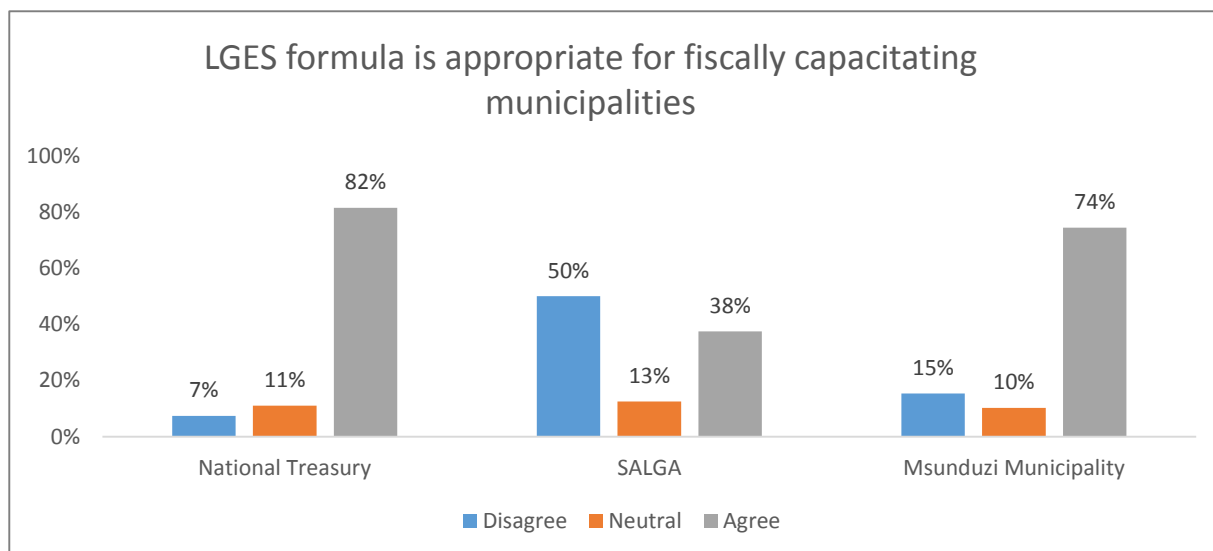
Figure 5.12: Respondents’ views on the LGES formula applying different costing for basic services



There is general acknowledgment that municipalities each have their unique characteristics that differentiate them from each other. These characteristics include population size, topography level of economic activity. This study recognises that there should be a differentiated approach applied to the funding of municipalities to account for the disparities. To this end, the findings of this study show a high level of agreement that the equitable share formula should apply a different costing for basic services for each of the 278 municipalities. This view was also cited in a number of consultative engagements that the National Treasury had with its stakeholders prior the introduction of the new LGES formula. Several stakeholders requested that LGES formula account for a number of elements that influence the cost of services in their respective

municipalities (Republic of South Africa National Treasury, 2012:4). However, the findings of this study show that this request was not incorporated in the new formula due to the absence of a pricing index for individual municipalities. This is an area of the LGES formula that continues to be a constraint to achieving appropriate resourcing for municipalities especially, those in remote areas.

Figure 5.13: Respondents view on the appropriateness of LGES formula for fiscally capacitating municipalities



The municipal finance and service delivery model discussed in Chapter Two, identifies the misalignment between expenditure functions and revenue bases of municipalities and highlights the need to ensure that intergovernmental transfers are sufficient to provide for the “structural gap” which is the variance between the requirements of the community and the available own sources revenue. Thus, the LGES is one of government’s programmes intended to close this structural gap and to assist municipalities with low fiscal capacity to deliver basic services to indigent communities in a sustainable manner.

It was therefore, important for this study to assess whether the new LGES formula allocates sufficient LGES to deserving municipalities in order to provide basic services. An average of 65% of the respondents agreed that the LGES formula is appropriate for fiscally capacitating the Municipality to provide basic services to poor households. It is worth noting that most respondents (82%) that supported this statement are from the National Treasury.

This response reveals that there is a level of appreciation from the respondents that the LGES formula, even with its weaknesses, is the most suitable equalisation mechanism available to address the problem of fiscal inequality between municipalities. However, it

is also noted that the LGES does not cover the entire structural gap. Therefore, national government should either allocate more funding towards the LGES or develop a programme that will assist municipalities to increase their own source revenue in order to reduce the structural gap.

5.8 Conclusion

This chapter presented an analysis of the data and interpretation of the findings with specific reference to the theories and literature. The objective of this research was to assess the appropriateness of the current LGES formula in fiscally capacitating municipalities to deliver basic services to indigent communities. The key findings of the investigation were summarised in each section, and the scores of percentages in the surveys reveal that the LGES formula and the process of allocation of resources to local government is not simple and transparent and therefore not understood particularly in municipalities. The LGES formula has also been found not to accurately capture the cost of providing basic services to communities and does not appropriately account for the fiscal capabilities of municipalities. There is a strong view that differentiated costing should be applied for each individual municipality to account for the differing capacities. The scores also reveal that despite the abovementioned deficiencies, the LGES formula remains the most appropriate mechanism of achieving equitable distribution of resources to municipalities.

CHAPTER SIX

CONCLUSION AND RECOMMENDATIONS

6.1 Conclusion

The purpose of this study was to assess the appropriateness of the new LGES formula in fiscally capacitating municipalities to deliver priority services to their constituencies. The results of the study reveal that there are limitations with regard to some components of the LGES formula which impact on the horizontal allocation of resources to municipalities. These limitations are constraints to achieving the objectives of the LGES which is to services indigent households. The shortfall of the LGES formula is primarily notable in the basic services component of the formula. The absence of costing data and a price index for basic services suggests that the LGES transferred to municipalities may not accurately match the expenditure requirements of those municipalities in as far as provision of basic services is concerned. Using Msunduzi Municipality as a case study, the study revealed that in some instances, the LGES allocation is not adequate to cover the cost of providing basic services to qualifying households. As a result, municipalities with low fiscal capacity are unable to meet their service delivery commitments. An unresponsive LGES formula and intergovernmental transfer programme means a slow and unsatisfactory response to service delivery challenges which results in the breakdown of trust between government and communities. Therefore, it is important that the LGES formula is continuously enhanced, so that it remains relevant and responsive to the needs of communities and particularly indigent households.

Notwithstanding the shortcomings of the LGES formula highlighted in this study, the results show that there is a general acceptance of the new LGES formula by government stakeholders. Approximately 94.9% of the Msunduzi Municipality respondents are of the view that despite its shortcomings, the LGES formula has contributed positively to the enhancement of the quality of lives of its local communities, which is a further important point of note for this study.

6.2 Recommendations

The findings of the study indicate that there are a number of challenges with the LGES formula and the context in which it operates that needs to be addressed by policy makers. The following recommendations are proposed for national government consideration.

- **Improve the differentiating methodology for municipalities**

It is accepted that each municipality has its unique characteristics which differentiates it from others. The characteristics are largely influenced by the areas' topography, spatial dynamics, population size and level of economic activity. This distinctiveness between municipalities provides a basis for developing a differentiated approach to equitable sharing of resources across municipalities. The area of contention among stakeholders (CoGTA, SALGA, Republic of South Africa National Treasury and municipalities) has always been the basis on which differentiation should occur. Nearly 90% of the respondents from Msunduzi municipality agree that the LGES formula should apply a cost differentiation with regard to providing for basic services. Currently, the basic services component of the LGES formula does not factor in the different fiscal capacities of municipalities. The differentiation approach, that is, a differentiation in costing for provision of services for each municipality, must be embedded in the LGES formula so that it responds to individual municipalities and their diverse fiscal capacities.

