CULTURE BEATS STRATEGY

The impact of culture on strategy in the development of a sustainable economy.

JOINT STANDING AND SELECT COMMITTEES ON FINANCE: PUBLIC HEARINGS

27 February 2023

Chartered Accountants Worldwide Member

SAICA DIFFERENCE MAKERS™

27 February 2023
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Dear Madam and Sirs

PARLIAMENTARY PUBLIC HEARINGS - COMMENTS ON THE 2023 BUDGET REVIEW

1. We present our comments and submissions on behalf of the South African Institute of Chartered Accountants' (SAICA) National Tax Committee on the 2023 Budget Speech released by Minister Godongwana on 22 February 2023.

2. We once again thank the Standing Committee on Finance (SCoF) and the Select Committee on Finance for the ongoing opportunity to provide constructive comments in this regard.

3. SAICA continues to believe that a collaborative approach is best suited in seeking solutions to complex challenges.

Yours sincerely

David Warneke
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Pieter Faber
Executive: Tax

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Project Director: Tax Advocacy

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CULTURE BEATS STRATEGY

4. The prevailing **Culture** in the country has become single biggest impediment to economic and fiscal policy implementation in South Africa.

5. It is therefore not a surprise that the Ministers' 2023 Budget Speech at least noted one of these problematic cultures, the **"Culture of Non-payment"** and correctly concluded that this culture cripples and undermines the country. The Minister then saddled National Treasury with the problem to "*encourage and improve*" this behaviour. Unfortunately, that statement talks to the **"Culture of Accountability**" or rather lack thereof. It would rather be the President as the CEO of SA Inc that would be accountable to "encourage behavioural change" across the whole of government. National Treasury's role is rather that it enforces the law when the lack of culture continues, especially as relates to fiscal discipline, and therefore creates a "**Culture of Discipline**".

6. Last year, the lack of implementation of policy was and continued to remain our main concern. The "**Culture of Procrastination**" has become the largest single impediment to ensuring South Africa's economic success and prosperity for all our country's people. Difficult decisions cannot be deferred into perpetuity and certain problems cannot be ignored in the hope that things will get better. Neither South Africa, nor the world in which we live, will fix, or correct itself.

7. We as a country must collectively start making the hard decisions and doing the hard work, driving a "**Culture of Unity, Collaboration and Delivery**". In the words of the Auditor General as it presented to the SCoF on 21 February 2023:

   "The AGSA's main focus was to <u>ensure that an unqualified audit opinion</u>, or a clean audit opinion, did <u>translate to the service delivery</u> and lived experiences of the South African citizens. That was what the AGSA wanted to see with the <u>culture shift in the public sector</u>."

8. We hope that our submissions below assist in enabling this culture shift that translates to service delivery.

Is Parliament performing its duty?

9. The fiscal framework is a framework for a specific financial year that gives effect to the executive government's macro-economic policy, and it includes, amongst others, ***estimates of all revenue,*** (budgetary and extra-budgetary, specified separately) expected to be raised during that financial year, as well as ***estimates of expenditure*** and ***estimates of borrowing*** for that financial year.

10. All the elements of the fiscal framework are interlinked. However, in analysing the estimates, one needs to consider what happened in previous years, even though SCoA and SCOPA address those matters, as it talks to the **credibility of the Budget** estimates in the current Budget and whether **people are held accountable to ensure Budgets are met and implemented as tabled**.

11. Section 42(3) of the Constitution states:

    The National Assembly is elected to <u>represent the people</u> and to <u>ensure government by the people</u> under the Constitution. It does this by choosing the

President, by providing a national forum for public consideration of issues, by passing legislation and by <u>scrutinizing and overseeing executive action.</u>

12. The Constitution therefore requires Parliament to scrutinise and oversee the actions of the executive arm of government and <u>hold the executive arm of government accountable on behalf of the people</u>.

13. Submission: Contrary to some views, Parliament's Constitutional duty is therefore to exercise what in accounting and auditing is referred to as "***professional scepticism***" <u>towards the executive arm of government</u>, not towards society and societal organisations that disagree with the actions and pronouncements of the executive. Parliament represents the peoples' views, not the governments. It checks the governments views against the will of the people.

14. It is on this basis that we submit our requests and questions to Parliament, in the hope that these do contribute to informing the will of the people and that Parliament will then be in a better position in holding the executive to account for the Budget.

15. In this regard, we must pose the question. Has SCoF found the Budget to be so accurate and aligned to policy of government, the needs of the people and the country that it did not have to make a single amendment since 2009 when it received the power to do so?

ECONOMIC & FISCAL OUTLOOK

Key risks

16. The Minister is to be commended for correctly "setting the scene" and for not sugar-coating what the country is facing. In his own words:

> The global recovery is slowing
>
> Domestically, load-shedding has become more persistent and prolonged, impacting on service delivery
>
> the medium-term growth outlook has deteriorated
>
> This is compounded by disruptions to freight and logistics networks
>
> Households are under pressure from the rising cost of living, and unemployment
>
> International Monetary Fund projects global growth to slow
>
> Global economic risks remain high, including those related to the ongoing war in Ukraine, and could impede growth if they materialise

17. He is correct that we need to be cautious and prudent given these risks.

18. He did however exclude 4 key risks, some even greater than the ones mentioned:

    18.1 The looming national water disaster that has been ignored for more than a decade

    18.2 Government's continual inability to implement its own policies

    18.3 The total implosion of much of local government

    18.4 The debt realisation of other SoE's besides Eskom.

19. These risks also exclude some of the other "unbudgeted expenditure" we have noted in our previous submissions, such as the billions of rands in legal claims and the uncosted wage bill (i.e., the part of the wage bill the Minister knows will be payable during the year and exceeds the current budget but has not determined the quantum due to the process followed).

20. So, the Minister seemed to have a sober take on the matter, but then stated:

    In this Budget <u>we are allocating additional resources towards these endeavours</u> without compromising the sustainability of public finances.

21. Notwithstanding the real and present dangers and risks the Minister noted (many of them much lower in 2019), we are now a mere R20 bn behind the elevated spending levels estimated in 2019. Is that the action of a fiscally cautious Minister?

22. As seen below, the Minister's words are not reflected by his actions; and actions speak louder than words.

23.

Table 3.5 Main budget expenditure ceiling

R million	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
2019 MTBPS	1 307 235	1 404 675	1 493 029	1 591 287	1 673 601		
2020 Budget Review	1 307 119	1 409 244	1 457 703	1 538 590	1 605 098		
2020 MTBPS	1 307 112	1 418 408	1 502 867	1 479 709	1 516 052	1 529 585	
2021 Budget Review		1 418 399	1 504 656	1 514 934	1 521 721	1 530 664	
2021 MTBPS		1 418 456	1 487 399	1 570 890	1 552 268	1 558 725	1 627 154
2022 Budget			**1 487 399**	**1 575 002**	**1 630 905**	**1 613 671**	**1 686 932**

Source: National Treasury

Table 3.5 Main budget expenditure ceiling

R million	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
2020 MTBPS	1 418 408	1 502 867	1 479 709	1 516 052	1 529 585		
2021 Budget	1 418 399	1 504 656	1 514 934	1 521 721	1 530 664		
2021 MTBPS	1 418 456	1 487 388	1 570 890	1 552 268	1 558 725	1 627 154	
2022 Budget		1 487 399	1 575 002	1 630 905	1 613 671	1 686 932	
2022 MTBPS		1 487 385	1 566 490	1 667 118	1 665 349	1 744 762	1 832 678
2023 Budget		**1 487 419**	**1 566 498**	**1 653 459**	**1 671 030**	**1 750 276**	**1 842 572**

Source: National Treasury

24. Submission: As stated in previous years, overspending is a concern, but it is more of a concern when government has an inability and lack of self-control to keep its base line that it set itself. If government subscribes to a circumspect Budget, it needs to table a circumspect Budget and keep to it.

Pillars of economic growth

25. The Minister states:

Our pursuit of higher growth remains anchored on three pillars.

Firstly, we are ensuring a stable macroeconomic framework to create a conducive environment for savings, investment and growth. Secondly, we are implementing growth-enhancing reforms in key sectors, particularly in energy and transport. And thirdly, we are strengthening the capacity of the state to deliver quality public services, invest in infrastructure and fight crime and corruption.

26. While we cannot fault these words, we question whether the Budget reflects these 3 pillars.

27. The macroeconomic framework is indeed stable, as it seems we have essentially had the same “plan” for the last 15 years. However, this is far from conducive to creating an environment for savings, investment and growth as the numbers and Budget reveal.

28. Key sectors like energy are in fact critical and we add water and sanitation for good reason. However, due to a culture of procrastination, all 3 of these sectors are imploding, notwithstanding the warning given to both the executive and to Parliament.

29. As to the quality-of-service delivery and capacity of the state, again, not much has happened and very little seems will change based on the Budget if we look at:

29.1 No performance reporting on *Ministers 2019 Performance Contracts*

29.2 No implementation yet of the Professionalisation of the Public Sector Framework

29.3 Local government councillors are not held accountable for service delivery, including offences (s49A) of poisoning our rivers and oceans in terms of the National Environmental Management Act 1998. Councillors had a duty of care to prevent this recurring (s28) under NEMA and MEC and Ministers have an enforcement obligation (s31N). Neither have been met.

30. Commentators made the following observations:

Government policy is no privatisation, yet multiple SoE's are going to market seeking privatisation, where is the economic policy and clarity to the investors?

The Minister complains there is a culture of non-payment hurting our economy. This was said 5 years ago as well with promised interventions and what has the Minister, as the Constitutional custodian of fiscal disciple done or even proposed to do?

Government policy was to save and relaunch SAA. It however still had 2 options, provide no funding and walk away from SAA or pay R3,5bn. The Minister decides to pay R1bn which was not an option, meaning SAA will be a problem for months to come.

The Minister says transport and logistics are a key pillar of the economy. Transnet says it has no money and ailing infrastructure. Prasa alone which is imploding our exports and hurting the economy says it needs R80bn. Where is the "Save Transnet" debt plan?

The President says in SONA there will be a Minister of Electricity, where is this Ministry's Budget appropriation for the year?

31. Unfortunately, under the current approach it seems there is in reality no plan, and the Budget is essentially merely an exercise to consolidate numbers from 40+ Ministries. Invariably, we cannot blame the Minister of Finance alone as the direction and plan is not his sole responsibility or mandate.

32. However, holding the whole of government accountable for this is Parliament's sole responsibility. Will Parliament have the will to do this?

An Investor's Perspective

33. In 2019 and 2020, the President affirmed the importance of Foreign Direct Investment to achieve economic growth.

34. The National Treasury graphs of investment potential, except for SoE and government debt, does not seem very promising.

