

**FREEBASICSERVICES
INTHE
WESTERNSCAPE**

JUNE2003

LIEBJLOOTS

FREE BASIC SERVICES IN THE WESTERN CAPE

FINAL REPORT

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1. BACKGROUND

In August 2002 the Provincial Minister for Local Government issued a statement in which he announced an investigation into the delivery of basic services in the Western Cape. This report is a summary of the findings of that investigation.

This report contains the results of the analysis of the information that was made as at mid-December 2002. A draft report was submitted to the Department for Local Government in the Western Cape at the start of 2003. The final report, of which this is a summary, has incorporated the comments received from the Department.

2. BRIEF FROM THE MINISTER

In his statement Minister Doman formulated the brief for the investigation.

“His terms of reference for the investigation include:

- To define the term “basic services” as applied in the Western Cape;
- To quantify the delivery of basic services as delivered by the municipalities in the Western Cape, the cost involved, as well as the financing of these costs;
- The level of free basic services and the current affordability;
- The identification of other free services delivered by municipalities;
- The identification of possible other free services that can be delivered and the cost involved;
- To determine whether the equitable share allocation to municipalities from national revenue is sufficient to finance free basic services;
- To investigate alternative sources of finance which can be utilised for the provision of free basic services.”

3. SURVEY

A draft questionnaire was tested at a few municipalities during August 2002 and finalised for the survey amongst the municipalities of the Western Cape. During September and October 2002 the municipalities in the Western Cape were visited to complete the questionnaire and collect the information. Follow-up work was done during November 2002 to complete and clarify the information.

All the information received from municipalities in the Western Cape was for the 2001/2002 municipal financial year.

Cape Town Metro Municipality could not provide any information as they were still busy implementing a new (SAP) financial system.

4. DEFINITION OF BASIC SERVICES

The definition of basic services is very important and can have far-reaching financial implications.

In the 1998 publication “Providing Affordable Basic Services: Towards an Indigents Policy for Local Government” basic services are defined as follows:

“From a household perspective, a package of *basic services* would typically include:

- Access to a minimum safe water supply (as defined by White Paper on Water Supply and Sanitation, 1994)
- Adequate sanitation (as defined in Sanitation White Paper)
- Solid waste removal
- Access to household energy supplies
- Mobility – locally and to areas of economic opportunity (access to and availability of roads and public transport)
- Protection from flooding (adequate drainage and storm water management)
- Availability of primary healthcare facilities
- Access to communication (access to telephone network)
- Access to education facilities (schools, libraries)
- Facilitation of community activities (access to community halls and recreation facilities).”

It is axiomatic that a service that is not affordable on a sustainable basis cannot be a basic service. Sustainable affordability is therefore an inherent and inseparable aspect of the definition of a basic service.

With respect to the costs of basic services, a 1998 publication stated:

“The actual cost per household in any specific context will depend on a large number of factors of which the most important are: (1) the *level of service* provided, (2) the *amount* consumed, (3) the technical efficiency of the service provision, (4) realisation of economies of scale, and (5) local physical factors such as topography, geology and climate. Hence unit services cost will typically vary widely between cities and towns.”

However, notwithstanding this apparent impossibility of formulating an universal, or even just a national, uniform definition of basic services, or perhaps even because of it, the inter-governmental fiscal system developed in South Africa is in fact an implicit recognition of the affordability principle. In other words, if a municipality cannot generate enough revenue to provide basic services to all its residents, especially those who cannot afford it, then there must be a transfer from the national government in order to make the delivery of those basic services affordable. Sustainability is therefore not just a local issue, but also a national concern. It also confirms the unavoidability of national standards for basic services, if all citizens must receive at least comparable basic services, and by implication a national definition of basic services.

In a paper by the erstwhile Department of Constitutional Development entitled “Targeting Poor Households in the Provisioning of Basic Municipal Services: A guideline for municipalities”, the above-mentioned list of services were repeated as a list of basic services. It refers, however, to the “Municipal Infrastructure Investment Framework” (MIIF) as a recommendation of what the level of each basic service should be, effectively therefore a definition of each basic service.

The MIIF recommendations do unfortunately not provide much assistance as seven potential levels of service delivery are given for each of the six services (the first six in the list above). It is apparently left to each municipality to decide at which level a service has to be delivered to the indigent. This effectively makes local affordability the criteria for a basic service. Moreover, the levels are also aimed at infrastructure rather than the ongoing provision of the

service. The levels are also relatively vague, for example for water the levels include the following: “unreticulated”, “communal standpipe”, “yard tank”, “yard tank (metered)”, “house connection”.

More information is given in a few departmental white papers on what the basic service level could be. The best example of this is the white paper of the Department of Water Affairs and Forestry (DWA), “White Paper on Water Supply and Sanitation” (1994). It defines basic water provision as follows:

“... a basic water supply ...

- the consumption of a minimum of 25 litres per capita per day (lcd);
- access to the water supply should be within 200 metres of each household;
- there should be a minimum flow at the source (for example, a tap) of 10 litres per minute;
- the water should be available on a regular daily basis;
- there should be a 98 percent assurance of the supply;
- the system must be effectively operated and maintained; and
- the water must be safe to drink.”

The efforts of other departments are less detailed and less useful.

In not one of the papers is the issue of affordability addressed specifically. The implication, and sometimes explicit assumption, is that basic services will be made available to the indigent through cross-subsidisation. It is, however, an assumption that is not workable for the majority of South African municipalities.

The approach that is proposed in this report is that basic services should be defined including the concept of sustainable affordability. Consequently, attention is first given to the costs of basic services after which we shall return to the definition of basic services.

However, there is another gap in the literature that must be addressed seriously. It is the implicit assumption that a household with a monthly income R1200 (or R1100 in some municipalities) or less cannot afford to pay for basic services but as soon as such a household earns one rand more it has to pay for basic services in full. Most municipalities in the Western Cape have effectively based their indigency policy on this implicit assumption.

The average monthly cost of (minimum) basic services per household is R320, or about 25% of the income of a marginal household (a household earning R1200 per month). Consequently, if a marginal household's income increases with one rand, the net income (gross income minus basic services) of this household decreases to R880 after payment for basic services (R320). Such an outcome is undesirable as it could serve as a disincentive.

It is even possible that this outcome could be regarded as unconstitutional as it could be argued that households are not treated equitably. It could be seen as inequitable that a poor household's net income decreased by R320 if it earned R1 more, whereas a wealthy household that also earns R1 more will not experience any decline in its net income.

It is also inevitable that the practice to provide basic services free up to the indigency cut-off point after which the full service tariff has to be paid will have negative social consequences. It could undermine the incentive to work if the work is remunerated at a wage low enough that the net income of the household after paying for basic services should decline as a result. It can hold a household that is trying to improve itself economically in a grip of declining or stagnant income.

