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FINANCIAL AND FISCAL RELATIONS

CONSTITUTIONAL ASSEMBLY
AMENDED SUBMISSION TO THEME COMMITTEE 3
PHASE 5

Draft 6

FINANCIAL AND FISCAL POWERS

Discussion

Constitutional Principle XXVI provides for the right of every level of government to an equitable share of revenue collected nationally to ensure that they (including local government) are able to provide basic services and execute the function allocated to them.

This Principle recognises that the major sources of revenue in the South African economy are collected nationally; in particular the major taxes, namely income tax (including company tax) and VAT.

The ANC does not favour the Canadian approach, which allows powers to levy any direct tax within the provinces in order to raise revenue for provincial purposes.¹ The German model represents a far more systematic approach to intergovernmental fiscal relations. In particular the German Basic Law gives the central state extensive legislative powers in the field of taxation, such that all major tax laws are central laws. This is considered to be in accordance with the wording and intention of Constitutional Principle XXVI.

Three inter-related questions are raised in this regard:

- The content of the formula for equitable shares (linked to the developmental objectives of the country),
- the manner in which the Financial and Fiscal Commission (FFC), responsible for making recommendations on the revenue sharing formula, should relate to the provincial and national legislatures, and

1 Sect 92(2), Canadian Constitution.

- the role of provinces (in the context of cooperative governance) in making decisions about the recommendations of the FFC.

Determining the formula

The ANC proposes that the formula not be stipulated in the final constitution, but be provided for in national, enabling legislation. The constitution should provide that the determination of the formula should be consistent with the developmental objectives of the country and arrived at through the following process:

- The FFC submits its recommendations on the revenue sharing formula to the relevant standing committees of Parliament and the provincial legislatures for comment on the norms and parameters encapsulated in the formula,
- the FFC submits its revised recommendations, after feedback from Parliament and the legislatures, to an appropriate intergovernmental forum,² which should include appropriate local government representation, for amendment through joint consultation between the provinces and national government, and
- the revenue sharing formula, with the proposed amendments from the intergovernmental consultation, is submitted to national Parliament for final consideration and enactment.

The ANC's view is that South Africa should have a predominantly unified legislative and administrative fiscal and public financial system. It should be a *joint* fiscal system, under leadership of national government, and not a rigidly *divided* system between national and provincial levels of government. In this regard there should be a *co-operative* rather than a *competitive* relationship between national and provincial governments. This would amount to the provinces being involved in decision-making about fiscal matters through the involvement of both their legislatures and executives in considering FFC recommendations and approving, where appropriate, policy frameworks, revenue sharing formulae, and the norms and standards forming the basis for intergovernmental grants. This will ensure that all governments concerned will accept responsibility for acting within frameworks agreed through the process as proposed.

Proposals

Giving effect to the above new arrangements, would require the following:

1. The final constitution should provide that the new Council/House of Provinces (Senate) be given an appropriate role in the passage of money bills.
2. Any recommendations in this regard should fit in with proposals to broaden and strengthen the role of Parliament in the passage of money bills.
3. Legislatures' standing committees and departmental representatives of the provinces should be actively involved in the process of agreeing on the norms and standards upon which the revenue sharing and grants formulae will be based. They should also be suitably involved in the preparation of their budgets. This will be facilitated through a multi-year budgeting process broken down into clear steps at which the participation and agreement of the legislatures will be required. The constitution should require that there be framework legislation to provide for an effective role of the legislatures in the budgeting process.

2 See in general the ANC submission on Intergovernmental Relations, Theme Committee 3, Phase 3.

4. A national *Budget Cooperative Council*, operating under the auspices of the new Council/House of Provinces (Senate), could be established by national legislation to achieve greater coordination over fiscal matters. With representatives from the standing committees and finance executives of both national and provincial government, and possibly an appropriate forum of local government representation, such a BCC could give provinces a role in the determination of the macro-framework. This could provide a rational context within which provinces could draft their own budgets. This process would empower provincial legislatures, as well as the national Parliament, to play a more meaningful role in the determination of the allocation of public resources and the building of a broad understanding of what governments are trying to achieve. All provinces should have equal representation on such a BCC, which should be chaired by the national Minister of Finance.
 - To this end it is proposed that the constitution shall in general terms empower national government to pass framework legislation to facilitate intergovernmental cooperation on fiscal matters.
5. Clauses similar to Sections 156(2), 157(1)(a), (b), (3) and 158(a) and (b) in the Interim Constitution should be carried over to the final constitution. These may have to be amended for greater clarity or consistency. For example, the formulation "surcharges on taxes" could be interpreted as allowing only a percentage to be added to the national tax rate (an undesirable mechanism), rather than a percentage to be imposed on the nationally determined *base* (e.g. personal income), which would avoid many of the negative features of the first interpretation. The ANC is of the view that these powers should be allocated and exercised in a manner consistent with the concept of cooperative governance.
6. Where it is more efficient to collect a tax locally, regionally or provincially, the appropriate level should be allocated this power and the right to use income thus collected.
7. The constitution should provide that the bulk of revenue should be apportioned at national level through a process like that proposed above, thus ensuring that provincial governments and legislatures, and, indeed, representative local government, participate³ in the formulation of the norms and standards upon which the FFC will have to make its recommendations.
8. A clause similar to Section 157(2) of the Interim Constitution should be included along the following lines:

"Loans referred to in [157(1)(a)] may be raised for bridging finance in the fiscal year subject to reasonable conditions as may be prescribed by an Act of Parliament passed after recommendation by the Financial and Fiscal Commission."

