NATIONAL TREASURY BRIEFING TO THE STANDING COMMITTEE ON FINANCE ON THE 2011/12 ANNUAL REPORT

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national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Introduction

- The National Treasury is responsible for managing South Africa's national government finances, and draws its mandate from Chapter 2 of the Public Finance Management Act, together with Chapter 13 of the Constitution

- Treasury contributes directly to outcomes **4** *(Decent employment through inclusive economic growth*), **9** (*A responsive, accountable, effective and efficient local government system*) and **12** (*An efficient, effective and development oriented public service and an empowered, fair and inclusive citizenship*)

- During the reporting period, we continued to respond to the 2008 recession with appropriate fiscal and other measures to promote sustainable growth

- A framework was also developed which provided for a shift in expenditure planning so that budgeting occurs by function rather than by department

- Promoting greater accountability and transparency in government remains one of our key focus areas, and we developed fraud detection guidelines and issued instruction notes strengthening supply chain management practices

Overview

- February macroeconomic forecasts projected GDP growth of 2.7 per cent in 2012 set to rise to around 4 per cent by 2014
- IMF latest growth forecast is 2.6 per cent this year and 3.0 per cent next year
- Inflation has moderated during the course of the year and is expected to remain within the target band
- Investment has been supported largely by government and public corporations
- Two credit rating agencies have downgraded South Africa's sovereign rating. They have cited concerns relating to the sustainability of the growth trajectory due to the slow pace of policy implementation and growing income inequality. They have kept SA on negative outlook
- Debt stock rose in line with wider budget deficit

Overview - continued

- Fiscal policy anchored on the principles of countercyclicality, sustainability and intergenerational fairness
- Bigger focus on value for money and the shifting of resources from consumption towards infrastructure investment, and support for economic competitiveness
- Need to strengthen efficiency in public spending, eliminate wastage, improve the alignment between allocations and policy priorities, and root out corruption

Major achievements

- **Among the highlights for the year was the training of 10 055 councillors across the country.**

  Improved budget support and oversight of local government remains a significant feature of the work of the Treasury.

- ***The revised gross borrowing requirement of R173 billion was successfully financed.***

  US$1.5 billion raised in the international capital market, R149 billion in the domestic capital market, and R5 billion from retail bond investors.

- ***Treasury continued to play its part in government's multilateral engagements.***

  The past year was marked by efforts to ensure the implementation of key recommendations agreed to by G20 heads of state and intended to reform global economic governance principles

Major achievements continued….

- ***The public service remuneration analysis and forecasting unit was established to monitor the impact of government's compensation policy on the fiscus***. Public service remuneration is the single largest component of the budget and in order to achieve fiscal sustainability an increased focus on public-sector remuneration is required.

- ***The National Treasury has begun implementing proposals to strengthen the financial regulatory system.*** This is being undertaken to ensure suitable oversight of international and national financial architecture, banking systems, equity and bond markets, and related institutions.

- ***The National Capital Projects unit carried out substantive work on feasibility studies for major national infrastructure projects*** in support of greater infrastructure investment and economic growth.

- ***Legal establishment of the Government Technical Advisory Centre (GTAC) has been completed to support the roll-out of various programmes in government.*** This is in support the effort to improve the overall performance of government. Further work will continue to prepare for the launch of the GTAC on 1 April 2013.

Sovereign rating developments

2011 / 12

		Moody's	S&P	Fitch	R&I
Lower Risk	Investment Grade	Aaa	AAA	AAA	AAA
		Aa1	AA+	AA+	AA+
		Aa2	AA	AA	AA
		Aa3	AA-	AA-	AA-
		A1	A+	A+	A+
		A2	A	A	A
		A3	A-	A-	A- (stable outlook)
		Baa1 (-ve outlook)	BBB+	BBB+ (-ve outlook)	BBB+
		Baa2	BBB (-ve outlook)	BBB	BBB
		Baa3	BBB-	BBB-	BBB-
High Risk	Speculative Grade / Non - Investment Grade	Ba1	BB+	BB+	BB+
		Ba2	BB	BB	BB
		Ba3	BB-	BB-	BB-
		B1	B+	B+	B+
		B2	B	B	B
		B3	B-	B-	B-
		Caa1	CCC+	CCC+	CCC+
		Caa2	CCC	CCC	CCC
		Caa3	CCC-	CCC-	CCC-
		Ca	CC	CC	CC
		C	C	C	C
		D	D	D	D