Allh/h									
10	1	2.87	5	3	20.53	<20	0	<20	0
15	0		6	21	18.14	20-<30	0	20-<30	0
20	7	6.19				30-<40	0	30-<40	0
25	1	7.04				40-<50	0	40-<50	0
30	1	7.71				50-<60	0	50-<60	0
40	0					60-<70	0	60-<70	0
50	0					70+	0	70+	0
Sub-total	10			24			0		0
Ave.	20.5	6.10	Ave.	5.87	18.44	Ave.	0	Ave.	0
Onlyindigent									
10	0		5	1	12.29	<20	2	<20	7
15	1	4.66	6	4	13.64	20-<30	3	20-<30	7
20	5	4.82				30-<40	6	30-<40	2
25	0					40-<50	3	40-<50	5
30	0					50-<60	3	50-<60	1
40	1	11.25				60-<70	1	60-<70	2
50	3	14.41				70+	6	70+	0
Sub-total	10			5			24		24
Ave.	31.67	8.71	Ave.	5.8	13.37	Ave.	50.15	Ave.	30.95
None	10	0		1	0		6		6
TotalH/h	30			30			30		30

A number of interesting observations can be made from Table 2.

First, the effect of the DWAF guidelines for basic water is noticeable. Most municipalities provide 6kl per month free to each household. This is significantly more uniform than with the other services.

The variation among municipalities in the estimated rand value for a quantity of water and electricity free to a household is relatively small in the case of water, but relatively large for electricity. However, the cost per litre for electricity is more similar.

The pattern that is observed with respect to electricity is to be expected. The estimated rand value is calculated on the basis of the estimated costs of the provision of the service and not on the tariff that the municipalities levy on it. It therefore excludes differences in profit margins (or cross subsidisation). If the cost per unit is more or less the same for electricity, the cost of free services must increase as the volume of free services increase. This does apply to water.

6. ANNUAL COST OF BASIC SERVICES

In this section the focus is only on the current cost of basic services to indigent households (not all households) and not whether the cost is reasonable or reflecting a satisfactory level of efficiency.

A simple method was used to calculate the cost of providing basic services free to the indigent.

First, the cost per household per year was obtained by dividing the total operating cost per service by the number of recipients (businesses and households or "account units") of that service. This calculated was then multiplied by the registered number of indigent households to obtain the total cost per municipality of providing the service free to indigent households.

The cost per household for the different services shows considerable variation. It reflects both cost differences, as well as differences in accounting practices and the extent to which “profit margins” differ with respect to cost recovery services.

For all the municipalities in the province the average cost per household is R2,237 for electricity, R759 for water, R478 for sewerage and R363 for refuse. This can be estimated to estimate the total cost of free basic services to the indigent in the province:

• Electricity—41,813 indigent/holds;	R93,833,497 cost of basic service;
• Water—58,603 indigent/holds;	R47,243,631 cost of basic service;
• Sewerage—42,657 indigent/holds;	R23,709,546 cost of basic service;
• Refuse—40,287 indigent/holds;	R16,942,691 cost of basic service.

This gives a total of R182,729,365 for the provision of free basic services to all registered indigent households in the province. This is an indication of the real cost of free services to the indigent, rather than the official financial or budgeted cost.

The latter, budgeted cost of free services to the indigent is not available for most municipalities. Moreover, free water, and in many cases also free electricity, are built into a restructured tariff structure. Some or other form of cross subsidisation is used to finance these basic services.

However, even if use is made of cross subsidisation, the method used here for estimating the cost of free services is probably accurate enough for the purposes of this analysis.

For comparative purposes, Table 4 presents the cost of providing a quantity of free water and electricity to all households. In most cases, as with free water and electricity to the indigent, the cost of free water and electricity to all households is financed by cross subsidisation (i.e. increasing the tariff on higher levels of consumption). Some municipalities also adjusted the “basic tariff” (or “availability tariff”) to include effectively at least part of the cost of the free quantity in this up-front tariff.

The free quantity of water and electricity has another kind of “cost” in terms of the uneven burden carried by similar consumers in the different municipalities. This is discussed in more detail in the next section.

TABLE3: COST OF BASIC SERVICES TO INDIGENT HOUSEHOLDS

MUNICIPALITY		Free/Indigent consumers(h/h)				Cost/year/household				TOTAL:Cost/year			
		Elec	Water	Sewer	Refuse	Elec	Water	Sewer	Refuse	Elec	Water	Sewer	Refuse
		No	No	No	No	No	No	No	No	No	No	No	No
Matzikama	WC011	3031	3031	3031	3031	1,556	657	521	287	4,716,236	1,991,367	1,579,581	870,845
Cederberg	WC012	1640	1640	1640	1640	2,331	689	450	403	3,823,010	1,129,666	738,658	661,595
BergRiver	WC013	829	829	829	829	2,204	627	322	294	1,827,399	520,149	266,565	243,553
SaldanhaBay	WC014	0	1593	1593	1593	2,306	1,503	555	506	0	2,395,046	884,296	806,068
Swartland	WC015	1863	2593	2593	2632	2,204	671	341	214	4,105,991	1,740,904	884,216	564,491
WestCoastDistrict	DC1	0	2560	134	144	2,435	1,035	0	323	0	2,649,819	0	46,467
Witzenberg	WC022	859	859	859	859	6,139	1,362	915	742	5,273,800	1,170,384	786,286	637,485
Drakenstein	WC023	0	1500	0	0	2,716	529	510	528	0	793,364	0	0
Stellenbosch	WC024	1167	1167	0	0	4,008	1,087	0	0	4,677,045	1,268,363	444	533
BreedeValley	WC025	2000	2000	2000	2000	2,703	1,257	821	658	5,405,553	2,514,650	1,641,073	1,316,932
BreëRiver/Wineland	WC026	2903	2903	2903	2903	2,952	773	425	324	8,569,204	2,243,004	1,234,481	939,716
BolandDistrict	DC2	0	250	0	0	0	5,320	664	0	0	1,329,964	0	0
Theewaterskloof	WC031	0	3635	3635	3635	4,115	823	530	363	0	2,993,135	1,924,968	1,321,182
Overstrand	WC032	2741	2741	0	0	1,898	939	554	377	5,203,193	2,573,471	0	0
CapeAgulhas	WC033	720	720	370	370	2,135	888	362	0	1,537,391	639,232	134,084	0
Swellendam	WC034	4311	4536	1462	1462	2,131	509	407	201	9,188,090	2,309,980	594,628	294,213
OverbergDistrict	DC3	0	475	475	475	0	0	0	0	0	0	0	0
Kannaland	WC041	1600	1600	0	0	1,759	131	126	162	2,813,855	210,157	0	0
Langeberg	WC042	1775	1775	1775	1775	1,721	434	274	222	3,054,034	770,152	487,237	393,697
MosselBay	WC043	3592	3676	3592	3559	2,310	1,044	632	316	8,298,551	3,837,854	2,269,398	1,125,731
George	WC044	2313	2313	0	0	1,738	1,309	863	402	4,020,225	3,028,252	0	0
Oudtshoorn	WC045	2850	2850	2850	2850	2,569	846	487	347	7,321,644	2,409,740	1,387,708	987,662
PlettenbergBay	WC047	0	5150	5150	5150	2,494	905	1,174	706	0	4,659,544	6,047,018	3,637,758
Knysna	WC048	3000	3000	3000	3000	2,226	685	581	909	6,677,800	2,055,545	1,743,643	2,726,700
GardenRoute/KleinKar	DC4	0	301	0	0	1,944	383	295	231	0	115,194	0	0
Laingsburg	WC051	306	593	593	593	1,762	248	203	168	539,024	146,996	120,443	99,731
PrinceAlbert	WC052	446	446	446	446	1,315	405	459	192	586,394	180,572	204,599	85,690
BeaufortWest	WC053	3117	3117	3117	731	1,651	425	214	221	5,144,972	1,323,387	667,381	161,268
CentralKarooDistrict	DC5	750	750	610	610	2,733	325	185	35	2,050,086	243,740	112,839	21,374