35. It says the economy is shrinking in comparative global terms!!

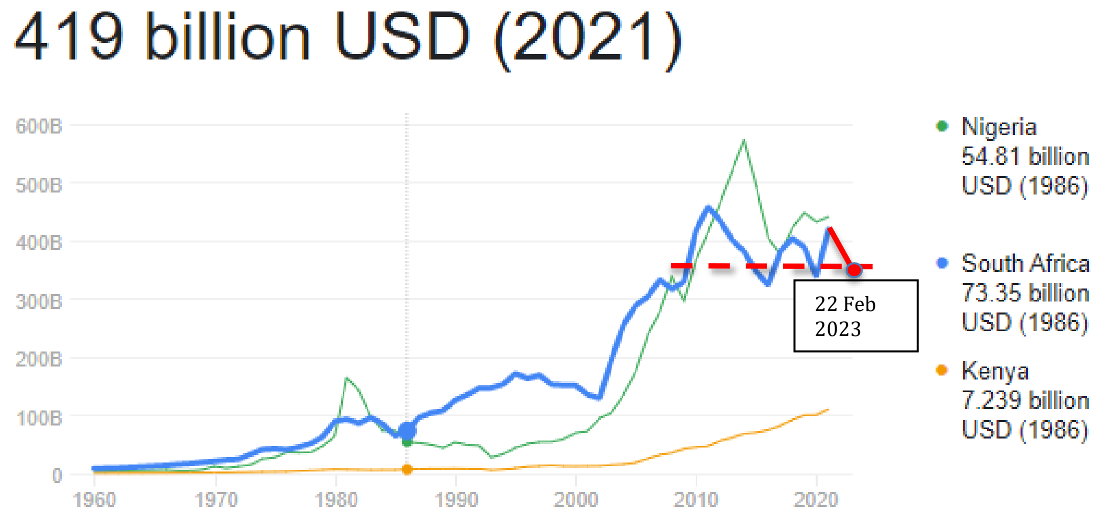
36. Foreign investors do not look at South Africa in SA Rand terms, but in foreign currency such as US$.

37. So, what do the numbers tell them about SA investment potential:

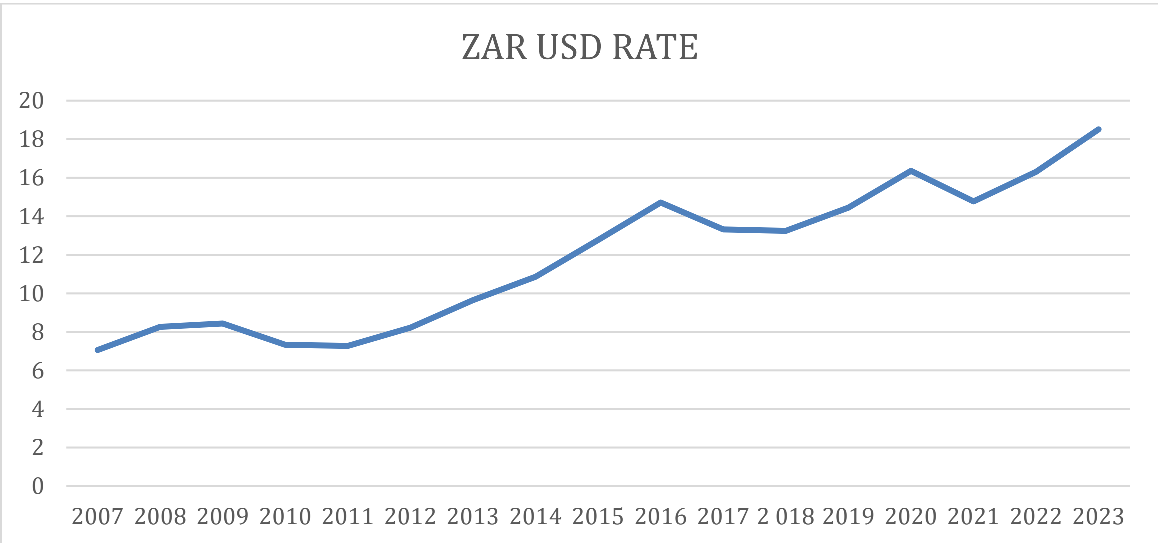
38. South Africa’s 2022/2023 GDP was by 17:00 on Budget Day 22 Feb 2023 at a USD exchange of 18,51/1 worth a mere US$351,14bn.

39. That means South Africa’s GDP is where it was 15 years ago before the financial crisis, and worse still, it is declining.

SOUTH AFRICA’S GDP IN USD



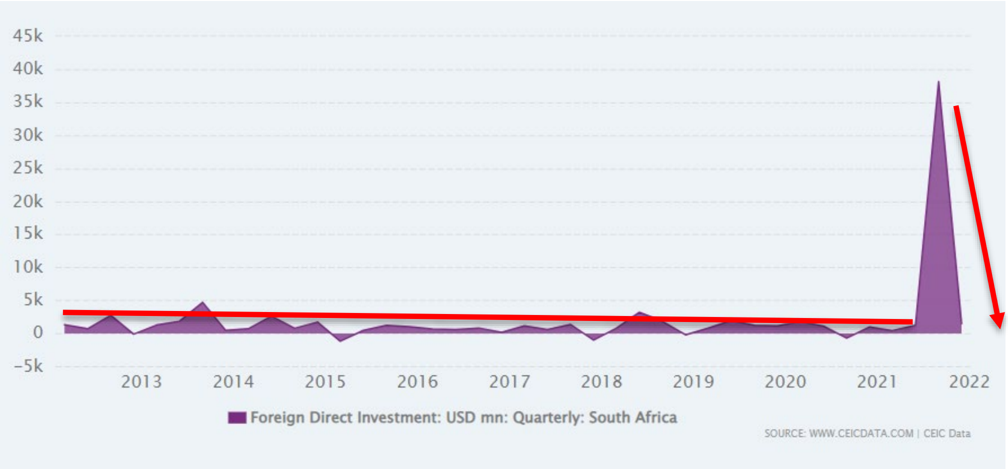
40. The above is despite nominal ZAR GDP growth. However, our currency has depreciated.



41. As such, if our GDP growth is flat, the currency devaluation will result in it shrinking.

42. So, does FDI show this lack of investment?

43. Below is the FDI for the last 10 years and other than the President’s investment drive in 2021, it has been flat and declining.



44. In September 2022 FDI for the third quarter had decreased to US$695m compared to the previous quarter of US$1,7bn. Q1 2023 will decline even further.

45. So why would an investor not readily invest in such circumstances?

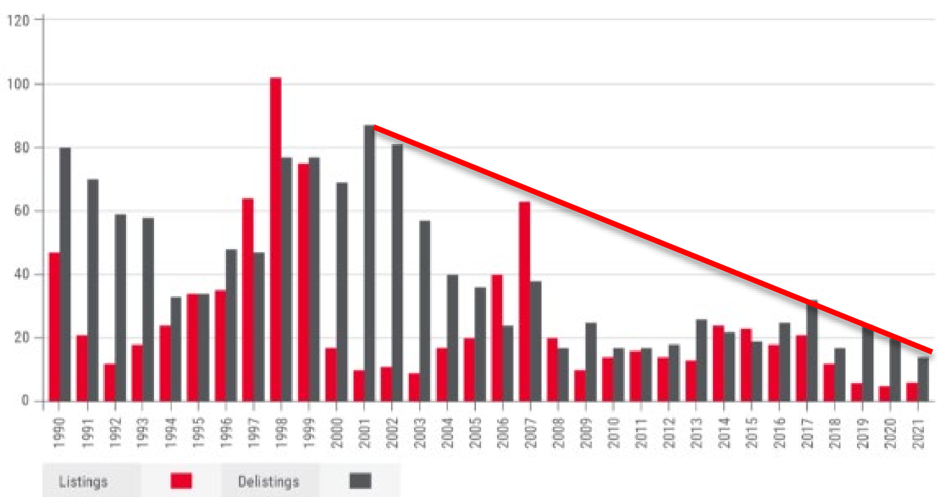
46. The following example explains:

47. If I had invested US$100m in a South African business in 2007 and received US$1m in dividends each year, that same investment amount is worth only US$38m today producing US$380k in dividends.

48. For that business to remain a worthwhile investment, it would have to grow in value and dividends flow faster than inflation (not real growth) and currency depreciation i.e., it would have to grow 160% in 10 years just to break even. Few good businesses achieve that.

49. The JSE has declined from 773 to just 330 companies in 30 years as shown below.

Graph 1: JSE: Number of new listings and delistings

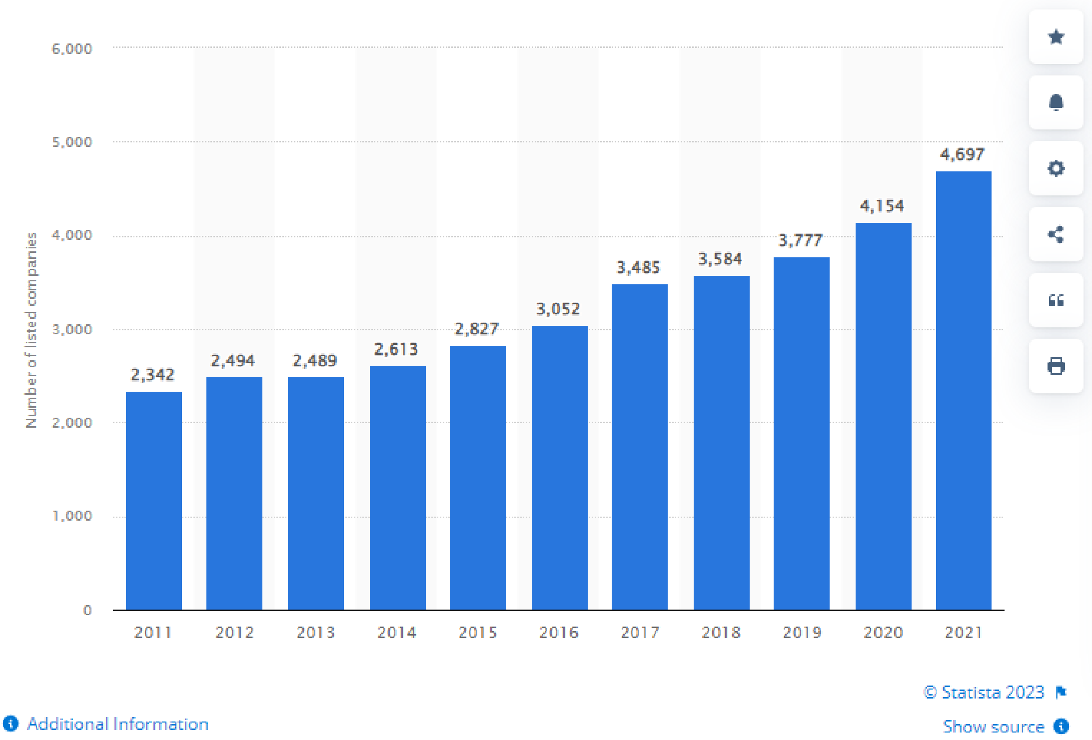


Sources: JSE Limited, Allan Gray research

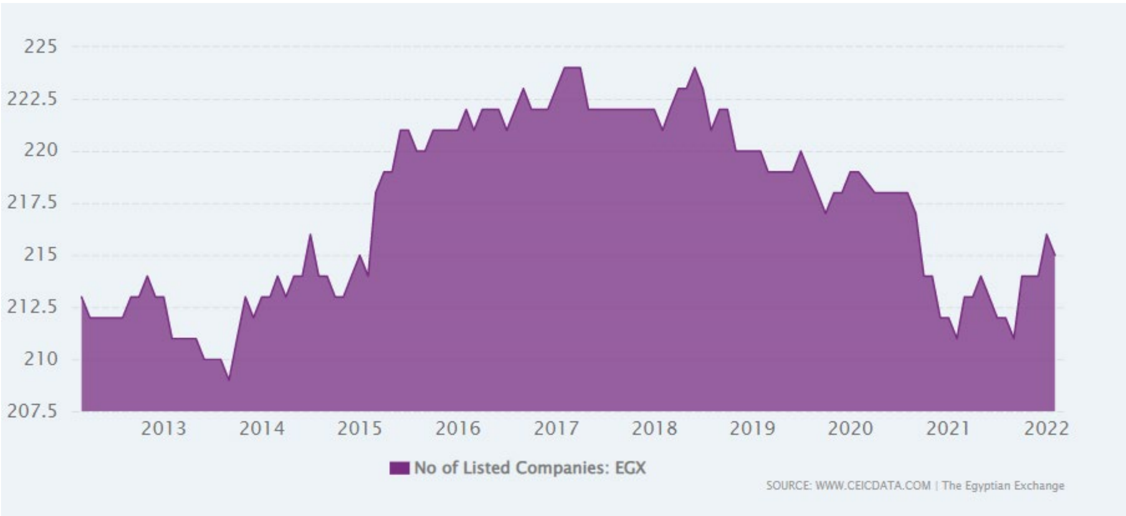
50. Some say this is a good thing as it means there is consolidation and small companies leave the JSE.