Current Rating

1st Rating assigned in 1994

- Moody's revised SA's credit outlook in November 2011 to negative from stable.
- This was followed by Fitch in early January 2012 and S&P in March 2012, both revising SA's credit outlook to negative from stable.
- R&I affirmed SA's stable outlook.

Constraints assigned by major rating agencies
2011/12

- ***Debt targets could be undermined by popular pressures ahead of the 2014 National and Provincial elections.***

- ***Expectations that growth will be slower than previously expected, insufficient to prevent already high unemployment rates from increasing further, thereby exacerbating social tensions.***

- ***South Africa's external finances are also deteriorating.***

- ***Slow progress on several long-standing structural issues have over time caused South Africa's economic performance to fall behind its peers.***

Treasury's view

- Our fiscal path remains realistic, achievable and sustainable
- It is framed within a context of tough global economic challenges:
  - Global growth is slow
  - Europe, our major trading partner, is in crisis
- We shall stay the course
  - Strike the balance between supporting the economy in ST
  - Fiscal consolidation
- Underpinned by fiscal guidelines
  - Countercyclicality, debt sustainability and fairness across generations

Programme 2: Economic Policy, Tax, Financial Regulation and Research

(Division 1 – Tax & Financial Sector Policy)

- Discussion paper on Medical Tax Credits published on 17 June 2011
- Financial Markets Bill and Credit Ratings Services Bill published in August 2011 and submitted to Parliament in February 2012
- Policy paper on retirement savings completed for Budget Day 2012, but only released in new financial year
- Rates and Monetary Amounts and Amendment of Revenue Laws Bill published on 13 March 2012
- Secondary Tax on Companies phased out on 31 March 2012
- Assisted the Department of Trade and Industry with the design of the manufacturing competitiveness enhancement programme
- Continued with improvements to economic models to enhance assessment of impacts of energy and tax policies

Programme 3: Public Finance & Budget Management
(Division 1 – Budget Office)

- Ensured that the budget frameworks for MTBPS and the Budget Review were tabled on time and included an estimate of the structural budget balance

- Provided comprehensive analysis of performance measurements and reporting by departments and entities in line with improved guidelines emphasising cost effectiveness and enhanced performance management

- Extended the scope of the draft regulations to encompass procurement that is particular to the construction environment, to cover the whole project life cycle of infrastructure projects, from planning to procurement

- The 2012 Budget process was characterised by decisions following a functional budgeting approach, which allowed for enhanced value-for-money assessments during the budget allocation process. This approach groups together national, provincial and local government, and government agencies, in terms of the function they perform

Programme 3: Public Finance and Budget Management
(Division 2 – Public Finance)

- Public Finance division is responsible for liaison with national departments on budgeting and expenditure monitoring issues, and supports the Minister of Finance in policy advice and inter-departmental correspondence and consultation.

- The broad functional groups established for the 2011/12 budget process have contributed to improved planning and coordination, which has provided a sound foundation for the 2012 MTEC process and preparation of next year's budget.

- Improvements to the *Estimates of National Expenditure* include revised programme structures and performance indicators, more comprehensive information on public entities in the detailed vote chapters (on website) and improved inter-departmental consultation

- A new quarterly expenditure reporting system has been developed for national departments, implemented with effect from the 1st Quarter 2012/13 report to the Standing Committee on Appropriations

Programme 3: Public Finance and Budget Management
(Division 3 – Intergovernmental Relations)

- Introduced reforms to the provincial and local government fiscal system to:
  - Improve its functioning,
  - Strengthen the conditions in the 2012 DoRA aiming to improve infrastructure delivery outcomes, and
  - Direct more resources towards poor resourced municipalities