TABLE 4: TOTAL "COST" PER YEAR OF FREE WATER AND ELECTRICITY TO ALL HOUSEHOLDS

MUNICIPALITY	Total households Electricity Number	Total households Water Number	Free Basic service Electricity Yes(1)/No(0)	Free Basic service Water Yes(1)/No(0)	Cost per consumer/p.y. Electricity Rand/consum	Cost per consumer/p.y. Water Rand/consum	Total Costp.y. Electricity Rand	Total Costp.y. Water Rand
Matzikama	6,234	5,688	1	1	1,556	657	9,700,184	3,739,233
Cederberg	3,375	3,134	0	1	2,331	689	0	2,158,764
Berg River	0	0	1	1	2,204	627	0	0
Saldanha Bay	15,973	16,649	0	1	2,306	1,503	0	25,031,462
Swartland	11,145	14,937	0	1	2,204	671	0	10,028,496
West Coast District	146	2,337	0	1	2,435	1,035	0	2,418,994
Witzenberg	4,033	8,008	1	1	6,139	1,362	24,760,459	10,910,871
Drakenstein	0	0	0	0	2,716	529	0	0
Stellenbosch	0	0	0	0	4,008	1,087	0	0
Breede Valley	16,166	14,204	1	1	2,703	1,257	43,693,087	17,859,044
Breë River/Wineland	11,592	20,412	0	1	2,952	773	0	15,771,338
Boland District	0	755	0	1		5,320	0	4,016,492
Theewaterskloof	2,609	9,897	0	1	4,115	823	0	8,149,398
Overstrand	18,452	20,500	0	1	1,898	939	0	19,247,049
Cape Agulhas	6,403	6,257	1	1	2,135	888	13,672,107	5,555,102
Swellendam	3,972	4,197	1	1	2,131	509	8,465,575	2,137,343
Overberg District	8	1,226	0	1			0	0
Kannaland	0	0	1	1	1,759	131	0	0
Langeberg	9,559	10,255	1	1	1,721	434	16,447,051	4,449,525
Mossel Bay	19,722	19,277	1	1	2,310	1,044	45,563,480	20,125,763
George	13,524	16,264	1	1	5,810	1,309	78,572,633	21,293,337
Oudtshoorn	0	0	0	1	2,569	846	0	0
Plettenberg Bay	0	0	0	0	2,494	905	0	0
Knysna	0	0	0	1	2,226	685	0	0
Garden Route/Klein Kar	0	0	0	1	1,944	383	0	0
Laingsburg	627	1,069	0	1	1,762	248	0	264,990
Prince Albert	1,147	1,087	0	1	1,315	405	0	440,094
Beaufort West	4,233	3,967	0	0	1,651	425	0	0
Central Karoo District	234	931	0	0	2,733	325	0	0
TOTAL							240,874,576	173,598,295

7. CURRENT FINANCING OF BASIC SERVICES

The financing of free basic services to indigent households can happen in one of the following ways:

- Cross subsidisation – where higher consumption is charged at a higher tariff to compensate for the lost revenue.
- Subsidies from general revenue – internal transfers from the general revenue account to the income account of the specific services to compensate for the forfeited tariff income.
- Equitable share allocation – transfers (based on a formula calculation by the DPLG) to the municipality from the revenue collected nationally.

Table 5 first gives an estimate of the annual cost to municipalities as a result of the free basic services to indigent households. It then gives the equitable share allocation received by the municipality. The assumption is made that the allocation is in the first instance used for the financing of assistance to the indigent. Some municipal councils also voted an amount for indigency support. This is given in the second last column of the table (own funds). The difference (surplus/shortage) between the total of these two sources of financing and the cost of indigent support is given in the last column.

TABLE5:FINANCINGOFFREEBASICSERVICES:INDIGENT

MUNICIPALITY	TOTAL:Cost/yearFreebasicservices	TOTAL				FINANCING		SURPLUS/ SHORTAGE	
		Electricity	Water	Sewerage	Refuse	EquitableShare	Ownfunds		
		Rand	Rand	Rand	Rand	Total	Total	Rand	
Matzikama	WC011	4,716,236	1,991,367	1,579,581	870,845	9,158,029	2,800,000	0	-6,358,029
Cederberg	WC012	3,823,010	1,129,666	738,658	661,595	6,352,929	2,567,999	0	-3,784,930
BergRiver	WC013	1,827,399	520,149	266,565	243,553	2,857,666	1,828,000	0	-1,029,666
SaldanhaBay	WC014	0	2,395,046	884,296	806,068	4,085,410	1,586,289	3,524,260	1,025,139
Swartland	WC015	4,105,991	1,740,904	884,216	564,491	7,295,603	236,727	0	-7,058,876
WestCoastDistrict	DC1	0	2,649,819	0	46,467	2,696,285	0	0	-2,696,285
Witzenberg	WC022	5,273,800	1,170,384	786,286	637,485	7,867,955	3,625,760	0	-4,242,195
Drakenstein	WC023	0	793,364	0	0	793,364	5,000,000	0	4,206,636
Stellenbosch	WC024	4,677,045	1,268,363	0	0	5,945,408	5,400,000	0	-545,408
BreedeValley	WC025	5,405,553	2,514,650	1,641,073	1,316,932	10,878,207	4,554,819	0	-6,323,388
BreëRiver/Wineland	WC026	8,569,204	2,243,004	1,234,481	939,716	12,986,404	2,745,077	0	-10,241,327
BolandDistrict	DC2	0	1,329,964	0	0	1,329,964	0	0	-1,329,964
Theewaterskloof	WC031	0	2,993,135	1,924,968	1,321,182	6,239,285	3,048,228	0	-3,191,057
Overstrand	WC032	5,203,193	2,573,471	0	0	7,776,664	2,054,577	0	-5,722,087
CapeAgulhas	WC033	1,537,391	639,232	134,084	0	2,310,707	1,415,605	0	-895,102
Swellendam	WC034	9,188,090	2,309,980	594,628	294,213	12,386,911	2,073,964	0	-10,312,947
OverbergDistrict	DC3	0	0	0	0	0	399,000	0	399,000
Kannaland	WC041	2,813,855	210,157	0	0	3,024,012	1,822,970	0	-1,201,042
Langeberg	WC042	3,054,034	770,152	487,237	393,697	4,705,120	1,695,820	0	-3,009,300
MosselBay	WC043	8,298,551	3,837,854	2,269,398	1,125,731	15,531,534	2,145,000	5,260,000	-8,126,534
George	WC044	4,020,225	3,028,252	0	0	7,048,477	2,698,278	4,660,760	310,561
Oudtshoorn	WC045	7,321,644	2,409,740	1,387,708	987,662	12,106,754	2,025,000	2,313,374	-7,768,380
PlettenbergBay	WC047	0	4,659,544	6,047,018	3,637,758	14,344,320	1,740,000	300,000	-12,304,320
Knysna	WC048	6,677,800	2,055,545	1,743,643	2,726,700	13,203,688	1,869,399	974,543	-10,359,746
GardenRoute/KleinKar	DC4	0	115,194	0	0	115,194	2,387,000	0	2,271,806
Laingsburg	WC051	539,024	146,996	120,443	99,731	906,194	1,880,368	0	974,174
PrinceAlbert	WC052	586,394	180,572	204,599	85,690	1,057,255	1,686,770	0	629,515
BeaufortWest	WC053	5,144,972	1,323,387	667,381	161,268	7,297,007	2,071,597	800,000	-4,425,410
CentralKarooDistrict	DC5	2,050,086	243,740	112,839	21,374	2,428,039	0	153,277	-2,274,762
TOTAL		94,833,497	47,243,631	23,709,101	16,942,155	182,729,365	61,358,247	17,986,214	-103,383,924