- **Develop an appropriate methodology for determining the basic services component of the LGES formula**

The BS component of the LGES formula is the most fundamental component as it accounts for 77.7% of the value of the LGES (Division of Revenue Act, 2014:93). Therefore, it is important that the different variables that make up this component are accurate as they have the greatest influence on the share of the LGES allocation transferred to municipalities. The LGES formula is not perceived as being fully responsive to the basic needs of the Municipality due to its ability to quantify the basic services needs of each individual municipality. Table 5.4 in Chapter 5 confirms this view by demonstrating the gap between the LGES allocation received by the Municipality and the actual cost of providing free basic priorities to indigent residents in the Municipality. The misalignment between the expenditure need and the LGES allocation is mainly attributed to the absence of credible household data at municipal level that can be used to determine the extent of the expenditure needs at municipal level. It is recommended that National Treasury in conjunction with StatsSA develop a more appropriate method of determining household

data at a municipal level and quantifying the structural fiscal gap in municipalities. These variables are essential in calculating the basic services component of the formula and ensuring that sufficient funding is allocated to deserving municipalities.

- **Develop a guide on quantifying the institutional component**

The institutional component of the LGES formula was highlighted in the study as an area that required further enhancement. According to Republic of South Africa National Treasury (2011:21), the institutional component of the LGES formula is not designed to provide for the entire administrative costs of municipalities but provides for basic administrative costs. However, it is not clear what constitutes basic administration and how the cost of basic administration is determined. In addition, the respondents highlighted that it not always possible to separate administration costs from operational costs making it difficult to determine the appropriate allocation for the institutional component.

The study also revealed that the institutional component is the most vulnerable to political interference. This is mainly due to the equation being based on the cost per councillor as well as the number of council seats in each municipality which is decided on by the Minister of CoGTA, a politician. This study recommends that a clear guide on how to measure the basic cost of administration in a municipality is developed. This will provide more transparency in the determination of the institutional component that should be allocated to a municipality and it will also lift the veil of political interference that is associated with this component.

- **Understanding the dynamic between expenditure needs, fiscal capacity and fiscal effort**

Bird and Smart (2002:4) note that the ingredients of a good transfer programme are: needs, capacity and effort. Despite the recent LGES formula review, there is still a notable deficiency in the current LGES formula with regard to quantifying municipal expenditure needs as well as measuring fiscal capacity in relation to fiscal effort. There is still no agreed methodology of measuring fiscal capacity, fiscal effort and expenditure needs in the South African context which, ideally, should form the basis for the local government fiscal framework.

The community services and institutional components of the LGES formula are the only two components in the formula that, to some extent, account for the different fiscal capacities of municipalities through the use of the revenue adjustment factor. The revenue adjustment

factor is calculated using the level of fiscal capacity in each municipal area using a number of factors to create a capita index. This index is then factored to the community services and the institutional components of the LGES formula to determine the size of the LGES share that should be allocated to qualifying municipalities. It should be noted that determining the revenue adjustment factor is a lengthy and tedious process and is somewhat opaque.

In addition, the revenue adjustment factor does not take into account the level of fiscal effort applied by a municipality to ensure that revenue capacity is optimised. Failure to account for fiscal effort compromises the credibility of the measure of fiscal capacity used to determine the LGES allocation. A local authority's fiscal capacity cannot be measured in isolation of its fiscal effort (Republic of South Africa National Treasury, 2011:38). An LGES formula that does not account for fiscal effort can compensate municipalities that do not raise revenue proportionate to their fiscal capacity. It is recommended that National Treasury takes lessons from countries such as Brazil, Nigeria and Columbia who have agreed on a measure for fiscal effort and have applied it in their equalisation and distributional transfer programmes (Bird and Smart, 2002:5). The adjustment factor should also be reviewed to ensure that it is more transparent and easy to understand.

Notwithstanding this, the LGES formula will still not be effective if the restraints on municipal own revenues sources are not resolved. It is thus recommended that, parallel to quantifying the fiscal structural gap, national government identifies the constraints to revenue generation and collection in municipalities and develop a programme to address these constraints to realise lasting sustainability of municipalities. The municipal finance and service delivery model advocates that good management and municipal governance systems will lead to enhanced service delivery whilst an inefficient municipal governance system can have the adverse effect. Therefore, in order to fix the LGES formula it is essential to fix some other fundamental aspects of the local government fiscal framework (Alm and Martinez-Vazquez, 2009:9).

- **Availability of current data**

Presently, there is insufficient information is obtainable at municipal level to support the design of a suitable LGES formula. The LGES formula relies heavily of data that is produced from Censuses which occur at 10 year intervals. Therefore, there is a pressing need to identify other reliable sources of municipal data that can be used in-between Censuses in order to account accurately for changes in topography resulting from revised demarcations,

changes in demographics and other factors that influence LGES allocations. In addition, the household data produced by the Census is controlled for housing units only and does not include collective living arrangements and transient populations (StatsSA, 2011:1). This is another limitation of current data that requires further improvement as it has a direct influence on the size of the LGES transferred to a municipality.

- **Improve the transparency and simplicity of the LGES formula**

There is a large percentage of respondents particularly from the Municipality (56.4%) and SALGA (44.4%) who are of the opinion that the LGES formula is not simple and transparent. As highlighted in Chapter Two, transparency is a key principle of good governance as it is essential in building shared trust between the government and communities through the provision and access to precise and sufficient information. Thus, National Treasury must make sure that the configuration of the LGES formula is precise and easy to understand and that the input data used in the LGES formula is easily accessible.

- **Create more awareness on the LGES formula**

The study revealed that there is not sufficient understanding of the LGES formula and the overall allocation of the LGES particularly at municipal level. The study shows that 18% of senior managers in Msunduzi Municipality do not fully understand the process of horizontal division of revenue. If the LGES allocation process is not understood at senior management level then there is a high probability that other officials within the municipality and members of communities also do not understand this process. More awareness needs to be created in this area in order to ensure full transparency and accountability in municipal resource allocation. It is proposed that National Treasury, in partnership with other relevant government departments, develops LGES formula training programmes or workshops to improve the level of knowledge on how the LGES is allocated within government as well as communities as the end users of the LGES.

- **Suggestion for future research**

This study's objective was to assess the appropriateness of the LGES formula in fiscally capacitating local authorities to provide basic services to indigent communities. However, owing to time constraints, the study limited its focus to Msunduzi Municipality. Therefore, there is a need to conduct further research and a longitudinal study to expand the analysis to the remaining municipalities to provide a broader sense of the impact of the new LGES formula in addressing issues of fiscal capacity in municipalities.

7. REFERENCES

- Advisory Commission on Intergovernmental Relations, 1986. Measuring State Fiscal Capacity: Alternative methods and their uses. *An Information Report M150*. Washington D.C.
- Allers, M.A., Ishemol, L.J. 2011. Fiscal capacity equalisation in Tanzania. *Environment and Planning Government and Policy Impact Factor*. 1.16. 29(3):487-501.
- Alm, J., Boex, J. 2008. The role of economic versus political factors in the incidence of intergovernmental transfers in Nigeria. *The Journal of Developing Areas*. 42(1):1:19.
- Alm, J. Martinez-Vazquez J. 2009. South Africa's Provincial Equitable Share: An Assessment of Issues and Proposals for Reform. *Working Paper(09-04)*. International Studies Program. Andrew Young School of Policy Studies. Atlanta Georgia.
- Alprerovich, G. 1984. The economics of choice in the allocation of intergovernmental grants to local authorities. *Public Choice*. 44(2):285-296.
- Amusa, H., Mabunda, R., Mabugu, R. 2008. Fiscal Illusion at the Local Sphere: An Empirical Test of the Flypaper Effect using South African Municipal Data. Working Paper (72). Financial Fiscal Commission. Midrand. South Africa.
- Auditor General, South Africa. 2011. Consolidated General Report on the audit outcomes of Local Government 2010-11. Johannesburg. South Africa.
- Auriacombe, C.J. 2010. Survey Research: Critical Considerations for Questionnaire Construction *Journal of Public Administration* 45(3):473-488.
- Balh, R. 2001. Fiscal Decentralization, Revenue Assignment, and the Case for the Property Tax in South Africa. *Working Paper 01-7*. International Studies Program. Andrew Young School of Policy Studies. Atlanta Georgia.
- Banful, A.B. 2011. Do formula-based intergovernmental transfer mechanisms eliminate politically motivated targeting? Evidence from Ghana. http://gssp.ifpri.info/files/2010/06/banfuldacfjune1forgsspshop_formula-based-transfer_june2.pdf. Accessed 8 August 2014.
- Barreiro, L. P. and Albandoz, J. P. 2001. Population and sample. Sampling techniques. *Management for mathematics for European Schools*. Seville: University of Seville.
- Barro, S.M. 2002. Macroeconomics versus RTS Measures of Fiscal Capacity: Theoretical Foundations and Implications for Canada. Queen's University. Working Paper (1):1-19.