- Implementing the City Support Programme
- Extension of energy efficiency conditional grant and introduce a new to fund internship for technical skills in municipalities

- Strengthening technical and leadership capacity in municipalities by providing:
  - Induction for new Councillors, Mayors and Municipal Managers and
  - In partnership with the University of Cape Town, World Bank Institute and SALGA delivered Leadership in Local Government for Mayors and Municipal Managers as one element of the City Support Programme

Programme 4: Asset & Liability Management

- Financed gross issuance of R185.4 billion
- Debt service costs of 2.6 per cent of GDP as projected
- Funding was below risk allocations by 2 percentage points, while the composition of government debt still deviated from long-term risk guidelines. The switch auction strategy on selected government bonds reduced the refinancing risk.
- Achieved a saving of up to 3.5% on borrowing costs due to intergovernmental cash coordination
- Monitored SOCs and development finance institutions on progress made in line with their strategic plans, borrowing and capital expenditure plans in particular those where their debt had been guaranteed by government
- Net debt provisions plus contingent liabilities increased to 46.15 per cent of GDP

Programme 5: Financial Accounting & Reporting

(Division 1 – Office of the Accountant-General)

- Departmental reporting framework for 2012/13 was finalised by 31 March 2012 and the draft framework for 2013/14 was finalised and published for comment;
- Sixteen generic financial management policies were developed;
- Consolidated Annual Financial Statements for departments and public entities for the 2011/12 financial year compiled and in process of being audited with a view to be tabled by 31st of October 2012;
- Strategic support plans developed and implemented for all prioritised entities;
- Financial management capacity building strategy updated to include local government;
- 22 financial management learning programmes developed;
- 1419 officials trained in financial management disciplines;
- Conducted internal audit/state of readiness reviews in 13 institutions;

Programme 5: Financial Accounting & Reporting

(Division 1 – Office of the Accountant-General) - continued

- Assessed financial management capabilities of national and provincial departments through the Financial Management Capability Maturity Model;
- Developed 30 new indicators to enhance monitoring and reporting of the implementation of the MFMA;
- Financial management implementation (technical) support availed to 69 small and rural municipalities;
- Conducted performance audits on major public procurement in 14 departments and municipalities;
- Conducted 11 forensic investigations that resulted in reports for further criminal investigation;
- Investigated contraventions of policies and regulations, the outcomes of which 26 criminal charges being laid with the South African Police Service and 32 disciplinary cases laid with the South African Police Service as part of the national government team that intervened in Limpopo in terms of section 100 of the Constitution.

Programme 5: Financial Accounting & Reporting
(Division 2: Specialist Functions)

SCM:

- Steady progress made towards development of procurement catalogue – all corporate contracts completed plus four transversal contracts
- Customization of PMM in NT lead site: BAS integration and certain critical gaps completed.
- Training material for Strategic Sourcing Principles was completed in collaboration with PALAMA and training commenced in 4th quarter (91 officials from all spheres attended training programme)
- Revised PPPFA Regulations came into effect on 7 December 2011 to align PPPFA with BBBEEA
- Guidelines issued to improve capacity i.r.o. Demand Management (Instruction note of 31 May 2011 introduced a mechanism to submit annual procurement plans)
- Of the 32 transversal contracts, 19 contracts were renewed,12 contracts were taken over by DOH, and 1 contract extended

Programme 5: Financial Accounting & Reporting
(Division 2: Specialist Functions), continued

Systems:

- Current systems (BAS, LOGIS, PERSAL, VULINDLELA) were available 99% of the time, as per target

IFMS:

- HRM Module: Completed at DPSA; FSDH continuing
- PMM Module: Completed at NT lead site; on going in DOD
- AMM Module: Completed at NT and 4 Limpopo lead sites
- BI Module: Completed during last quarter. Testing started
- Tenders for payroll was advertised by SITA and tender adjudication processes in progress
- Tender for Finance has been awarded
- Inventory Management module is being developed in house (Bespoke)

Programme 6: International Financial Relations

The division made significant strides in advancing the interests of SA in bilateral and multilateral engagements, with a strong focus on economic development of the African continent. Some of the **highlights** in 2011/12, include:

International engagements

- Engagements dominated by an uncertain global economy, especially the euro debt crisis;
- Actively engaged in a lobby for the reform of the international financial architecture;
- Strengthened the operations of the SA,Nigeria, Angola constituency in the World Bank, and of the African constituency in the IMF.
- Strengthened cooperation with other departments to enhance advancement of SA policy imperatives in BRICS and G20;
- Forged relations with a select number of BRICS, G20, African and Nordic Finance Ministers.