Most municipalities have a shortage and in some cases the shortage is rather large. This shortage is an indication of the extent to which cross subsidisation is required as a mechanism with which to finance free basic services to the indigent.

Given this as an assumption the conclusion can be made that cross subsidisation in the Western Cape financed about 56% of the the cost of free basic services in 2001/02. The equitable share allocation contributed about 34% to the financing of the cost and the council allocation (own revenue or rate payers) financed about 10%.

8. AFFORDABILITY OF FREE BASIC SERVICES

In this section the affordability of free basic services is discussed from the perspective of the municipality.

The affordability of free basic services depends on a number of factors:

- The efficiency with which basic services are delivered.
- The cost at which basic services can be delivered.
- The ratio of indigent and poor households provided with the service to the number of households that can afford a full economic tariff.
- The feasible and desirable extent to which use can be made of cross subsidisation.
- The tax base from which the municipality can generate revenue.
- Inter-governmental transfers and fiscal arrangements that can be used for the subsidisation of basic services.

EFFICIENCY WITH WHICH BASIC SERVICES ARE DELIVERED

It was not possible within the constraints of this investigation to analyse the efficiency with which basic services are delivered. However, two comments are worth making in this regard.

The first comment is that although the efficiency will affect the affordability of the free delivery of basic services, it is not a factor that ought to be brought into consideration when calculating any form of subsidy or transfer to a municipality. The reason for this is that it will reduce the incentive to a municipality to be as efficient as possible.

The second comment is that it would not be possible to measure the efficiency with which a municipality delivers a basic service, at least not on a regular basis. It is therefore not practically feasible to bring efficiency into consideration when measures to help municipalities make free basic services affordable are designed.

THE COST AT WHICH THE BASIC SERVICES ARE DELIVERED

The cost per household of delivering a basic service was discussed in Section 6. However, the estimates used in that analysis were only for the provision of free basic services to the registered indigent. It did not include the cost or potential cost of providing basic services to the unregistered indigent and the poor who cannot afford to pay a full economic tariff.

Even so, however, the cost of providing basic services free to the registered indigent is already substantial. R185 million and more for the Western Cape is a significant amount and one that suggests that it would probably not be possible to continue with the current level of free basic services with it having a negative effect on the financial health of municipalities.

THE RATIO OF INDIGENT AND POOR HOUSEHOLDS

The lower the ratio of indigent and poor households (that cannot afford the full economic tariff) to the total number of consumers, the more affordable will the provision of free basic services be. Not only will that mean that fewer consumers will have to be subsidised, but also that the potential for cross subsidisation will be bigger.

TABLE 6: RATIO OF INDIGENT TO TOTAL HOUSEHOLDS

MUNICIPALITY	Total	Official	Estimated	Indigent	Ratio
	Consumers	Residential	Residential		
	Units	Households	Households	Consumers	Indigent
	Number	Number	Number	Households	to
				Number	Total/h
					consumers
Matzikama	6365	5688	5688	3031	53.29%
Cederberg	5051	3134	3134	1640	52.33%
Berg River	6450	0	6056	829	13.69%
Saldanha Bay	18044	16649	16649	1593	9.57%
Swartland	15821	14937	14937	2593	17.36%
West Coast District	2560	2337	2337	150	6.42%
Witzenberg	8849	8008	8008	859	10.73%
Drakenstein	32859	0	30854	1500	4.86%
Stellenbosch	16925	0	15892	1167	7.34%
Breede Valley	15343	14204	14204	2000	14.08%
Breë River/Wineland	12036	20412	20412	2903	14.22%
Boland District	774	755	755	250	33.11%
Theewaterskloof	10525	9897	9897	3635	36.73%
Overstrand	20935	20500	20500	2741	13.37%
Cape Agulhas	6659	6257	6257	720	11.51%
Swellendam	4536	4197	4197	4536	34.83%
Overberg District	1230	1226	1226	475	38.74%
Kannaland	3229	0	3032	1600	52.77%
Langeberg	11394	10255	10255	1775	17.31%
Mossel Bay	19549	19277	19277	3676	19.07%
George	17504	16264	16264	2313	14.22%
Oudtshoorn	11615	0	10906	2850	26.13%
Plettenberg Bay	12360	0	11606	985	8.49%
Knysna	22000	0	20658	3000	14.52%
Garden Route/Klein Karoo	1319	0	1239	301	24.30%
Laingsburg	1132	1069	1069	593	55.47%
Prince Albert	1214	1087	1087	446	41.03%
Beaufort West	7420	3967	3967	3117	78.57%
Central Karoo District	978	931	931	750	80.56%

It is clear from Table 6 that there is a big variation with respect to the percentage indigent households in a municipal jurisdiction. As the figures were provided by the municipalities themselves who might not have used comparable procedures for arriving at these numbers, Table 7 was compiled with 1996 Population Census data.

The dependency ratio in Table 7 is the number of households that earned less than R1100 per month expressed as the total number of households in a municipal area.

