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NATIONAL PARTY SUBMISSION

THEME COMMITTEE 3

GOVERNMENT FINANCE AND INTERGOVERNMENTAL FISCAL RELATIONS

In this submission the above subjects are discussed with reference to the provisions contained in the Interim Constitution.

**Introduction**

It is essential that the fiscal relations between the three tiers of Government should reflect the spirit of the Constitution, take cognisance of competences and functions allocated to the various levels of Government by the Constitution and enable them, by granting them on an equitable basis access to the country's tax base and financial resources, to reasonably perform their respective functions.

The ideal would be, in particular, to grant greater fiscal autonomy to the provinces. However, various factors militate against the implementation of such a fiscal model and **a more pragmatic approach, dictated by the realities of the South African situation, is therefore appropriate - namely a revenue sharing model, as outlined in the Interim Constitution.** It should nonetheless not be viewed as confining the provinces to the role of agents having to perform certain functions on behalf of the National Government. The fact that a revenue sharing model is supported, does not impair the competence of the provinces to manage the expenditure sides of their budgets. Furthermore, several examples of revenue sharing models exist in other countries.

The following economic imperatives need to be taken into account in the shaping of **fiscal** relations between the various tiers of Government:

- The **skewed distribution** of income and wealth, socioeconomic backlogs, also in respect of infrastructural services in certain regions, and the uneven distribution of economic activities and of the total population.
- **The tax base and its growth potential are extremely limited in certain regions** and as a consequence these regions will be almost entirely dependent on transfer payments from a national source **to maintain minimum standards** in respect of the functions assigned to them

in terms of the Constitution. The alternative is a vast migration of people to the existing cities which will in any event increase the fiscal burden of these growth metropolises.

- **It is impractical for each province to have its own tax administration and to raise its own taxes.** Such a tax dispensation may also give rise to the problem which reared its head under the previous constitutional system where some TBVC-states not only used the tax system (lower taxes) to attract enterprises but also failed to collect taxes efficiently and then expected the central Government to compensate them, through transfer payments and Government guaranteed loans, for the resultant loss of revenue. Great difficulty is currently being experienced to upgrade the administration of Inland Revenue and it will be an impossible task to establish competent tax administrations in each province. It is also in the interest of the provinces that the efficiency of Inland Revenue be improved without delay.
- **Maintaining fiscal discipline and macro-economic stability is of paramount importance and remains to a large extent the responsibility of the National Government.** The Provinces will in the final analysis, however, be key players in maintaining fiscal discipline. South Africa's total tax burden, for a developing country, is already high and additional tax revenue should rather be generated by higher economic growth than an increase in the total tax burden. The deficit before borrowing in the national budget is also too high and should be reduced. The assumption has always been that tax revenue from the National Government would be transferred to the provinces in respect of the functions for which they assume responsibility and that a higher tax burden should not result as a consequence - taking cognizance of the fact that loans are to some extent currently used to finance recurrent expenditure.

- **There is furthermore concern about the capability of some provinces to manage their financial affairs prudently** and it is consequently essential that their powers to raise taxes and loans be subject to checks and balances.
- **All taxes**, in respect of which the revenues thus collected have to be deposited in the National Revenue Fund for sharing with the provinces, **have to be raised via the budget** presented by the National Government.

**The point that needs to be emphasised is that the principle of transfer payments is well established in South Africa and that the centralised system of tax collection (for revenue sharing purposes) is an**

**unavoidable consequence of the structure of the economy.** It should, however, not distract from the competences of the provinces to perform the tasks assigned to them by the Constitution - within the constraints of available resources.

In order to protect the integrity of the office of the Commissioner of Inland Revenue from political interference in its performance as tax collector, it is deemed desirable that the Commissioner should be granted independent status and that his office should fall under a supervisory body similar to the Audit Commission.

#### **Prohibition on the withholding of a province's share of revenue**

**The fiscal relations between the National Government and the Provinces should furthermore be structured in such a manner that the National Government cannot abuse these financial relations to coerce provinces to implement policies dictated by it for reasons other than financial maladministration.** It will create an untenable situation should the National Government attempt to use the centralised tax collection system, the product of practical considerations, to dictate policies to the provinces - which may in any event infringe their constitutional competences and impact adversely on the people of such provinces.

It is consequently proposed that the following provision be inserted after Section 155(3) of the Interim Constitution:

"The amounts referred to in subsection (1), without any deductions, shall be transferred to the Provinces and no share thereof shall be withheld other than on the basis of a resolution by Parliament following a report by the Auditor-General confirming gross maladministration by a Province."

**The existing fiscal arrangements between the National Government and the Provinces as arranged in terms of the Interim Constitution**

The Sixth Schedule to the Interim Constitution, read in conjunction with Section 126, details the functions which fall within the competences of the Provinces. This matter may still be open to negotiation.

