

# FREE BASIC SERVICES IN THE WESTERN CAPE

## SYNOPSIS OF FINAL REPORT

In August 2002 the Provincial Minister of Local Government announced in a press release the investigation into the provision of free basic services in the Western Cape. This report is the product of that investigation.

Sustainable affordability is an inherent and inseparable aspect of the definition of a basic service. The approach that is recommended here is that basic services be defined including the concept of sustainable affordability. If it were to be determined, whether by national, provincial or local government policy, that the "breadline" (minimum income) for an average household is a certain amount (for this analysis it was assumed to be R1200 per month) without including the cost of basic services, a household will not be able to afford a basic service if it will push the net household income (after the payment of basic services) to below the "breadline".

Cross-subsidisation finances on average about 56% of the cost of free basic services to indigent in the Western Cape. The equitable share allocation finances about 34% of the cost and the rest (about 10%) is financed by a council vote, i.e. by taxpayers. It is clear that for some municipalities the provision of free basic services to indigent households would not be affordable if it had to be done through cross-subsidisation.

However, there are also poor households that can perhaps afford a partial tariff for a basic service, but not the full economic tariff. The percentage poor households increases considerably if an income of less than R1800 per month is taken as an indication 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 were to be subsidised by 50% of tariffs (and the indigent 100%), then the tariffs of full paying consumers would increase by between 22% and 85%. This gives an indication that the affordability of subsidised basic services, if use was made exclusively of cross-subsidisation, should be seriously questioned. The "breadline" principle is that basic services should be provided free or subsidised and that rebates should be given on property rates, to the extent that is necessary to prevent that the net income of a household declines to below the "breadline".

Between about 5% and 25% of the annual income of households in the Western Cape already go to the municipality in the form of tariffs or property rates. Most municipalities are probably close to the optimum utilisation of their economic base. There is a danger that a municipality that is close to the optimum exploitation of its economic base and tries to generate more income, can undermine that very same economic base. The local economy can experience an outmigration of ownership and capital if a municipality tries to redistribute too much.

A consideration behind the launch of this investigation, is the policy question of whether it is perhaps necessary to extend the free delivery of basic services (electricity, water, sewerage and refuse) to other services. The extension of free services must, however, not really be to other services, but rather the extension of the current basic services to the partial subsidisation thereof to poor households.

The affordability of the basic services depends on whether the equitable share allocation is

sufficient for the financing of free or subsidised basic services. As a percentage of municipal own revenue, the equitable share allocation varies between about 1% and 9% for most municipalities. The equitable share allocation is therefore a relatively unimportant source of revenue for most municipalities.

For the Category B municipalities the average equitable share allocation is 39% of the cost of free basic services to indigent households. Even if the equitable share allocation was therefore utilised only for the financing of free basic services (as currently defined), the average allocation will not be sufficient to cover the cost of free basic services to indigent households.

The extent to which the equitable share would be able to finance part of the extension of subsidised services to the poor in 2002 was investigated. For all the Category B municipalities the average percentage (equitable share as a percentage of the cost of free and subsidised services) is 18%. With the exclusion of the three outliers, this percentage declines to only 17.4%. In other words, the equitable share allocation would, in 2002, only have been about 18%.

After the analysis and discussion of all the relevant aspects of the provision of basic services to indigent and poor households the definition of free basic services was again investigated.

The conclusion was that a free basic service be defined as that quantity (or level) of any existing municipal services (appropriate to the **urban** or **rural** context in which the recipients live) that is essential for a household, that 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 revenue 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.

## **RECOMMENDATIONS**

It is recommended that:

- The Provincial Administration of the Western Cape takes 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 sliding tariff 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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