TABLE7:POPULATIONCENSUS–POORHOUSEHOLDSANDTOTALHOUSEHOLDS

MUNICIPALITY	Census Total H/holds	Census H/holds <R1100pm total	Percentage <R1100pm total	Provincial Indigent Consumers H/holds Number	Survey Ratio Indigent To TotalH/holds
Matzikama	10721	2954	27.56%	3031	53.29%
Cederberg	8618	2062	23.93%	1640	52.33%
BergRiver	9870	1819	18.43%	829	13.69%
SaldanhaBay	14084	1272	9.03%	1593	9.57%
Swartland	17320	3380	19.52%	2593	17.36%
WestCoastDistrict				150	6.42%
Witzenberg	18238	4398	24.12%	859	10.73%
Drakenstein	46196	6494	14.06%	1500	4.86%
Stellenbosch	29395	3739	12.72%	1167	7.34%
BreedeValley	32839	6076	18.50%	2000	14.08%
BreëRiver/Wineland	17310	4166	24.07%	2903	14.22%
BolandDistrict				250	33.11%
Theewaterskloof	20519	4462	21.75%	3635	36.73%
Overstrand	12384	1861	15.03%	2741	13.37%
CapeAgulhas	6053	824	13.61%	720	11.51%
Swellendam	6709	1585	23.63%	4536	34.83%
OverbergDistrict				475	38.74%
Kannaland	5277	1481	28.06%	1600	52.77%
Langeberg	10559	1988	18.83%	1775	17.31%
MosselBay	16643	1868	11.23%	3676	19.07%
George	28446	3363	11.82%	2313	14.22%
Oudtshoorn	17668	2432	13.76%	2850	26.13%
PlettenbergBay	5522	1169	21.16%	985	8.49%
Knysna	12385	2214	17.87%	3000	14.52%
GardenRoute/KleinKar				301	24.30%
Laingsburg	1622	438	26.97%	593	55.47%
PrinceAlbert	2382	671	28.17%	446	41.03%
BeaufortWest	8016	1189	14.83%	3117	78.57%
CentralKarooDistrict				750	80.56%

The Population Census approximation of the indigent ratio shows less variation than the figures of the provincial survey. However, it does appear as if a correlation exists between the Census derived indigent ratio and the Survey indigent ratio.

There can be a number of possible explanations for the differences between the two sets of estimates. These include the likelihood that conditions have worsened since the 1996 Census. However, there are also reasons why the Survey data may be relatively reliable:

- In most cases the Survey information is actually derived from an administrative process that is subject to periodic renewal, thus making the income data more reliable; and
- There is an incentive for municipalities to keep the number of registered indigent as low as possible.

The following conclusion therefore seems justified: municipalities are not equally capable to finance free basic services through cross subsidisation. In some municipalities it is hardly affordable at all if they had to rely on cross subsidisation.

**TABLE 8: PERCENTAGE INDIGENT AND POOR HOUSEHOLDS
MUNICIPALITY**

MUNICIPALITY	POPULATION CENSUS 1996			POPULATION CENSUS 1996			
	Census Total H/holds	Census H/holds <R1099pm total	Percentage <R1000pm total	Census H/holds R1100-R1499	Census H/holds R1500-R1799	Census H/holds <R1800pm total	Percentage <R1800pm total
Matzikama	10721	2954	27.56%	1361	753	5068	47.28%
Cederberg	8618	2062	23.93%	1570	754	4387	50.90%
BergRiver	9870	1819	18.43%	1393	772	3983	40.36%
SaldanhaBay	14084	1272	9.03%	1308	1055	3636	25.81%
Swartland	17320	3380	19.52%	2356	1206	6942	40.08%
WestCoastDistrict							
Witzenberg	18238	4398	24.12%	2942	1569	8909	48.85%
Drakenstein	46196	6494	14.06%	5889	3700	16082	34.81%
Stellenbosch	29395	3739	12.72%	3545	2419	9703	33.01%
BreedeValley	32839	6076	18.50%	4777	2560	13414	40.85%
BreëRiver/Wineland	17310	4166	24.07%	2726	1398	8290	47.89%
BolandDistrict							
Theewaterskloof	20519	4462	21.75%	3300	1774	9535	46.47%
Overstrand	12384	1861	15.03%	1158	670	3689	29.79%
CapeAgulhas	6053	824	13.61%	655	396	1875	30.97%
Swellendam	6709	1585	23.63%	974	467	3026	45.11%
OverbergDistrict							
Kannaland	5277	1481	28.06%	664	402	2547	48.27%
Langeberg	10559	1988	18.83%	1352	835	4176	39.55%
MosselBay	16643	1868	11.23%	1632	1424	4924	29.59%
George	28446	3363	11.82%	2579	2026	7969	28.01%
Oudtshoorn	17668	2432	13.76%	1980	1499	5911	33.46%
PlettenbergBay	5522	1169	21.16%	759	412	2340	42.37%
Knysna	12385	2214	17.87%	1681	887	4782	38.61%
GardenRoute/KleinKa							
Laingsburg	1622	438	26.97%	247	148	833	51.36%
PrinceAlbert	2382	671	28.17%	454	199	1324	55.58%
BeaufortWest	8016	1189	14.83%	1068	971	3227	40.26%
CentralKarooDistrict							

It is clear from Table 8 that the dependency ratio increases considerably if an income of less than R1800 per month is taken as a measure of poverty. The average percentage for the three highest municipalities is 52.61% and for the three lowest municipalities it is 26.03%.

If the poor (with incomes between R1100 and R1800 per month) were to be subsidised by 50% of the tariffs of basic services (in addition to the 100% free basic services to the indigent with monthly incomes less than R1200 per month), the tariffs that paying consumers would have to pay would go up by between 22% and 85%. It confirms that cross subsidisation is not appropriate as a mechanism for financing the additional subsidisation of services to the poor.

THE USE OF CROSS SUBSIDISATION

In addition to the feasibility of using cross subsidisation as discussed above, there is also the question of the desirability of using it to finance free or subsidised basic services. Municipalities have always made use of some degree of cross subsidisation and it is a generally accepted fiscal principle. However, the issue here is the extent of the cross subsidisation that will be required in most municipalities.

An important fiscal principle is that the redistribution of incomes should be undertaken at the national level rather than at the local level. If it were to be done to any significant degree at

the local level there is the danger that it can happen to varying degrees in different municipal jurisdictions. This can lead to undesirable and disruptive economic and social consequences.

This position has been accepted by implication in the Constitution of South Africa by making provision for the allocation of an equitable share of revenue collected nationally to provincial and local governments. The objective is clearly stated. It must enable lower tier authorities to perform the functions assigned to them, especially the provision of basic services to all citizens. The implication is that such allocations offer a more equitable mechanism for financing free basic services than cross subsidisation that will distribute the burden of redistribution unequally among people in different municipal jurisdictions.

THE ECONOMIC BASIS FOR THE GENERATION OF INCOME

It could be argued that the provision of free or subsidised basic services would be more affordable if a municipality were to exploit fully the economic base for the generation of revenue. In principle, it does not depend whether the revenue is generated by means of rates (property tax) or by means of high tariffs on income-generating services. It would still come from the same economic base. (There are of course fiscal considerations about the proper balance among the various revenue sources and the effect of any excessive rate or tariff on the local economy, but that is not the focus of this investigation.)

Table 9 gives an indication of the extent to which municipalities in the Western Cape already claim a percentage of the income of households in their jurisdiction. Although municipalities also generate revenue from businesses, it can be assumed for the purposes of this analysis that in the (non-metro) municipalities investigated here that a considerable proportion of such costs on businesses would be passed onto consumers. The net effect is therefore not likely to lead to results that will differ significantly from the estimates in this table.