- Basheka, B.C., 2012. The Paradigms of Public Administration Re-examined: A Reflection. *The Journal for Public Administration*. 47(1):25-67.
- Bird, R.M. and Smart, M. 2002. Intergovernmental Fiscal Transfers: International Lessons for Developing Countries. World Development. Article in Press.
- Brand, D. 2007. Financial Intergovernmental Relations in South Africa. Policy Paper 1(2007):1-23.
- Boex, J. 2009. Fiscal Decentralization and Intergovernmental Finance Reform as an International Development Strategy. *IDG Working Paper 2009(06)*: 1-24.
- Boex, J., Heredia-Ortiz, E., Martinez-Vazquez, J. Timofeev, A. and Yao, G. 2006. Fighting Poverty through Fiscal Decentralisation. United States Agency for International Development.
- Burger, R. 2005. What Have We Learnt From Post-1994 Innovations in Pro-poor Service Delivery in South Africa: A Case Study- Based Analysis. *Development Southern Africa*. 22(4):484-499.
- Boex, J. Martinez-Vazquez, J. 2004. The Determinants of Incidence of Intergovernmental Grants: A survey of the International Experience. *Public Finance and Management*.4 (06-52):454- 479.
- Boschmann, N. 2009. Fiscal Decentralization and Options for Donor Harmonisation. Development Partners Working Group on Local Governance and Decentralization DPWG-LGD. Berlin.
- Cakata, N.W., 2011. An Analysis of Service Delivery Challenges in the Eastern Cape Province of South Africa: The Case of Mnquma Local Municipality (2005-2010). Unpublished Masters mini thesis, University of Fort Hare, Alice.
- Chernick, H. 1998. Fiscal Capacity in New York: The City versus the Region. *National Tax Journal*. 5(3):531-540.
- Chervin, S. 2007. Fiscal Effort, Fiscal Capacity, and Fiscal Need: Separate Concepts, Separate Problems. Tennessee Advisory Commission on Intergovernmental Relations. iii: 1-12. www.state.tn.us/tacir . Accessed on 25 August 2014.
- Chitinga-Mabugu, M., and Monkam N. 2013. Assessing Fiscal Capacity at the Local Government Level in South Africa. *Department of Economics Working Papers Series*. 2013(76). University of Pretoria. Pretoria.

Commonwealth. 2005. Guidelines for Public Financial Management Reform. Finance Ministers Meeting. Hilton Hotel, Barbados, 18-20 September 2005.

Cordes, J.J. 2003. Reconciling Normative and Positive Theories of Government. *The American Economic Review*. 87(2):169-172.

Creswell, J.W. 2009. *Research Design: Qualitative, Quantitative and Mixed Methods Approach*. 3rd Ed. California: Sage Publications Inc.

Creswell, J.J. and Clark, V.L.P. 2011. *Designing and Conducting Mixed Methods Research*. 2nd Ed. California: Sage Publications Inc.

Cronje, F. 2014. Behind the rise of protest action in South Africa. *Politicsweb*: 19 February 2014. <http://www.politicsweb.co.za/politicsweb/view/politicsweb/en/page71619/page71619?oid=547431andsn=Detailandpid=71619>. Accessed on 29 September 2014

Department of Cooperative Governance and Traditional Affairs (CoGTA). 2009. State of Local Government in South Africa. Overview Report. Working Documents. Pretoria.

Department of Cooperative Governance and Traditional Affairs (CoGTA). 2010. Budget Vote Speech by Minister Scelo Shiceka. Pretoria: Government Printers.

Derichs, A. and Enfield, C. 2006. Fiscal Decentralisation and Intergovernmental Fiscal Relations in South Africa. World Bank Seminar.

Dewett, K.K. 1996. Modern Economic Theory. 21st Ed. New Delhi. Shyam Lal Charitable Trust.

Du Plessis, P. and Majam, T. 2010. Mixed Method Research – A New Paradigm? *Journal of Public Administration*. 45(3):456-472.

Elhiraika, A. B. 2007. Fiscal Decentralisation and Public Service Delivery in South Africa. Economic Commission for Africa. *Work in Progress*. 58:1-26.

Engida, T.G., and Bardill, J. 2013. Reforms of the Public Sector in the Light of the New Public Management: A Case of Sub-Saharan Africa. *Journal of Public Administration and Policy Research*. 5(1):1-7.

Financial and Fiscal Commission 2011. Financial and Fiscal Commission. Submission for the 2012/13 Division of Revenue. Technical Report. Midrand, South Africa.

Financial and Fiscal Commission. 2013: Sustaining Local Government Finances Review of the Local Government Fiscal Framework. Midrand, South Africa.

Financial and Fiscal Commission. 2015. Financial and Fiscal Commission Submission on Stoppage of Local Government Equitable Share Allocations. Midrand, South Africa.

- Girishankar, N., DeGroot, D., Pillay, T.V. 2006. Measuring Intergovernmental Fiscal Performance in South Africa. Issues in Municipal Grant Monitoring. *Working Paper (98)*. Africa Region.
- Grant, L. 2014. Research shows sharp increase in service delivery protests. *Mail and Guardian*: 12, February 2014. <http://mg.co.za/article/2014-02-12-research-shows-sharp-increase-in-service-delivery-protests> . Accessed on 21 March 2015.
- Hollands, G. & Mageza, Q. 2010. Basic Service Delivery and Local Government. Unpublished essay, University of Fort Hare, Alice.
- Holtzhausen, N. and Naidoo, G. 2011. Effective Governance as an Approach to Promote Service Delivery by Local Government in South Africa: The Case for Soul City. *Journal of US-China Public Administration*. 8(7):735-747.
- Hughes, O.E. 2003. *Public Management and Administration*. 3rd Ed. Palgrave Mcmillan. New York.
- Hope, K.R. 2001. The New Public Management: Context and Practice in Africa. *International Public Management Journal*. 4(2):119-134.
- Hussein, L. 2013. Impact of public sector reforms on service delivery in Tanzania. *Journal of Public Administration and Policy Research*. 5(2):26-49.
- Joshua, L. 2009. Fiscal Decentralisation and Public Financial Management Reforms in Central Asia Challenges and Opportunities. www.unicef.org/Laurie_Joshua_Background_Document_eng_fin.doc. Accessed on 12 March 2013.
- Kenyon, S. 2012. Local Government Fiscal Framework. Paper presented at the Financial and Fiscal Commission Public Hearings. Pretoria, 4 June 2012.
- Kirigia, D.G. 2009. Beyond Needs-Based Health Funding: Resource Allocation and Equity at the State and Area Health Service Level in New South Wales- Australia. Unpublished PhD thesis, University of New South Wales, New South Wales.
- Ladi, S.2008. Good Governance and Public Administration Reform in the Black Sea Economic Cooperation Member States. *Xenophon Paper*. No 8. Athens. Greece. http://icbss.org/media/110_original.pdf. Accessed on 8 August 2014.
- Lee, M. 2003. Conceptualizing the New Governance: A New Institution of Social Coordination. Paper presented at the Institutional Analysis and Development Mini-Conference, Indiana University, Indiana, 3 -5 May 2003.