3 Also by way of the new Council/House of Provinces (Senate).

FINANCIAL AND FISCAL COMMISSION

Discussion

Constitutional Principle XXVII specifies that the new constitution shall provide for a Financial and Fiscal Commission in which each province shall be represented to:

“recommend equitable fiscal and financial allocations to the provincial and local governments from revenue collected nationally, after taking into account the national interest, economic disparities between the provinces as well as the population and developmental needs, administrative responsibilities and other legitimate interests of each of the provinces.”

The ANC is of the view that many of the broad principles contained in Sections 198 to 206 of the Interim Constitution should be carried into the final constitution, but consider much of the detail included in these sections should be dealt with in national legislation rather than the constitution.

At present there is considerable lack of clarity in the wording of the applicable sections of the Interim Constitution. In particular:

- The reference to “equitable financial and fiscal allocations” leaves open to doubt whether the section refers exclusively to vertical equity⁴ or accommodates horizontal equity. It should refer to both.
- Section 199(1)(b), which refers to revenue collected at national level, could mean one of the following:
 - Revenue collected in the nation as a whole, i.e. by all levels of government, or revenues collected by the national government, whether for its own account or as an agent on behalf of the other levels of government, or
 - revenues collected at the national level, including the shares of the taxes specified in Section 155, but excluding revenues collected on an agency basis on behalf of other jurisdictions⁵, or
 - revenues collected at the national level, but excluding the specified shares of income tax, VAT and the fuel levy that has to go to the provinces, and excluding revenues collected on an agency basis on behalf of other jurisdictions.
The ANC submits that it should refer to the third definition.⁶
- It is uncertain as to what distinction should be drawn between taxes, levies, imports and surcharges in Section 199(1)(c).
The ANC submits that an alternative phrasing to the effect that “any form of tax regardless of the name given to it” is more precise.
- Section 199(1)(d) speaks of the “raising of loans”. The Financial and Fiscal Commission has submitted that this ought to cover any form of credit or advance to a provincial or local government or any agency owned or controlled by such a government. The ANC concurs in

4 Sect 199(1)(b).

5 E.g. transfer duties.

6 Concurring with the submission by the FFC of 5 June 1995.

7 *Ibid.*

- Section 178(2) states that local governments are “competent to levy and recover such property taxes, levies, fees, taxes and tariffs as may be necessary”. Once again it is not possible to draw a clear distinction between these terms, but the implication is that local governments are not subject to the same constitutional restraints as provinces. The clauses should be consolidated into one coherent and consistent section with a formulation similar to the above proposed new Section 199(1)(c). Local government powers of taxation and borrowing should be correspondent to those of provincial governments.

Proposals

9. The provisions relating to the establishment, objects and functions of the Financial and Fiscal Commission in Sections 198 to 199 of the Interim Constitution should be incorporated in the final constitution in abbreviated and revised⁸ form.
10. The constitution should provide that the Financial and Fiscal Commission shall be an independent statutory body, composed of persons with knowledge, experience and expertise in the fields as defined in Section 200(3)(b) of the Interim Constitution.
11. The constitution should provide that members of the Commission shall be appointed by the President in consultation with both the Cabinet and a cooperative council composed of representatives of the Executive Committees of the provinces, provided that if representatives of provinces in which the largest majority party is different from that in the National Assembly are dissatisfied with the composition of the Financial and Fiscal Commission as it emerges from this process, they may nominate persons of their own choice that meet the requirements in terms of expertise, in accordance with the number of seats in their provincial legislature as a proportion of the total number of seats in all provincial legislature.
12. While the constitution should specify the method of appointment (and possibly also the method of impeachment) of commissioners to ensure their independence, national legislation should specify the number of members of the FFC, their full-time or part-time status, and the manner of choosing a chair and deputy chair, to allow for flexibility in terms of numbers and extent of participation, and to take account of the experience of the present Financial and Fiscal Commission and international practice.⁹
13. The provisions for meetings, remuneration, co-optation and length of office that are covered by Sections 200 to 206 of the Interim Constitution shall be provided for in national legislation.
14. The constitution should state clearly that the Financial and Fiscal Commission has advisory and mediatory powers which must be reflected in the procedures for drafting budgets and fiscal legislation.
15. The constitution should provide that the Financial and Fiscal Commission present regular reports both to Parliament and to provincial legislatures in a manner to be determined by national legislation.

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⁸ See the above discussion.

⁹ It would also reinforce the position that the FFC is an independent, expert body, in which all the members have the same function and lines of accountability.