51. However, that is not the only reason and market consolidation seems to be the exact opposite of what the National Development Plan (NDP) seeks to achieve.

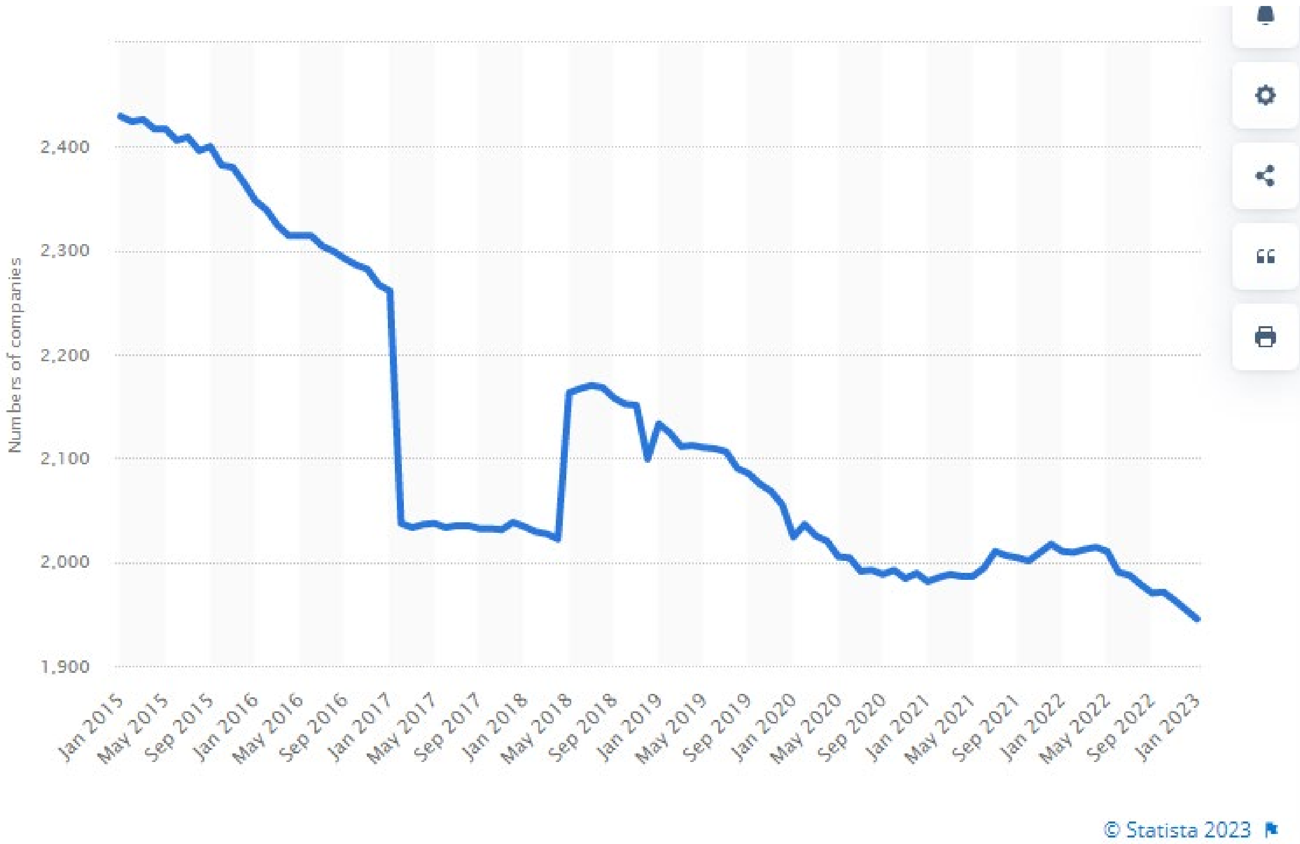
52. In China growth in its listed companies has matched the exponential growth of its economy.



53. In Africa's third largest economy Egypt, the growth of its listed companies in numbers tracked economic growth.



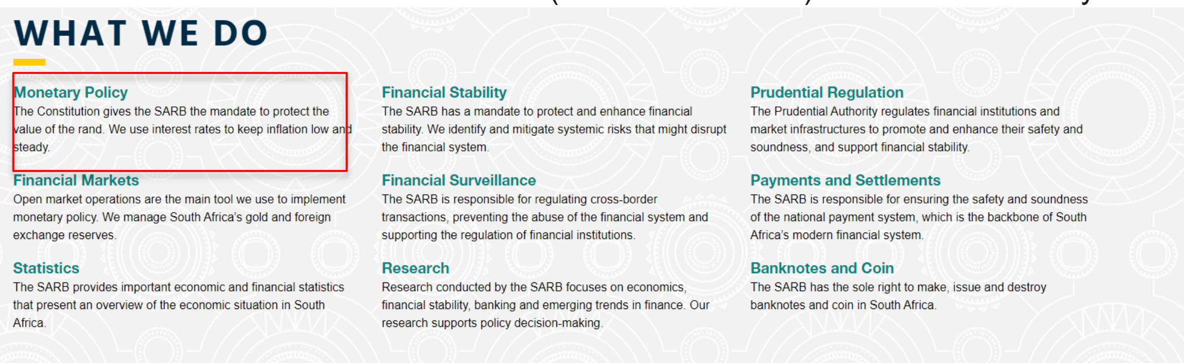
54. Compare this to another economy that has stagnated over the last 20 years, the UK, and the London Stock Exchange.



55. Therefore, there does seem to be a positive correlation between a growing economy and the number of listed companies. A stagnant economy seems to result in "company consolidation".

56. It is thus not necessarily a weak or strong currency that is required for FDI, but a stable currency.

57. It is therefore unclear why we still have policy uncertainty in this regard as seen by this extract from the SA Reserve Bank Act (and its website) vs What it says it does



WHAT WE DO

Monetary Policy
The Constitution gives the SARB the mandate to protect the value of the rand. We use interest rates to keep inflation low and steady.

Financial Stability
The SARB has a mandate to protect and enhance financial stability. We identify and mitigate systemic risks that might disrupt the financial system.

Prudential Regulation
The Prudential Authority regulates financial institutions and market infrastructures to promote and enhance their safety and soundness, and support financial stability.

Financial Markets
Open market operations are the main tool we use to implement monetary policy. We manage South Africa's gold and foreign exchange reserves.

Financial Surveillance
The SARB is responsible for regulating cross-border transactions, preventing the abuse of the financial system and supporting the regulation of financial institutions.

Payments and Settlements
The SARB is responsible for ensuring the safety and soundness of the national payment system, which is the backbone of South Africa's modern financial system.

Statistics
The SARB provides important economic and financial statistics that present an overview of the economic situation in South Africa.

Research
Research conducted by the SARB focuses on economics, financial stability, banking and emerging trends in finance. Our research supports policy decision-making.

Banknotes and Coin
The SARB has the sole right to make, issue and destroy banknotes and coin in South Africa.

:

Act No. 90, 1989 SOUTH AFRICAN RESERVE BANK ACT, 1989

Primary objectives of Bank

3. In the exercise of its powers and the performance of its duties the Bank shall pursue as its primary objectives monetary stability and balanced economic growth in the Republic, and in order to achieve those objectives the Bank shall influence the total monetary demand in the economy through the exercise of control over the money supply and over the availability of credit.

58. Until monetary policy in practice is to first ensure a **stable currency** before considering inflation, economic growth will continue to struggle.

59. Inflation targeting may be important, but it can be damaging to an economy as well, especially when inflation is driven not by demand or consumption but by external factors such as war in other countries resulting in shortages of wheat, natural gas, oil, and fertiliser.

ESTIMATES OF REVENUE

Tax-to-GDP

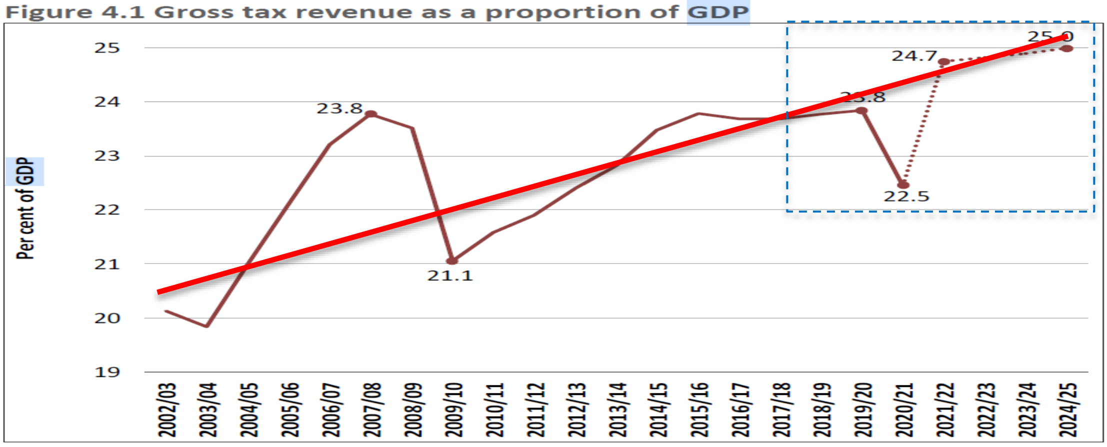
60. The tax-to-GDP ratio continues to grow, continuing its upward trend. In fact, the ratio continues to grow even above the last 12 months' estimates. The Minister puts this down to certain sectoral windfalls and better collections, however this higher ratio was also on a higher base given that GDP growth was higher than estimated.

61. The OECD describes this ratio as follows.

"Total tax revenue as a percentage of GDP indicates the share of a country's output that is collected by the government through taxes. It can be regarded as one measure of the degree to which the government controls the economy's resources."

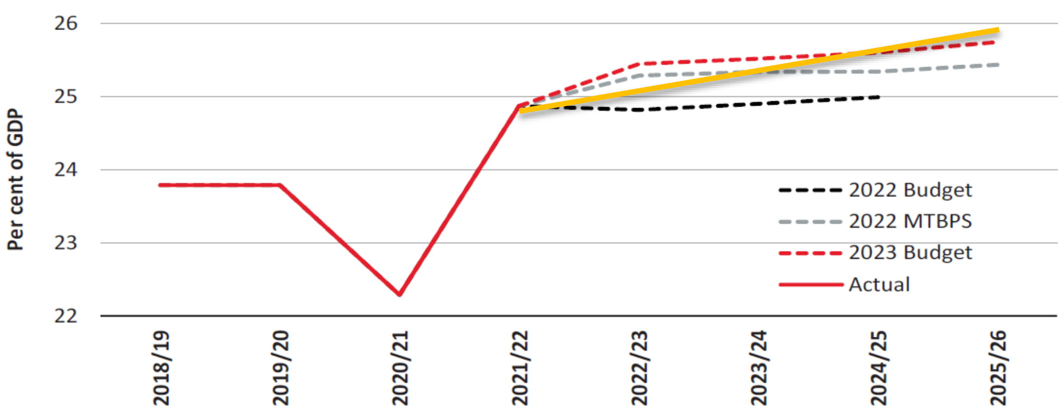
62. Given the continually upward trend, it would then seem that government policy intends to continually expand its control over the economy's resources, notwithstanding government's inability to turn such economic resources into growth, i.e., the Return on Investment is underperforming.