- Leedy, P.D and Ormrod, J.E. 2005. Practical Research: Planning and Design. New York: Macmillan Publishing Company.
- Levin, J., Milgrom, P .2004. Introduction to Choice Theory. <http://www.milgrom.net>. Accessed on 24 July 2015.
- Liddo, G., Longobardi, E, and Porcelli, F. 2014. Measuring Horizontal Fiscal Imbalances: The Case of Italian Municipalities. *Series Working Paper (49)*. <http://dx.doi.org/10.2139/ssrn.2494218> Accessed 28 September 2014.
- Mabugu, R., Maisonnave, H., Ribichaud, V., and Chitiga, M. 2012. Realising Millennium Development Goals through Intergovernmental Fiscal Transfers. Submission for the 2012/13 Division of Revenue. Technical Report. Pretoria. Financial and Fiscal Commission.
- Mafunisa, M.J. & Dzegwa, S. 2007. The Role of Critical Theory in Public Administration. *Journal of Public Administration*. 42(8):765-775.
- Manias, M.J. and Dzegwa, S. 2007. Role of Critical Theory in Public Administration. *Journal of Public Administration*. 24(8):765-766.
- Mahabir, J. 2010. An Assessment and Review of the South African Local Government Equitable Share Formula Research. Technical Report in support of the Financial and Fiscal Commission Submission for the Division of Revenue 2007/08, Financial and Fiscal Commission. Midrand, South Africa.
- Maharaj-Sampson, N., and Ferreira, G. 2015. The Role of Public Utilities in Accelerating Growth. A Case Study of Umngeni Water in the Mbizana Local Municipality. *Administratio Publica*. 23(2):115-136.
- Martinez-Vazquez, J. and Boex, L.F.J. 1997. Fiscal Capacity: An Overview of Concepts and Measurements Issues and their Applicability in the Russian Federation. *International Center for Public Policy Working Paper Series No. 97-03*. International Center for Public Policy, Andrew Young School of Policy Studies, Georgia State University.
- Matthews, B. and Ross, L. 2010. Research Methods. A practical Guide for the Social Sciences. London: Pearson.
- Momoniati, I. 2001. Fiscal Decentralisation In South Africa: A Practitioner's Perspective. <http://info.worldbank.org/etools/docs/library/128819/Momoniati%202001%20South%20Africa.pdf>. Accessed 25 April 2013.
- Msunduzi Municipality 2010. 2009/10 Annual Report. Government Printers. Pretoria.

- Musgrave, R.A. and Musgrave, P.B. 1989. *Public Finance in Theory and Practice*. 5th Ed. New York: McGraw-Hill.
- National Development Plan. 2011. Vision 2030. <http://www.npconline.co.za/medialib/downloads/home/NPC%20National%20Development%20Plan%20Vision%202030%20lo-res.pdf>. Accessed on 5 May 2012.
- Ncube, M. 2013. Improving the Performance of Municipalities through Performance based grants. Submission to the 2014/15 Division of Revenue. Technical Report. Midrand, South Africa.
- Nel, D. 2015. Pre and Post Public Administration, Management and Governance Reform. *Administratio Publica*. 23(2):73-97.
- Ngxoxo, M. 2003. Non-payment of Municipal Rates and Service Charges with Reference to the Nelson Mandela Metropolitan Municipality. Unpublished dissertation, Port Elizabeth Technikon, Port Elizabeth.
- Nikolov, M., Josifov, G. 2006. Measurement of Fiscal Capacity for Macedonian LGU. www.cea.org.mk/.../Measurement_of_fiscal_capacity.pdf. Accessed on 21 March 2014.
- Nkuna, N.W. 2013. The Etymological context of Governance in South African Public Administration: A Missing Link in Reconceptualising the Concept for Contemporary Reality. *Journal of Public Administration*. 48(1):138-151.
- Nomvalo, S., 2008. Public Financial Management Reforms. What really works- A South African Perspective. Washington D.C.
- Nzimakwe, T.I. 2005. An Analysis of the Theory and Practice of Governance in the Kwazulu-Natal Provincial Authority. Unpublished PhD thesis, University of KwaZulu-Natal, Westville.
- Oates, W.E. 1999. An essay on Fiscal Decentralisation. *Journal of Economic Literature*. 37(3):1120-1149.
- Ojo, O. 2009. Efficient Financial Management for Local Governments: The Nigerian Experience. *Journal for Public Administration and Policy Research*. 61(2):36-44.
- Ostrom, V. and Ostrom E. 1971. Public Choice: A different Approach to the Study of Public Administration. *Public Administration Review*. 31(2):203-216.
- Peters, S. 2013. Municipal Consumer Debt in South Africa. Commission. Submission to the 2012/13. Division of Revenue Technical Report. Financial and Fiscal Commission. Pretoria.

Pinho, M.M., and Viegas, L.G. 2005. The Determinants of Intergovernmental Grants in Portugal: a Public Choice Approach. Annual Meeting of the European Public Choice Society, Durham, 2005. Durham: University of Durham.

Pooë, R.I.D., and Mafini, C. 2012. Business Development Challenges in a Rural District Municipality in South Africa: A Case of Fezile Dabi District Municipality. *The Southern African Journal of Entrepreneurship and Small Business Management*. 5(128):89-109.

Pressman, S. 2013. Social Democracy for the 21st Century: A Post Keynesian Perspective. <http://socialdemocracy21stcentury.blogspot.co.za/2013/02/steven-pressman-on-public-choice-theory.html>. Accessed 21 March 2015.

Quist, R.E., Certun, C., Dendura, J. 2008. Republic of South Africa Public Expenditure and Financial Accountability. Public Financial Management Performance Report. European Commission Delegation South Africa. Netherlands.

Rajasekar, S., Philominathan P., and Chinnathambi, V. 2013. Research Methodology. <http://www.google.co.za/url?sa=t&drct=j&dq=andescr=sandsource=webandcd=17andved=0CDoQFjAGOAoandurl=http%3A%2F%2Farxiv.org%2Fpdf%2Fphysics%2F>. Accessed on 7 October 2014.

Rao, M. G. 2003. *Intergovernmental Finance in South Africa: Some Observations*. National Institute of Public Finance and Policy.

http://www.researchgate.net/publication/23691528_Intergovernmental_finance_in_South_Africa_Some_observations/file/3deec52145ef58b395.pdf. Accessed on 12 May 2013.

Republic of South Africa. 1996. Constitution of the Republic of South Africa. Pretoria: Government Printer.

Republic of South Africa. 1997. Intergovernmental Fiscal Relations Act, No.97 of 1997. Pretoria: Government Printer.

Republic of South Africa White Paper on Local Government. 1998. Pretoria: Government Printer.

Republic of South Africa. 2005. Intergovernmental Relations Framework Act, No.13 of 2005. Pretoria: Government Printer.

Republic of South Africa. 2003. Municipal Finance Management Act, No.56 of 2003. Pretoria: Government Printer.

Republic of South Africa. 2004. Municipal Property Rates Act, No.6 of 2004. Pretoria: Government Printer.

Republic of South Africa. 2007. Municipal Fiscal Powers and Functions Act, No.12 of 2007. Pretoria: Government Printer.