African engagements

- Engagement in Africa premised on economic opportunities, institutional reform; and outreach;
- Participate in development of regional economic integration strategies and infrastructure financing mechanisms;
- Negotiating changes to SACU revenue-sharing formula with BLNS countries;
- Support to AfDB constituency office, and facilitated the opening of a Regional Resource Centre of the AfDB;
- Strengthened PFM outreach programmes through CABRI.

Programme 8: Technical & Management Support and Development Finance

- The Technical Support and Management and Development Finance programme provides specialised infrastructure development planning and implementation support and technical assistance to aid capacity building in the public-sector.

Highlights include:

- The *Technical Assistance Unit (TAU)* supported 86 projects, focusing mainly on the areas of organisational development, strategic planning and performance budgeting
- The *Public Private Partnership* (PPP) unit focused on concluding partnership agreements, increasing oversight capacity and promoting capital investment, especially in the social sector
- The neighbourhood development programme provided technical assistance to 60 municipalities and contributed R50.1 million towards long-term township regeneration, planning and coordination in local government. Expenditure against the direct grant amounted to R783.3 million (98 per cent of the budget amount)

Programme 8: Technical & Management Support and Development Finance - continued

- The *Infrastructure Delivery Improvement Programme (IDIP)*
  - delivered draft construction procurement standards for use by provincial treasuries to assess and improve compliance by implementing departments, and
  - Concluded an agreement with the University of Pretoria as a pilot site for the development and management of an Infrastructure Delivery Management Toolkit training course.
- The *Municipal Finance Improvement Programme (MFIP)* is a new multi-year programme that was established to render technical assistance and support in implementing financial management reforms in local government.
- The *Jobs Fund*, which was allocated R2 billion for the 2011/12 financial year, has been established. To date R1.8 billion has been allocated to 34 projects and 21 000 jobs were created.

Programmes 7, 9 and 10

These programmes are primarily relate to fiscal transfers

- **Programme 7 (Civil and Military Pensions)** deals with the payment and administration of special pensions, military pensions, other statutory pensions, and post-retirement medical subsidies. More information is available on page 94 of the Annual Report

- **Programme 9 (Revenue Administration)** refers to transfers made to the South African Revenue Service during the 2011/12 year. See page 97 for transfers made in the 2010/11 financial year

- **Programme 10 (Financial Intelligence and State Security)** refers to transfers made to the Financial Intelligence Centre and Secret Services to combat financial crime including money laundering and terror financing activities, and to gather intelligence for purposes of national security, defence and combating crime.is also a programme that refers to transfers made during the 2011/12 year.

Programme 1: Administration

This programme provides leadership, strategic management and administrative support to the department.

Highlights include:

- Increased awareness on risk management and corruption;
- First national department to close its financial books for the year;
- Strategic sourcing and its economies of scale is yielding desired cost reduction;
- A secured environment ensured no leakage of economic or financial policy matters

Human Capital

- Total staff complement of 1150: 55 % female, 80% black. At senior management level, 57% black and 43% female.
- The National Treasury had a vacancy rate of 9.5 % (121 posts) at the end of the 2011/12 financial year.
- Of the 239 offers made, 223 accepted while 16 declined
  - *Reasons advanced for declining offers relate to salaries, counter offers, and other developmental career choices.*
- A total of 125 critical skills positions were filled during the financial year.
- In partnership with Disabled People South Africa, National Treasury is increasing attraction of candidates with disabilities. NT achieved 1.04% of the 2% target.
- The employee lifestyle management programme is utilised by 87.3 % of employees;
- 68 % of Directors and 85 % of Chief directors participated in the Leadership development programme