Figure 4.1 Gross tax revenue as a proportion of GDP



Source: National Treasury and SARS

Figure 4.1 Tax-to-GDP ratio



Source: National Treasury and SARS

63. We reiterate that the calculation methodology used by National Treasury does not properly represent this ratio. The OECD explains this ratio as:

"The tax burden is measured by taking the total tax revenues received as a percentage of GDP. This indicator relates to government (all government levels) and is measured in million USD and percentage of GDP"

64. As stated in our 2022 Submission, there are various tax items excluded from the Treasury calculation, including local government taxes.

65. Is the ratio important at all?

66. Treasury continues not to answer that question, rather questioning the veracity of concerns whether the current levels are bad for the economy. If this ratio is not that important why raise it at all?

67. Our call to SCoF in the last few years was to at least follow through on historical decisions to have Treasury properly calculate and research this question as was decided by JSCoF in 1996.

68. We therefore again ask the committee members: are you properly informed to make an informed decision as required to approve the Budget without significant amendment to Budget 2023?

69. What does this inaction say about the culture of accountability?

70. Does the Committee agree that there is a level at which high taxes (fiscal policy) become detrimental to the economy (macroeconomic policy)?

71. Why has the Committee still not **imposed** (it does not need to only suggest) its own recommendations of 1996 to interrogate the 25% and will it be setting a deadline for this to be done by National Treasury?

Revenue Estimates

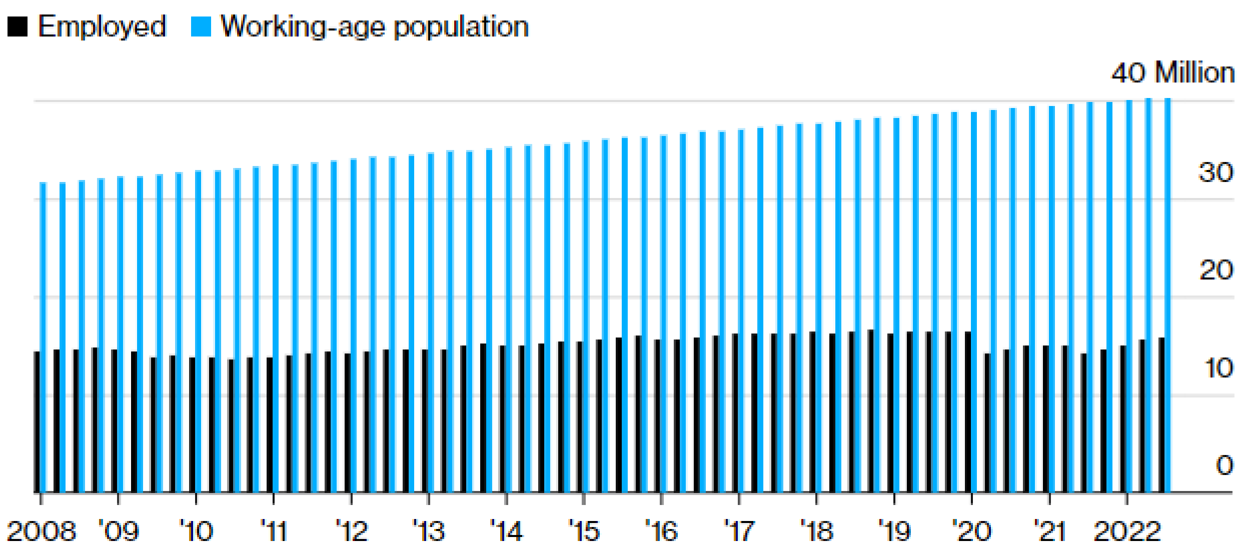
72. The Minister notes that the temporary commodity price upswings remained strong and a good compliance enforcement, of which the returns on enforcement are expected to moderate over time, were particularly responsible for the small surplus in tax collections.

73. The stable revenue can also be attributed to relatively stable employment and consumption, although both were partly funded by increased debt in both public and private sectors

.

74. This does not detract from the fact that in 2022 43,1% of our people were unemployed with more than 28 million on social grants. South Africa has in effect become a welfare state but given its small base of taxpayers, this poses severe risks for the country.

75. This stagnant employment is also a risk and shows why the tax to GDP ratios have been increasing as well.



Source: Statistics South Africa

76. It is particularly those in lower-paying jobs that are at risk when household debt gets out of control, but given the economic risks, no jobs are safe as seen globally with global unemployment set to rise and pressure on salaries, even in this era of high global inflation[1].

77. This stable revenue source from employees' tax is therefore under pressure, and it is also the largest contributor to the fiscus of all the taxes. Treating it as an inexhaustible revenue resource in the medium term is a risk.

Greylisting – Impact and Oversight

78. The Financial Action Task Force (FATF) sets global standards to combat money laundering and the financing of terrorism across national borders and South Africa has been a member since 2003.

79. On 24 February 2023, National Treasury announced[2] the official decision of the FATF to list South Africa as a "jurisdiction under increased monitoring", or more commonly referred to as the "grey list".

80. This comes after the results of the FATF's October 2021 mutual evaluation report (MER) on South Africa, which identified several deficiencies in our legislative framework and implementation in addressing the threat of money laundering and terrorist financing.

81. The impact of the grey-listing was acknowledged in the Budget Review:

> *…the potential greylisting of South Africa by FATF [Financial Action Task Force] and the dire impact on the economy that this outcome could have, particularly on foreign direct investment, the exchange rate, access to corresponding banking and cross-border trade…*

82. National Treasury has addressed a number of these deficiencies by introducing/amending legislation and regulations, for which it earned praise from the FATF at its 13 January 2023 meeting. However, the legal framework is only one of the many areas for which deficiencies were identified in the MER.

83. The FATF notes South Africa must still *demonstrate a sustained increase in investigations and prosecutions of serious and complex money laundering and the full range of Terrorist Financing activities in line with its risk profile.*

84. This point is a continuation of the following risks FATF identified in its 2019 mutual evaluation report:

> *Incidents of corruption and bribery are widespread, across state-owned, provincial, and municipal entities, particularly irregularities in procurement involving the private sector. Governance weaknesses, including in supply chain management, performance reporting and inadequate oversight coupled with a lack of consequences for transgressors increase the scope for bribery and corruption.*

[1] wcms_865332.pdf (ilo.org)
[2] https://www.treasury.gov.za/comm_media/press/2023/2023022401%20Media%20statement%20-%20Response%20to%20FATF.pdf

85. This is the reason the FATF recommended that the South African government:

Provide the SAPS Directorate for Priority Crimes Investigations (with more staff, especially financial investigators, and forensic accountants, so that it can better use financial intelligence and place more emphasis on proactively identifying and investigating ML cases, particularly high level and complex cases such as those related to "State capture" and others involving third party laundering, foreign predicates, money-laundering networks, and professional enablers[3].

86. Government was thus aware of the issue over 3 years ago.

87. While National Treasury is of the view that *the increased monitoring will have limited impact on financial stability and costs of doing business with South Africa,* an IMF working paper, titled *The Impact of Gray-Listing on Capital Flows: An Analysis Using Machine Learning*, provides evidence to the contrary.

88. The paper analysed the impact of grey-listing on capital flows in a sample of 89 emerging and developing countries between 2000 and 2017. Findings include:

- Capital inflows decline on average by 7.6% of GDP
- FDI (foreign direct investment) inflows decline on average by 3% of GDP
- portfolio inflows decline on average by 2,9% of GDP and
- other investment inflows decline on average by 3.6% of GDP.

89. The likely reduction in foreign investment will affect projected tax revenue, calling into question the tax collection figures contained in the 2023 Budget.

90. Submission: Why was Parliament no aware about the 2019 review process and progress made given the previous findings in 2008?

91. National Treasury has largely addressed the deficiencies (noted by the FATF) that are within the scope of its portfolio.

92. However, are members of Parliament satisfied that as a collective, they could not have done more to hold the Police and Justice Ministries accountable for finalising the investigations and prosecutions mentioned in the FATF Report, as this is likely to have had a major impact on preventing the grey-listing?

93. The country now faces a January 2025 deadline to address further deficiencies noted at the most recent 2023 FATF meeting, and National Treasury has already demonstrated a sense of urgency in addressing the deficiencies that are within its control. This is likely to continue as the deadline draws near.

94. However, are members of Parliament satisfied that the same can be said for the Police and Justice Ministries and will the necessary measures be taken to ensure that these government departments fulfil their responsibilities in contributing to South Africa's removal from the grey-list?

[3] https://www.fatf-gafi.org/content/dam/fatf/documents/reports/mer4/Mutual-Evaluation-Report-South-Africa.pdf

95. The Minister said Treasury is prepared for grey listing: will he share with us that he has done to prepare?

Impact on Farming

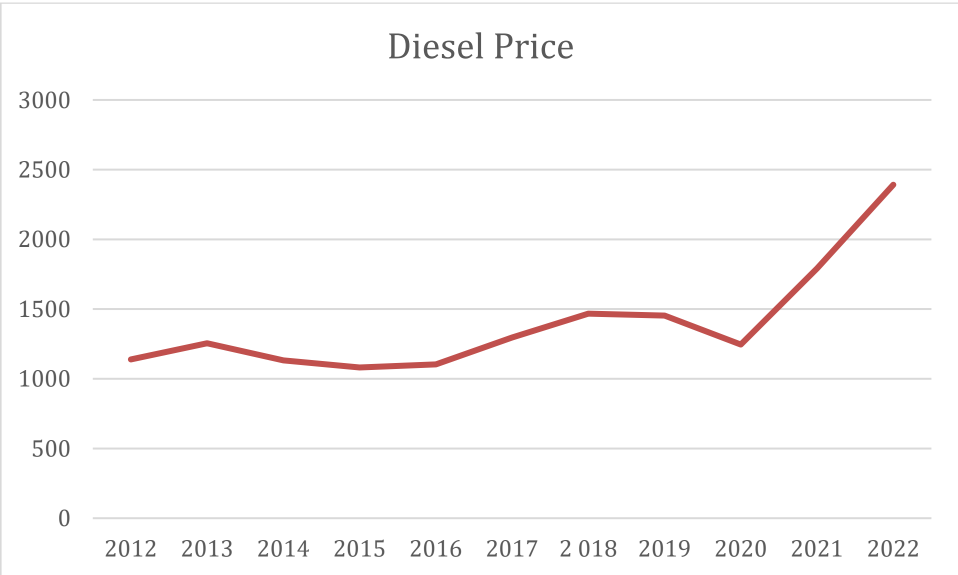
96. Farmers in South Africa face extensive challenges including security.

97. The war in Ukraine and loadshedding have been particularly harsh on what is a primary industry, something we cannot be without to ensure food security.

98. The war in Ukraine has created much political debate regarding those countries that support Ukraine and those that do not, while we are fortunate to not have suffered the destruction and death the conflict has brought about in Ukraine.

99. However, the war in Ukraine creates a very real impact for us, especially for the agriculture sector that ensures our food security.

100. Below is the diesel price increase over 10 years.



101. Due to both Ukraine and Russia being key fertiliser producers, the price of phosphates, urea and potash have increase by 190%, 170% and 280% respectively.