Republic of South Africa National Treasury. 2012. Local Government Equitable Share Formula Review. Discussion Paper 2: Analysis of the Current Local Government Equitable Share Formula. Pretoria. Government Printer.

Republic of South Africa National Treasury. 2011. 2011 Local Government Budgets and Expenditure Review. Pretoria. Government Printer.

Republic of South Africa National Treasury. 2014. The State Of Local Government Finances and Financial Management as at 30 June 2014. Pretoria. Government Printer.

Republic of South Africa National Treasury. 2008. South Africa's Intergovernmental Fiscal System. Pretoria. Government Printer.

Republic of South Africa National Treasury. 2014 [b]. Budget Review. Pretoria. Government Printer.

Republic of South Africa National Treasury. 2013. Budget Review. Pretoria. Government Printer.

Republic of South Africa Division of Revenue Bill. 2013. Pretoria. Government Printer.

Republic of South Africa Division of Revenue Bill. 2014. Pretoria. Government Printer.

Republic of South Africa Division of Revenue Bill. 2015. Pretoria. Government Printer.

Rodden, J. 2002. The Dilemma of Fiscal Federalism: Grants and Fiscal Performance around the World. *American Journal of Science*. 46(3):670-687.

Rosen, SH.S. 2002. Public Finance: Essay for the Encyclopedia of Public Choice. CEPS Working Paper (80). www.princeton.edu/ceps/workingpapers/80rosen.pdf. Accessed on 15 June 2014.

Ryan, AB. 2006 Post-Positivist Approaches to Research. Researching and Writing your thesis: a guide for postgraduate students. MACE: Maynooth Adult and Community Education.

Ryu, J.E. 2014. *The Public Budgeting and Finance Primer: Key Concepts in Fiscal Choice*. M.E. Sharpe Inc. New York.

Salazar, J.G. 2007. Decentralisation, Politics and Service Delivery in Mexico. *Institute of Development Studies Bulletin*. 38(1):1-9.

South African Local Government Association (SALGA). 2011. Municipal Financial Viability. Municipal Managers Network. Pretoria

- Schoeman, N.J., 2006. Rethinking Fiscal Decentralisation in South Africa. *Journal for Public Administration*. 41(2):110-127.
- Schurink, W. 2010. The Importance of Theorising in Proposal Writing. *Journal of Public Administration*. 45(3):420-432.
- Schoeman, N.J., 2011. Fiscal Performance and Sustainability of Local Government in South Africa—An Empirical Analysis. *Working Paper (201)*.
www.econrsa.org/papersw_papers/wp201.pdf. Accessed on March 2013
- Siswana, B. 2007. Leadership and governance in the South African Public Service: An Overview of the Public Finance Management System. Unpublished PhD thesis, Pretoria University, Pretoria.
- South African Cities Network (SACN). 2008. Securing municipal finance in Southern Africa. Paper presented at Sustainable Municipal Finance in South Africa Conference, Johannesburg.
- Statistics South Africa (StatsSA). 2011. Community Survey: Municipal Report KwaZulu-Natal. Report No. 03-01053. Pretoria. Government Printers.
- Statistics South Africa. 2013. Millennium Development Goals, Country Report 2013. Pretoria: Statistics South Africa.
- Subban, M. and Wissink, H. 2015. Key Factors in Assessing the State of Local Government in South Africa. Crisis Management of Facing the Realities of Transformation? *Administratio Publica*. 23(2): 33-56.
- Summers, F.W. 1975. The Use of Formulae in Resource Allocation: Effective Resource Allocation in Library Management. *Library Trends*. 23(4):631-642.
- Sunday, A.M., Ocheni, S., Okechukwu, N.D. 2014. Local Government Finance in Nigeria: Challenge and Prognosis for Action in a Democratic Era (1999-2013) *Journal for Good Governance and Sustainable Development in Africa*. 2(1):84-96.
- Teko, J., Nkote, I., Jannat, N.S. 2014. An Analysis of the relationship between capacity building and fiscal capacity in Uganda Local Government. *Journal of Research in International Business and Management*. 4(3):56-63.
- Tresch, R.W. 2002. *Public Finance: A Normative Theory*. 2nd Ed. Academic Press: Massachusetts.

- Tuli, F. 2010. The basis of Distinction between Qualitative and Quantitative Research in Social Science: Reflection on Ontological, Epistemological and Methodological Perspectives. *The Ethiopian Journal in Education*. 6(1): 97-108.
- Ulbrich, H. H. 2011. *Public Finance in Theory and Practice*. 2nd Ed. New York: Routledge Taylor and Francis Group.
- UMgungundlovu District Municipality. 2013. Annual Report 2012/13. http://www.umd.gov.za/index.php?option=com_docman&Itemid=221. Accessed on 11 January 2014.
- Vyas-Doorgapersad, S., Ababio.S. 2010. The illusion of ethics for good local governance in South Africa. *The Journal for Trans-Disciplinary Research in Southern Africa*.6 (2): 411 – 427.
- Wessels, J.S. 2010. Institutional Affiliation and the Selection of Research Methods in Public Administration: A south African Perspective. *Journal of Public Administration*. 45(3):532-548.
- Wildasin, D.E. 2006. Local Government Finance in Kentucky: Time for Reform? *Institute for Federalism and Intergovernmental Relations Working Paper 2007(02)*:1-26.
- Yemek, E. 2005. Understanding Fiscal Decentralisation in South Africa. Cape Town: Budget Information Service, Idasa.
- Yilmaz, S. 2002. Equalization across Subnational Governments: Fiscal Capacity. World Bank Institute. www1.worldbank.org/publicsector/decentralization/fiscal%20capacity.doc. Accessed on 30 June 2014.
- Yilmaz, S., Hoo, S., Rueben, K. S., Nagowski, M. and Tannenwald, R. 2006. Measuring Fiscal Disparities across the U.S. States: A Representative Revenue System/Representative Expenditure System Approach, Fiscal Year 2002. *State Tax Notes* 45(12). <http://ssrn.com/abstract=1014528>. Accessed 5 November 2013.
- Yin, R. K. 2009. *Case study research: Design and Methods* 4th Ed. Thousand Oaks, CA: Sage
- Yulianti, I., Tung W. 2013. The Relationship among Brand Experience, Brand Image and Customer Satisfaction of Facebook Users in Indonesia. *World Applied Sciences Journal (Economic, Finance and Management Outlooks)*. 28(2013):100-113.

ANNEXURES

15 July 2014

Ms Kolile Mpumela (201294791)
School of Management, IT & Governance
Westville Campus

Protocol reference number: HSS/0802/014M
Project title: Equitable Share Formula and fiscal capacity in municipalities with particular reference to Msunduzi Municipality

Dear Ms Mpumela,

Full Approval – Expedited Application

In response to your application dated 07 July 2014, the Humanities & Social Sciences Research Ethics Committee has considered the abovementioned application and the protocol have been granted **FULL APPROVAL**.

Any alteration/s to the approved research protocol i.e. Questionnaire/Interview Schedule, Informed Consent Form, Title of the Project, Location of the Study, Research Approach and Methods must be reviewed and approved through the amendment/modification prior to its implementation. In case you have further queries, please quote the above reference number.

PLEASE NOTE: Research data should be securely stored in the discipline/department for a period of 5 years.

The ethical clearance certificate is only valid for a period of 3 years from the date of issue. Thereafter Recertification must be applied for on an annual basis.

I take this opportunity of wishing you everything of the best with your study.