For households in the different municipalities in the Western Cape already between 5% and 25% of their annual income is probably already going to the local authority in the form of tariffs or rates. If it is considered that the total tax burden imposed by national and provincial governments is already approaching 30% of national income, then most municipalities are probably close to, if not beyond, the optimum exploitation of their economic base.

There is a real danger that a municipality that is close to that optimum level of exploitation of its economic base will thereby undermine that base and therefore its future ability to raise revenue. Many municipalities are already experiencing an emigration of skilled people and capital as a result of shrinking of its economic base. That process could be accelerated by excessive tariffs and rates, thus creating a vicious cycle of economic decline and increasing tariffs and rates in order to finance subsidised basic services.

TABLE9:UTILISATIONOFECONOMICBASE

MUNICIPALITY	CENSUS		PROVINCIALSURVEY				Total Income	TotalMun. Income/ H/hold Income %
	Annual household income (2002) Rand	Income from Saleof Electricity Rand	Income from Saleof Water Rand	Income from Saleof Sewerage Rand	Income from Saleof Refuse Rand	Income from Property Tax Rand		
Matzikama	495963291	16880480	5779550	3622760	1655720	7174260	35112770	7.08%
Cederberg	352268241	12209223	4195946	2778466	1828220	6351277	27363132	7.77%
BergRiver	477256672	15785000	4420000	2132000	2164000	7075000	31576000	6.62%
SaldanhaBay	796729053	45819779	29528582	9579799	10053096	32880222	127861478	16.05%
Swartland	867831749	36253638	9773871	6291514	5012125	15721562	73052710	8.42%
WestCoast District		524494	2785554	0	178464	153809	3642321	
Witzenberg	736138621	23364971	8286191	9690596	6220517	13384236	60946511	8.28%
Drakenstein	2394210148	167523881	33824780	10506470	19948369	49001311	280804811	11.73%
Stellenbosch	1641876191	86387070	19594565	13364022	10597099	41112060	171054816	10.42%
BreedeValley	1554407771	64621550	18966516	10160718	10761298	25245269	129755351	8.35%
Breë River/Wineland	769722479	44996401	11478893	6273784	3712307	11571055	78032440	10.14%
BolandDistrict		0	5828357	2765526	0	0	8593883	
Theewaterskloof	820550844	14303883	8403275	6395994	4965270	12017637	46086059	5.62%
Overstrand	754466993	31158211	8144731	15975535	12484369	36673775	104436621	13.84%
CapeAgulhas	350276443	18781210	6193702	3205176	0	8884000	37064088	10.58%
Swellendam	319188636	10393390	4263350	2844700	1708070	4868750	24078260	7.54%
OverbergDistrict		14533.02	387695.7	197154	221546	575084.4	1396013.07	
Kannaland	220478334	4386473	741764	1234518	584869	1435545	8383169	3.80%
Langeberg	530174801	20529689	6838457	4685495	3179017	8875420	44108078	8.32%
MosselBay	943543390	58826982	22396181	16621018	8538015	19352391	125734587	13.33%
George	1653553225	95880635	29896216	22686482	13879519	62754669	225097521	13.61%
Oudtshoorn	896988808	28332662	8513279	5846359	3758806	15750221	62201327	6.93%
PlettenbergBay	276057476	20443814	11182906	9198512	5103457	22637240	68565929	24.84%
Knysna	635890241	42500000	21370000	11482000	8486000	26299000	110137000	17.32%
GardenRoute/KK		1626780	1134437	310136	213574	465092	3750019	
Laingsburg	54822960	1550931	519804	513382	362080	469495	3415692	6.23%
PrinceAlbert	87286517	2014980	445180	658257	336608	634030	4089055	4.68%
BeaufortWest	349041149	13681612	5098215	4403077	1555100	6904327	31642331	9.07%
CentralKarooDis		749816	229005	119788	78727	205000	1382336	

INTER-GOVERNMENTALANDFISCALARRANGEMENTS

In this section we explore the effect of inter-governmental transfers on the affordability of free or subsidised basic services. Table 10 presents all the transfers from the national government to municipalities during the national financial year 2002/03. Four categories of transfers are shown.

In the last column these transfers are compared with the total income generated by municipalities from services and property tax. Although the years in Table 10 are not the same, the estimates still serve to give an indication of the extent to which municipalities received national financial support in the form of grants and transfers. For most municipalities it is between 2% and 16%. For a few municipalities it is significantly more and for all district municipalities it is even more than their own revenue.

TABLE10:ALLOCATIONSANDTRANSFERSTOMUNICIPALITIES

MUNICIPALITY	TRANSFERSFROMNATIONALGOVERNMENT					OWN INCOME	PERCENT Transfers/ Owninc.
	Equitable Share	Infrastructure transfers	Current transfers	Indirect transfers	Total allocations		

	2002-03 Rand	2002-03 Rand	2002-03 Rand	2002-03 Rand	2002-03 Rand	2001-02 Rand	%
Matzikama	2,976,922	754,800	119,165	820,000	4,670,887	35,112,770	13.30%
Cederberg	2,472,806	80,600	238,330	120,000	2,911,736	27,363,132	10.64%
BergRiver	1,761,866	364,000	238,330	0	2,364,196	31,576,000	7.49%
SaldanhaBay	1,473,044	364,000	685,200	0	2,522,244	127,861,478	1.97%
Swartland	3,219,868	3,155,600	2,685,200	2,441,000	11,501,668	73,052,710	15.74%
WestCoastDistrict	1,639,799	7,050,331	2,119,165	7,227,000	18,036,296	3,642,321	495.19%
Witzenberg	4,179,210	3,280,872	923,535	0	8,383,617	60,946,511	13.76%
Drakenstein	6,765,444	4,696,655	1,191,655	600,000	13,253,754	280,804,811	4.72%
Stellenbosch	3,735,837	2,741,904	2,423,535	0	8,901,276	171,054,816	5.20%
BreedeValley	6,108,881	2,748,234	1,072,300	0	9,929,415	129,755,351	7.65%
BreëRiver/Wineland	4,167,907	1,831,559	1,042,700	0	7,042,166	78,032,440	9.02%
BolandDistrict	1,994,671	5,369,900	2,299,200	0	9,663,771	8,593,883	112.45%
Theewaterskloof	3,826,871	31,200	895,325	0	4,753,396	46,086,059	10.31%
Overstrand	2,003,736	1,040,000	1,185,200	850,000	5,078,936	104,436,621	4.86%
CapeAgulhas	1,097,095	880,000	119,165	0	2,096,260	37,064,088	5.66%
Swellendam	1,950,169	600,000	214,500	0	2,764,669	24,078,260	11.48%
OverbergDistrict	982,502	5,513,111	399,200	150,000	7,044,813	1,396,013	504.64%
Kannaland	2,307,579	281,200	275,080	1,000,000	3,863,859	8,383,169	46.09%
Langeberg	2,274,962	462,800	1,042,700	200,000	3,980,462	44,108,078	9.02%
MosselBay	2,087,709	2,340,000	804,370	0	5,232,079	125,734,587	4.16%
George	3,632,756	3,558,433	3,304,370	1,441,000	11,936,559	225,097,521	5.30%
Oudtshoorn	2,712,367	1,404,604	1,191,655	360,000	5,668,626	62,201,327	9.11%
PlettenbergBay	1,827,880	100,000	458,790	0	2,386,670	68,565,929	3.48%
Knysna	2,393,444	1,168,800	3,149,450	1,441,000	8,152,694	110,137,000	7.40%
GardenRoute/KleinKar	2,223,638	7,065,311	2,418,370	4,867,000	16,574,319	3,750,019	441.98%
Laingsburg	1,707,342	117,150	506,455	400,000	2,730,947	3,415,692	79.95%
PrinceAlbert	1,980,927	1,000,000	238,330	776,000	3,995,257	4,089,055	97.71%
BeaufortWest	1,937,036	2,656,280	458,790	150,000	5,202,106	31,642,331	16.44%
CentralKarooDistrict	3,947,746	20,800,673	3,025,620	2,000,000	29,774,038	1,382,336	2153.89%
CapeTown	97,946,101	99,739,410	3,000,000	1,441,000	202,126,511	0	