102. Input costs have therefore soared to record highs with no relief from government.

103. Loadshedding impacts refrigeration for milk producers, chicken farmers and irrigation systems resulting in billions in losses. Again, with no relief from Government.

104. A looming risk is that sewage-polluted water (due to municipalities) will start impacting farmers' ability to irrigate crops without having to incur mitigating costs.

105. Lastly, the crumbling of Transnet has meant that exporting and transporting produce to silos and harbours has become a logistical nightmare with additional cost implications.

106. Submission: Is Parliament satisfied that this Budget does enough to assist in securing our country's food security?

Impact of Natural Water Disaster on Revenue

107. We discuss in more detail below the **National Water Disaster** impact on municipal funding, exacerbated by loadshedding.

108. The Minister, through his allocations and undertakings of additional oversight and controls, does little to allay fears that the taps will not run dry, and that SA is one drought away from a National Water Disaster.

109. The irony of dams and towns flooding while Gauteng municipalities implement watershedding has not gone unnoticed.

110. Submission: Why has Parliament, as with loadshedding, been so silent on this matter?

111. Is Parliament comfortable that both financially and through enhanced financial oversight, the Minister is meeting his Constitutional mandate to avert the looming disaster?

ESTIMATES OF EXPENDITURE

Wage Bill

112. Wage negotiations are ongoing, and it already seems that the Minister has budgeted less than what is already on offer to unions.

113. The 2018 wage agreement process started in October 2017 i.e., in the 2017/2018 financial year and was signed on 8 June 2018, for 3 years i.e., in the 2019 fiscal year with retrospective application to 1 April 2018. Consequently, the Budgets prepared for 2018/2019 by departments were incorrect and the National Budget tabled in Parliament in February 2018 was materially understated.

114. The current wage agreement expired in 2021 and currently wage negotiations are underway for the current year.

115. It is of much concern to hear that the "technical" court decision regarding the previous wage agreement will be circumvented through a "blank cheque" approval by National Treasury. This is not something we believe is possible in law as per the judgment, the law requires amounts over the Budget to be specifically approved by Treasury i.e., the amount must exist and be known by the time that the approval is given.

116. In this regard we agree with the Unions that Government should be held to its agreements.

117. However, we do not see why being held to agreements and fiscal stability should be in opposition to each other.

118. What was clear from the court judgment is that it is Government's flawed Budget and wage negotiation approach is what has created this problem. It "puts the cart before the horse" by negotiating salaries outside of Budget cycles and retrospectively.

119. The current mechanism for out-of-Budget cycle increases in the wage Budget, was meant for unavoidable increases, not for standard wage negotiations.

120. Had salary negotiations been done prospectively and timeously, the Minister would have been able to table the correct wage Budget and Parliament would have been able to exercise proper oversight.

121. Other Ministries conduct is therefore making it impossible for the Minister to table an accurate and reasonable budget.

122. <u>Submission</u>: It is submitted that wage offers be negotiated by the Public Service Administration with National Treasury's input and then when consensus is reached, before the wage agreement is signed, the budgeted wage offer is tabled in the Budget and approved. Then, no midyear "finding of money" would be required and no further Treasury approvals would be required to legitimise wage offers.

ESTIMATES OF DEBT

123. The frank statement must be that the Minister's estimates of debt can only at best be wishful thinking.

124. This is supported by the fact that National Treasury and the Minister in office at that time, have not met a single debt ceiling or turnaround target in 15 years.

125. It begs the question how prudently Parliament has exercised its oversight role and whether it seriously seeks to hold government to its own plans and policy.

126. We should never forget that the low debt levels in 2007 came at a huge cost to the People of South Africa who were promised that their patience would be rewarded. That same generation is now being told that because of Governments overspending since 2007, there is no money, and they have to wait again.

127. Furthermore, this debt must be repaid. As the single largest expense, future generations, including those sitting in Parliament, will be deprived of setting the financial needs of the country in future as they will have to deal with the debt this Parliament and current government approved. It is unfortunate that this was the same position the first government of the new SA was faced with in 1994 and that history is repeating itself.

Wage Budgeting

128. The current wage negotiations will again have a retrospective and material impact on the Budget.

129. This current process undermines Parliament's oversight as it means the Budget, Debt and Appropriations are in fact wrong and known to be wrong. Should Treasury have to find R45 bn+ each year for 3 years, then programs tabled as funded will not be funded or debt as tabled would not be accurate.

130. <u>Submission</u>: Is Parliament satisfied that in meeting its Constitutional obligations, it is approving a Budget it knows is materially incorrect?

Implosion of local government

131. As we have presented over numerous years, local government, as the custodian of primary service delivery is imploding, and fast.

132. The Auditor General's report on the 2021 MFMA outcomes starts as follows:

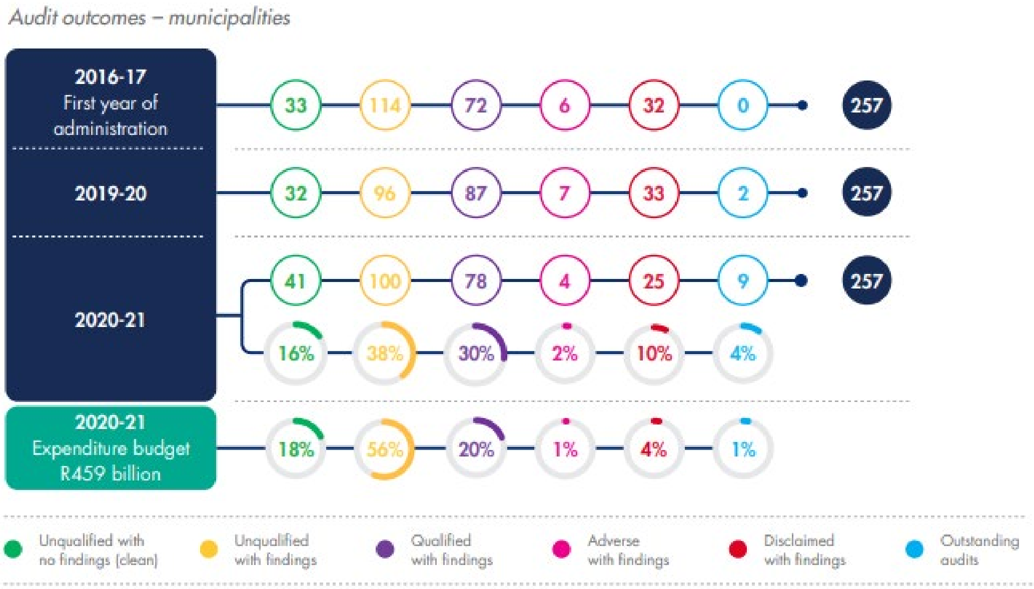
The country's aspirations to improve the quality of life of all citizens should be most evident at municipal level through the provision of water, sanitation, electricity, refuse services, roads, and infrastructure, as well as through enabling economic development. <u>Unfortunately, this is not the case.</u> Low levels of trust and public frustration at the lack of service delivery and financial mismanagement are high. The frustration finds expression in several ways, from service delivery protests to citizens opting out of public services in favour of providing their own services or using private services. <u>Citizens have also resorted to litigating against municipalities for failure to deliver services. Businesses are moving out of municipal areas with poor service delivery, resulting in increased unemployment and a loss of municipal revenue in those areas.</u>

133. Where is Parliament while this is happening: is Parliament not supposed to be the People's representatives and champions? Why must the People use the courts?

134. In 2007, eight municipalities were dysfunctional and under administration. By 2022 that number had grown to 33 whereby provincial and national government had to take over their functions.

135. The report makes for grim reading as it shows that financial mismanagement goes far beyond 33 municipalities.

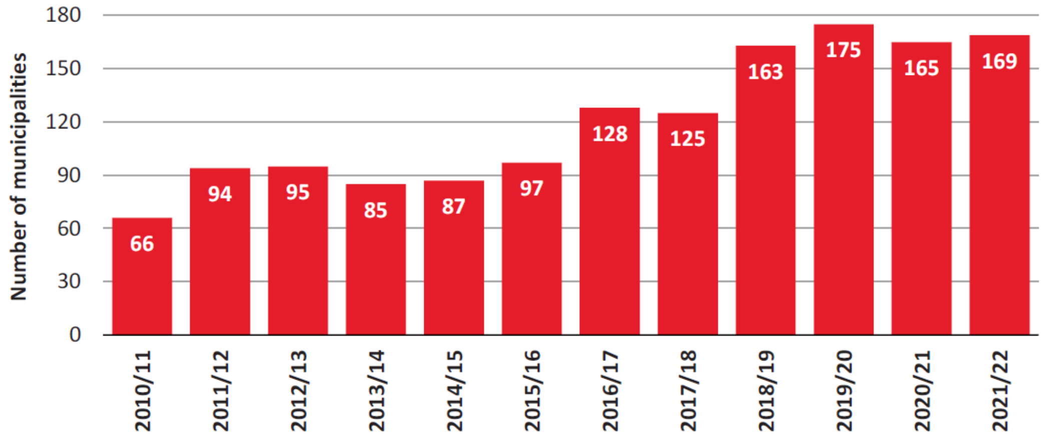
136. How has the Minister budgeted for this trend and where will the financing come from?



137. This situation is confirmed by National Treasury's own data with 169 municipalities under financial distress and there does not seem to be a plan to improve this.

The National Treasury's 2022 *State of Local Government Finances* report found that 169 municipalities were in financial distress at the end of 2021/22. The report noted a continued pattern of deterioration: only 66 of the 257 municipalities had been in financial distress at the end of 2010/11. Revenue management was the most prevalent factor contributing to this financial distress.

Figure 6.1 Municipalities in financial distress



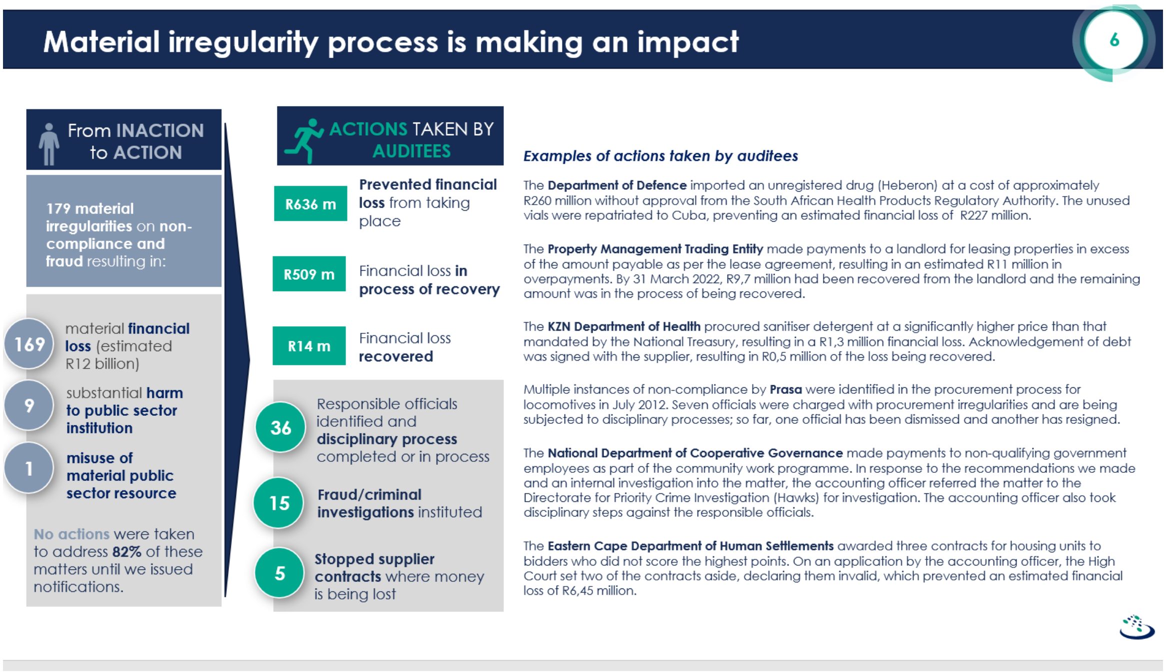
Source: National Treasury

138. So other than noting the implosion, what has the Minister done and what is his plan going forward, as he has given none?