Yours faithfully



.....
Dr Shenuka Singh (Chair)

/ms

Cc Supervisor: Dr Mogle Subban
Cc Academic Leader Research: Professor Brian McArthur
Cc School Administrator: Ms Angela Pearce

Humanities & Social Sciences Research Ethics Committee

Dr Shenuka Singh (Chair)





Westville Campus, Govan Mbeki Building

Postal Address: Private Bag X64001, Durban 4000

Telephone: +27 (0) 31 260 3587/8359/4557 Facsimile: +27 (0) 31 260 4609 Email: ximbap@ukzn.ac.za / snymann@ukzn.ac.za / mohupo@ukzn.ac.za

Website: www.ukzn.ac.za

 1910 - 2010 
100 YEARS OF ACADEMIC EXCELLENCE

Franchising Campuses:  Edgewood  Howard College  Medical School  Pietermaritzburg  Westville



national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Private Bag X115, Pretoria, 0001 - Tel: (+27 12) 315 5111 Fax (+27 12) 315 5045
Enquiries: Malijeng Ngqaleni (012) 395 6557 Fax: (012) 315 5993 Email: malijeng.ngqaleni@treasury.gov.za

The Researcher
Ms Xolile Mpumela (201294791)

Dear Ms X Mpumela

PERMISSION TO CONDUCT RESEARCH AS PART OF THE POST GRADUATE PROGRAMME

I am pleased to inform you that permission has been granted to you to conduct research on Equitable Share Formula and the fiscal capacity in municipalities with particular reference to Msunduzi Municipality.

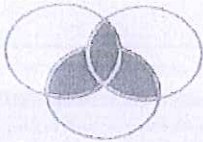
Please note the following:

1. The research can only commence once we have received confirmation of our ethical clearance for this study.
2. Ensure that our office is informed before you commence your research.

Yours sincerely

MS M NGQALENI
DEPUTY DIRECTOR GENERAL: INTERGOVERNMENTAL RELATIONS

Date: 20/06/2014



SALGA
South African Local Government Association

Eng: Mbali Mahlobo
Tel: 012 369 8000
Fax: 012 369 8001
E-mail: mmahlobo@salga.org.za
Date: 10 July 2014

Ms. Xoli Mpumela
Student: (201294791)
University of KwaZulu-Natal

Email: xmpumela@gmail.com

RE: PERMISSION TO CONDUCT RESEARCH EQUITABLE SHARE FORMULA AND FISCAL CAPACITY IN MUNICIPALITIES WITH PARTICULAR REFERENCE TO MSUNDUZI MUNICIPALITY

Dear Ms Mpumela,

Your request for permission to access SALGA information, dated 09 June 2014, refers.

I, Adv. RC Baatjies, duly authorised and on behalf of the South African Local Government Association (SALGA), hereby permit access to our information which will be availed to you for purposes of conducting your study on "Equitable share formula and the fiscal capacity in municipalities with particular reference to Msunduzi Local Municipality". This includes interviews to be conducted with SALGA staff members.

This permission is conditional on the grounds that the study is made available to us upon completion and that the integrity (including confidentiality where appropriate) of the Association is at all times upheld. We wish you success with this very important study and look forward to seeing its outcomes for the betterment of local government

Yours in the service of developmental local government

ADV. R.C. BAATJIES
HEAD OF INTERGOVERNMENTAL RELATIONS

- SALGA National
Block B
Menlyn Corporate Park
175 Corobay Ave
Cnr Garfontein Rd
Waterkloof Glen X11
Pretoria 0181
Tel: 012 369 8000
Fax: 012 369 8001
- Eastern Cape
1st Floor
3 Berea Terrace, Berea
East London 5214
Tel: 043 727 1150
Fax: 043 727 1156
- Free State
36 McGregor St
East End
Bloemfontein 9300
Tel: 051 447 1960
Fax: 051 430 8250
- Gauteng
3rd Floor Braampark
Forum 2, 33 Heald St
Braamfontein 2017
Tel: 011 276 1150
Fax: 011 403 3636
- KwaZulu-Natal
4th Floor Clifton Place
19 Hurst Grove
Muggrave
Durban 4000
Tel: 031 817 0000
Fax: 031 817 0034
- Limpopo
127 Marshall St
Pretokwane 0699
Tel: 015 291 1400
Fax: 015 291 1414
- Mpumalanga
SALGA House
11 Van Rensburg St
Nelspruit 1200
Tel: 013 752 1200
Fax: 013 752 5595
- North West
Suite 100, Jade Square
Cnr O R Tambo &
Margaretha Prinsloo St
Klerksdorp 2570
Tel: 018 462 6290
Fax: 018 462 4662
- Northern Cape
Crescent House
1 & 2 D'Arcy St
Kimberley 8300
Tel: 053 836 7900
Fax: 053 833 3628
- Western Cape
SALGA House
7th Floor, 44 Strand St
Cape Town 8000
Tel: 021 446 9800
Fax: 021 418 2709

The Msunduzi Municipality

Private Bag X 321
Pietermaritzburg
3200
(033) 392 2002

City Hall, Chief Albert Luthuli Street
Pietermaritzburg
3201
www.msunduzi.gov.za



Enq: Bongani Ngobese

Tel: 033 392 2138

E-mail: Bongani.Ngobese@msunduzi.gov.za

25/6/2014

University of Kwazulu-Natal
University Rd
Westville
4000

Xolile Mpumela
Student no: 201294701
Email : Xolile.Mpumela@treasury.gov.za

Dear Madam

RE : Equitable Share Formula and the fiscal capacity in municipalities with particular reference to Msunduzi Municipality.

Please be advised that you hereby granted permission to conduct your research within Msunduzi Municipality, subject to the following conditions:

- I. You will forward a copy of the completed research report to the Office of the Municipal Manager, c/o Ms Madeleine Jackson-Plaatjies as per the above contact details;
- II. None of the information and/or findings obtained during the research project will be used to construe the Municipality in a negative light and/or against the Municipality in any court of law.

I trust the above is in order
Yours sincerely

MS M JACKSON-PLAATJIES
MANAGER: OFFICE OF THE MUNICIPAL MANAGER

OFFICE OF THE MUNICIPAL MANAGER

Telephone/uCingo: 033 3922002
Facsimile/iFekisi: 0868047309

Private Bag / Isikhwama: X321
Pietermaritzburg/ePietermaritzburg 3201

Language Practitioner/Specialist: Language in Education

T. Reddy

B.A. ; U.E.D. (Natal); B.A. Hons. (UNISA); M.A. (Linguistics); Cert. in TESOL (Pittsburgh, USA);

Fellow English Speaking Board (Int.) UK

Tel (h) : 031 564 6975

Cell : 083 784 6975

e-mail : tcdreddy@gmail.com

To whom it may concern

Date 15 November 2015

Re: Language Practitioner Report

Student Xolile Mpumela Number 201294791

Dissertation : Equitable Share Formula and fiscal capacity in municipalities with particular reference to Msunduzi Municipality

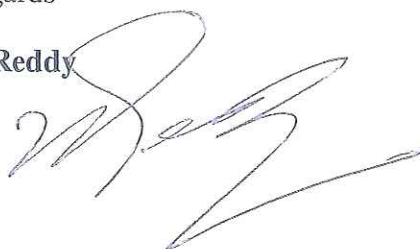
I have had the pleasure of reading the above dissertation submitted for the degree of Master of Administration, School of Management, Information Technology and Governance at the College of Law and Management Studies, and found the language usage fluent and free of any grammatical inaccuracies.

The work has been read for punctuation, fluency and congruency, and meets the language and stylistic writing at this postgraduate level.

I deem the dissertation acceptable for final admission.

Regards

T. Reddy





School of Management, Information Technology and Governance

Master's in Public Administration Research Project

Researcher: X. Mpumela (201297791)

Contact details: 0734647989 / xmpumela@gmail.com

Research supervisor: Dr M. Subban

Contact details: 031 260 7763 / subbanm@ukzn.ac.za

Research Office: Mrs Mariette Snyman

Contact details: 0734647989 / xmpumela@gmail.com

Dear Participant,

I am a registered Masters in Public Administration student at the University of KwaZulu- Natal. You are kindly invited to participate in this research study titled: ***Equitable Share Formula and the fiscal capacity in municipalities with particular reference to Msunduzi Municipality.*** The objective of this study is to assess the appropriateness of the current local government equitable share formula in addressing the fiscal capacity of municipalities.