Outcome: Expenditure

2011 / 12

Programmes	2011/12 Final Budget	2011/12 Final Outcome	Variance	% Variance
R'000				
1. ADMINISTRATION	281,067	254,534	26,533	9.4%
2. ECONOMIC POLICY, TAX, FINANCIAL REGULATION AND RESEARCH	210,364	140,467	69,897	33.2%
3. PUBLIC FINANCE AND BUDGET MANAGEMENT	209,878	196,429	13,449	6.4%
4. ASSET AND LIABILITY MANAGEMENT	825,860	821,907	3,953	0.5%
Operational budget	*75,860*	*71,907*		
Transfer to Land Bank	*750,000*	*750,000*		
5. FINANCIAL SYSTEMS AND ACCOUNTING	608,020	504,861	103,159	17%
Operational budget	*534,416*	*431,662*		
Transfers	*73,604*	*73,199*		
6. INTERNATIONAL FINANCIAL RELATIONS	876,839	857,787	19,052	2.2%
Operational budget	*34,120*	*25,930*		
Transfers	*842,719*	*831,857*		
SUBTOTAL	**3,012,028**	**2,775,985**	**236,043**	**7.8%**
Operational Budget	1,597,899	1,363,188	234,711	14.7%
Transfer Budget	22,241,572	19,998,860	2,242,712	10.1%
Operational vs Transfer	7.2%	6.8%	10.5%	
Programmes				
R'000				
7. CIVIL AND MILITARY PENSIONS, CONTRIBUTIONS TO FUNDS AND OTHER BENEFITS	3,776,909	3,314,173	462,736	12.3%
8. TECHNICAL SUPPORT AND DEVELOPMENT FINANCE	4,641,940	2,863,296	1,778,644	38.3%
Operational budget	*178, 590*	*169,060*		
Transfers	*4,463,350*	*2,694,236*		
9. REVENUE ADMINISTRATION	8,653,573	8,653,573	0	
10. FINANCIAL INTELLIGENCE AND STATE SECURITY	3,755,021	3,755,021	0	
TOTAL	**23,839,471**	**21,362,048**	**2,477,423**	**10.4%**

Outcome: Economic Classification

Per economic classification	Final Budget for 2011/12	Actual expenditure for 2011/12	Variance	Variance as a % of final appropriation
	R’000	R’000	R’000	%
Compensation of employees	600,814	537,101	63,713	10.60%
Goods and services	899,104	733,834	165,270	18.40%
Transfers and subsidies	21,568,944	19,330,844	2,238,100	10.40%
Payments for capital assets	20,609	9,061	11,548	56.00%
Payments for financial assets*	750,000	751,208	-1,208	-0.20%
Total per economic classification	23,839,471	21,362,048	-2,477,423	10.40%

* The transfer is for Land Bank

Outcome of the AG Audit report

- Unqualified audit report but with emphasis of matters

  – Material impairment of R17.2 million relates to Programme 7, specifically Special Pensions, due to the Board misinterpreting the Special Pensions Act (Act 69 of 1996) as **752 beneficiaries had committed schedule 1 offences.** The spending due to difficulty of recovery needs to be considered as a write off/loss.

  – Material underspending of R2.477 billion. Details of spending deviation shown on following slides.

Main Reasons for Spending Deviations

- ***Lags in Spending:***
  - Jobs Fund established in 2011 with administration based at DBSA – actual spending lags behind commitment of funds
  - IFMS: project implementation delays
  - NDPG: Although deviation percentage is small, actual amount is relatively large
- ***Post-retirement medical benefits, Special Pensions and the Political Office Bearers Pension Fund***
- ***Personnel Vacancies*:**
  - Although departmental vacancy rate reduced from 14% in 2010/11 to 9.5% in 2011/12, there was a spending deviation observed.
- ***Capital spending and building refurbishment:***
  - Delay in finalising the refurbishment of 38 Church Square building results in delay in procurement of the security system, information technology and furniture & fittings. This is not shown in the Table on the next slide, as the deviation amount is less than R20 million.