139. Who other than National Government will have to fund these municipalities and who will pay to protect councillors when civil unrest increases? Was it not the Minister's and Treasury's constitutional duty to have prevented this in the first place through not only prescribing the MFMA but enforcing it?

140. To compound this problem, as set out in the National Water Disaster section of this submission, municipalities are overly reliant on the profits from water and electricity, two commodities they are finding scarcer to buy and harder to sell for profit due to theft and losses.

141. We are however glad that the AG is making some progress.



142. Submission: Will Parliament and National Treasury also be making more progress in saving our municipalities and recovering monies lost due to mismanagement?

143. What is the Minister's plan, if any, in this regard?

Logistics Infrastructure

144. The Minister notes that logistics are key to a growing economy.

145. That includes roads, rail, air, shipping, and bulk pipelines.

146. For such a critical part of the economy, the Budget seemed extremely light on how an indebted SANRAL, Municipalities, PRASA and Ports Authority (Transnet in general), who have all dilapidated infrastructure due to mismanagement and non-maintenance, will play their part in enabling economic growth.

147. Potholes, broken railways, and non-working ports seem to be the order of the day and Government Policy as to involving the Private Sector in these areas seems conflicted and ambiguous at best.

148. Submission: Is Parliament satisfied that the Minister has in fact addressed both the debt challenge at our custodians of logistics and their financing requirements, to rebuild these arteries of our economy?

OMISSIONS

Greylisting – State of Readiness

149. To address the risk of greylisting, the Treasury and Minister sought legislative intervention in haste and tabled the General Laws Amendment Act.

150. In the Budget, the Minister notes that they have prepared for the impact of greylisting, yet we remain unconvinced as he did not take us into his confidence as to what the preparations were.

151. On 24 February 2023, the FATF confirmed our greylisting and it was rumoured that South Africa would request a review in July 2023.

152. Given that the most impactful changes were to be action that should have been taken by the Minister of Justice and Minister of Police which they have not done since the 2019 review process started, there seems little chance of success of such a quick review. The Minister of Finance's Budget proposals also do little to allay fears, not only as to funding but ensuring a reduction in financial mismanagement in those Ministries.

153. It is ironic that only after the greylisting, the SARS, Hawks and Police have signed a memorandum to share information, nearly 4 years after the country's review process began.

154. For a successful review, at a minimum the matters addressed in the Act would have to be implemented.

155. Below we set out our views on the state of readiness of government and the persons to which these new laws apply.

<u>MASTERS OFFICE</u>

Obligation imposed

The General Laws Amendment Act introduced a definition of 'beneficial owner' in response to the FATF's concern that there is no transparency with regards to the identities of the ultimate owners and controllers of trust.

The changes to the Trust Property Control Act requires that trustees and the Master now has additional obligations and responsibilities which includes the following:

TRUSTEE must keep information on BO

- Name
- Date of birth
- Nationality
- Official ID, indicating type and country of issues
- Residential address
- Address for service notice
- Other mean of contact
- Grounds on which person is BO
- Date on which person became BO
- Date on which person ceased to be BO
- Certified copy of ID of EACH BO

MASTER's register (electronic)

- Access through username & password
- Security measures
- Trustee to load and update info on each BO
- Trustee to upload documents

TRUSTEES	MASTER
• Disqualification requirements • Disclose position as trustee to AI & • Identify transaction relate to trust property • Establish and record BO • Keep record of info • Lodge register with Master • Update information • Make information available when required as prescribed	• Keep register of disqualified persons • Notify trusts of trustees – with order /conviction • Approve persons appointed as trustees from outside SA • Keep register of prescribed information re BO • Make info available when requested

155.1 These records and information must be submitted by trustees to the Master's office by 1 April 2023.

155.2 The Department of Justice released Regulations for public comment to specify the information that will be required to be kept by trustees and submitted to the Master's Office. The final regulations has not yet been published. When finalised trustees and the Master will be required to keep and update the following information :

155.3

156. Submission: This is a very large amount of information and records that trustees are expected to compile and submit to the Master's Office within the next one month in respect of all trusts registered within the Republic. There is no clarity on information relating to children and which trustee are required to keep this information. Will every trustee of a trust keep this for fellow trustees and beneficial owners, leads to duplication and security risk.

157. The Master's Office itself is expected to have the computer systems in place to receive and store these records within the next one month, which also necessitates suitably skilled staff to carry out the new obligations imposed by the recent legislative amendments.

158. Is Parliament satisfied that 1 April 2023 is enough time to enable both trustees and the Master's Office will be able to achieve this?

CIPC

Obligation imposed by recent amendments

In terms of the current Companies Act, an annual return must be submitted to the CIPC by every company. The General Laws Amendment Act now places the following additional requirements on companies:

Section 33 – Annual return

Amendment

- Submit copy of securities register
- Submit copy of register of disclosure of beneficial interest as prescribed in S56(7)(aA) (AFFECTED COMPANY)
- Commission must make AR available to persons as prescribed

.

56(7)(aA) An AFFECTED COMPANY must establish and maintain a register of persons who hold beneficial interest equal to or in excess of 5% of the total number of securities issues by the company, which register must be updated as per the information received via a notice.

S50(3A)Companies that are not an "affected company"

MUST must record in its securities register

- prescribed information regarding the natural persons who are the beneficial owners of the company,
- in the prescribed form, and
- must ensure that this information is updated within the prescribed period after any changes in beneficial ownership have occurred

.

S56(12)

- Must file a record with the Commission
- In the prescribed form
- Containing the prescribed information
- Update by filing notice with the CIPC
- Within the prescribed period after changes happened

159. Submission: Given the necessary systems changes needed by the CIPC to collect and store the data which will be received from companies, does Parliament once again consider it reasonable that 1 April 2023 is a suitable date to enable both company administrators and the CIPC to meet these additional obligations?

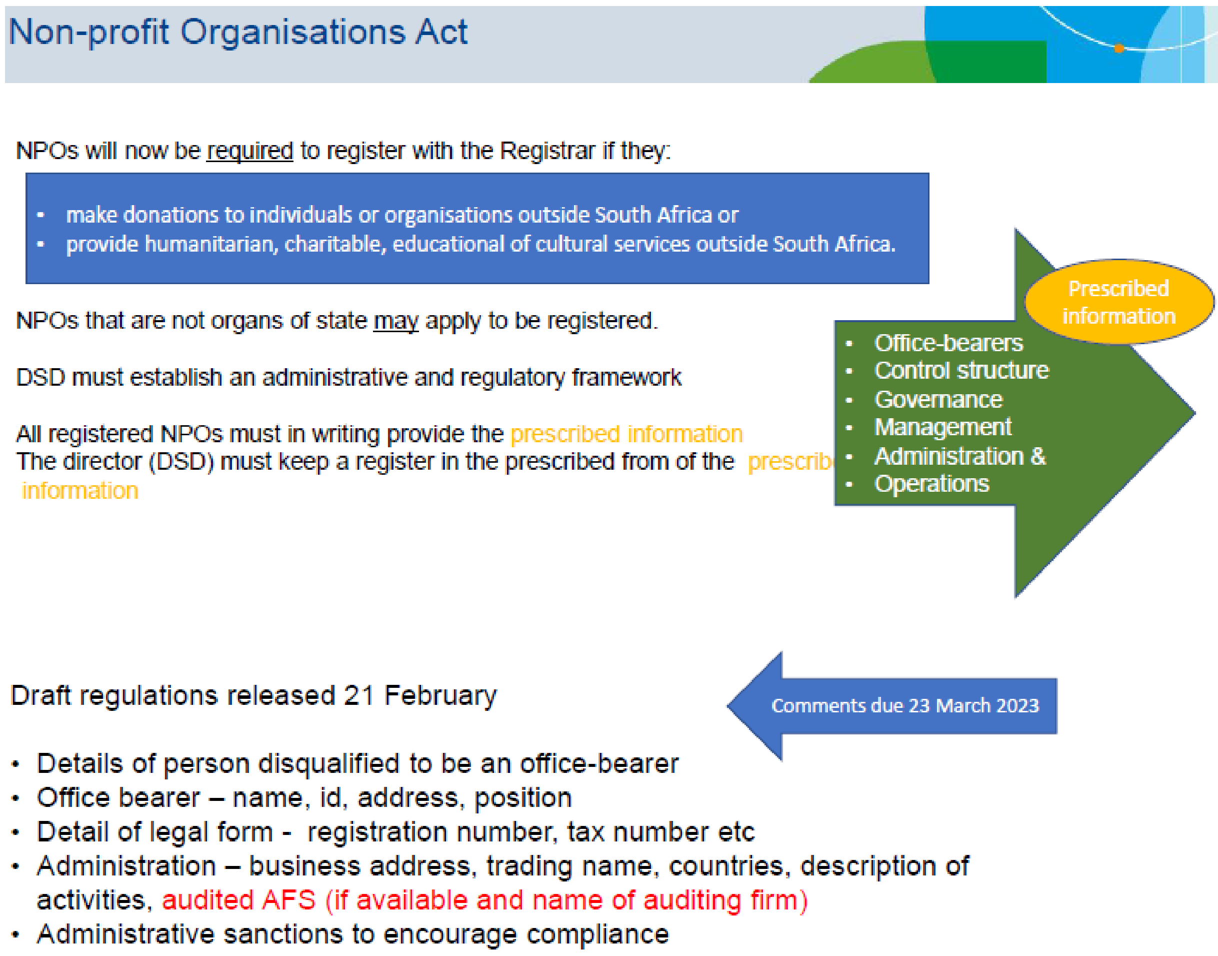
160. We also believe that those impacted have not had sufficient or reasonable time to implement these requirements, which by and large they still do not have the details of.

Dept of Social Development

Obligation Imposed

160.1 The FATF has noted its concern that South African non-profit organisations (NPOs) are used for money-laundering purposes.

160.2 In response to this deficiency within our legislative framework:



161. Most notably, the Department of Social Development is expected to establish an administrative and regulatory framework to monitor South African NPOs. This alone is a very extensive exercise, likely to take some months to accomplish.

162. Furthermore, the department is known to have had serious administrative difficulties in enforcing compliance within the NPO sector.

163. The above-mentioned draft regulations themselves are still undergoing public consultation. This will end on 23 March 2023 and will commence to apply from 1 April 2023.

164. Submission: Is it possible for the department to address these difficulties within the next one month?

165. Do the impacted NPO's even have an idea who they are and what they must do?

FIC

166. The additional FIC obligations

Change to who is an accountable institution

- Legal practitioners
- Co-operative banks
- Credit providers
- High value goods (valued in R100 000 or more)
- South African Mint Company (RF)(Pty)(Ltd)
- Persons carrying on the business dealing with various crypto-assets
- Trust and company service providers. (TCSP)

167. However as per our previous submissions, one of the key functionaries under the law is an “accountable institution, however it remains unclear who are “accountable institutions” under the amended law?