**It is vitally important that absolute clarity be obtained about the functional competences of the various tiers of Government as this aspect has serious implications for intergovernmental financial relations. However, we are more concerned here about the financial principles involved than the actual distribution of functions between the various tiers of government.**

**(a) Revenue sharing between the National and Provincial Governments.**

The factors that impact on the fiscal relations between the National Government and Provinces, as alluded to above, had been taken into account in the drafting of the Interim Constitution. **The National Party is therefore broadly supportive of the tax revenue sharing model as outlined in Section 155 of the Interim Constitution - read in conjunction with Section 199.**

The National Party proposes that the following taxes and incomes should be collected nationally and be deposited in the National Revenue Fund for **revenue sharing purposes**:

- . Direct taxes: personal and corporate plus mining taxation
- . VAT or any other sales tax
- . Fuel levies
- . Customs and excise duties and any levies imposed thereon
- . Estate duties

**The servicing of national debt should have first claim on the taxes collected nationally and the balance should be shared between the National Government and the Provinces on the basis of formulae recommended by the Financial and Fiscal Commission - as outlined in Section 155 (4), but subject to the condition that the fiscal competences of and the taxes raised by the Provinces, in view of the limited extent of the sources of revenue available for this purpose, shall not be taken into account to determine the share of revenue to be allocated to each Province.**

**(b) Levying of taxes by Provinces.**

The National Party proposes that the taxes listed hereunder should fall within the **exclusive** competences of the Provinces. There should be provision to add to this list on recommendations by the Financial and Fiscal Commission.

- \* Stamp duties
- \* Transfer duties
- \* Vehicle licences
- \* Toll taxes
- \* Taxes, levies and duties imposed on casinos, gambling, wagering, betting and lottery tickets.

The rate of stamp and transfer duties shall, however, be determined by the National Government in consultation with the Provinces and it shall also have the right to abolish these duties if so recommended by the Financial and Fiscal Commission.

The National Party also proposes that a provincial legislature should be competent to enact legislation authorising the imposition of user charges, as provided for in Section 156 (3) of the Interim Constitution.

**The National Party is of the opinion that the Provinces should in principle have the competence to impose levies on taxes raised by the National Government, as provided for in Section 156(1) of the Interim Constitution.**

All revenues accruing to a Province shall be paid into a Provincial Revenue Fund.

**(c) Raising of loans and Government guarantees**

The National Government currently uses loan funds to finance some consumption expenditure and it implies therefore, as long as this undesirable practice persists, that a portion of the loan funds raised by the National Government will have to be included as part of the transfer payments to the Provinces.

**The National Party is of the opinion that the Constitution should provide for the establishment of a Loans Authority to co-ordinate the issue of loan stock and to determine policy for the**

**management of the debt of the three tiers of government and guarantees provided by them.**

The details should be contained in an act of Parliament.

**The National Party proposes that the three tiers of government may not borrow to finance current expenditure.**

Borrowing by the Provinces (see also Section 199 (1)(d) of the Interim Constitution), which may be in lieu of loans raised by the National Government, imposes demands on the South African capital market and affects the general government's total budget deficit before , borrowing. It is

therefore essential that the borrowings by the general government institutions shall be properly co-ordinated. The NP proposes that a Committee under the chairmanship of the Minister of Finance be established to co-ordinate the borrowing requirements of the general government which should also take into account the ability of the public sector bodies to service such debt. General Government faces a possible debt trap and it is therefore essential that strict control should be exercised on its total loan requirements as well as the management of the debt of the three tiers of government.

As far as the competence of Provinces to raise loans is concerned, the National Party supports the principles as enunciated in Section 157 of the Interim Constitution.

(d) **Expenditure by Provinces**

**As in the case of the National Government, the servicing of Provincial debt should have first claim on the revenues accruing to the Provinces.**

Allocations to the Provinces to finance the provision of services have to be based on nationally determined minimum criteria - as laid down by Sections 126 and 199(e) of the Interim Constitution. The National Government can in terms of Section 126 of the Interim Constitution withhold the allocation of tax revenue to a Province which does not maintain minimum standards of services. The reason for this provision is obvious. The NP is, however, of the opinion that it should be scrapped and that the Provinces should enjoy greater autonomy to determine spending priorities in respect of the functions they have to perform and the standard of the services provided by them.

It is essential that the Provinces should maintain financial records in accordance with established accounting standards and introduce effective auditing procedures - to the satisfaction of the Auditor-General. **The NP also proposes that the National Government should have the power to take over the financial management of a province, or certain elements thereof, should a**

**Province, in the view of Parliament after a report to that effect from the Auditor-General, be regarded as incompetent to perform this task or certain elements thereof.**

### **The fiscal competences of Local Authorities**

The NP is in agreement with the powers and functions accorded to Local Authorities in terms of Section 175 of the Interim Constitution, the sources of taxation reserved for them in terms of Section 178 and the provision for transfer payments from the Provinces - in accordance with criteria recommended by the Financial and Fiscal Commission. The National Party is of the opinion that the revenue from property rates and land taxes should accrue to Local Authorities.

The borrowing activities of Local Authorities should also be subject to the surveillance and disciplines applicable to the Provinces. The Provinces shall be obliged to transmit to the Local Authorities all funds received from the National Government earmarked for Local Authorities.

### **The Financial and Fiscal Commission (FFC) (Sections 198 to 206)**

The NP is of the opinion that the Constitution should provide for the FFC, in much the same way as outlined in the Interim Constitution. The NP furthermore proposes that experts on local authority finances should gain greater representation on the Commission.

### **Provincial FFC's**

The NP proposes that the Constitution should provide for the establishment by Provincial Statute of a body similar to the FFC in each Province to deal with the financial and fiscal relations between the Province and Local Authorities in its area of jurisdiction. Each Province and the Local Authorities within its boundaries should have equal representation on the proposed Commission.