Deviations in Spending

2011 / 12

Source of Deviation	Amount ('R million)	Final Budget ('R million)
Employment Creation Facilitation Fund (ECFF)	1,724	2,000
Civil and Military Pensions	463	3,777
Vacant Posts (across the National Treasury)	65.2	602.3
IFMS and Financial Systems	63.5	325.3
Neighbourhood Development Partnership Grant (NDPG)	41.6	850
Other (Several items)	119.7	N / A

Appropriate remedial actions

- Appropriate remedial actions
  - 752 cases deemed to be incorrectly interpreted in terms of the Act - the SIU and National Treasury legal department advised that High Court determination needs to be obtained but raised concerns that it will be difficult to rescind the payments as expectations have already been created. **The matter will be dealt through accounting treatment.**
  - The Jobs Fund allocation has been reviewed in line with the revised disbursement schedules which have been diligently assessed. Spending for 2012/13 for the Jobs Fund are aligned with the planned milestone achievements.

Jobs Fund
Overview

- The Jobs Fund (JF) was established to encourage innovation and support public and private sector initiatives with sustainable employment potential.
- The aim of the JF is to utilise public money to catalyse innovative and partnership based approaches to job creation and promote opportunities that lead to the long term improvement of employment prospects of the unemployed, especially young people and women.
- **JF Target** – the creation of about 150,000 sustainable jobs
- The **JF** is a programme that will be implemented over a five year period
  - 2011/12 is the establishment year of the Fund
  - 2012/13 (year 1) to 2016/17 (year 5) is the project implementation period
  - 2017/18 is a close-out year wherein final programme evaluations, audits and learning will be consolidated and disseminated

Jobs Fund

Main Reasons for Spending Deviation

- Detail design and embedding the implementation of a new funding instrument
- Establishing administrative capacity
- Finalising the governance framework
- Manual assessment of 2600 applications
- Contracting with Grantees (ensuring conditions precedent are met)

Jobs Fund

Progress, 2012 / 13

- 2^{nd} Call for proposals issued, successful implementation of on-line application process, applications currently being assessed to be completed by end November
- We anticipate that another billion rand will be allocated by the Investment Committee to fund a new tranche of projects, this will result in a change to the projected disbursement profile over the MTEF
- The initial budget for the Jobs Fund was an indicative budget, the results of the 1^{st} and 2^{nd} call for proposals has informed a review of the MTEF allocations. The budget has been rescheduled.
- Estimated grant transfer to DBSA for 2012/13 - R438 531million
- Adjustments to the Jobs Fund Budget will be reviewed on an on-going basis – since the open architecture of the Fund implies that we do not know how much grant funding future applicants will request, neither the applications that will be approved by the Investment Committee
- To date 19 grantees from the 1^{st} call for proposals have been contracted
- The first grant disbursement to grantees was made in April 2012.
- Training sessions hosted for Grantees

Other Areas of Spending Deviation

- ***Personnel Vacancies*:**
  - Progress has been made in reducing the departmental vacancy rate from 14% in 2010/11 to 9.5% in 2011/12.
    - Challenges faced in attracting the right skills for the identified positions.
    - 5% of offers made have been turned down for various reasons including salaries, counter offers, and other developmental career choices.
- ***IFMS***
  - Delays experienced in awarding procurement for development of inventory management, finance and payroll modules
    - Finance module development awarded in May 2012 and spending has begun;
    - Inventory Management procurement cancelled – SITA to develop in-house and spending expected to begin during 2012 / 13 financial year; and
    - Procurement module development yet to be awarded – this may continue to affect spending
- ***NDPG***
  - The NDP recorded an 41.6m (4.9%) underspend out of a total allocation of R850m. This amount was withheld in terms of the conditional grant requirements.
  - Non-compliance by municipalities related to low value for money. Challenges included low-quality or no project planning submissions, project delays due to high staff attrition and variances between budgeted project approval amounts and actual contractor spend.