However, these percentages are not really appropriate as some of these allocations are earmarked for specific objectives or not available for the financing of basic services. In Section 11 only the equitable share allocations are assumed to be available for the financing of basic services.

9. OTHER FREE SERVICES

Some municipalities also give certain other services free or at a reduced fee to indigent or poor households. These services include cemetery costs, basic medical services, social and welfare services, support to pensioners, and other diverse services, including roads and other infrastructure.

However, the impression obtained from municipal officials who were interviewed is that this class of services is very limited and that at this stage it is appropriate that it be left to municipalities to identify such services and to decide how to handle the provision of such services to the poor. This has the implication that a rebate on property tax amounts to the provision of most of these other services free. A household that meets the indigent criteria by definition do not have the ability to pay for services, they also do not have the ability to pay rates. By exempting them from rates, they will in fact also receive most of these other services free.

The conclusion this leads to with respect to the extension of free basic services to other services is that such an extension is likely to be very limited but that it is best dealt with at the local level and through the reduction of property rates. Moreover, it is beginning to

emerge that a more significant extension of subsidised services will be to extend the free provision of the four basic services to the indigent to subsidisation of these services for the poor whose net income will decline as a result of earning a higher income.

10. AFFORDABILITY OF OTHER FREE SERVICES

As mentioned above, most other services that can be provided free or subsidised are normally financed out of the general revenue account of the municipality. The most important source of revenue for this is property rates. This applies to the recurrent or operating costs of these services. The capital or infrastructure spending is financed in different ways, but is not the focus of this investigation.

However, capital projects have a growing implication for the affordability of basic services. There is a high probability that every beneficiary of a sub-economic housing project will qualify as an indigent or will not be able to afford the full economic tariff of basic services. Therefore, most houses built in housing projects and most extensions of the social infrastructure in poor areas will contribute to the fiscal burden on a municipality as a result of free or subsidised basic services.

It follows that the affordability of other free (or subsidised) services, as well as the affordability of the four basic services, will increasingly depend on municipalities receiving external revenue in addition to its own revenue from tariffs and rates.

11. EQUITABLE SHARE ALLOCATION AS FINANCING FOR BASIC SERVICES

Table 11 compares the equitable share allocation to a municipality with:

- own revenue (see discussion above);
- the cost to municipalities of free basic services to the indigent; and
- the combined cost of free basic services to indigent households and a 50% subsidy for these services to poor households (earning between R1100 and R1800 per month).

In each case the equitable share is expressed as a percentage of the comparable figure.

Table 11 must be interpreted with care, given the nature of the equitable share allocation and the differences among municipalities with respect to the provision of free services. The district municipalities provide very few basic services and also have a revenue base that is very different from that of primary municipalities and must therefore not be compared with Category B municipalities.

The following discussion only applies to Category B municipalities.

TABLE 11: EQUITABLE SHARE ALLOCATION AND COSTS OF FREE AND SUBSIDISED SERVICES

MUNICIPALITY	EQUITABLE SHARE allocation 2002-03 Rand	OWN INCOME 2001-02 Rand	PERCENT Equitable share/Own Income %	Cost Free Services Rand	PERCENT Equitable share/costs free services %	Cost Subsidies Rand	PERCENT Equitable share/costs subsidies %
--------------	--------------------------------------------	----------------------------	-----------------------------------------	----------------------------	--------------------------------------------------	------------------------	----------------------------------------------

Matzikama	2,976,922	35,112,770	8.48%	9,158,029	32.51%	12,234,918	24.33%
Cederberg	2,472,806	27,363,132	9.04%	6,352,929	38.92%	11,672,495	21.18%
BergRiver	1,761,866	31,576,000	5.58%	2,857,666	61.65%	8,293,585	21.24%
SaldanhaBay	1,473,044	127,861,478	1.15%	4,085,410	36.06%	9,060,115	16.26%
Swartland	3,219,868	73,052,710	4.41%	7,295,602	44.13%	14,754,137	21.82%
<u>WestCoastDistrict</u>	<u>1,639,799</u>	<u>3,642,321</u>	<u>45.02%</u>	<u>2,696,286</u>	<u>60.82%</u>		
Witzenberg	4,179,210	60,946,511	6.86%	7,867,955	53.12%	44,728,905	9.34%
Drakenstein	6,765,444	280,804,811	2.41%	793,364	852.75%	32,020,717	21.13%
Stellenbosch	3,735,837	171,054,816	2.18%	5,946,385	62.83%	27,691,845	13.49%
BreedeValley	6,108,881	129,755,351	4.71%	10,878,208	56.16%	41,918,581	14.57%
BreëRiver/Wineland	4,167,907	78,032,440	5.34%	12,986,405	32.09%	25,037,124	16.65%
<u>BolandDistrict</u>	<u>1,994,671</u>	<u>8,593,883</u>	<u>23.21%</u>	<u>1,329,964</u>	<u>149.98%</u>		
Theewaterskloof	3,826,871	46,086,059	8.30%	6,239,285	61.34%	23,440,735	16.33%
Overstrand	2,003,736	104,436,621	1.92%	7,776,664	25.77%	9,562,696	20.95%
CapeAgulhas	1,097,095	37,064,088	2.96%	2,310,707	47.48%	4,265,545	25.72%
Swellendam	1,950,169	24,078,260	8.10%	12,386,911	15.74%	12,386,911	15.74%
<u>OverbergDistrict</u>	<u>982,502</u>	<u>1,396,013</u>	<u>70.38%</u>	<u>0</u>	<u>0</u>		
Kannaland	2,307,579	8,383,169	27.53%	3,024,012	76.31%	4,055,295	56.90%
Langeberg	2,274,962	44,108,078	5.16%	4,705,120	48.35%	7,887,646	28.84%
MosselBay	2,087,709	125,734,587	1.66%	15,531,534	13.44%	18,215,982	11.46%
George	3,632,756	225,097,521	1.61%	7,048,477	51.54%	19,242,813	18.88%
Oudtshoorn	2,712,367	62,201,327	4.36%	12,106,754	22.40%	18,609,849	14.57%
PlettenbergBay	1,827,880	68,565,929	2.67%	14,344,320	12.74%	14,344,320	12.74%
Knysna	2,393,444	110,137,000	2.17%	13,203,688	18.13%	17,124,979	13.98%
<u>GardenRoute/KK</u>	<u>2,223,638</u>	<u>3,750,019</u>	<u>59.30%</u>	<u>115,194</u>	<u>1930.34%</u>		
Laingsburg	1,707,342	3,415,692	49.99%	906,194	188.41%	1,191,914	143.24%
PrinceAlbert	1,980,927	4,089,055	48.44%	1,057,255	187.37%	2,098,124	94.41%
BeaufortWest	1,937,036	31,642,331	6.12%	7,297,008	26.55%	7,435,113	26.05%
<u>CentralKarooDist</u>	<u>3,947,746</u>	<u>1,382,336</u>	<u>285.59%</u>	<u>2,428,039</u>	<u>162.59%</u>		
<u>TOTALOnlyB</u>	<u>68,601,658</u>	<u>1,910,599,736</u>	<u>6.12%</u>	<u>176,159,882</u>	<u>38.94%</u>	<u>387,274,342</u>	<u>17.71%</u>