168. On 20 January 2023, Guidance on Trust and Company Service Providers Guidance in terms of Schedule 1 of the FIC Act for public comment.

169. However, this document still does not answer and clarify the critical scoping question.

170. There were also no transitional provisions following the effective date of 19 December 2022.

171. The FIC has tried to solve some of these teething problems by issuing a notice that no penalties will be levied in the first 18 months. That however does not make the relevant person any less non-compliant and that can have serious repercussions.

172. Submission: Is Parliament confident that the obligations imposed are proper and fair and that FIC and those it impacts are able to comply to the satisfaction of FATF?

173. Should the law now not be postponed given that greylisting has happened and we should not make matters worse?

Accounting and finance control

Grap Accrual Accounting

174. The modernisation of financial accounting and reporting the public sector was adopted by the ASB in April 2012 to move government to modern accrual accounting.

175. This would also align it to the private sector.

176. Hover 11 years later this has still not been implemented and as raised in previous years, even SARS and Treasury seem to find this challenging.

177. We have in previous years made detailed submissions how cash accounting has been creating loopholes and abuse at for example local government and SARS and causes matters such as non-payment of SME’s and refund delays.

178. Submission: Is Parliament aware of what is preventing the implementation of GRAP and why is it not concerned by the constant delays?

Integrated Financial Management System

179. We welcome National Treasury's presentation to SCoF on 21 February 2023 that IFMS will be proceeding to realise these benefits of a standardised and integrated finance system.

180. What is however not clear is if the data will be available in real time to Treasury across all levels of government and automatically consolidated?

181. This would be the function necessary to enhance accountability, oversight and decision making and reduce the time spent by government in managing financial data and decrease the time for oversight bodies such as Treasury and Parliament to action interventions.

182. Submission: Does Parliament know if the above functionality is available in IFMS and clearly understanding how oversight bodies will benefit from it?

National Water Disaster

183. The National Water and Sanitation Master Plan[4] is titled "Addressing the crisis" and begins thus:

South Africa is facing a water crisis caused by insufficient water infrastructure maintenance and investment, recurrent droughts driven by climatic variation, inequities in access to water and sanitation, deteriorating water quality, and a lack of skilled water engineers. This crisis is already having significant impacts on economic growth and on the well-being of everyone in South Africa.	

184. We consider this issue to be of greater importance than loadshedding because access to safe, drinking water is crucial to our survival.

185. The Minister has noted the plan to spend R132.5 billion over the next three years, mainly by the water boards.

[4] National Water and Sanitation Master Plan Volume 1: Call to Action v 10.1 31 October 2018

Table 5.11 Economic development expenditure

R million	2022/23	2023/24	2024/25	2025/26	Percentage of total MTEF allocation	Average annual MTEF growth
	Revised estimate	Medium-term estimates				
Economic regulation and infrastructure	112 445	124 863	143 768	159 158	55.3%	12.3%
of which:						
Water resource and bulk infrastructure	*27 544*	*34 092*	*38 368*	*48 801*	*15.7%*	*21.0%*

186. This initially seems adequate, until one looks at the 2019 National Water Masterplan, which highlights the inadequacy of these budgeted amounts by showing that South Africa needs at least R89bn per annual for 10 years to fund water infrastructure:

Funding Gap over the next decade

Funding Requirement	-	Funding Available	=	Funding Gap
• R 898 billion		• R 565 billion		• R 333 billion (37%)

187. These estimates were before the current flood damage and damage due to loadshedding and therefore may have significantly increased.

188. The Minister's Budget allocation for water infrastructure also assumes that these funds are (or will be) in fact effectively and efficiently spent, a fact we will dispute below.

189. South Africa, an already water scarce country, faces a water crisis caused by insufficient water infrastructure maintenance and investment and a lack of skilled water engineers.

190. 56% of waste-water treatment works (which remove and eliminate sewage from wastewater) and 44% of water treatment works in South Africa are said to be totally dysfunctional.

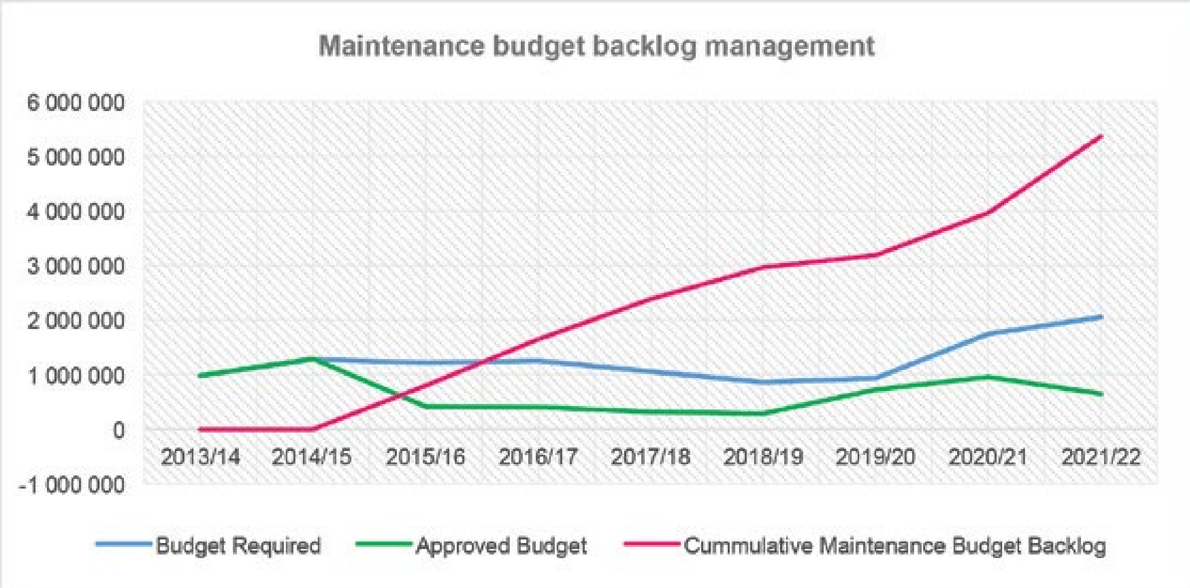
191. Water demand continues to outpace supply, leaving the potential for a looming shortage with Gauteng already experiencing "watershedding" in 2022 even with dams nearly 100% full.

192. The "new reality", according to the National Water and Sanitation Master Plan, is not only that will water become more expensive, but that everyone must use less water for the same activities[5].

193. South Africa's average daily domestic water usage is 64 litres per person per day more than the world average. In addition, municipalities lose 35% of water through burst pipes, leaks, etc and the magnitude of our nation's water problem becomes clearer.

194. There is also a R36 billion backlog in maintenance and refurbishment of national water resources infrastructure, which continues to grow year by year.

[5] National Water and Sanitation Master Plan, Call to Action



195. This backlog pertains only to maintenance, and not the additional water and sanitation infrastructure so desperately needed.

196. While the 2023 Budget Speech contains more references to water infrastructure than any other in recent memory, the negative is that the intended plans mentioned may be "too-little-too late", as capital-intensive projects take many years to complete.

197. We are simply not completing critical water and sanitation infrastructure projects on time, with the Minister himself mentioning that of all the critical infrastructure projects underway in the water and sanitation, energy, and transport sectors, only R3.9 billion worth of those projects have been completed. R134.2 billion are still only in the procurement phase, while R232.3 billion are still in construction.

198. The 2023 Budget Review has further pointed out that notwithstanding an allocation of funds to address water/sanitation infrastructural development, poor administration continues to undermine actual spending and the completion of projects:

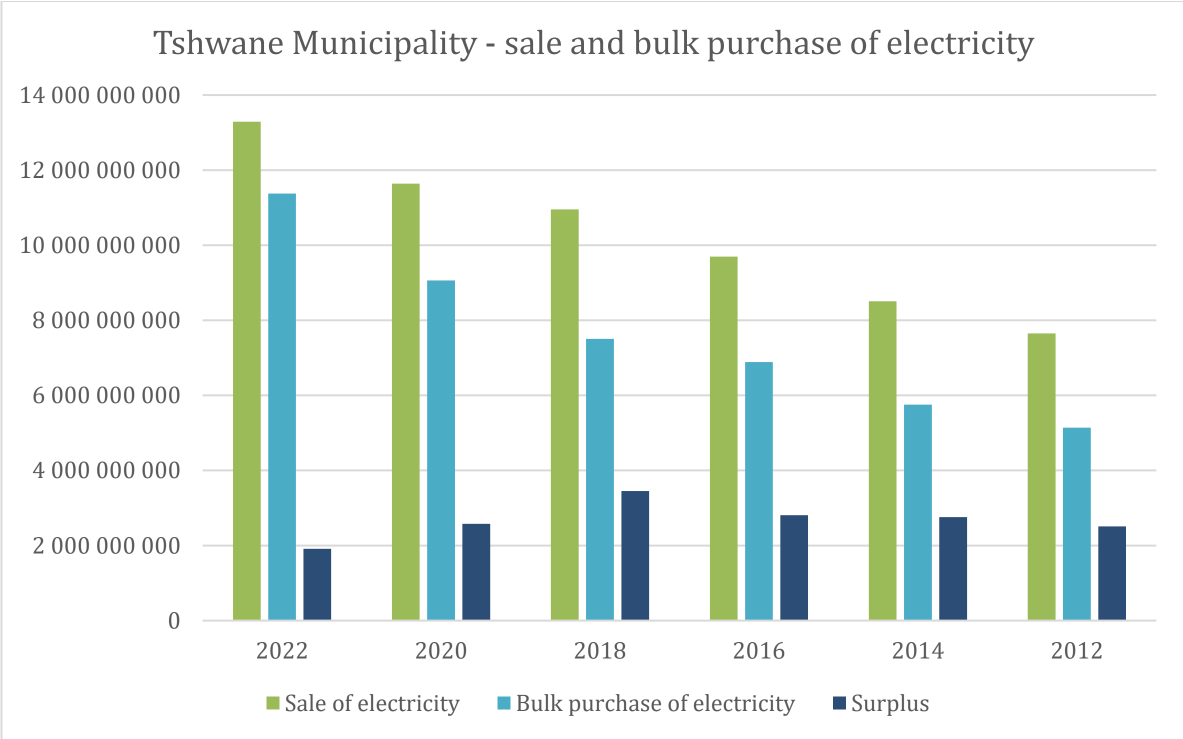
> *With regards to the Vaal River Pollution Remediation Project, <u>the Department of Water Affairs and Sanitation, together with the National Treasury,</u> should <u>ensure that project planning for the Regional Bulk Infrastructure Grant projects is properly done timeously to avoid funds being rolled over to the next financial year or returned to the fiscus</u>. The Committee believes that the failure to spend on infrastructure Budgets continues to undermine government's commitment to implement an infrastructure-led economic recovery.*
>
> [own emphasis]