Your participation in this study is voluntary and you may withdraw your participation at any time with no negative consequence, should you wish to do so. Please note that there will be no monetary gain from participating in this study. Your participation in this study will be treated as confidential and your anonymity will be maintained throughout the duration of this project.

Should you have any questions with regard to your participation or completion of the questionnaire, you may contact me or the research supervisor on the contact details provided above.

Yours sincerely,

Xolile Mpumela

Student: Master's in Public Administration

University of KwaZulu- Natal

Date: 10 July 2014

Protocol reference number: HSS/0802/014M

QUESTIONNAIRE: NATIONAL TREASURY

INSTRUCTIONS

- Thank you for taking time to respond to the research questionnaire.
- The questionnaire is for a Masters study titled: *Equitable Share Formula and fiscal capacity in municipalities with particular reference to Msunduzi Municipality*, and will not take you longer than 10 minutes to complete.
- Mark the relevant box with a cross (X), and furnish brief responses where applicable.
- Please be assured that your responses will be confidential.

SECTION A: PROFILE OF RESPONDENT

SECTION A: PROFILE

1. Gender:

Male	
Female	

2. Age

18 < 35	
36 < 40	
41 < 50	
51 < 65	

3. Number of Years in Organisation

0- 6 years	
7- 12 years	
13- 18 years	
< 18 years	

4. Designation

Non-supervisory level	
Supervisory level	
Middle management	
Senior management	

5. Level of Education

Secondary school	
Matric	
Tertiary (degree or diploma)	
Postgraduate (Honours , M-level, PhD)	

SECTION B: PRACTICAL CONTEXT

National Treasury:

B1. Ensure transparency, accountability and sound financial controls	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B2. Supports efficient and sustainable financial management and good governance	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B3. Ensures that nationally raised revenue is shared equitably across all spheres of government	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B4. Educates municipalities on the process of horizontal division of revenue	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B5. Has no obligation to compensate municipalities that do not raise revenue proportionate with their fiscal capacity and tax base	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B6. Ensures that the Equitable Share is disbursed to all municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B7. Regularly monitors the expenditure on the Equitable Share for all municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B8. Ensures consistency between the Equitable Share allocation and the disbursed funds to municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B9. Ensures timeous disbursement of the Equitable Share to municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B10. Ensures that the Equitable Share is spent in an effective and efficient manner	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

B8. Equitable Share allocation mainly provides for the following basic services

Water	
Sanitation	
Electricity	
Roads	

B9. Equitable Share:

A. Is a funding mechanism for fulfilling governments' developmental agenda	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Main objective is to ensure equitable distribution of funds across municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Supports national government's priorities for sustainable access to basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
D. Is the main source of revenue for most municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
E. Enables municipalities to build administrative and governance capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
F. Provides the total cost of providing basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

B10. New Equitable Share formula:

A. Ensures that all South Africans have access to basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Ensures that resources are allocated in an efficient and equitable manner	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Is the most appropriate mechanism of achieving equitable distribution of resources to municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

SECTION C: PRINCIPLES AND STRUCTURE OF THE EQUITABLE SHARE FORMULA

C1. New Equitable Share Formula:

A. Is informed by the fiscal conditions of municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Addresses fiscal imbalances in municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Different costing for basic services for each municipality is applied	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
D. Provides for equitable sharing of resources	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
E. Is transparent and simple	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
F. Is objective and fair	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
G. Recognises diversity among municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
H. Provides for predictability and stability	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
I. Allocates greater resources to municipalities with low fiscal capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
K. Considers the municipality's effort to generate own revenues	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
L. Allocates greater resources to municipalities to with greater needs	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
M. Provides certainty regarding the municipality's allocation over the Medium Term Expenditure Framework period	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

N. Allows municipalities to plan and budget effectively	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
O. Fully reflects the Constitutionally mandated basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
P. Accurately captures the cost of providing basic services for each municipality	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Q. Poverty measure correctly captures the socio-economic needs of each municipality	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
R. Institutional component promotes good governance in the municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
S. Promotes efficient utilisation of finances in local government	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
T. Is immune to subjective adjustments that favour particular municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
U. Considers the uniqueness of the municipality	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
V. Data cannot be manipulated	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
W. Is dynamic and responds to changes in the circumstances of municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
X. Is flexible and can respond to data and policy changes	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Y. Is immune to political influence	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

C2. The following components of the formula require further review (please, also provide reasons):

a)

b)

c)

d)

SECTION D: EQUITABLE SHARE FORMULA AND SERVICE DELIVERY

D1. Equitable Share

A. Supports national priorities for sustainable access to basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Enables municipalities to provide of basic services to poor communities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Enables municipalities with limited revenue bases to afford basic administrative capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
D. Enables municipalities with limited revenue bases to afford basic governance capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
E. Encourages municipalities' own revenue raising efforts	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
F. Discourage the municipality's own revenue raising efforts	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
G. Can weaken the long-term financial sustainability of municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
H. The Equitable Share can create fiscal dependency in many municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

I. Strengthens the long-term financial sustainability of municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
J. Is mechanism for promoting good governance in municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

D2. New Equitable Share Formula:

A. Creates incentives for efficient service delivery	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Creates a foundation for sustainable provision of basic services to communities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. New Equitable Share formula is appropriate for fiscally capacitating municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

Thank you for your participation

QUESTIONNAIRE: SOUTH AFRICAN LOCAL GOVERNMENT ASSOCIATION (SALGA)

INSTRUCTIONS

- Thank you for taking time to respond to the research questionnaire.
- The questionnaire is for a Masters study titled: *Equitable Share Formula and fiscal capacity in municipalities with particular reference to Msunduzi Municipality*, and will not take you longer than 10 minutes to complete.
- Mark the relevant box with a cross (X), and furnish brief responses where applicable.
- Please be assured that your responses will be strictly confidential.

SECTION A: PROFILE

6. Gender:

Male	
Female	

7. Age

18 < 35	
36 < 40	
41 < 50	
51 < 65	

8. Number of Years in Organisation

0- 6 years	
7- 12 years	
13- 18 years	
< 18 years	

9. Designation

Non-supervisory level	
Supervisory level	
Middle management	
Senior management	

10. Level of Education

Secondary school	
Matric	
Tertiary (degree or diploma)	
Postgraduate (Honours , M-level, PhD)	

SECTION B: PRACTICAL CONTEXT

B1. SALGA promotes the interests of local government	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B2. SALGA transforms local government to enable its developmental role	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B3. SALGA participates in all fiscal, budgetary or financial decisions affecting municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B4. System of horizontal distribution of revenue is understood clearly within the organisation	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B5. New Equitable Share formula is the most appropriate mechanism for equitable distribution of revenue to local government	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B6. Equitable Share is the main source of revenue for most municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B7. Equitable Share main objective is to ensure equitable distribution of resources across municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B8. SALGA regularly monitors the expenditure on the Equitable Share for all municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B9. There is consistency between the Equitable Share allocation and the disbursed funds to municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B10. Equitable Share is always disbursed on time	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B11. Municipalities spend the Equitable Share in an effective and efficient manner	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

B12. Equitable Share allocation mainly provides for the following basic services:

Water	1
Sanitation	2
Electricity	3
Roads	4

B13. Equitable Share:

A. Promotes the Constitutional goal of ensuring that all South Africans have access to basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Is a funding mechanism for fulfilling governments' developmental agenda	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Supports national government's priorities for sustainable access to basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