As a percentage of a municipality's own revenue, the equitable share allocation varies between about 1% and 9%, except for the three exceptional municipalities (Kannaland, Laingsburg and Prince Albert).

For most municipalities the equitable share allocation is a relatively unimportant source of revenue. However, the Constitution makes specific reference to the provision of basic service to the whole population. The Government has also put special emphasis on the provision of free basic services, especially to those who cannot afford it. The perception has consequently developed that the equitable share allocation is intended for free basic services.

The second comparison in Table 11 is with the cost of free basic services to indigent households. The equitable share allocation varies as a percentage of the cost of free basic services to the indigent between a low 13% (Plettenberg Bay) and a high 853% (Drakenstein). These large differences are probably the consequence of the cost differences in the delivery of basic services and differences with respect to free basic services.

For example, the cost of free basic services is the highest by far in Plettenberg Bay, partly because Plettenberg Bay provides free services to indigent households with respect to water, sewerage and refuse. The cost of Drakenstein, on the other hand, is the lowest of all the municipalities and free services are also provided for water.

A significant observation is that for Category B municipalities the average contribution of the equitable share to the financing of free basic services to indigent households was probably not enough in 2002, the average percentage being 39%. Therefore, if the

equitable share is only used to finance free basic services to the indigent, the allocation is currently enough to deliver those services free to registered households.

The last comparison in Table 11 focuses on the extension of subsidised basic services to poor households (R1100 to R1800 per month). The cost of free basic services to the indigent plus 50% of the cost of delivering such services to poor households is compared with the equitable share allocation by expressing the latter as a percentage of the former.

For all the Category B municipalities the average percentage (equitable share/cost of free and subsidised basic services) is 17.7%. If the three outliers are excluded this percentage decreases only to 17.4%. In other words, the equitable share (as it was in 2002/03) was on average probably not more than about 18% of the cost of the extended subsidisation of basic services.

12. ALTERNATIVE SOURCES OF FINANCING

The preceding analysis illustrates the dilemma faced by municipalities. An equitable treatment of all poor households will require the partial subsidisation of basic services to poor households whose net income will fall below the “breadline” (indigency cut-off criteria). However, if municipalities were to do this, the equitable share allocation would (in 2001/02) only have covered about 18% of the cost of this subsidisation.

Cross subsidisation is probably already at a level in most municipalities where it would have negative social and political consequences if it were to increase significantly. Own revenue from property rates is also under great pressure and many municipalities probably do not have scope for increasing it much more.

A further limitation on the tax revenue capacity of municipalities is the likelihood that households that qualify for free or partially subsidised basic services will also have to be given a discount on property rates. If not, equity will be compromised if the payment of property tax will decrease the net income of a poor household below the indigency cut-off (“breadline”) level.

The implication of this is that if society wants equity and fairness to be applied in the provision of basic services to the poor, it will have to make it affordable or it will not be a basic service, i.e. some households will not receive it because they cannot afford to pay for it in full. In South Africa the mechanism for that was created in the Constitution by demanding that revenues collected nationally must be shared.

This reasoning emphasises that there are ultimately only two alternative sources of financing available to municipalities with which basic services to the indigent and the very poor can be financed. First, there is the extension of the equitable share allocation in a manner that will give a greater weight to the actual provision of basic services to poor, as well as indigent, households. Second, there is the introduction of a conditional grant from national government to municipalities for subsidising the delivery of basic services to a particular target group of poor people such as the recipients of a social pension.

13. FREE BASIC SERVICES DEFINED

As indicated at the start of this report, the analysis and discussion of all the relevant aspects of the provision of basic services to indigent and poor households will allow us to complete the circle by returning to the task of defining free basic services.

It is recommended that a free basic service be defined as that quantity (or level) of any existing municipal service (appropriate to the **urban or rural** context in which the recipients live) that is essential for a household, who does not earn enough income to pay for it in full, to live with human dignity, basic health and hygiene, and that can be made affordable by an allocation or grant from revenues collected nationally. This definition has the following implications:

- The income that is necessary for a household to live with human dignity, basic health and hygiene before paying for any municipal services, must be statutorily defined. (The “breadline” income.)
- The volume or level of each of the main municipal services that is necessary for a household to live with human dignity, basic health and hygiene must be statutorily defined. (The “breadline” service.)
- Every household must receive a subsidy (or discount) on any tariff or rates large enough that no payment of municipal tariffs for a “breadline” service or municipal rates will reduce the household’s net income (after payment for any “breadline” service) to below its “breadline” income. (The “breadline” subsidy.)
- The equitable share allocation plus any appropriately targeted conditional grant from national government must be at least enough to cover the sum of all the “breadline” subsidies to which individual households are entitled in terms of the points above.

14. **RECOMMENDATIONS**

It is recommended that:

- The Provincial Administration of the Western Capetakes the lead in formulating the principles according to which free basic services, as defined above, should be financed, including the desirability and sustainability of providing a certain quantity of water and electricity free to all households.
- The “breadline” principle receives particular consideration as a potential basis according to which free or partly subsidised basic services to the indigent and poor households can be provided in a sustainable manner.
- The Province compiles a policy framework with guidelines to municipalities about the provision of free or subsidised basic services and the financing of it.
- The Province launches an investigation into the manner in which the equitable share allocation to local authorities is calculated in order to be able to submit a well-motivated recommendation to the national government that the formula for the calculation of the equitable share allocation be reviewed.
- The equitable share formula must give specific recognition to the actual delivery of basic services and the introduction of a sliding scale according to which the poor can be given discounts on basic service tariffs.
- The Province launches a policy investigation into the introduction for a specific target group (e.g. pensioners) of a conditional grant from the national government to municipalities for the introduction of a tariff sliding scale according to which a discount can be given to poor households in that target group so that their net income (after the payment for tariffs and rates) will not fall below the “breadline”, and the likelihood of submitting a proposal in this regard to the national government.

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