The impact of declining municipal income from water/electricity

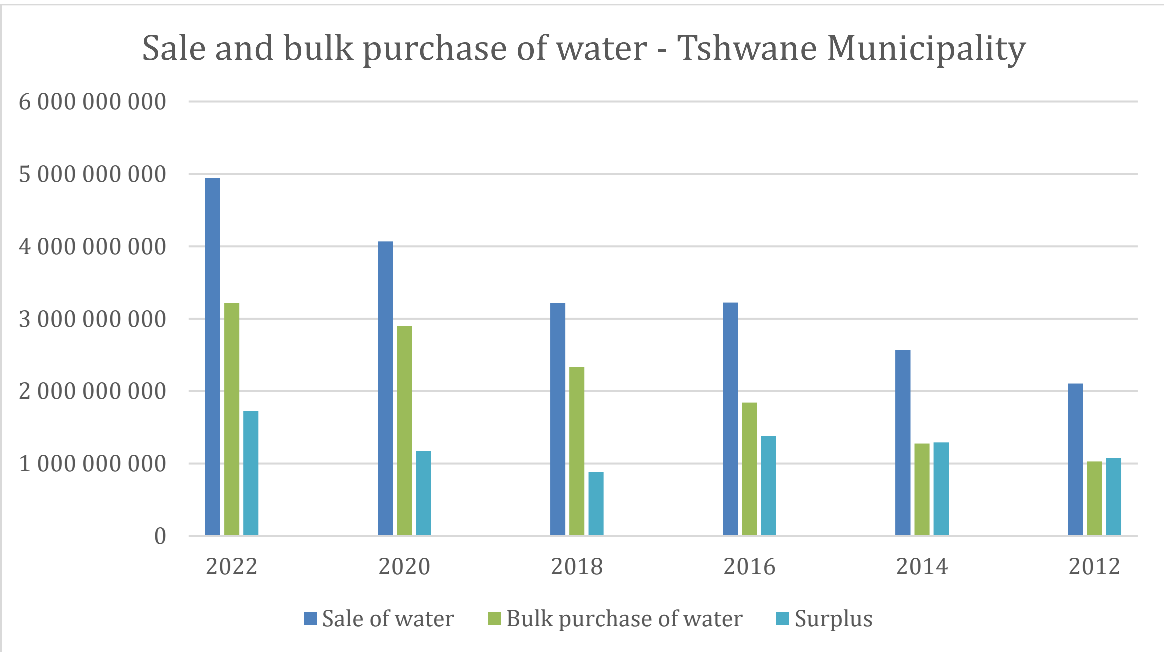
199. Municipalities make bulk purchases of electricity and water and then mark it up when it is billed to ratepayers. This is, in the first place, to fund the provision of electricity and water for free to

certain residents in the municipality and to cover technical losses and use of electricity and water not paid for – i.e., non-technical losses due to theft.

200. Using the Tshwane Metro as a case study, in the last 10 years, electricity sales have increased exponentially but the profits have declined, showing something seriously wrong.



201. Water has a similar trend though not as drastic with sales more than double but profits not matching it.



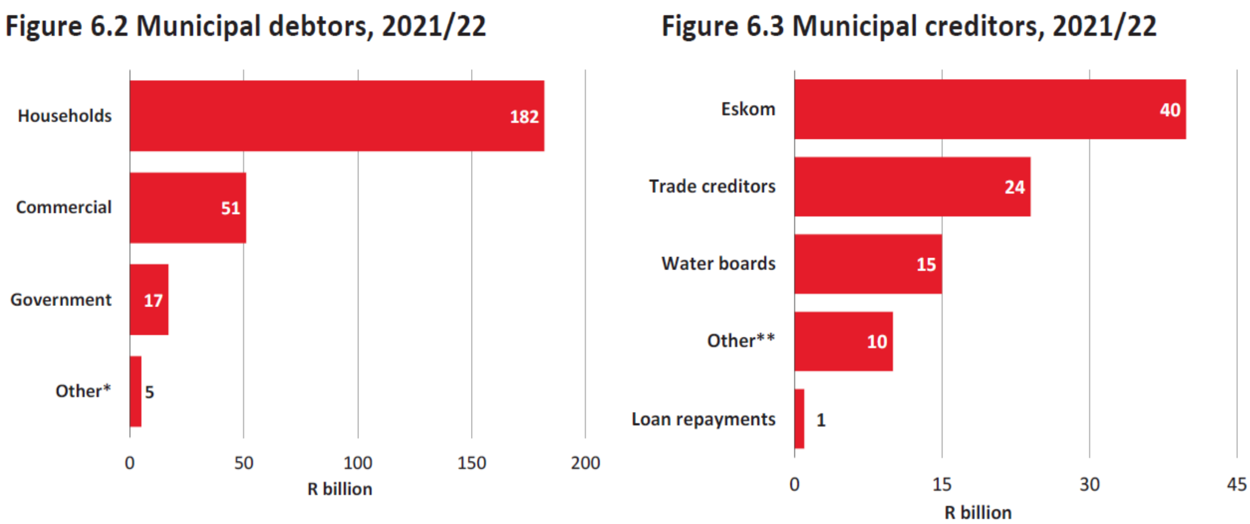
202. The Minister has stated that:

South African Local Government Association (Salga), together with the Department of Water Affairs, the Department of Cooperative Governance and Traditional Affairs, the University of Pretoria and the Development Bank of Southern Africa, should <u>continue to intensify capacity building efforts to assist municipalities to address infrastructure repairs and maintenance challenges, particularly with regards to water treatment plants to address sewage spillage in certain areas.</u>

203. Only 59% of South Africans pay for their water, meaning that municipalities do not charge for 41% of the water they provide.

204. Municipalities therefore lose about 1660 million m³ per year through "Non-Revenue Water[6]" (i.e., water provided to citizens "for free"). At a unit cost of R6 per cubic metre, this amounts to an annual amount of R9.9 billion that government could have earned had this water been provided for a fee. Government will have no choice but to charge for at least some of this water going forward.

205. Even with the aforementioned 59% of users who do pay for water, a further analysis of this group leaves little to be desired, with billions of Rands currently owed to municipalities for the provision of both water and electricity. The below[7] paints a startling picture of the current situation:



**Includes rental and equipment leases income, interest on arrears and other recoveries, and outstanding payments from national or provincial government for projects carried out by municipalities on their behalf*
***Includes PAYE deductions, output VAT less input VAT, pensions or retirement and Auditor-General*
Source: National Treasury

206. In short, private households currently owe municipalities R182 billion, who, in turn, owe Eskom and the water boards (Rand Water, etc) R40 billion and R15 billion respectively.

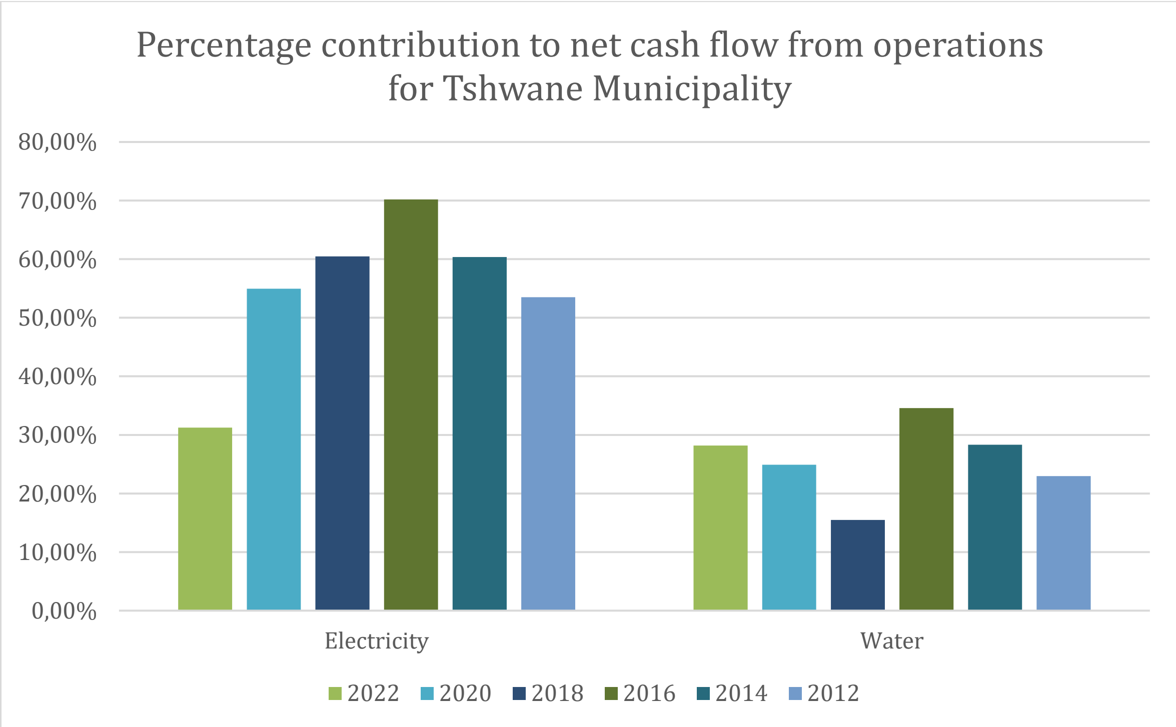
207. Rand Water has specifically noted in its 2022 Annual Report that defaulting customers cause a reduction in its income, thereby affecting the implementation of its infrastructure expenditure[8].

[6] National Water and Sanitation Master Plan, Call to Action
[7] 2023 Budget Review
[8] https://www.randwater.co.za/media/annual_reports/RANDWATER-%20INTEGRATED%20ANNUAL%20REPORT%202021-22.pdf

208. Partial payment of the debt owed to municipalities by households would create a positive domino effect which would alleviate some of the financial pressure faced by the municipalities and ultimately, Eskom and the water boards.

209. The overall situation is unsustainable, forcing government to resort to debt in order to fund additional water infrastructure expenditure. This begs the question, is South Africa one drought away from a self-made water disaster?

210. To get some perspective on the municipalities' reliance on the profits from the sale of water and electricity and water, we look at profits from water and electricity and a percentage of net cash flow from operations.



211. As is illustrated, the surpluses from the sale of electricity and water, make a significant contribution to the funds of the municipalities.

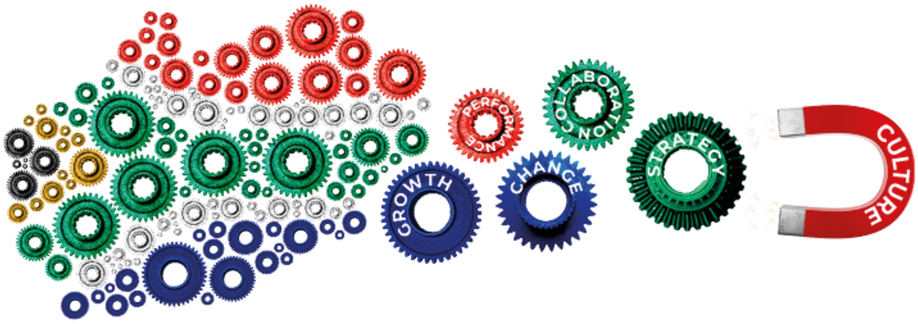
212. However, there is a decline in the contribution in the last two years for Tshwane, in particular. For Tshwane, the contribution dropped to 31.25% and 28.18%, which is significantly lower than the previous year's contributions for electricity and water respectively.

213. The drop in the contribution, for electricity, is due to the loadshedding and lack of sufficient maintenance of infrastructure. The drop in the contribution for water, in a year where the municipalities had above average rainfall, is also due to the loadshedding to a lesser extent and lack of maintenance of infrastructure.

214. The risk faced by municipalities, because of load shedding and the badly maintained water and electricity infrastructure, is that it will get a reduced contribution from the sale of electricity and water, to fund its operations.

215. This is all before many more paying consumers start migrating off the municipal grid with particularly, rural municipalities at financial risk. Whilst municipalities are already financially

imploding as is quite apparent from the Auditor General's report, this will only push them further into the abyss.



PERFORMANCE
COLLABORATION
STRATEGY
CULTURE
GROWTH
CHANGE

BUDGET 2023