SECTION C: PRINCIPLES AND STRUCTURE OF THE EQUITABLE SHARE FORMULA

C1. New Equitable Share Formula:

A. Is informed by the fiscal conditions of municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Addresses fiscal imbalances in municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Different costing for basic services for each municipality should be applied	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
D. Provides for equitable sharing of resources	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
E. Is transparent and simple	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

F. Is objective and fair	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
G. Recognises diversity among municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
H. Provides for predictability and stability	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
I. Allocates greater resources to municipalities with low fiscal capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
K. Considers the municipality's effort to generate own revenues	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
L. Allocates greater resources to municipalities to with greater needs	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
M. Provides certainty regarding the municipality's allocation over the Medium Term Expenditure Framework period	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
N. Allows municipalities to plan and budget effectively	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
O. Fully reflects the Constitutionally mandated basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
P. Accurately captures the cost of providing basic services for each municipality	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Q. Is immune to political influence	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

C2. Equitable Share:

A. Enabled municipalities to build administrative capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
--	-------------------	----------	---------	-------	----------------

B. Enabled municipalities to build governance capacity	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Provides the total cost of providing basic services	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

C3. The following components of the formula require further review (please, also provide reasons):

a)

b)

c)

d)

SECTION D: THE EQUITABLE SHARE FORMULA AND SERVICE DELIVERY

D1. Equitable Share:

A. Enables municipalities in fiscal distress to provide basic services to their communities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Weakens the long-term financial sustainability of the municipality	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Creates fiscal dependency in many municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
D. Strengthened the long-term financial sustainability of the municipality	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
E. Is mechanism for promoting good governance in municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
F. Has contributed positively to the enhancement of the quality of lives of local communities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

D2. New Equitable Share formula:

A. Creates incentives for efficient service delivery	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
B. Creates a foundation for sustainable provision of basic services to communities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
C. Is appropriate for fiscally capacitating municipalities	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

Thank you for your participation

QUESTIONNAIRE: MSUNDUZI MUNICIPALITY FINANCE UNIT

INSTRUCTIONS

- Thank you for taking time to respond to the research questionnaire.
- The questionnaire is for a Masters study titled: *Equitable Share Formula and fiscal capacity in municipalities with particular reference to Msunduzi Municipality*, and will not take you longer than 10 minutes to complete.
- Mark the relevant box with a cross (X), and furnish brief responses where applicable.
- Please be assured that your responses will be confidential.

SECTION A: PROFILE

11. Gender:

Male	✓
Female	

12. Age

18 < 35	
36 < 40	13.
41 < 50	
51 < 65	

14. Number of Years in Organisation

0- 6 years	✓
7- 12 years	
13- 18 years	
< 18 years	

15. Designation

Non-supervisory level	
Supervisory level	
Middle management	
Senior management	✓

16. Level of Education

Secondary school	
Matric	
Tertiary (degree or diploma)	17.
Postgraduate (Honours , M-level, PhD)	

SECTION B: PRACTICAL CONTEXT

B1. Municipality generates its revenue from the following sources:

User charges, Rates and Taxes	18.
Intergovernmental Grants	19.
Borrowing	
Other (please specify)	20.

B2. Municipality:

A. Is entitled to an equitable share of national government revenue	Strongly Disagree	Disagree	Neutral	21. Agree	Strongly Agree
B. Understands the process of horizontal division of revenue by national government	Strongly Disagree	Disagree	Neutral	22. Agree	Strongly Agree
C. Receives an Equitable Share from national government	Strongly Disagree	Disagree	Neutral	23. Agree	Strongly Agree
D. Main source of revenue is the Equitable Share	Strongly Disagree	24. Disagree	Neutral	Agree	Strongly Agree
E. Uses the Equitable Share to provide basic services to communities	Strongly Disagree	Disagree	Neutral	25. Agree	Strongly Agree
F. Ability to deliver services is dependent on the equitable share allocation	Strongly Disagree	Disagree	Neutral	26. Agree	Strongly Agree

B3. Municipality uses the Equitable Share allocation to provide the following basic services:

Water	27.
Sanitation	28.
Electricity	29.
Roads	30.

B3. The Equitable Share:

A. Promotes the Constitutional goal of ensuring that all South Africans have access to basic services	Strongly Disagree	Disagree	Neutral	✓ Agree	Strongly Agree
B. Is a funding mechanism for fulfilling governments' developmental agenda	Strongly Disagree	Disagree	Neutral	✓ Agree	Strongly Agree
C. Supports national government's priorities for sustainable access to basic services	Strongly Disagree	Disagree	Neutral	✓ Agree	Strongly Agree
D. Is always received on time	Strongly Disagree	Disagree	Neutral	✓ Agree	Strongly Agree
E. Allocated to the Municipality is consistent with the funds disbursed to the Municipality	Strongly Disagree	Disagree	Neutral	✓ Agree	Strongly Agree
F. Is spent in an effective and efficient manner	Strongly Disagree	Disagree	Neutral	✓ Agree	Strongly Agree

B4. Municipality reports regularly on the performance of the Equitable Share to the following organisations:

National Treasury	✓
CoGTA	✓
SALGA	
Other (please specify)	

SECTION C: PRINCIPLES AND STRUCTURE OF THE EQUITABLE SHARE FORMULA

C1. New Equitable Share formula:

A. Is informed by the fiscal conditions of municipalities	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
B. Is transparent and simple	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
C. Is objective and fair	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
D. Provides for predictability and stability	Strongly Disagree	Disagree	Neutral ✓	Agree	Strongly Agree
E. Provides certainty regarding the municipality's allocation over the Medium Term Expenditure Framework period	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
F. Allows the municipality to plan and budget effectively	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
G. Considers the municipality's potential to generate own revenues	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
H. Considers the municipality's effort to generate its own revenues	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
I. Fully reflects the Constitutionally mandated basic services	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
J. Accurately captures the cost of providing basic services for the municipality	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
K. Poverty measure correctly captures the Municipality's socio-economic needs	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
L. Institutional component of the formula promote good governance in the Municipality	Strongly Disagree	Disagree	Neutral ✓	Agree	Strongly Agree

M. Should apply different costing for basic services for each municipality	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
N. Is immune to political influence	Strongly Disagree	Disagree	Neutral ✓	Agree	Strongly Agree
O. Is the most appropriate mechanism of achieving equitable distribution of resources to municipalities	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree

C2. Equitable Share:

A. Enables the Municipality to build administrative capacity	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
B. Enables the Municipality to build governance capacity	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
C. Provides the total cost of providing basic services to poor households	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree

C3. The following components of the formula require further review (please, also provide reasons):

- a)
- b)
- c)
- d)

SECTION D: THE EQUITABLE SHARE FORMULA AND SERVICE DELIVERY

D1. New Equitable Share Formula:

A. Encourages the Municipality's own revenue raising efforts	Strongly Disagree	Disagree	Neutral ✓	Agree	Strongly Agree
B. Creates incentives for efficient service delivery in the Municipality	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
C. Discourages the Municipality's own revenue raising efforts	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
D. Weakens the long-term financial sustainability of the Municipality	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
E. Creates fiscal dependency in the Municipality	Strongly Disagree	Disagree ✓	Neutral	Agree	Strongly Agree
F. Strengthens the long-term financial sustainability of the Municipality	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
G. Is appropriate for fiscally capacitating the Municipality	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree

D2. Equitable Share:

A. Enables the Municipality to provide basic services to poor households	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
B. Creates a foundation for sustainable provision of basic services to communities	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree
C. Has contributed positively to the enhancement of the quality of lives of local communities	Strongly Disagree	Disagree	Neutral	Agree ✓	Strongly Agree

Thank you for your participation